COPPERWYND FINANCIAL

“Patience will be required as this plays itself out.”

MARCH 2020

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Market Commentary

Nassim Taleb, in his 2001 book ‘Fooled by Randomness’, described ‘Black Swan Events’ as high-profile, hard-to-predict and rare events that are beyond the realm of normal expectations in history, science, finance, and technology.

Black Swan Events are named for real-life black swans, which at one time were widely believed to not even exist. Second Century Romans even had a phrase: ‘Rara avis in terris nigroque simillima cygno’, to describe someone or something as so rare or unlikely to exist that it would be like seeing a black swan. Centuries later, however, black swans were discovered to actually exist, in Australia!

The sudden spread of the Covid-19 coronavirus, and the subsequent worldwide shock that it has produced, has now infected the stock market. Whether this is a true Black Swan event can probably be debated. What we do know is that Thursday, February 27th, was the largest point-drop ever for the Dow 30, although given the lofty levels of the previous high, it’s nowhere among the historical largest percent-drops.

The S&P 500 and the Nasdaq both set new all-time highs just a week and a day ago (February 19th), and the Dow a week before that (February 12th); but since then, each has lost more than 12% in a cascade of multi-hundred-point down-days.

The S&P 500 is now back to where we were in mid-October of last year. In the big picture, being set back by four months in the market doesn’t typically raise an eyebrow, as that’s a pretty common occurrence; such corrections have happened dozens of times in history. What makes this time seem different, however, is the speed of the decline ... that’s the argument for a ‘black swan’ event label.

Thursday was the third day in the last week with a hugely-lopsided down-to-up volume ratio (almost 30:1 Down:Up among S&P 500 stocks on Thursday). Usually, such a tremendously-oversold condition leads to an imminent rally. The most memorable such episode in recent times would be December 24th, 2018 and December 26th, 2018, going from worst-in-a-decade, new Maximum Drawdowns for many investment portfolios, to a months-long steep and unabated run-up commencing the very next market day. That being said, we can’t say exactly how things may play out this time, of course.

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Several of our stock models have a risk-off component, and we have raised some cash going into and through this past week. Given the severity of the markets declines this week, it still probably won't feel like enough. Rotation decreased stock exposure and added to bonds. The Growth model lightened its exposure to stocks by 20%. The balance of the stock portfolios are still fully invested.

On the bond side of the equation, we have rotated to cash out of bank loans, high yield bonds and preferred stocks. We haven't seen that much cash raised in bonds in several years. Typically, bank loans and high yield bonds go out of favor early in the recessionary cycle as they are sensitive to default risk. Are they playing the role of "canary in the coal mine" this time around? Are we on our way into a global recession?

There will certainly be economic consequences to the massive reaction to this virus. It wouldn't be imprudent to say an over-reaction. Quarantine of tens of millions of people, companies cancelling travel and schools closing are steps that have been taken that we normally don't see during a typical flu season, and maybe rightfully so as this isn't the flu. Yet all of these things and more are part of the daily news and the effects will mean lower productivity, higher costs as companies attempt to outsource products from other countries, lower profits as sales lag and hiring freezes join the news. All these things and more have we already been hearing from our business clients. The end game could very well be a global recession.

It is our feeling, however, that this recession, if it occurs, will be short and shallow. There will be a vaccine or simply an abatement in the number of cases of the virus. It will run its course at some point, and once that has happened, we will start to see all of the money that the Federal Reserve and the Central Bank in China (and Japan and Europe) have printed make its way into the stock markets. Patience will be required as this plays itself out.

In the meantime, markets such as these provide clarity on our personal tolerance for risk and if you find you are not sleeping well because the drops in the market have been too upsetting, then it would be fair to say we need to revisit the stock exposure in your portfolio. We encourage your calls and meetings to work together to refine your plan to keep you on track.

Financial Planning Tip

Emergencies, by their nature, are unpredictable. When they happen, they can derail your financial stability. A sudden illness or accident, unexpected job loss, or even a surprise home or car repair can devastate your family's day-to-day cash flow if you aren't prepared.

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While the size of your emergency fund will vary depending on your lifestyle, monthly costs, income, and dependents, the rule of thumb is to put away at least three to six months' worth of expenses. This amount can seem daunting at first, but the idea is to put a small amount away each week or two to build up to that goal. You may also want to consider adjusting the amount based on your bill obligations, family needs, job stability, or other factors.

Emergency savings are best placed in an interest-earning bank account, such as a money market or interest-earning savings account, that can be accessed easily without taxes or penalties. The concern with placing your emergency savings in investment accounts, is that they may lose value if the funds needed. Always remember, something is better than nothing.

While the hope is to never need these funds for something sudden or unexpected, any successful financial plan will always seek to mitigate risk. If you are unsure how much you should be setting aside in your own personal emergency fund, call as at the office to discuss!

Tax Planning Tip

Student loan debt has become one of the largest classes of consumer debt in the country. In fact, it affects as many as 45 million Americans. According to a report from Forbes, student loan debt reached almost $1.5 trillion in early 2019, with the average borrower from the class of 2017 owing as much as $28,650 in student debt. For many years, 529 plans have been a great way to help your kids and grandkids with the ever-escalating cost of education.

