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MEMORANDUM

TO: All Clients
FROM: Meketa Investment Group
DATE: February 25, 2020
RE: COVID-19 Update

In our memorandum dated February 13, 2020, we provided a brief background on COVID-19 (the official name of the coronavirus) and potential market and economic impacts. Given the increase in cases outside of China, and the recent market reaction to the spread, we provide a brief update on the situation below.

In the past two weeks, the number of cases of COVID-19 has increased to over 80,000, with a growing number of cases outside of China, including a troubling acceleration of cases in South Korea, Iran, and Italy. Countries continue to play catch-up as they seek to head off the spread of the disease. Italy imposed quarantines on villages surrounding Milan, South Korea isolated approximately 7,000 troops after some tested positive for the virus, and other countries are beginning to cancel travel to areas with high infection rates. While the World Health Organization has not labeled this outbreak a pandemic, they indicated that the disease has “pandemic potential.” With an incubation period of potentially up to four weeks, COVID-19 is difficult to detect, making the isolation of infected individuals a challenge.

Outside of the human toll, economies are showing signs of strain. An increasing number of companies have highlighted the negative impact that COVID-19 is expected to have on their businesses. Sectors particularly hit include travel, tourism, and those that rely on China’s manufacturing sector. Projections of future economic activity, such as Purchasing Managers’ Indexes (PMI), have also shown a COVID-19 related deterioration for a number of countries. In the US the Composite PMI dropped sharply to 49.6 (a reading below 50 indicates contraction), with both the Manufacturing PMI and the Service PMI dropping from January levels. Investors are reacting to these data points and to the spread of the virus and have been moving out of riskier asset classes (equities), into perceived safer investments including gold and US Treasuries.

The recent spread of the virus outside of China has finally captured the market’s attention. As of this writing, the US yield curve is, by some measures, again inverted (i.e., short-term rates are higher than long-term rates), with the 10-Year Treasury yield at 1.31%, its lowest level since 2016. The 30-Year Treasury is at 1.79%, its lowest level in history. Last week, the S&P 500 was at an all-time high mid-week, but has since declined close to 5% with over 3% of the decline coming yesterday. International markets are also experiencing a stiff sell off. The Stoxx 600 (Europe) is down 3.8% over the last week and Seoul’s Kospi Index declined 7.2%, given the spread of the virus there. Markets continue to decline, with the S&P 500 down between 2% and 3% today.

Despite the headline declines yesterday, the US market finished back at levels it reached at the end of January. A correction is typically considered a 10% market decline, and a Bear Market a 20%+ decline. Thus, we would have a long way to go to reach these more common technical definitions. Although sell-offs like this can be concerning, they are a reminder of the value of a truly diversified portfolio. Long-term investors, with commensurate time horizons, should have strategic asset allocation policies that anticipate this type of volatility, allowing them to focus on their long-term objectives.

If you have any questions about your portfolio's positioning, please do not hesitate to reach out to your client service team.

Disclaimers