



# Lakeshore Financial Planning

## The Case for Long-Term Optimism – Part III

I've made it my policy to write a letter of this nature every time there is a sharp market decline (over 20%), with high levels of fear and anxiety about the future. I hope these words will help calm you by adding some perspective to the current environment. I share your same emotions as I write, but it's important we not let current events shape our long-term view and plans. Because your individual situation is unique, this letter will not contain specific portfolio recommendations or advice.

In the depths of the Great Recession, fall 2008, I sent out a letter listing 10 reasons for long term optimism, and I had the distinct feeling many of our clients thought I had lost my mind. Experts were predicting a collapse that would forever change society and financial markets. In early 2009, with the S&P 500 Index down approximately 66% over the previous twelve months, I read this quote from a Wharton Business School professor, "If everyone you know is betting that the world is going to end, place your money on the opposite bet because what do you have to lose?" In other words, if the global economy did collapse, it wouldn't matter what kind of investments we owned. Even gold would be worthless, and we would all be bartering for food and water. Thankfully, the collapse never happened, nor do I believe it ever will. The panic selling of stocks and hoarding of essential goods today reminds me of those fearful times one decade ago. Thus, the reason for the letter you are reading now.

Exactly one month ago from the writing of this letter, we held our Annual Economic and Market Update. On that day, February 20<sup>th</sup>, most U.S. equity indexes stood at or near all-time high levels. The mood in the room that evening was lighthearted and even cheerful. Ironically, the only issue that night was that we ran low on food!

Thirty days later the dual impact of the Coronavirus and a collapse in oil prices has sent the S&P 500 index lower by approximately 30% from its peak. There has been virtually no place to hide in this decline. What this means for most everyone is that our March investment statements will show the largest monthly decline in our investing lives. I'm sure you are wondering how pointing this out is supposed to make you feel any better. I promise the optimism section of this letter is coming, but I don't want to minimize or downplay the financial impact of this past month.

A couple of weeks ago a good friend of mine told me not to be surprised if more people end up dying from stress and anxiety induced heart attacks, strokes and suicides than from the virus itself. The cruel reality is that our response thus far has taken away many of the activities we turn to for comfort and relaxation. We are being asked to not gather in groups, keep our distance from one another, and spend more time at home. It is important that we follow this advice, but my fear is that many are spending this extra time at home glued to the news.

I would never recommend not staying informed, but we need to remain mindful of the sources of our information. CNN and Fox News are seeing their highest ratings in over a decade – since the last financial crisis. Those ratings generate big advertising dollars and the networks get to select the "experts" we hear from and the pictures we are shown. The fact is that the media personalities and

programmers are being paid to keep us tuned in. This tells me we are smart to stay informed but also to filter the information we are getting through the lens of underlying motivation.

It's impossible to estimate how much more economic and human damage the virus will cause in the days, weeks, and months ahead. Truthfully, I don't think anyone has many answers at this point, and this uncertainty is what we all find so unsettling. My focus here is on the potential economic impact, but this in no way diminishes the human tragedy. In fact, this crisis is very personal to me because my daughter Lauren is an Emergency Room Physician Assistant at South Shore Hospital in Boston. She is on the front line with other quiet heroes (I don't use that term lightly) working to treat patients and contain the impact of the virus.

The most important issue now is how we as investors react and respond to this unexpected series of events. Former heavyweight boxer Mike Tyson is more known for his fists than his wisdom, but I think he was onto something when he said, "Everyone has a plan, until they get punched in the mouth." This virus has been a punch in the mouth, and it hurts, but we can't let it knock us out.

We can't let the shock of these recent events cause us to abandon our long-term strategy. This is much easier said than done. I see plenty of challenges and difficulties ahead. There is no question that a significant economic downturn is in our near-term future. Corporate earnings will fall, and unemployment will spike up this quarter. This contraction is expected, but it seems that almost everyone is taking the most current facts and extrapolating them way into the future. This would imply that events will continue under the most negative conditions, without adjustments in behavior or activity by individuals, organizations, or governments. I believe adjustments will, and in fact are, being made to avoid the potential worst-case scenarios.

