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COVID-19 Uncertainty Continues to Impact Markets

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Our hearts and thoughts are with the families across the globe that have been touched by COVID-19. We encourage our staff, suppliers, families and business clients that we serve to observe CDC guidelines to ensure their safety, and the safety of others, during these challenging times. As our expertise resides in the area of wealth management, not health management, our comments below are specifically in relationship to financial markets.

Continued uncertainty around the COVID-19 virus has caused financial markets to remain volatile following a dramatic decline in prices across almost all risk assets. The health and economic impact of the virus will likely worsen before improving, and the magnitude will depend on the ability to contain it. However, a sensible asset allocation and proper diversification should help investors weather the duration of any economic slowdown that will occur in the near term. Further, we believe that the sharp sell-off is beginning to create pockets of attractive investment opportunities for long-term investors.

Several money managers we've spoken to in recent days have indicated to us that they're cautiously adding capital to existing holdings and opportunistically buying new securities. We believe that companies with strong balance sheets and structural competitive advantages are likely to survive a downturn and generate attractive returns if purchased at appropriate valuations. However, given the potential severity of the ongoing economic slowdown, it's possible that some companies may experience permanent capital impairment. Proper security selection and diversification can help avoid permanent losses and help mitigate the impact from unexpected shocks to any individual company.

The fear and anxiety caused by the Coronavirus and the market decline are entirely understandable; however, we remain confident that a calm, well-reasoned approach remains the proper one for a long-term investor. The best investment results are derived by taking a long-term view and positioning oneself accordingly, rather than rapid responses to the news cycle and short-term market fluctuations.

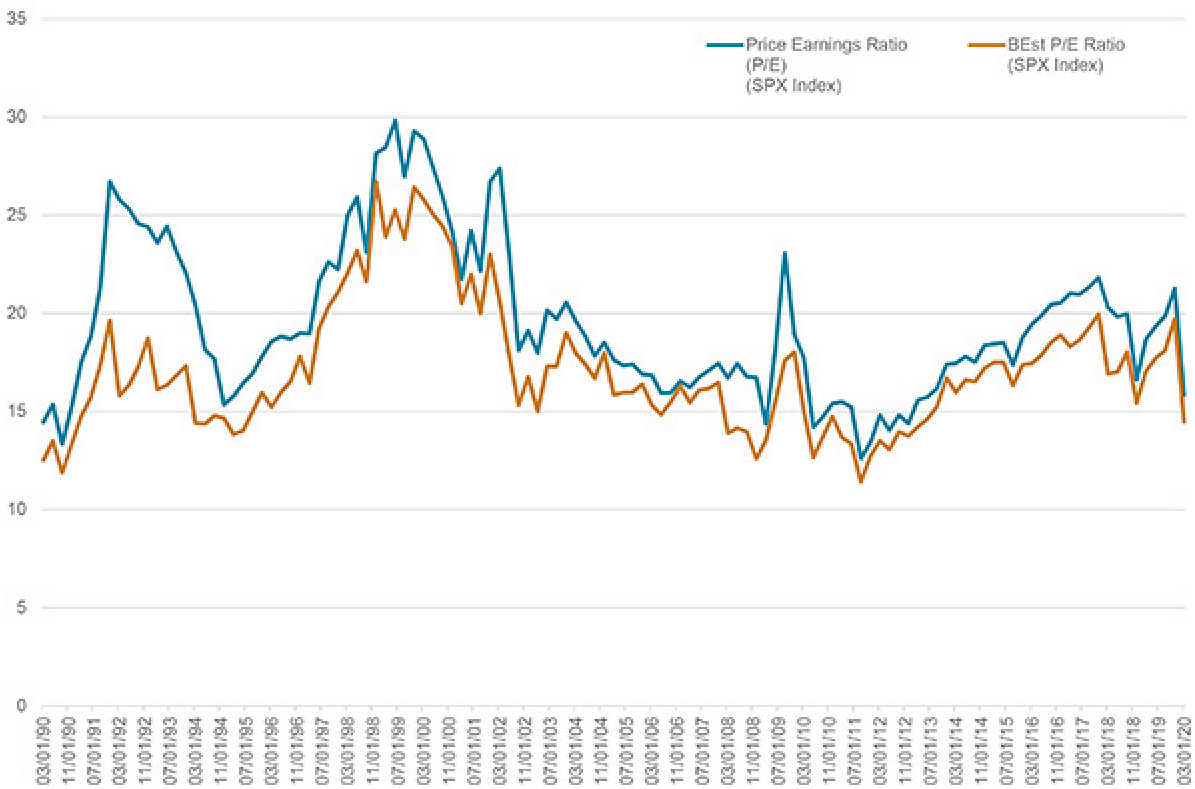
Please see below for additional market commentary across various asset classes:

