POLARIS WEALTH ADVISORY GROUP

The Polaris Perspective

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A Quarter Like No Other

I have never been one to be short on words (as most of you know). But I have found starting this quarterly update incredibly hard. What we are all going through and the changes to all of our lives is... hard to have imagined just a few weeks ago.

What was considered China's problem in January, like SARS before, the COVID-19 coronavirus has turned into a worldwide pandemic and a global financial crisis. As I write, there are 763,832 confirmed cases in the United States, with over 40,000 deaths blamed on the virus. 2.4 million people worldwide have been infected, with over 165,000 people dying.

The general markets shrugged off the beginning of COVID-19. The biggest concern was if the corporate shut downs in China would impact our supply channels. As the virus spread into South Korea, Iran, Japan, and Italy, the S&P 500 dropped from its February 19th high. What ensued in the days to come was the fastest 30% drop in S&P 500 history (22 trading days). The S&P 500 dropped 33.92% from its high on February 19th to its March 23rd low (see chart below).

S&P 500 Index • Down 29% from its Peak

Source: Standard & Poor's, Polaris Greystone

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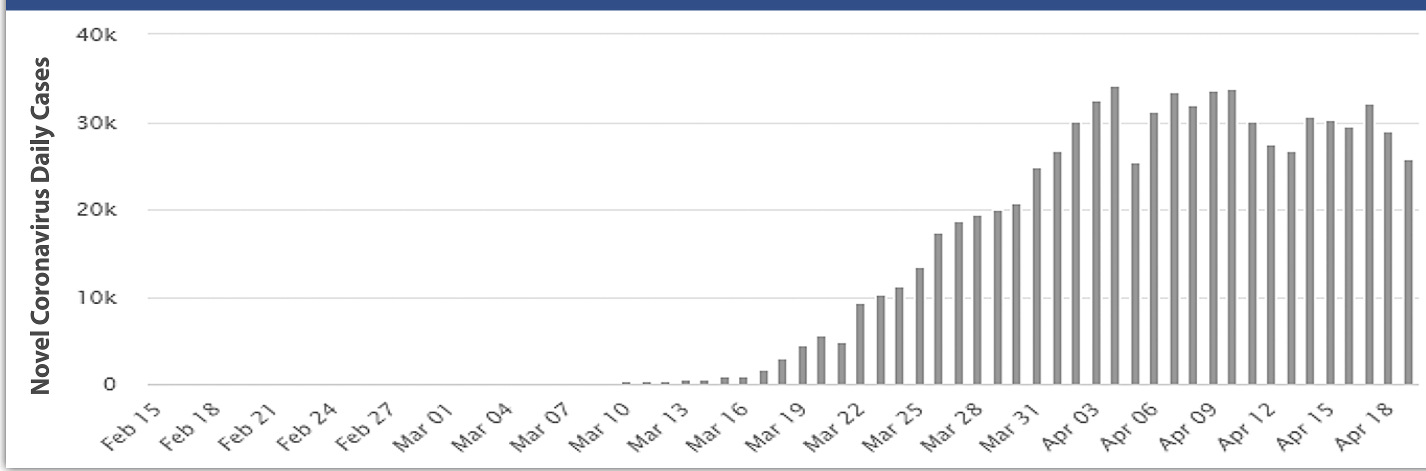
Summary of Q1 Activity

- Shelter in place – 42 of 50 states.
- More than 300 million Americans are currently sheltering in place.
- All 50 states are under disaster declaration for the first time ever.
- Oil prices have dropped to 1947 prices, as the Russians and Saudis fight over production levels.
- Fastest drop from new high into bear market territory (down 20%), EVER.
- Fastest 30% drop in market history (22 trading days).
- Highest closing for the volatility index, ever! (82.7 on March 16th).
- The S&P 500 ended the quarter down 20.00%.
- Growth outperformed Value across all three capitalization tiers (Large, Mid, and Small), with Large-Cap Growth being the top performing segment of the markets during the quarter.
- T-Bonds were the best performing asset class, up 20.90% for the quarter.
- Gold rallied, up 4.48% during Q1 2020.
- Other commodities didn't fare as well. The S&P Goldman Sachs Commodity Index dropped 41.42%.
- International investments struggled. Emerging markets dropped 19.05%, whereas the EAFE (companies in developed countries in Europe, Australia, and Far East) fell 20.55%.