Just as when I wrote to you during the financial crisis in 2008, I'm not trying to forecast when this market might bottom or to make predictions. I learned long ago that trying to predict the short-term direction of markets is sheer folly. Instead, I'm wanting to look out past this current crisis and objectively evaluate some of the positive actions and trends that are not being talked about. If you want doomsday information, turn on your TV or go online. If you want some cause for long term optimism and, I think, realism, please read on.

**Interest rates at historic low levels** Currently, the 10-year U.S. Treasury Bill is yielding just over 1%. Just a few days ago the yields dropped below .5% (1/2% of 1%) in a massive global flight to quality. These rates have unleashed a flood of refinancing that mortgage lenders are having a hard time keeping up with. In fact, if you haven't refinanced in a while, it may be worth looking into.

This means many Americans will be getting a raise in the form of lower monthly payments. With most everything entertainment related being shut down right now, I expect this extra money will go to savings or to pay down debt. However, once our country opens for business again, many people will have extra disposable income and should do what Americans do best – spend!

The other advantage of this low interest rate environment will play out on a much broader scale. How much money do you think individuals, and institutions will eventually want to keep in U.S. Treasuries yielding around 1%? Most of this money is parked in Treasuries temporarily out of fear and uncertainty. And we aren't talking a few hundred million, we are talking about many billions of dollars. In addition to these funds in U.S. Treasuries, there is a tremendous amount of money sitting in cash earning even less than 1% interest. I hope you see my point. Again, I'm not making a specific forecast, but at some point in

time some or most of this massive pile of money earning almost nothing will be looking for a new home. If history is any indication, the currently beaten down U.S. equity market will be the destination of choice for a good percentage of these funds.

**Falling Oil Prices** This has been a nightmare scenario for the energy sector, as oil prices have fallen over 50% in a matter of weeks. The original decline in prices was the result of a production disagreement between Saudi Arabia and Russia which now has been accelerated by falling global demand. However, what is bad for the energy sector and countries like Russia and Venezuela is ultimately good for the American consumer. If you have filled up your tank lately, you've noticed how far a dollar goes at the pump these days. These lower prices put money directly into the pockets of consumers. This has the same direct impact on the economy as a tax cut. Low gas prices were a key factor in the recovery from the economic downturn in 2009. Oil is a volatile commodity and neither Saudi Arabia nor Russia can afford to continue their spat for more than a few months, so it's doubtful that prices will stay this low for long.

**A massive fiscal stimulus package** The government's response to this crisis is another topic best left for others to debate. What we do know is that there will be a massive amount of spending to help those most damaged by the crisis. It's very tempting to get political and preachy regarding this stimulus package. Who should get help and who shouldn't and why bail out an airline when they have used over 90% of free cash flow in recent years to buy back company stock to hit bonuses? I think we all agree that there are people and businesses (mostly small) who need help to get through this crisis. It's not going to be fair, but it seldom is. It looks like we will be providing help now and debating later. The details of this plan are still being worked out but I would expect to hear more information in the next few days. The sooner the better. In an economic crisis our government can be very effective as the lender or spender of last resort, so to speak. This emergency response doesn't represent a permanent change in our economy any more than limitations on gathering together or the closing of a large portion of our service industries.

**A better prepared society (and world)** There are many already asking the question: Why weren't we better prepared for this virus? It's a valid question, but not particularly important for our purposes today. I suspect the finger pointing will go on for years and this could certainly play a role in the upcoming election. I think the much better question today is: Will this help us be better prepared for future viruses or other disruptive events? Or, more directly: Will we learn from this event and be able to respond more quickly and efficiently in the future? For example, this crisis could become the incentive we need to improve current supply chains for critical medical resources.

The Coronavirus and the 9/11 terrorist attacks are very different, but both are Black Swan events. These are defined by Nassim N. Taleb in his book "The Black Swan" as very rare events that are difficult to forecast and can have extreme consequences. We made changes and adjustments after 9/11 to make our country safer, and it's certainly possible we will take proactive steps after the virus passes. If nothing else, and at an absolute minimum, maybe we will all just wash our hands more often and that small act alone will greatly reduce future flu outbreaks. I can tell you from this day forward you will always see a bottle of Purell Hand Sanitizer as you enter our offices.

