DANN ASSET ADVISORS, LLC

Interim Update
Recent Market Volatility
February 26, 2020

Following a record high just last Wednesday, the market (as measured by the S&P 500 index of large U.S. companies) declined 7.6% through yesterday's close. The primary cause of the decline was the recent spread of the coronavirus beyond China, with the implication that the U.S. and other economies could see a more substantial slowing than previously expected. Already, several large U.S. companies (Apple, Coca Cola, Mastercard, for example) have announced that the virus has reduced demand for their products or interrupted their supply chains, such that first-quarter earnings will be below initial expectations.

On the surface, the U.S. market had been incredibly resilient since news of the coronavirus broke in January. However, looking deeper, early 2020 was largely a continuation of 2019, with large company growth stocks, technology-related in particular, leading the market and other sectors (small company, value and international stocks) trailing materially. A market that's led higher by just a select group of companies often is ripe for a correction, and we believe that's at least part of what's happening now. In our recent January 13, 2020, update, we wrote that, "… we judge that a lot of positives already are reflected in stock prices and that any negative development could cause a material decline." As often happens, the specific negative development is impossible to predict.

Current thinking. As telegraphed by leading companies, the coronavirus is going to negatively impact first-quarter earnings. We've not yet heard managements speak about an impact beyond March, but clearly the more the virus spreads, the greater and more prolonged the impact will be. In a worst-case scenario, a slowdown caused by the virus could lead to a recession. In a best-case scenario, quarantine efforts might mitigate spreading, a vaccine and/or cure could be found and economies (and earnings) could rebound quickly with pent up demand.

We of course have no idea how this will play out. While we believe the market was priced for near perfection at the beginning of 2020 (the impetus for several portfolio changes we made for most clients the past several weeks), the recent decline already reflects at least some of the negative impact of the virus. While it's tempting to trade based on eye-catching headlines, we don't believe in trading based on unknowable outcomes. Accordingly, at least for the time being, we're happy with the changes we've made to date in 2020 and are confident that the investments underlying the actively managed mutual funds owned by most clients will do well when virus impacts subside.

Other issues that bear watching in our opinion are:

- Record low 10-year U.S. bond yields – could just be a sign of investors temporarily searching for safety or, together with other interest rate moves, indicate a substantial economic slowdown coming.
- Actions by the Fed – had been on hold prior to coronavirus, may now be more accommodative.
- U.S. elections – the stock market likely and certain stock sectors almost definitely will react differently depending on whether the president or the currently leading Democratic candidate wins in November.

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