Equities

Stocks have been punished across the board. The S&P 500 Index dropped nearly 28.7% since its market peak on February 19, 2020 through March 19, 2020. Small cap stocks fared even worse during this period with the Russell 2000 Index plunging 37.3%. Non-U.S. stocks also followed suit, as the MSCI EAFE Index dropped 31.3%, while the MSCI Emerging Markets Index fell 30.4%. The declines in small and non-U.S. stocks were sizable enough to push both asset classes into negative territory over the trailing three- and five-year periods as of this writing.

A silver lining to the precipitous decline in stock prices is that valuations are more reasonable than at any time in recent years. The S&P 500 Index's trailing P/E ratio fell from 22 times earnings to start 2020 at around 15 times earnings as of the time of this writing. Small cap valuations are similarly trading at much more attractive valuations compared to just a few months ago.

S&P Price to Earnings Ratio has fallen significantly over the past three months



Source: Bloomberg

Fixed Income
Volatility within normally sleepy portions of the bond market emphasizes the degree of uncertainty and concern rolling through financial markets. A need for cash, combined with increasingly illiquid trading markets and concerns over credit quality, have caused some bond markets to show signs of dislocation, enough so that the Federal Reserve announced crisis-era steps to stabilize markets. These steps include a $700 billion bond purchase program and further steps to provide stability to money market funds. Despite these moves, Treasury rates across the yield curve swung rapidly. For example, in just the past month, 10-year Treasury rates fell from 1.56% to 0.54% back up to 1.18% as of March 18.

Concerns over the severity of a slowdown have caused corporate bonds prices to drop across the credit quality spectrum. Investment grade corporate bonds have dropped in value and spreads have jumped from around 100 basis points over Treasuries to start February 2020 to 300 bps as of March 19, 2020. Investors also fled from high yield bonds, resulting in spreads shooting past 900 basis points over Treasuries. While some investors we've spoken with suggest that high yield bonds are attractively priced following this spread-widening, others indicate that profits could deteriorate further, and these bonds have additional room to decline. While opportunities exist, cautious security selection remains paramount in the corporate bond market.

High Yield bond spreads increased 900 points over Treasuries

Source: Federal Reserve Bank of St. Louis

Even the traditionally stable municipal bond market has shown signs of concern over a potential decline in tax revenues that could destabilize municipalities. The ratio of municipal bond yields to Treasury yields has jumped from 66% at the beginning of 2020 to more than 200% for some maturities, but this market continues to experience more volatility than normal.

Commodities

While the COVID-19 virus remains top of mind for investors, a price war in oil has added fuel to the fire. Oil prices, which started the year at more than $60 per barrel, quickly dropped to almost $20 a barrel in a matter of weeks following an announcement that Saudi Arabia would increase supply despite declining demand. The drop in oil prices caused the equity of some weaker oil and gas companies to drop as much as 90% in a short amount of time. Gold prices provided stability in 2019 but became a less reliable hedging tool so far this year, falling almost 3% year-to-date through March 19.

The S&P 500 Index, often abbreviated as S&P 500, is an American stock exchange market index based on the market capitalizations of 500 large companies having common stock listed on the NYSE or NASDAQ. The S&P 500 index components and their weightings are determined by S&P Dow Jones Indices.

The Russell 2000 Index measures the performance of the small-cap segment of the US equity universe. It is a subset of the Russell 3000 and includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership. Russell Investment Group is the source and owner of the trademarks, service marks and copyrights related to the Russell Indexes. Russell® is a trademark of Russell Investment Group.

