



Level Four Capital Management

# SPECIAL COMMENTARY

## THE CORONAVIRUS AND THE MARKET

Market activity this week has caused a heightened level of investor angst. With the S&P 500 Index and the Dow down 8.30% and 10.23% respectively, many stocks are moving in and out of correction territory (10% decline). While market drops are an inevitable factor of investing, when volatility spikes it is nonetheless alarming. Below, please find insight and commentary reflecting our view of the markets and this fast-moving event.

### HEADLINE THEMES

- The human element of this unfolding epidemic is indeed a tragedy and too many lives have been lost. We believe that containment of the virus globally will be key to establishing a sense of outlook and resumption of “normal” market activity reflecting fundamentals versus macro themes.
- While news sources are focusing headlines on the growing count of new confirmed cases of the virus, according to [www.worldometer.com](http://www.worldometer.com), active cases versus confirmed cases (total confirmed cases, minus deaths and recoveries) has declined.
- The U.S. has indicated that it will deploy considerable resources and money to contain the spread of the virus in the US.
- We have been here before: At the height of the SARS virus back in 2003, the S&P 500 index fell by 12.8%. During the Zika virus outbreak, the market fell by 12.9%. Historically, there are other similar epidemic/pandemic episodes that have caused the market to react negatively to uncertainty and fear. As with those historical market movers, we think this too shall pass.
- Though we have seen increased market volatility in recent days, these daily levels of market movement are not unusual in historical market context. In the S&P 500 index data to the right from 1950-2019, the years with the largest daily percentage market movements are shown. The largest recent daily change in the S&P 500 was less than 4.5%, which would rank 15th out of the 69 years of data. This is in the top half of most volatile days in a given market year, but far from the top. If you look closely at the data you will notice that often a large positive day may happen around a large sell-off. For example, the second highest percentage gain was two days after the largest percentage loss.

Largest daily percentage changes per year [\[ edit \]](#)

Largest daily percentage gains per year					Largest daily percentage losses per year				
Year	Date	Close	% Change	Weekday	Year	Date	Close	% Change	Weekday
2008	2008-10-13	1,003.35	+11.58	Monday	1987	1987-10-19	224.84	-20.47	Monday
1987	1987-10-21	258.38	+9.10	Wednesday	2008	2008-10-15	907.84	-9.03	Wednesday
2009	2009-03-23	822.92	+7.08	Monday	1997	1997-10-27	876.99	-6.87	Monday
2002	2002-07-24	843.43	+5.73	Wednesday	1998	1998-08-31	957.28	-6.80	Monday
1997	1997-10-28	921.85	+5.12	Tuesday	1988	1988-01-08	243.40	-6.77	Friday
1998	1998-09-08	1,023.46	+5.09	Tuesday	1962	1962-05-28	55.50	-6.68	Monday
1970	1970-05-27	72.77	+5.02	Wednesday	2011	2011-08-08	1,119.46	-6.66	Monday
2001	2001-01-03	1,347.56	+5.01	Wednesday	1955	1955-09-26	42.61	-6.62	Monday
2018	2018-12-26	2,467.70	+4.96	Wednesday	1989	1989-10-13	333.65	-6.12	Friday
2000	2000-03-16	1,458.47	+4.76	Thursday	2000	2000-04-14	1,356.56	-5.83	Friday
1982	1982-08-17	109.04	+4.76	Tuesday	1950	1950-06-26	18.11	-5.38	Monday
2011	2011-08-09	1,172.53	+4.74	Tuesday	2009	2009-01-20	805.22	-5.28	Tuesday
1962	1962-05-29	58.08	+4.65	Tuesday	2001	2001-09-17	1,038.77	-4.92	Monday
1974	1974-10-09	67.82	+4.60	Wednesday	1986	1986-09-11	235.18	-4.81	Thursday
1957	1957-10-23	40.73	+4.49	Wednesday	2002	2002-09-03	878.02	-4.15	Tuesday
2010	2010-05-10	1,159.73	+4.40	Monday	2018	2018-02-05	2,648.84	-4.10	Monday
1963	1963-11-26	72.38	+3.98	Tuesday	1982	1982-10-25	133.32	-3.97	Monday
1978	1978-11-01	96.85	+3.97	Wednesday	2015	2015-08-24	1,893.21	-3.94	Monday
2015	2015-08-26	1,940.51	+3.90	Wednesday	2010	2010-05-20	1,071.59	-3.90	Thursday
1991	1991-01-17	327.97	+3.73	Thursday	1974	1974-11-18	69.27	-3.67	Monday
1980	1980-04-22	103.43	+3.64	Tuesday	1991	1991-11-15	382.62	-3.66	Friday
1988	1988-01-04	255.94	+3.59	Monday	1961	1961-04-18	68.20	-3.61	Tuesday
1955	1955-07-06	43.18	+3.57	Wednesday	2016	2016-06-24	2,037.41	-3.59	Friday
2003	2003-03-17	862.79	+3.54	Monday	2003	2003-03-24	864.23	-3.52	Monday
1999	1999-10-28	1,342.44	+3.53	Thursday	2007	2007-02-27	1,399.04	-3.47	Tuesday
1961	1961-04-17	68.68	+3.48	Monday	1953	1953-02-09	25.69	-3.09	Monday
2019	2019-01-04	2,531.94	+3.43	Friday	1996	1996-03-08	633.50	-3.08	Friday
1975	1975-01-27	75.37	+3.27	Monday	1973	1973-11-19	100.71	-3.05	Monday
1971	1971-08-16	98.76	+3.21	Monday	1990	1990-08-06	334.43	-3.02	Monday
1990	1990-08-27	321.44	+3.19	Monday	1980	1980-03-17	102.26	-3.01	Monday
1973	1973-12-26	95.74	+3.06	Wednesday	2019	2019-08-05	2,844.74	-2.98	Monday
2007	2007-09-18	1,519.78	+2.92	Tuesday	1979	1979-10-09	106.63	-2.96	Tuesday
1966	1966-10-12	77.04	+2.84	Wednesday	1957	1957-10-21	39.15	-2.93	Monday