What's Happening With COVID-19?

Most medical professionals don't believe that we will have a vaccine for public use until the spring of 2021. The only thing that is keeping the COVID-19 coronavirus from spreading is the "social distancing" we are doing by sheltering in place. There is a major risk of opening up the country too quickly and seeing a spike in new cases. As you can see from the chart below, our sacrifices seem to be paying off with a decline in the total number of daily new cases.

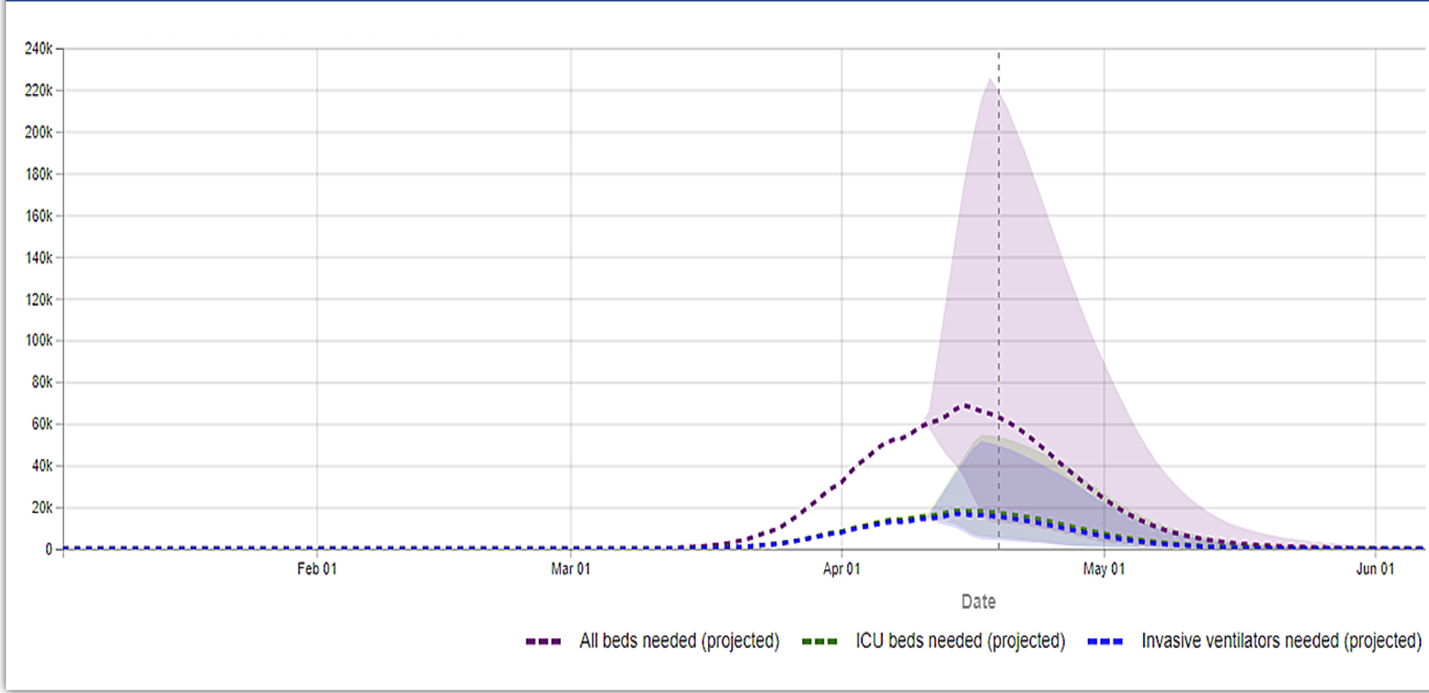
United States Daily New Cases



Source: worldometers.com

While many states have "peaked" in the number of new cases a day, and the pressure placed on the medical system is lessening by the day, other states have not peaked. According to the projections conducted for the CDC, the graph below shows that the pressure placed on our medical system peaked on April 14th and should gradually decline as we continue to shelter in place. My concern is if we lift our restrictions too soon these numbers could reverse. For example, on May 1st it is projected that we will still have over 24,000 people hospitalized, with 7,350 patients in the ICU with 6,000 of them on ventilators. Waiting just a few additional weeks lowers the number to only a few thousand people remaining in the hospital system. It's not projected that we will be COVID free until July 1st.

