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OBSERVATIONS ON THE MARKET

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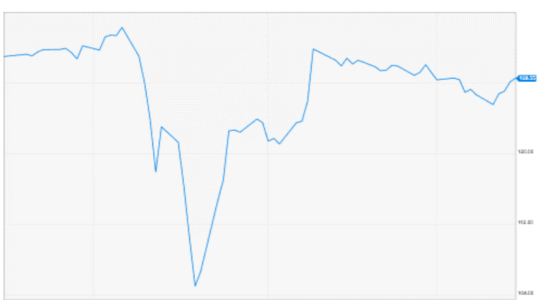
It seems like two separate worlds, the one we live in and the one we invest in. You know the one you live in is not going well, but then you see the world of money, which appears to be operating in another universe. As an example, one year ago, the S&P 500 was at the same level it is at now. In our world, however, it is difficult to find anyone who has not had their life turned upside down. It is easy to be uneasy about the future; what if these two worlds suddenly collide? Reconciling the two is an exercise in faith.

In 2008 congress, the Federal Reserve, and the Treasury argued over what approach should be taken and whom should be bailed out. They drew the line with Lehman Brothers, and the financial world responded by seizing up within 24 hours. One lesson learned from 2008 is that in the age of instant information, financial viruses can infect the world in a matter of hours, not weeks or months. In March when many parts of the economy were shut down and panic began to grip the markets, the Fed reacted within days. It is best illustrated in the chart of LQD, which is the index



of investment grade corporate bonds. Prices declined by 30% in only a few weeks. The Fed stepped in and started buying bonds, as well as the index fund LQD. Within a few more weeks, the market looked as if nothing had happened. With the bond market stabilized, the stock market soon followed. Even though the economy is still 'closed', the financial world was given its vaccine. The Federal Reserve openly stated that they will continue to support the credit markets until the world we live in catches up. How much does this medicine cost, you ask?

Here is the great news, almost nothing. The more they borrow, the cheaper it becomes. Interest rates on 1-5-year treasuries are basically zero. You pay them on short-term debt. Treasury debt that matures in ten years only costs .65%. Before you think that this cannot last very long, Japan has been in this situation for decades. This is not in any way implying the same will hold true for us. We all know that the economy must return to whatever its new normal is soon. Fortunately, parts of it continues to function, and, in niches like grocery stores and technology, even well.

If you look at the top 25 companies of the S&P 500, only a few are experiencing any real challenges. Exxon is the only one that looks like a company who is operating in an economy that is partially shut down. The top 25 represent 40% of the index's market value. The current earnings estimate for the S&P 500 for 2020 is $113, down from last years $157. Currently, analysts expect $164 for next year. Of course, everything depends on how fast the economy restarts. A few encouraging signs are out there. Disney in Shanghai opened at 30%, and tickets sold out in 3 minutes. It also appears that people are still willing to attend NFL football games. Demand for tickets appears to be strong. However, when an economy goes from the best employment number in 50 years to the worst in 80 years in only a few weeks, short-term predictions are hazardous at best.

The politics of the reopening is the big debate. No matter where you stand as to the pace of the reopening, the people will probably ultimately decide. It has been 75 years since Americans were told what they could buy and when. Back then, the World War had a common enemy, this situation is much less well defined. A quote from Robert Grant, a medical statistician sums it up best: "I've studied this stuff at university, done data analysis for decades, written several NHS guidelines (including one for an infectious disease), and taught it to health professionals. **That's why you don't see me making any coronavirus forecasts…**"