The MSCI EAFE Index is a stock market index that is designed to measure the equity market performance of developed markets outside of the U.S. and Canada.

The MSCI Emerging Markets Index is an index designed to measure equity market performance in global emerging markets.

The ICE BofA US High Yield TR USD measures the performance of short-term US dollar denominated below investment grade corporate debt publicly issued in the US domestic market. Qualifying securities must have at least 18 months to final maturity at the time of issuance, at least one year remaining term to final maturity as of the rebalancing date, a fixed coupon schedule and a minimum amount outstanding of $100 million. It is capitalization-weighted.

The Dow Jones Commodity Index Gold is designed to track the gold market through futures contracts.

West Texas Intermediate (WTI) oil, also known as Texas light sweet, is a grade of crude oil used as a benchmark in oil pricing. This grade is described as light because of its relatively low density, and sweet because of its low sulfur content.

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Client Update: Recent Financial Markets and COVID-19

Market volatility has increased considerably in response to the spreading of the Coronavirus (COVID-19) and falling oil prices. Understandably, this may lead to questions about whether changes are needed to investors' portfolios.

We continue to focus on the importance of proper asset allocation and diversification, as both play important roles in helping our clients meet their financial goals. Investors should confirm that their short-term needs can be met via conservative, liquid investments such as cash, money market funds, or high-quality short-term bonds. A proper allocation that meets short-term needs can help insulate investors from volatility and prevent the need to sell equities in a downturn.

Many investors are tempted to 'time the market' during periods of significant volatility. We understand the temptation, but caution that selling at low prices or sitting on the sidelines for an extended period of time can have a dramatic impact on long-term performance. For example, $1 million lump sum invested in the S&P 500 Index in 1999 would have been worth $3.9 million at the end of 2019. However, if an investor missed just the best 10 days in the market over that time, that initial investment would only be worth $1.9 million[1]. It is impossible to know when a significant upswing in the market will occur, which reinforces the need to stay invested despite significant ongoing volatility.

We believe that one cannot reliably invest based on short-term prognostications and we are confident that stocks remain attractive for investors with a long-term time horizon. Our conviction in this belief will only strengthen if stocks fall further and become even more attractively valued. These beliefs are supported by the realization that the alternative, shifting from equities to bonds today at all-time lows in yields, may lock in sub-par returns and even some declines in value if rates were to increase.

We recognize that there are certain elements at play that are out of our individual control, including how the market will react to the news any given day or week. Rather than panicking over what we can't control, it is more constructive to focus on the things we can control. In our financial lives, we should verify that we have appropriate liquidity and a suitable asset allocation that matches both our needs and our risk tolerance while also keeping an eye open for opportunities.

We are here to help and answer any questions you may have. Please don't hesitate to contact us.

1 FactSet, S&P Dow Jones Indices as of December 31, 2019.

S&P 500 Index: Measures the performance of the 500 leading companies in in the large cap segment of the market. Companies are chosen based upon their market size, liquidity and sector. Together these companies represent approximately 80% of the available market capitalization.

The indices are unmanaged and do not incur management fees, transaction costs or other expenses associated with investable products. It is not possible to directly invest in an index

