

Greetings:

Much ink will be spilled in coming years attempting to explain the historically swift and severe declines now taking place in global financial markets. However, for us, all these explanations will come down to one word – uncertainty. With the economy and markets now dealing with multiple interrelated shocks from the spreading coronavirus outbreak and collapsing oil prices, there is a lot that is still unknown, and events are evolving quickly.

Over the weekend, Spain became the second European country to go on lockdown, with other EU nations also moving to shut down places where groups of people gather as the number of coronavirus cases rises. In the U.S., developments have been equally quick and historic as a growing number of cities and states are now recommending or requiring mass closure, even mass self-isolation. Around the country, a rolling shutdown is underway of businesses, schools, restaurants, travel, and entertainment venues, with no clear indication when restrictions will be lifted.

Given this, we now expect a faster and deeper impact to U.S. economic growth and earnings than had been previously modeled, with two and possibly more quarters of significant negative GDP and earnings. Though considerable uncertainty remains, the only good news is that we see this recession as one which should recover as quickly as it has unfolded.

Event driven recessions, while sometimes deep, are typically much shorter lasting with growth recovering to normal as the shock abates and policy easing gains traction. Announcements by the Federal Reserve and officials in Washington over this weekend are reassuring in this regard. With the economy in an increasingly vulnerable position, moves to cut rates and inject liquidity into the financial system are timely and appropriate, as are relief measures passed by the federal government and the increasing, albeit belated, rollout of testing kits, which will be critical for authorities to getting a handle on the virus spread.

We believe the U.S. economy was on solid footing before these shocks, and policy action could be help cushion the fallout in coming quarters. Still, the most effective stimulus will be containment of the outbreak. From this perspective, developments in China and South Korea, which have been hardest hit, offer some encouragement for the path forward. With aggressive government response slowing the number of new coronavirus cases dramatically, many Chinese companies that were shuttered in February have started to reopen with employees beginning to return to work and supply disruptions are slowly abating as factories come back online.

For financial markets, the uncertainty driven by the unprecedented developments underway will likely keep volatility high in coming months as investors struggle to assess the impact on the economy and earnings as well as non-fundamental forces such as programmatic trading and emotional selling that are playing a significant role in exacerbating market movements.

As difficult as times like these are, we remain optimistic that markets will eventually recover as the present crisis fades. Typically event driven bear markets have quicker recoveries than those caused by banking system failure, and we expect that to be the case in this episode. We also expect lower rates and lower oil prices to provide stimulus for a strong rebound in financial markets once this crisis is behind us.

Going forward, we will closely monitor our economic indicators. If the situation deteriorates further than expected, we will be ready to take more decisive action. However, we also see opportunity ahead where valuations are depressed and future returns look very attractive. Once we see signs of stabilization in our indicators, the market should present opportunities on which to capitalize. We are not at that point yet, until then we believe the actions we have taken have helped fortify portfolios.

(City National Rochdale *March Market Madness*; www.cnr.com; 03/16/2020)

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Regards,
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