

MARKET UPDATE

The Dawn Will Come

Monday March 23, 2020

“Abnormally good or abnormally bad conditions do not last forever.”
~ Benjamin Graham

The coronavirus pandemic continues to intensify as the world that appeared mostly unconcerned just eight weeks ago has now gone into a full-blown meltdown. The best visual for this crisis in economic terms might be a medically induced coma. The governments of Europe and the US, following the examples of China and Japan, have put forth historic restrictions on social interactions. As I discussed in my prior memo, the global economy has been interrupted in an extreme and unprecedented way as a means of ‘flattening the curve’. The level of fear and panic in the general public has risen exponentially just like the cases of COVID-19 across the globe. Americans are adjusting to the closing of schools, hotels, bars, and cinemas. All sporting events have been cancelled and restaurants are attempting to adjust to a take-out only business model. Simply stated, we are living in abnormally bad conditions that are unlike anything seen in modern history. **The good news is that this too shall pass.**

Unlike the dust bowl during the Great Depression, we do know with reasonable scientific accuracy that this will be temporary. The best and brightest minds in the pharmaceutical industry are working on both treatments and vaccines. The treatments will save lives this year and the vaccines will help defend us from future outbreaks. Governments are working on monumental fiscal stimulus packages of an unprecedented scale. The adversely affected industries will need more help than they get, but the sheer size of the stimulus being discussed should calm markets and accelerate our recovery. The Federal Reserve is taking Herculean measures to stabilize frightened credit and equity markets until the medical and fiscal aid arrives. These actions will not prevent a truly historic rise in the American unemployment rate. Europe will also see unprecedented economic declines and job losses as they battle the spread of the virus. The news will be frightening and discouraging, but an investor also needs to take heart that these headlines also ensure that governments will take action to offset the economic damage. An investor also needs to remember that many of these headlines are lagging economic indicators, such as unemployment. That means the unemployment rate doesn’t provide us any insight to the next move in the economy or the stock market. Instead, that data simply confirms what has already occurred. In this situation, the rise in unemployment is by design to slow the coronavirus. At some point in this crisis, restrictions will be lifted. Do not let your fears cause you to doubt the resiliency of the American people, nor the leadership of great businesses around the world.

“A pessimist sees the difficulty in every opportunity; an optimist sees the opportunity in every difficulty.” ~ Winston Churchill

At a time of such immense uncertainty and fear, I find it helpful to look beyond the current crisis. None of us knows the duration or depth of this pandemic or the recession created to mitigate its spread, but at least 7 ½ billion people in the world and more than 325 million Americans will welcome in the new year. We don't know how many businesses will close and fail to reopen. We do not know how high the unemployment rate may go during the downturn, nor do we know how quickly those furloughed and unemployed workers will find gainful employment. However, we do know with very high certainty that 325 million Americans will be consuming every day. I am just as confident that the 500 million people in the European Union along with billions of people in China, India, Japan, Korea, and the rest of Asia will do the same. I am certain that my teenagers will be back at Starbucks. My young nephews will still get excited at the sight of a Happy Meal from McDonald's. There will be Nestle bottled water in my fridge and Gatorade (PepsiCo) at my daughter's tennis match. My son will still like Polo (Ralph Lauren) shirts and Nike shoes almost as much as his X-Box (Microsoft). My friend Joel will still want a Polaris ATV for his military ministry and my wife will still get my aftershave from Christian Dior (LVMH). Costco will still be full of eager shoppers looking for a deal and there will be Walmart boxes on my door delivered by a Fed Ex truck. There will be new John Deere equipment at work on farms around the country and the ABC stores will be open in case you need to pick up a bottle of Old Forester (Brown-Forman). I do not believe that the rest of the developed world will be all that different from my family and friends. There are activities that may never be the same after COVID-19, but much of life will return to normal. The future earnings power for many companies will likewise be no different after this recession than they were before COVID-19.

