



Direct from Dudack Wash Your Hands

Yesterday the World Health Organization declared the coronavirus to be a global pandemic. At 9 pm last night President Trump announced a 30-day travel ban with Europe. This combination suggests a recession might already be in place in Europe and this could easily hurt the US economy.

Last night I spoke to a doctor from the Mayo Clinic. She indicated that the hospital is expecting the spread of the virus to rise dramatically over the next two weeks. The reason for this is that coronavirus is a new virus, and no one has immunity. Statistically a normal person with the flu might infect 1.7 new people, but a coronavirus victim appears to infect 2.5 people. A coronavirus-infected person is symptom free for 3 to 5 days and is contagious during this time. While the normal flu virus can live on tabletops and other surfaces for two hours, the coronavirus can survive for two days or more. The reason some experts are suggesting staying six feet away from others (social distancing) is that the virus appears to infect an area three feet around someone with coronavirus. And finally, the fever that accompanies the coronavirus could reach 104 degrees and have symptoms of pneumonia in some cases. These are the factors that make it more deadly for the elderly and those with compromised immune systems.

She added that there is no need to panic and to a large extent this is much like a very bad flu; but in coming weeks and months it is important that everyone protect themselves by regularly washing their hands with plain soap and water for 20 seconds. The elderly and those with compromised immune systems should consider social distancing or perhaps self-quarantining.

Given what we know today, it is likely that the coronavirus epidemic will become much worse in the next two weeks. In the interim, we should expect the financial markets to remain under pressure.

The positive in the current situation is that this is a medical crisis and not a financial crisis. The 2008 crisis triggered systemic risk in the global banking systems. Had a liquidity crisis ensued it could have spiraled out of control. This is not true today; our financial system is well capitalized. In addition, President Trump has indicated that he will recommend to Congress that small and medium sized companies affected by the epidemic be offered credit during this period and employees suspended due to the crisis should continue to be paid. The US economy demonstrated good momentum up until the end of February and once this medical crisis is over it should spring back quickly. However, in the near term there are many unknowns. Financial markets handle bad news well, but they handle unknowns poorly.

In times of great uncertainty, we measure the worst-case scenario with trailing SPX operating earnings. Earlier this week we wrote: *"If we measure downside risk using the average PE of 15.6 and SPX's 2019 earnings of \$158, we find a low-risk valuation target of SPX 2465. Note: this is 9.8% below this week's intraday low of SPX 2734. Also supporting the equity market is the fact that the SPX dividend yield is now 152 basis points above the 10-year Treasury yield. This is the highest spread since March 1955."*

The bottom line is everyone should protect themselves and their families by being wise in terms of socializing and washing their hands frequently throughout the day with simple soap and water.

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