We are living through a time where superlatives seem to no longer suffice. The fastest 35% decline in the market since 1933 is followed by the fastest 25% rally in market history. The 27.2% gain in the S&P 500 over the last three weeks represents the best 15-day move in nearly 90 years. An unprecedented global crisis created an unprecedented market meltdown, which in turn precipitated an unprecedented fiscal response from both policy makers and central banks. You would think that it should be impossible to use the word, unprecedented, three times in the same sentence, but how else could you describe the circumstances that have preceded this historic market rally. Even in this most extraordinary times, the old maxim applies: Don't Fight the Fed.

Recent optimism aside, we think it is way too early to say with certainty that the worst is over. The future course of the virus is uncertain, and what we don't know is far more important than what we think we know. The range of possible outcomes is still far too broad to take comfort in any one forecast. For now, the bears have more facts and figures to support their view than the bulls.

At the beginning of February, the U.S. employed a work force of 164-million people. In the last four weeks, more than twenty-one million of them have filed initial unemployment claims, and this probably understates the true number since they can only count the claims that have been processed, not just filed. The unemployment rate is now projected to rise to somewhere between 15% and 20%, far above earlier estimates, and forecasts from sources we consider to be knowledgeable are that the number could approach 30% before this is over.

The early data for March has confirmed the unprecedented (again) hit to the economy on a month-to-month basis. Manufacturing output experienced its sharpest decline since 1946, when war production ended, and retail sales fell at the fastest rate since such surveys were initiated. Given that panic buying actually inflated the March numbers, and social distancing measures were not widespread until the second half of the month, April's report will likely be even worse. Unsurprisingly, the University of Michigan Consumer Confidence Index saw its biggest monthly decline on record, though it remains above the levels measured during the 2008-09 financial crisis. It is likely to fall further if the current crisis extends much into the next quarter.

Why is the market rebounding while the virus continues to spread and the economic news is worse than expected?

The first reason has already been mentioned. Investors are reacting to the stimulus measures taken by policymakers to soften the blow of the economic downturn for individuals and businesses. Of course, the effectiveness of these plans will depend entirely on their execution rather than their intent, so we will have to wait and see. Also, the Fed has essentially backstopped the bond market through a variety of programs, including the buying of junk bonds and consumer loans. It is even reaching into the muni market to keep distressed cities and states afloat. The Fed's actions, while supportive and perhaps necessary in getting us through the current crisis, have also served to distort the risk/return curve for the moment. How does one value a junk bond versus a Treasury bond, when the U.S. government or one of its agencies serves as a guarantor for both. All of these temporary measures will come with a price, and we can hope that they don't establish a precedent for future crises that may be more self-inflicted. But those are tomorrow's concerns.

The other reason why equities are doing so well in the face of historically bad economic news is that there are signs that the coronavirus news may be growing "less worse." To investors, less worse is every bit as important as actually getting better. While the media and most people are focused on raw numbers or trends, forward looking investors focus on the rate of changes in trends, the second derivative in technical terms. Before a trend can change direction, it must first change more slowly in its current direction.

The rate of growth of daily new infections in Italy is trending down. The same is true in Spain. China has begun to reopen its economy, but we have learned to regard reports from this area with more than a few grains of salt. The curve appears to be flattening in thirteen states and in New York City, even though the governor has extended social distancing through May 15. Projected U.S. deaths from the virus have begun to stabilize or even come down in many cases, and it appears that we will end up nowhere near the original worst case estimate of 500,000.

There is encouraging news on the treatment front, as well. Gilead's drug, Remdesivir, has been approved for use on a trial basis, and initial reports are that it has been effective in helping patients recover from the worst symptoms of the coronavirus. The FDA is moving more rapidly to approve new antibody tests, and several new vaccines have been introduced into the testing pipeline. In all, 14 companies have drugs in various stages of testing. Full deployment of the antibody tests is probably weeks or months away, and no one knows when an effective vaccine will be approved, much less manufactured and distributed. But, as is the case with the rate of new infections, the treatment news is less worse than it was, and investors can begin to see the re-opening of the economy as a viable prospect.

For us, it is still too early to begin adding risk back into our portfolios in a meaningful way. The course of the exogenous event that controls our destiny at the moment is way beyond our ability to forecast, and the measures that will be required to contain it will likely continue to affect our economy for a period that is yet unknown. We're not saying that a rapid recovery isn't possible, we're saying that there is no basis for assuming that a recovery is likely, or even possible, two quarters from now or a year from now, nor even to estimate the new baseline from which such a recovery will be launched. If the future that the market is now discounting proves to be too optimistic, we could easily see a return to the March lows. We can assume that a return to "normal" is unlikely until an effective treatment is available, and there is no timeline for that, and coronavirus will be a factor in our lives until a vaccine is produced. Until that time, the best we can hope for is that its effects will become intermittent and manageable.

For those who have been invested for the long term, the good news is that from the market's trough in the financial crisis of 2008-09 to its trough last month, the S&P 500 is still up approximately 225%, an average of 11.3% per year. For those of you who are new to the market with a long time horizon, we would only say that as unique and scary as the current situation is, it will eventually be overcome as have all other crises in the past.

As someone once said, if the mountain was smooth, you couldn't climb it.

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