It is only fear and uncertainty that have shaken our confidence about the future. There will be some in every country that don't recover financially or emotionally, but I am confident most of us will find that there is life after COVID-19. Just like life, the stock market will eventually return to normal as well. Based on history, the stock market should look better long before the headlines about the pandemic or the recession are over. The stock market is a leading economic indicator. That means it will move in anticipation of changes in the economy, not at the same time as those changes. I do not believe this time will be any different. We are investors in high-quality businesses. We are confident that we can earn an attractive return by owning a diversified portfolio of the world's leading companies. During moments of duress, stock prices for even high-quality businesses will fall, but a disciplined investor will recognize that today's price may be significantly below the fair value of those shares and won't sell at these prices. Instead, we will continue to seek opportunities to improve the quality of our portfolio and take advantage of the uncertainty. Fear is both crippling and contagious. It leads to emotional decisions and panic. For an investor, panic inevitably leads to the destruction of wealth. In moments of fear, we look for reasons to be hopeful and to have faith that these abnormally bad times will not last forever.

We care deeply about your long-term financial wellbeing and embrace our fiduciary responsibility. We won't make emotional decisions but will make prudent portfolio changes as the situation and the facts change. We are invested with you and our firm's success is directly correlated to your success. Winston Churchill is generally associated with the old adage that it is darkest before the dawn, but Thomas Fuller penned the original phrase back in the 17th century when he wrote "It is said that the darkest hour of the night comes just before the dawn." We do not yet know when this crisis will truly reach that darkest hour, but we do know that there will be dawn on the other side of it. We also know from history that the sun should shine on the stock market long before the economists and the politicians have the data to explain it.

“For 240 years, it has been a terrible mistake to bet against America.”
~ Warren Buffett

The news has been overwhelmingly negative over the past month, but many of our companies have also shown leadership amid the crisis.

Date	Headline
March 13, 2020	Janssen (Johnson & Johnson unit) enters into agreement with Beth Israel to develop preventive vaccine candidate for COVID-19.
March 16, 2020	Louis Vuitton uses cosmetics plants in France to make hydroalcoholic gel for hand sanitizer that they are giving to French authorities. The company is providing the hand sanitizer for free to government and healthcare workers.
March 17, 2020	McDonald's announces 95% of China stores are back operating normally and additional healthcare benefits for hourly workers.
March 18, 2020	Abbott Labs receives FDA Emergency Authorization for COVID-19 testing kits and ships 150,000 immediately to existing customers. Production will reach 1 million tests per week by end of March.
March 19, 2020	Microsoft announced 44 million daily active users on MS Teams as more people work from home. Users include 93 of the Fortune 100. The number of daily active users has more than doubled since November.
March 20, 2020	PepsiCo plans to hire 6,000 new full-time workers and raises compensation for 90,000 frontline employees
March 20, 2020	Microsoft expands partnership with Adaptive Biotech to decode COVID-19 immune response to help advance treatment for pandemic. They are researching why one person's immune system responds more aggressively than another.
March 21, 2020	Walmart plans to hire 150,000 temporary workers before May 31 and pay \$365 million in special bonuses to hourly associates

“The idea that a bell rings to signal when investors should get into or out of the market is simply not credible.”
~ Jack Bogle

A look back at historic market declines and the subsequent 1-year price gains for the S & P 500 index from the bottom. Large declines have historically been followed by large rallies.

Market Low	Decline from Peak	Gain over the next 12 months
Friday, December 6, 1974	-48%	33%
Thursday, August 12, 1982	-28%	59%
Monday, October 19, 1987	-33%	24%
Monday, August 31, 1998	-20%	38%
Wednesday, October 9, 2002	-49%	34%
Friday, March 6, 2009	-57%	71%
Thursday, February 11, 2016	-16%	28%
Wednesday, December 26, 2018	-19%	38%

Source: FactSet Data, Standard & Poor's, Dow Jones

“One principal that I have used throughout my career is to invest at the point of maximum pessimism. That is, the time to be most optimistic is at the point of maximum pessimism.”
~ Sir John Templeton

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Meet the Team



Pictured from left to right: Kevin Mishoe, Mike Absher, Jennifer Oravsky and Zak Wahdan

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