United States Hospital Needs



Source: covid19.healthdata.org

Is This A Real Rally?

As I mentioned in the last Polaris Perspective piece, most rallies after waterfall drops in the market are followed by at least one major retesting of prior lows. The S&P 500 has rallied hard off of the lows on March 23rd. This rally is exclusively sentiment based, as investors hope that there is light at the end of the tunnel and that the country can reopen quickly and recover quickly. Historically, 70% of the time, the markets retest their prior lows and find even lower lows.

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Below is a chart of the S&P 500 during the Great Recession. The S&P 500 hit an all-time high of 1565.15 on October 9, 2007. It would not see these levels again until 2013. The S&P initially slid 18.64% over six months to find a temporary low on March 10, 2008 (Red 1). The markets then rallied 12%, hitting 1462.63 on May 19th (Green 1). The markets reversed direction and dropped over 14% (Red 2) finding a temporary support level at 1214.91 on July 15th. Most markets don't go straight down. The S&P rallied for about a month, climbing 7% (Green 2) to 1305.31 on August 11th. Then the wheels began to come off. The S&P 500 dropped 34% (Red 3) from these lower levels, briefly bottoming on October 27th at 848.92. A one-week rally saw the S&P pop up 18% (Green 3) to 1005.75 on November 4th. This was a false rally. The S&P dropped another 25% to 752.44 (Red 4) on November 20th. The S&P attempted another rally, gaining 20% through January 6, 2009 (Green 4). The roller coaster was almost over. The S&P 500 declined another 25% (Red 5) finding it's ultimate low on March 9, 2009 at 676.53. From high to low, the S&P 500 experienced a 56.77% price decline. But as you can see from the ebbs and flows during this time, there were many times that you could have pushed too many chips into the game only to lose significantly.

S&P 500 • September 2007 – April 2009

Source: Standard & Poor's, Polaris Greystone Financial Group

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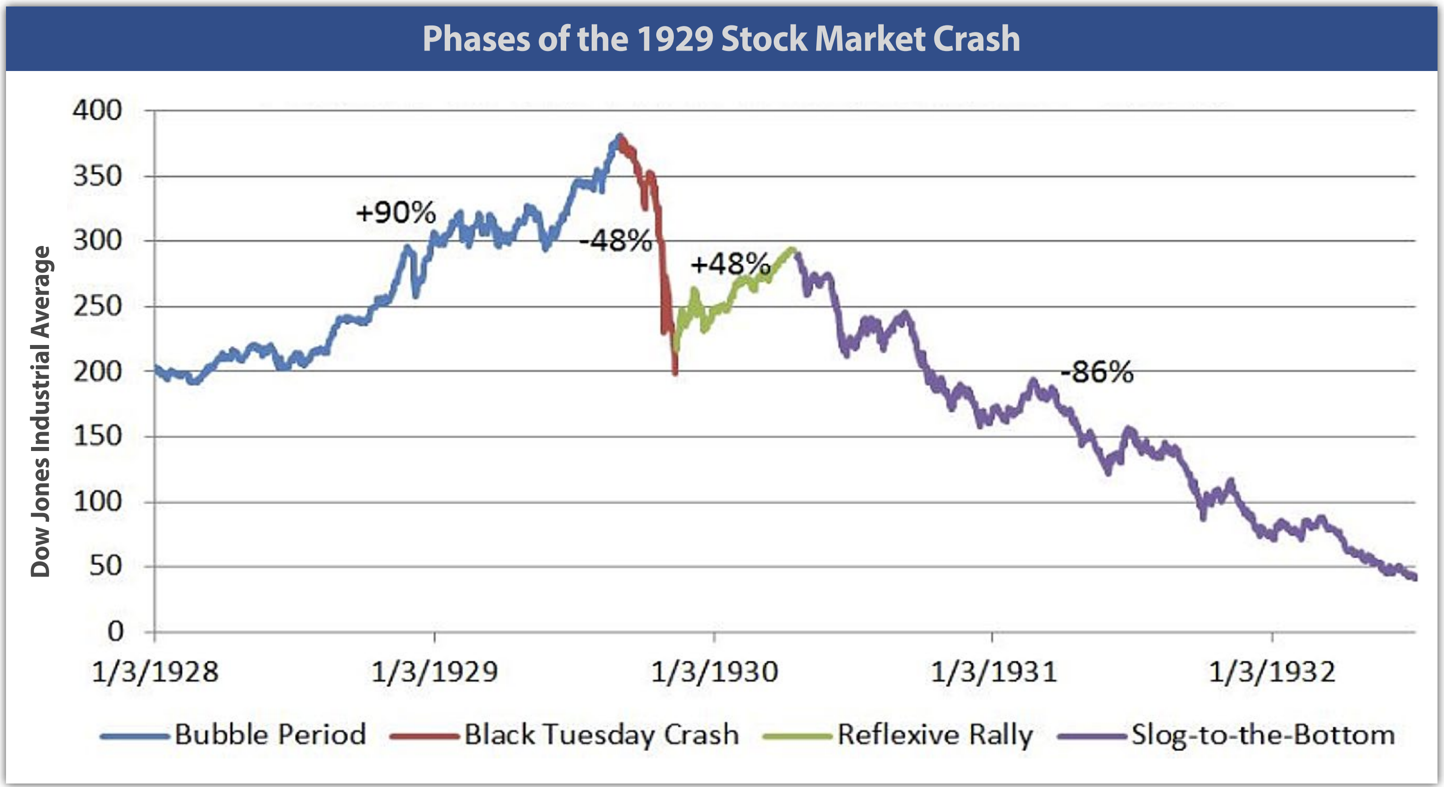
The initial decline during the Great Depression was in October of 1929. The Dow Jones Industrial Average lost 48% of it's value in a few short weeks. If you had a $1 million portfolio, you were down to approximately $500,000. When the DJIA rallied 50% in late 1929 / early 1930, your $500,000 would have gone up to $750,000 before seeing the markets sell off over the next two years. This was a major "head fake" or what professionals call a "relief rally." Even during the "slog-to-the-Bottom" part of the chart, there were multiple 20%+ rallies that fooled investors.



