Hamilton-Bates
Market Update

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The stock market began 2020 the same way it finished 2019—on a strong run spurred by a supportive Federal Reserve and hopes that the trade deal will re-ignite growth prospects. Even an outbreak of a virus of unknown origin barely put a blip in the market's uptrend. A brief one-day decline followed by a week straight of gains has the major averages right back to their highs.

The stock market is trading as though the Corona Virus is no big deal. We hope the rest of the world can avoid the human disaster that is facing China right now. 60 cities and 400 million people (more than the entire US population) are quarantined to their homes. It is an event of gargantuan scale. Even if the worst of the outbreak is limited to mainland China, the economic impact is likely to be felt globally. Much of China is off-line. Economic activity will take a big hit there, and growth prospects and earnings hits will likely be felt around the globe.

Economics, Earnings, and Interest Rates

The latest economic data show that the US economy is still doing well—the January payroll report showed 225K jobs created, well above expectations of 165K. The widely watched 3 month average is above 200K jobs, showing that the US labor market remains robust. Looking ahead much will depend on how long China is shut-down, and how contained the outbreak remains. Even contained to China, economic activity will probably be as much as a couple percentage points lower than it might otherwise have been—and thus earnings this quarter could take a hit.

Somewhat ghoulishly, the market has taken the 'bad news' about the virus as 'good news' since it means more Central Bank largess. Such belief has been the major catalyst to this week's rebound. The fact is Central Banks have indeed been supportive in the wake of the corona virus, with a number of rate cuts in Asia and comments that more could be done if needed. It is the market's belief that friendly Central Banks can solve every problem—that belief could be tested in the weeks ahead.

Market Outlook

The market was looking stretched at the end of January, and virus concerns were enough to trigger to a pretty sharp 1-day pullback. But Central Banks filled the breach with talk of liquidity and rate support, and the markets quickly recovered.

The corona virus has put the trade war to the back burner, with tariffs cut on some US goods by China; and we could see reciprocity by the US. The outbreak could also make China more amenable to a full deal later this year—a longer term positive. With economic slowing likely , at least for the next quarter or so, US bonds remain attractive with interest rate differentials favoring the US. Another round of global rate cuts would only help US bonds.

For the stock market, the negative effects of a slowdown in economic activity could be offset by a supportive Fed and other Central Banks. The extent of this offset will depend on how long the outbreak lasts, how far it spreads, and how deep any hit to earnings. Much of that just cannot be known right now.

The good news regarding Corona Virus, is that the mortality rate is much lower outside of China, a positive sign. If help can reach China to stem it there, the outbreak could be limited to a 1-2 quarter event, and economic activity picks up quickly thereafter—much like SARS in 2003.

We have not done significant trading in Managed

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Portfolios in 2020, with a minor trim in equity holdings in late January (ahead of the big drop), and we continue to hold that bit of extra cash. We'd look to deploy that capital on a dip lower than we saw last week, closer toward key levels around 3100.

If things go well, and the virus does not morph into a pandemic (and we don't expect it to right now), the choppy first half of the year followed by strength later could remain the game-plan that we laid out early last month.

Key support for the S&P 500 remains just above 3000.

S&P 500 Long-Term Chart

S&P Pushes to New Highs

The S&P quickly reversed the late January virus dip, but is once again a bit extended above the long-term trend.

Still, as long as the S&P remains above its 10-month average (blue line) the trend remains bullish and they remain in control.

A dip toward that average would actually be healthy, and we'd look to add on such a move. The key level is now around 3030-3050 on the S&P 500.