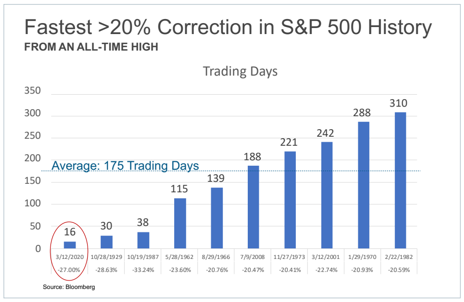
MEEDER INVESTMENT MANAGEMENT

ADVISORY CONSULTING

The Greater The Uncertainty, The Greater The Volatility

In January, we introduced the concept of 2010–2019 being a historic decade. While we anticipated more volatility in the next decade, we certainly did not think it would occur this soon.

Looking back, 2010–2019 was the first decade on record without a recession. It also never experienced a 20% decline in the S&P 500 index...the only other decade without a 20% S&P 500 drawdown was the 1990s. The decade that followed, the 2000s, brought two recessions, including the Great Recession of 2008.



Not even three months into this new decade, the stock market has already experienced the fastest drawdown of greater than 20% in S&P 500 history. At the time of this writing, the drawdown exceeds 29% and the U.S. economy appears to be grinding to a halt. Large banks are shutting down their branches, retail stores are reducing their hours of operation and some states are temporarily closing businesses, including movie theaters, shopping malls, and restaurants.

WHAT CAUSED THIS?

COVID-19

At this point, we have all have been impacted by the spread of COVID-19, which is popularly known as the coronavirus. Coronaviruses are a category of viruses that cause respiratory illness. This includes viruses like the common cold and flu. These can originate in animals and can occasionally infect people. MERS and SARS are examples of types of a coronavirus. This new specific strain, the COVID-19, was first reported in Wuhan, China in December 2019. While officials are still unsure of how the disease was spread to humans, the infection is believed to have come from wildlife that was sold at a local farmer's market. Wuhan is the 11th largest city in China and is home to more than 11 million people.

According to the World Health Organization, some of the symptoms include aches and pains, fever, cough, runny nose, shortness of breath and breathing difficulties. In severe cases, infection can cause pneumonia, severe acute respiratory syndrome, kidney failure and even death.

Currently the number of confirmed cases around the globe exceed 240,000 and there have been nearly 10,000 fatalities. The World Health Organization has declared this a global pandemic. The sheer uncertainty of how this will impact the health and lives of people, not to mention the impact that this will have economically, is unknown. When there is uncertainty, there is volatility.

OIL PRICES

Saudi Arabia and Russia have essentially entered a price war, with both producers recently increased oil production. This comes at the same time demand around the world has collapsed. As a result, oil prices have dropped by over 60% since the beginning of the year. While the Saudis and Russians attempt to gain market share, this dispute also impacts higher cost producers such as the shale producers in the United States. Under normal circumstances, lower oil prices might help energy costs for U.S. businesses and consumers. Ironically, so few people are traveling right now, reducing these potential benefits.

WHAT IS THE GOVERNMENT DOING TO HELP?

The Federal Government can accomplish amazing things when partisan politics are put aside. In addition to the funding and medical assistance they are providing to help slow the spread of COVID-19, they are also making strides economically. So far, the Federal Reserve is doing everything they can to provide liquidity to the economy. A liquidity crunch is what exacerbated problems that the U.S. experienced during 2008–09.

- The Fed cut short-term interest rates to **zero** earlier this month to make borrowing less expensive and to provide liquidity for the economy.
- The Fed is implementing a quantitative easing program with no limits to purchase U.S. Treasuries and mortgage-backed securities, providing more liquidity to these crucial markets.
- Earlier this week, the Fed announced the creation of both a commercial paper and a money market lending facilities, two areas that experienced difficulties during the financial crisis.
- Congress is currently working on a $1 trillion stimulus that could involve sending two payments of up to $1,000 each to taxpayers, along with additional benefits for children.

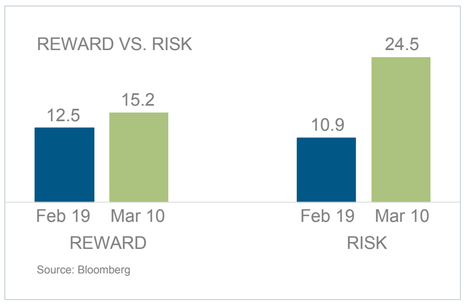
Congress is considering tax deferrals for both U.S. citizens and corporations.

HOW IS THIS IMPACTING PORTFOLIOS?

We utilize quantitative models to determine the risk relative to the reward in the marketplace. Our equity exposure to the stock market is determined by comparing the **reward** value and the **risk** value. If the reward value is greater than the market risk, our portfolios will be fully invested in the stock market. However, when the reward value is less than the risk value, we will adopt a defensive position.

$$\text{EQUITY EXPOSURE \%} = \frac{\text{Reward Value}}{\text{Risk Value}}$$

It's hard to believe that, just about a month ago, the market was at an all-time high on February 19th. At that time, the reward value was 12.5 and the risk value was 10.9. Due to the favorable environment, we were 100% invested.



On March 13, after the stock market's historic decline, the reward value remarkably remained near its same level. Despite trend and momentum factors deteriorating in the model, investor sentiment has become extremely negative during the past few weeks, reaching levels we haven't seen since late 2008. As a reminder, we view investor sentiment from a contrarian perspective, and this investor pessimism helped support the reward score. Despite the relatively favorable reward score, the risk has increased dramatically from February to March. At this point, the risk in the stock market far exceeds the reward, leading us to establish a significant defensive position.

WHY MEEDER?

This environment is a perfect example of why it is **imperative** that investors have a tactical manager within their portfolio. As this situation continues to unfold, it is important that a systematic process is in place to make fact-based decisions, removing emotion from the decision-making process.

For nearly half a century we have navigated just about every kind of market one could imagine. Despite the uncertainty, we will get through this.

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