SEEING THE FOREST THROUGH THE TREES

The first earnings season of the coronavirus recession is coming up soon, and the results will not be good reading. Through February it appeared that the economy and corporate earnings were on track for a steady expansion, but by early March it was clear that this would not be the case as the full extent of what we were facing became apparent. Current analyst estimates are for S&P 500 earnings to fall 5.5% in the first quarter, 13.3% in the second, and 3.8% in the third. There is consensus in forecasting positive growth in the fourth quarter, which assumes that the country goes back to work over the summer. The three biggest drags on the economy will be in the energy, industrial, and consumer discretionary spending sectors, and it is quite possible that nearly all current economic data series will show record weaknesses. Unfortunately, with the novel COVID-19 virus having no immediately effective drugs or vaccine, there was only one option: shutting down economic activity to slow the spread and buy time for doctors and scientists to apply current treatments and devise new pharmacological solutions. This resulted in 6.6 million U.S. unemployment claims for the final week in March—on top of the 3.3 million claims from the prior week. These statistics are expected to increase in April.

In response to this national emergency, the Federal Reserve Bank cut its benchmark interest rate to near zero and began a campaign of open-ended bond purchases. The Fed's moves will prevent credit from drying up and allow companies to borrow cheaply. Most global central banks have created similar programs.

On March 27th the CARES Act was signed into law at the urging of the Administration and a congressional majority. This will be the biggest fiscal stimulus package in modern history, totaling almost $2.3 trillion or approximately 9% of U.S. GDP. It specifically targets households, with $250 billion in direct payments to tax filers and an additional $250 billion going to expanded unemployment benefits. $367 billion is earmarked for loans and grants to impacted small businesses. An additional $425 billion goes to the Federal Reserve to provide loans and liquidity via the Fed to financial markets. Support to state and local governments, hospitals, and farmers totals $330 billion. Additional stimulus packages are in the works by the Federal Reserve, the Administration, and Congress. All of these measures are unlikely to actually stimulate growth, at least until the economy is no longer shut down. Rather, they are a means to cushion the economic impact from the virus containment policies.

Forecasts of the economic downturn and recovery vary wildly, but most see a recovery underway by the end of this year, and historically equity prices anticipate a recession end by about four months. Clearly, enough money is being pumped into the economy to make the recovery vibrant when it takes hold, with low interest rates and more progressive economic and regulatory policies. We believe the lows for the popular averages registered on March 23rd may have been what technicians would call "the internal lows," accompanied by maximum selling pressure. The lows may be tested again, but if so, and with less selling pressure, we can assume that a new upturn is in place.

As such, we are optimistic about the future.

April 2020

PLEASE NOTE: Unless otherwise stated, the firm and any affiliated person or entity 1) either does not own any, or owns less than 1%, of the outstanding shares of any public company mentioned, 2) does not receive, and has not within the past 12 months received, investment banking compensation or other compensation from any public company mentioned, and 3) does not expect within the next three months to receive investment banking compensation or other compensation from any public company mentioned. The firm does not currently make markets in any public securities.

Tel: (212) 320-2000 140 Broadway, New York, NY 10005 Fax: (212) 320-3040