**World Class Health Care Workers** Please notice I'm highlighting the workers and not the system. Our country has, without question, the best trained health care workers in the world. Remember people still come from all over the world to be trained in the U.S., and many stay. The key right now is for us to help these professionals by not overwhelming the system and by providing them with the proper

protection and equipment to do their jobs. My daughter in Boston tells us they are extremely low on many supplies, including their own protective gear. It sounds like there is a large mobilization effort, including private industry to get supplies and resources to our health care professionals. If we are ranking priorities right now, I would put this at number one. Perhaps for a few weeks we can pay less attention to the overpaid NFL and NBA ego maniacs and focus more on the real heroes in our society. Frankly, I could care less where Tom Brady ends up playing football and for how many millions.

**Renewed Commitment to Advanced Medical Research** I saved for last what I believe is the best reason for long-term optimism. I think it has now been fully exposed where our country is the most vulnerable. I don't know what we spend as a country on advanced medical research, but I would be willing to wager that the number will rise significantly. I'm fascinated with the process of innovation and I've read widely over the years about the origins and nature of scientific advancement. Dollars and resources will almost undoubtedly pour into research on virus prevention where great minds will make progress; however, the vast amount of scientific discoveries originate in completely unexpected ways. Alexander Fleming didn't set out to discover penicillin. He returned from a vacation and was surprised by some mold growth in one of his petri dishes. It turns out his "mold juice" ultimately saved millions of lives in the years to come. His discovery was a positive Black Swan event.

The point is that increasing funding for advanced medical research could produce innovations and discoveries in areas and ways that we cannot even imagine today. Right now, working in a university or corporate lab somewhere (most likely in the U.S.) could be the next Pasteur (cholera), Wolfman & Enslow (chlorination), Foegle (smallpox), or Enders (measles). Or perhaps even the next Jonas Salk whose vaccine against polio – the disease that killed thousands per year, paralyzed Franklin Roosevelt, and sent many children into iron lungs – was proven safe on April 12, 1955. On that day, according to historian Richard Carter, "people observed moments of silence, rang bells, honked horns, blew factory whistles, drank toasts, smiled at strangers and forgave enemies." Could we have our own day like this in the future? An enhanced research commitment to identify and prevent Corona and future viruses could lead to breakthrough treatments for diseases like cancer, Alzheimer's, and neurological diseases like Multiple Sclerosis. Let's direct more resources into the hands of the brilliant minds in our country and let them work their magic for the benefit of everyone.

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**The Days and Weeks Ahead** I don't know how much this virus will change society and the way we live over time. I think that very much depends on how the next few weeks and months play out. I expect that once we have the virus under control it will still take the economy time to heal. In past times of national crises, the stock market has begun recovering well before the general economy - it has been a good leading indicator. Our hope is that most of the economic damage to come is already priced into stocks today.

There will be a day in our future when the CDC announces the number of infections is declining or that a vaccine has been discovered. At that point the uncertainty will be lifted and we will know when our economy will be allowed to fully reopen for business. I believe that announcement will trigger a large, possibly massive, flow of funds from cash and U.S. Treasuries into the U.S. stock market. I wrote earlier in this letter that the upcoming March statements will be the worst statements most investors have ever received. However, any signal that we have turned the corner in controlling this virus, I believe, could be the beginning of a rapid recovery. Never any guarantees, but we could see a rebound more powerful than most feel possible at this time of extreme pessimism.

What I'm most looking forward to on that day is feeling the change in our national psyche and driving down the street to see our businesses and restaurants full again. It can't happen fast enough for any of us. We have parades for our Super Bowl, World Series, and Stanley Cup champions. I believe once we've beaten this virus, every city should hold a parade for our health care workers.

Right now, we are taking every precaution at our office. We are working in rolling shifts and only conducting appointments by phone. **However, we have already agreed that on the day the restaurants reopen, we will be closing our computers and leaving at noon to celebrate. Our destination will be Fishbone's on Jefferson and 9 Mile. Please consider this your official invitation to join us. The first beverage of your choice is on us.**



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**The following is a list of books I recommend for a dose of optimism in this difficult time:**  
**"Enlightenment Now: The Case for Reason, Science, Humanism, and Progress" by Steven Pinker**  
**"The Rational Optimist: How Prosperity Evolves" by Matt Ridley**  
**"Fewer, Richer, Greener" by Lawrence Siegel**  
**"Unleashing the Second American Century: Four Forces for Economic Dominance" by Joel Kurtzman**

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