Source: Wikipedia.org

## LFCM PORTFOLIO STRATEGY

From a valuation standpoint, the market was fairly valued to slightly overvalued when this crisis began, as opposed to other similar outbreaks. Currently, the LFCM equity models hold more cash than we have historically held due to recent sells in names that were overvalued. We are looking to take advantage of any oversold condition, especially in names that we have been monitoring and would like to include but for which we could not justify the high valuation. We see this as an opportunity to spend cash in the models when the time is right to add positions, and perhaps more importantly, an opportunity to upgrade some names we currently own.

In the LFCM asset allocation models, we continue to maintain an overweight exposure to U.S. equities relative to our benchmark, and maintain a factor overweight to low volatility. These allocations have generated alpha during this time of market volatility. We will continue to carefully monitor the evolution/resolution of the Coronavirus situation and will make appropriate adjustments as market events dictate.

## WHAT SHOULD INVESTORS DO?

In our view, this is a transitory event that will eventually pass. And when it does, we believe that inventories and demand will eventually catch up and mitigate concerns of a global economic recession. Of course, we do not know the length or depth of this event, but it will end and we are focused on being well positioned to take advantage of the market's resumption once we have moved through this crisis.

The current market pullback on its own should not necessarily cause investors to change their long-term investment plans, unless their own individual plans have in fact changed. Looking ahead, we will continue to focus on fundamentals when evaluating securities for inclusion in the portfolios. Certainly, if our research indicates a change is needed, we will make the necessary adjustments. We believe when stock prices correct for macro reasons, it creates an opportunity to buy companies with solid fundamentals that generate excess-free cash flow at a further discount to the intrinsic value of the business. Remember, just because the headlines change, it does not necessarily mean the bottom up fundamentals of the business owned in a portfolio will also change.

### **Investors should:**

- First and foremost, continue to review and consider if your current allocation continues to align with your individual risk-tolerance and long-term investment plan.
- Do not try and time the market or sell out of fear. Market data supports that market fluctuations in the short-term, are historically followed by periods of significant market recovery.
- Most importantly, we urge and encourage you to consult with your advisor in case you have questions about your portfolio's strategy.

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