

# TRANSITIONS

## THE BLACK SWAN VIRUS

In the investment community, a “Black Swan” refers to a one-off event that is a surprise. It is a high profile, hard to predict, and rare event beyond normal expectations in finance that has a major effect. Wall Street never sees it coming. Back when the markets were reaching new highs in mid-February, everything was rosy far into the future. Then we learned the coronavirus was far more widespread in China and was moving across the world, infecting both the infirm and the healthy people. This was the Black Swan event.

**Market Correction:** A real Black Swan event triggers a market correction. This particular correction is interesting due to its speed and intensity. As most of you know, I have been looking for the market to experience a real correction for some time. This is a healthy part of markets, where excesses in pricing are corrected to points of value. For a real correction to occur, we need to see both a steady decline in prices and a time period of weeks or months of a bottoming out process. As the markets have marched up higher over the last decade without a bona-fide correction consisting of both a price decline and a time period lasting beyond a few days, this may be the first real correction that many investors have experienced.

**China:** What is interesting is the permanent damage this coronavirus has done to China. When their leaders decided to suppress critical information from the world while commerce travel to China continued, their actions made sure this virus would move worldwide. Having done nearly everything wrong in terms of managing an outbreak, they have caused great damage to the national brand of China. If material supply chain interruptions occur from this virus, then it will become imperative that companies geographically diversify their supply chains out of China without regard to cost. Although a great loss to China, this will provide stimulus to other countries, including the United States.



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**Federal Reserve:** The Fed bowed to political pressure to lower interest rates to combat the coronavirus. This is completely absurd. Using the monetary policy tool of lower interest rates simply can't stop the spread of a virus. Lower rates do not help factories that are lacking raw materials from abroad. The Fed's action does not get the Chinese to go back to work in their factories. With interest rates already close to zero, should our economy dip into a recession, the Fed now has limited policy tools left. A far better approach is the use of fiscal policy from the White House that directs efforts to develop a vaccine.

**Volatility:** With the first experience of a Black Swan event, the markets are displaying volatility. Large swings up and down in market indexes and stock prices are part of this correction process. As long as you do not need immediate cash tomorrow from your portfolio, and maintain the same long term perspective we have, these short term market movements are just short term activity.

**When does it end:** What makes a Black Swan unique is they are "unknown unknowns". These arise from situations that are completely unexpected, "the first unknown"; along with "the second unknown" which there is no past experience in handling such events. Not one person on Wall Street, or in our Government, or any industry leader in corporate America, have a handle on how to manage the impact of this corona virus to our economy. The good news is we have a nation of very talented people who collectively will figure out a path from which to proceed.

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