Source: St. Louis Federal Reserve

The markets have rallied significantly off of their lows in face of disastrous economic reports. Unemployment jumped to 4.4% at the end of March, but over the past four weeks 22.034 million workers have filed for unemployment benefits. It is believed that unemployment is closer to 20% right now. Housing starts have fallen 22.3%. The Philly Fed General Business Activity Index plunged 43.9 points to a record -56.6. The NY Empire State Manufacturing Survey plummeted 57 points to -78.2, its lowest level ever. There are countless other economic datapoints that are in similar condition. And earning season is just beginning. There are a lot of mines in this mine field.

Restarting our economy isn't like flipping a light switch. The $2 trillion CARES Act was the fourth stimulus package announced, and there is already talks of a fifth stimulus package to be announced this upcoming week.

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What Is Polaris Wealth Doing?

We are a tactical investment manager. As we discussed in our March 18th Polaris Perspective, we got very defensive during the decline. We significantly lowered our exposure to the stock market, and we moved into defensive segments of the market with our limited exposure. By taking these measures, our clients saw substantially less loss during this tumultuous downturn.

We started buying (nibbling) on the second day of the rally. As we already mentioned, 70% of the time, the markets retest their previous lows. This also means that 30% of the time, they climb and never look back. While we feel there is still a lot of risk in this market, we have kept adding to our equity exposure, trying to take advantage of the "work from home" theme and buying "great companies at really cheap prices." We are not fully invested. We are taking a middle line stance at the moment. We feel that even if every state ended their "shelter in place" mandate, it will take a lot longer for the economy to recover. Colleges and Universities are talking about continuing their distance learning for their fall semesters. Marin County's (where I live) education department is telling their school to not expect schooling to go back to normal until the 2021/22 school year. There will be major social changes as a result of this pandemic. Until there is an effective vaccine being given to our entire population, life will be different. Our investment team is constantly tracking trends and trying to take advantage of this information.

Please stay safe. Be patient during these trying times. Know that we are here for you. Please feel free to call us to talk about your portfolios or just to catch up. Social distancing is not easy for any of us. We welcome a good conversation.