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INNOVATIVE STRATEGIES + PERSONAL FOCUS

Timely Topic

- March 2020 -

Stocks "Spring Forward" Into Worst Trading Day in 10* Years

First let us say, rest assured, we are watching the events and monitoring this situation in real time. We know the current headlines bring a lot of uncertainty, and the normal reaction is to want to "do something" to feel like we have better control (especially when it impacts our money). We want to share with you our thoughts of what is happening and why it is important to stay the course, with the hope that it reminds you of the work we've done to determine your risk tolerance and build your portfolio accordingly.

The breakdown of the OPEC+ alliance over the weekend triggered an oil-price war between the Saudis and the Russians, causing the biggest collapse in oil prices since 1991 and added to financial market distress over the spreading coronavirus. Yesterday morning, global equity markets plummeted on this news, which prompted a 15-minute halt in New York Stock Exchange trading shortly after markets opened and the S&P 500 dove 7%. These "circuit breakers'' were adopted after the October 1987 Black Monday to help calm panic selling and have been triggered several times over the last decade for various reasons.

Now, for a reminder of our advice to you:

1) **Focus on your individualized plan.** We have worked with you to understand your short-term and long-term goals, and created a plan to balance your long-term goals, need for cash from the portfolio, and your risk tolerance. At this point, we believe it is still appropriate to stick to the plans that we have created. Remember we have included assets in portfolios that are designed to help provide a reduction in volatility for markets such as this. That part of your portfolio has generally held up better against the market volatility (and therefore is not what you are hearing about in the news). When investing in the stock market, we are assuming the funds invested will not be utilized for at least five years in the future. Therefore, if your time horizon and objectives have not changed, we have already accounted for the possibility (and probability) of volatility in your portfolio.
2) **Be careful not to follow the panic….and keep this in perspective.**
   - Utilizing our "rear view mirror", it is clear to see that the best times to invest historically were when fear was at its highest – and we believe that we will someday come to the same conclusion with this current market. Remember that even if you don't have excess cash to put to work now, getting out of the stock market will lock in the losses over the course of the last several weeks, and it's impossible to know the "right time" to get back in.
   - Even with significant volatility last week (2 days of Dow Jones Industrial Average (DJIA) swings of more than 1,100 points), most of our diversified portfolios have held up against this market volatility.
   - There are many headlines that reference or compare this downturn to 2007-2009. However, we believe this is an inappropriate comparison. The fundamentals of the economy (employment, home starts, etc.) are in far better shape than 2007 (see our "positives thoughts" below for more information).
   - The worst mistake that people generally made in the market downturn of 2007-2009 was exiting the market. Record amounts of money left the stock market during the financial crisis, and many of those investors missed a large portion of the 281% S&P 500 increase from February 2009 and today (source: Yahoo Finance). The importance of staying invested is illustrated as follows: If you invested $100,000 in the S&P 500 at the beginning of 1999 and remained fully invested during two of the top five market corrections in history (Y2K/technology bubble/9-11 from 2000-2002 and the financial crisis from 2007-2009), you would have had more than $400,000 in your account by the end of 2019. However, if you missed out on only the ten best days during that 20-year period, you would have not even doubled your money (source: FactSet). Further, it's important to note that some of the best days in the market occur in the midst of the worst days, so staying invested is key[1].