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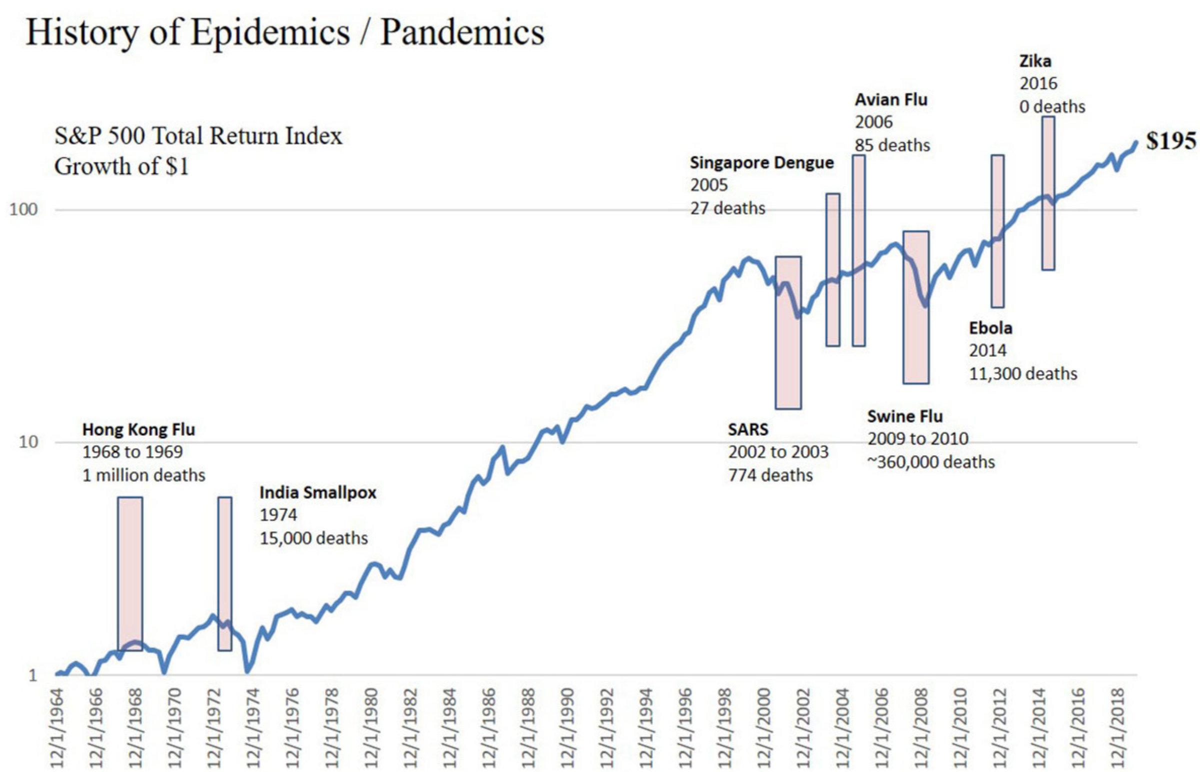
Client Update: The Coronavirus and Market Outlook

The Coronavirus appears to be stabilizing in China, but new cases are emerging in other countries around the world. Financial markets have moved sharply downward as concerns have grown over the global spread of the virus. This has justifiably led many individuals to be concerned about not just their own health, but also about the health of their portfolio. While it is impossible to predict exactly what the epidemiological path of the virus will look like, there are helpful reference points that can give guidance over likely market outcomes.

When facing a "known unknown," like the Coronavirus, it can be helpful for an investor to step back and view their investments from a couple of different perspectives. First and foremost, exogenous shocks like these are a good reminder of why it makes sense to maintain a balanced portfolio allocation that addresses meeting near-term needs and providing stability of capital, along with the desire for long-term growth. In these environments, cash and bonds serve as a ballast and can be used to meet expenses, keeping a long-term investor from being a forced seller of equities into market weakness.

Second, equities are long-term investments in individual businesses. While the prices of stocks often move rapidly in reaction to changes in near term earnings expectations, the intrinsic value of underlying businesses often change much more slowly. This is not meant to understate the human and economic impact that is likely to take place this year as supply chains are interrupted and consumer behavior changes. However, using previous epidemics such as Ebola, bird flu, SARS, and West Nile Virus as a guide, the impact to the long-term cash flows of businesses is likely to be minor. It is these long-term cash flows that determine the value of a business. Below is the S&P 500 Index's previous performance through various health epidemics.



Source: Morningstar Direct and Centers for Disease Control and Prevention

While we don’t underestimate the severity of the Coronavirus, we also realize that healthcare scares like this one eventually end. From that perspective, we view the impact as a short-term phenomenon and we do not expect significant changes to the long-term viability of most high-quality businesses.

As one investment manager recently pointed out to us, financial markets have seen multiple shocks over the past quarter century, including prior epidemics, multiple wars, and a global financial crisis, yet the S&P 500 Index increased ninefold over that time frame. In our opinion, markets thrive despite these macro shocks because macro-shocks are often temporary and do not impact long-term cash generation.

Please don't hesitate to contact us if you have any questions or concerns.

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