Until now, 529 funds could not be used to repay student loan debt. But the SECURE Act opens the door for families to take tax-free 529 plan distributions of as much as $10,000 for student loan repayment. The law includes an aggregate lifetime limit of $10,000 in qualified student loan repayments per 529 plan beneficiary and, very significantly, an additional $10,000 per each of the beneficiary's siblings. Siblings may include brothers, sisters, stepbrothers or stepsisters. A 529 plan account owner can change the beneficiary at any time without tax consequences. Also, you can use their 529 accounts to cover expenses related to any registered apprenticeship program attended by the beneficiary. This includes any additional costs such as fees, equipment, books, and other supplies.

If you are looking for ways to help plan for your kids and grandkids current college plans or how to help them manage the repayment process, please call us at the office for a review!

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401k Allocation

We now move to the maximum risk off for each risk level. If you feel you are still too exposed, you should consider moving down a risk level in the chart in order to decrease your stock exposure.

The amount of money currently being printed by both the Federal Reserve and the Bank of China will eventually find its way into this market. The coronavirus will eventually exhaust itself or we will find a suitable vaccine. And then it will be off to the races again – and you have some “dry powder” with which to profit when that time comes. Fair warning that that day may not come in the next month as we will be facing a very interesting earnings season the first part of April, so patience will be necessary. These are the days that help give us clarity on our personal risk tolerance.

March 2020					
		Agg. Growth	Growth	Moderate	Conservative
Bonds / Cash		25%	30%	55%	85%
	Stable Asset - OR - Short Term Bond	15%	15%	35%	50%
	Total Return	10%	15%	20%	35%
	High Yield Bonds				
	World Bond	0%	0%	0%	0%
	Inflation Protected Bond	0%	0%	0%	0%
Large Cap:		60%	55%	35%	15%
	Large Cap Growth	30%	30%	20%	5%
	Large Cap Value	30%	25%	15%	10%
Mid Cap:		15%	15%	10%	0%
	Mid Cap Growth	5%	5%	0%	0%
	Mid Cap Value	10%	10%	10%	0%
Small Cap:		0%	0%	0%	0%
	Small Cap Growth	0%	0%	0%	0%
	Small Cap Value	0%	0%	0%	0%
International:		0%	0%	0%	0%
	Developed International	0%	0%	0%	0%
	Emerging Markets	0%	0%	0%	0%

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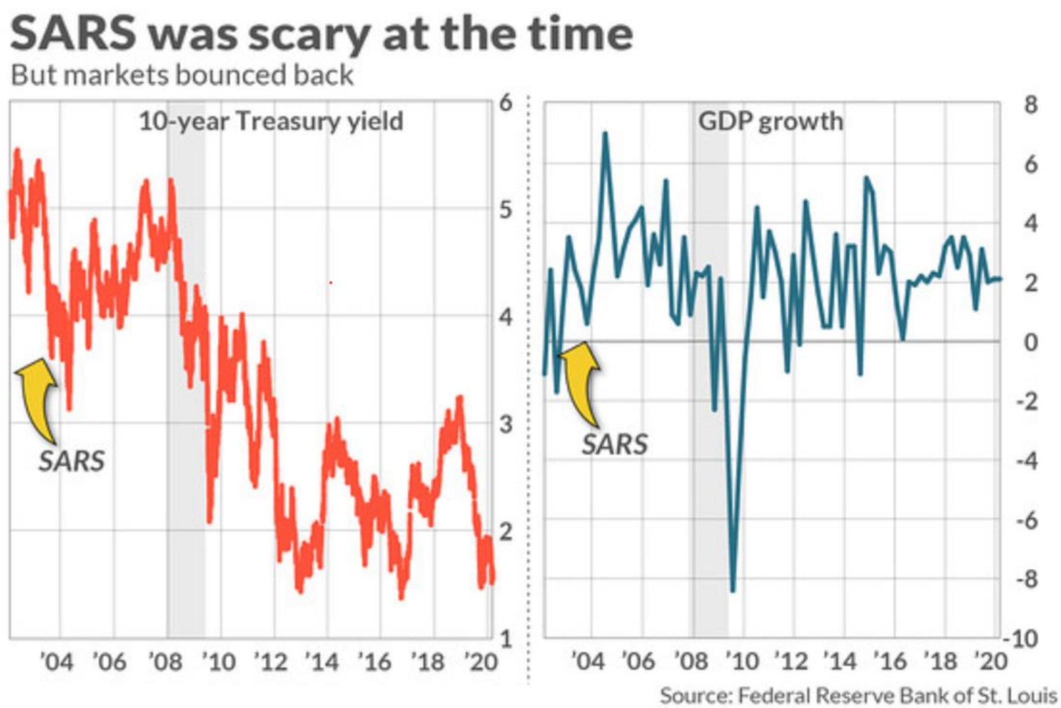
Graphic of the Month

GDP went from a low of 0.6% in the fourth quarter of 2002 and then snapped back to 7% the next year. The 10-year Treasury fell 105 bps during SARS. When all was said and done, we ended 25 basis points higher than the level when SARS news first hit.



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