MARKET VOLATILITY CONTINUES

The longest bull market in U.S. history is over. It ended with an all-time high for the S&P 500 on February 19. From that day forward, the U.S. equity market has suffered the quickest-ever descent into a bear market from an all-time high (18 trading days). As of press time, this bear market has already produced a 20% drawdown, though earlier this week markets had declined by over 30%.

Catalysts for bear markets have historically included financial crises, Fed policy mistakes, and event-driven shocks. The COVID-19 bear market clearly falls into the last category. Historically, event-driven bear markets have bottomed more quickly than the others. These bear markets have averaged six months in length, with an average drawdown of 22%. Crises caused by surprise events have a predictable pattern: the event occurs for a discrete and usually short period of time, markets fall, policymakers respond, and markets recover. We acknowledge this event-driven bear market is more complicated, primarily because COVID-19 has not yet reached its peak. In the short term, the driver of market direction is likely to be the path of the coronavirus itself. But we believe that the policy actions in place, and those to come, are building a platform for recovery.

First, let's acknowledge that public health measures designed to contain the spread of COVID-19 have accelerated dramatically in just the last week and are likely to continue as we move to a high-speed rolling quarantine of sorts. While the President has provided conflicting messages, state governors and public health officials are adamant that physical distancing must continue in order to maintain any progress in our goal to flatten the curve.

Meanwhile, central banks around the world have pulled out almost all the stops. In less than a week, the Federal Reserve rolled out 11 different initiatives. The highest profile measures came from the Great Financial Crisis playbook: a return to a policy interest rate range of 0.00%-0.25% and the aggressive purchases of government and mortgage securities. The other measures were more technical in nature but are focused on improving liquidity in parts of the credit markets that were not functioning normally: commercial paper, repurchase agreements, certain money market funds and corporate and municipal bonds. The Fed doubled down on Monday morning, announcing unlimited support for the Treasury and mortgage markets as well as massive liquidity backstops for other stressed parts of the credit markets.

Finally, we have fiscal policies which typically take longer because they are subject to the political and legislative process. To date, targeted programs have been passed to extend paid sick leave, unemployment benefits, and other limited measures. At press time, the Senate has passed a $2 trillion stimulus plan focused on addressing the very real liquidity problems that businesses and households will have as we fight the virus by shutting down and staying in. Other countries have extended similar fiscal largesse and the International Monetary Fund (IMF) is actively working with the most at-risk countries to stabilize their economies.

Even so, our expectation is that the second quarter will show one of the biggest drops in economic activity in the nation's history. Likewise, there will be a significant jump in unemployment and a plummet in consumer spending and manufacturing output. These trends will be echoed around the world.

A brutal second quarter is largely discounted in financial markets, including a significant drop in corporate profits. At this time, we believe the third quarter will probably be "less worse" than the second, and a true recovery likely emerges before year-end. But at this time, there are still too many unknowns to be sure.

Significant events, like COVID-19, often drive volatility, which tests our composure as investors. When such volatility gets most extreme, it is good to take a step back and remind ourselves of the nature of the markets. Volatility is part of investing, and by the markets' nature, they eventually recover. We are here to speak with you about your portfolio and what to do, and what not to do, as it pertains to your unique situation, especially in these uncertain times.

Please click here for our team contact information.

RELIEF FOR U.S. TAXPAYERS

The IRS will allow individuals to defer filing 2019 federal income tax returns and paying federal income tax bills that would normally be due on April 15 until July 15 without interest or penalties. This includes outstanding 2019 tax payments and any 2020 estimated quarterly tax payments due by April 15. This deferral also applies to trusts, estates, partnerships, and corporations.

The deadline for contributions to individual retirement accounts (IRAs) has also changed: you have until July 15 to make contributions for 2019.

It is important to note that state and municipal taxes are not affected by this IRS announcement. While some locations (including New York and California) are allowing deferred filings and payments to some extent, you will want to check with your state or local government or your tax advisor.

For those who work with Ropes & Gray's tax service department, please stay tuned for more guidance about how they are handling the adjusted federal filing deadlines.

A PLANNING OPPORTUNITY WITH ROTH CONVERSIONS

As difficult as it is to watch, the recent decline in the stock market may present an opportunity for long-term investors to take advantage of the option to convert a traditional IRA or qualified retirement plan to a Roth equivalent. Retirees who have yet to take required minimum distributions from their retirement plans, are currently in a low tax bracket, and have liquid assets available to pay the tax due on a Roth conversion may find the opportunity particularly attractive.

Click here to learn more.

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