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- Keep things in perspective. The US stock market as measured by the S&P 500 (as of end-of-day Monday – 2,746) was still up ~9.6% over December 2018 lows (2,506) and still in line with levels from May 2019 (2,752) (source: Yahoo Finance). As a reminder, although most media reports market movements based on the Dow Jones Industrial Average (DJIA), we watch the S&P 500 as our measure as we believe that it provides a better representation of our domestic large company stock market since the DJIA is a benchmark of only 30 US stocks, while the S&P 500 tracks 500 companies.
- Understand if headlines reference % losses or point losses. – Over the last couple weeks (and definitely including yesterday), markets have seen a sharp increase in volatility, as represented by the Dow Jones Industrial Average falling or rising by more than 1,000 points on five different days. Learning of large swings like this may lead you to believe that the market is currently more volatile than it has been historically. It's important to remember, however, that when the market is trading at higher levels, "normal volatility" will lead to larger point fluctuation. In other words, a 1,000-point swing would mean almost twice the volatility back in the 2007-2009 recession (when the Dow was trading in the 6,500-13,000 range) than it does today when the Dow is trading at ~24,000 levels. Therefore, be careful to understand what the media is reporting (% or $) when they claim something like "worst trading day in history" – are they speaking in point swings or % swings?

3) **We don't know what we don't know….**and neither does anyone else. Be careful of headlines and media talking heads (remember they are all paid to get you to watch their programs or read their material – not communicate facts).
    a. For everyone that communicates the sky is falling there is someone who espouses the opposite, and only history will tell who is right. Again, none of us know for sure what will happen. Yes, the market may continue to go down, but historically investors with cash on the sidelines have found buying opportunities from the decline, thereby jumping in and helping drive the market back up. The best move, historically, has been to stick to your plan.
    b. Going forward, there are two options that the economy can follow. 1) "V" bounce – This is when the market hits a bottom and bounces back up in a short window of time (think back to the losses we had in late 2018 that were mostly/fully recovered by the end of the first quarter of last year). We believe this possibility will depend largely on the US consumer. 2) Move towards the dreaded "R" word – Recession. Even if this were to occur, we will continue to focus on our long-term planning and help you make small tweaks to your financial plan to avoid making decisions that have long-lasting impacts.

A summary of our more positive thoughts on the market and economy (ie. the things you probably aren't hearing in the news):

We enter this period of distress with labor markets and the consumer in an incomparably strong position. Last Friday's jobs report showed that hiring has proceeded at the fastest pace in nearly four years. The consumer is benefitting from a 50-year low in unemployment, wage growth, record-low borrowing costs, and inexpensive gasoline prices that are certain to fall even further. Since the US economy is largely driven by consumption, we believe these are positive things we must keep in the back of our minds.

In the end, the behavior of the U.S. consumer may determine the outcome. Key data to watch will be mortgage/home sales/starts activity and jobless claims/job growth. Are lower mortgage rates helping (they did last week)? Are consumers losing jobs or is the labor market still healthy (data last week favored the latter)? Housing and employment are, in this consumer-led economy, much more important than manufacturing data, which we know will be ugly. While spending on discretionary items such as traveling, hotels, restaurants and cultural events are likely to fall because of the virus, two key factors suggest spending won't collapse:

1) Financing conditions are easy, tax refunds are in full season, inflation is low, and household balance sheets are strong (debt-to-income is at an *18-year low* and the broader financial obligations ratio measuring debt burden to disposal income is near *a record low*).

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2) Consumers rarely react much to negative sentiment shocks. Investors are stuck in a blind spot until the evolution of the virus and its impact on the economy plays out. Until there is a peak in the daily new infection rate outside of China, more downside is certainly possible. The second-largest economy in the world, and the epicenter of the virus, is getting back to business. Here in the U.S., consumer and corporate balance sheets have rarely been so flush with cash.

Our assumption is that we will see further policy response in the coming days and weeks, and that despite the acute pressure on the economy and markets in the short-term, stabilization eventually will occur, followed by reacceleration later in the year. Certainly, the risks to this view are higher than they were a week ago, before the oil-price war, but we will continue to diligently monitor events as they occur.

Thank you for your continued trust in us. We are always available if you would like to discuss how this is impacting your individual accounts. We continue to believe that the market will recover (like it has in the past), and we encourage you to stay focused on your long-term goals when listening to the current headlines.

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[1] Please note, this is a hypothetical example for illustration purposes only and does not represent an actual investment. Actual investor results will vary.

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