COVID-19, Y2K and the Stock Market

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After the rout in NASDAQ last week, more than one market observer predicted that a major rotation was underway or that the rally in growth stocks was over. The rationale was that the plague of the Coronavirus was coming to an end and all those companies that witnessed the rise in their stock prices due to their ability to prosper during the virus were about to suffer as the economy returned to normal. Already, many states are "opening up" and allowing consumers to participate in group endeavors. We have heard more than one story of friends being turned down for dinner reservations because the restaurant was at capacity. While we do not know the exact date of when the victory over the virus will be declared, we do know that such a date is not too far in the future. After that date, equity markets are expected to return to normal and there will be greater balance between growth and value stocks. If the recently approved fiscal stimulus package of $1.9 trillion will give another "shot in the arm" to the economy, the rotation may not produce any sustained losses among sectors of the stock market. A commitment by the Federal Reserve to insure a viable economic recovery is another factor in expecting a continuation of the bull market.

Another such example of stock market exuberance existed in the late 1990s when fears of a computer meltdown due to the change in the millennium on January 1, 2000 propelled stocks higher. Prior to the event, there was an explosion in spending on information technology, media and telecom software and hardware to avoid the catastrophe. As a result, stocks in these sectors surged for years before the arrival date. Even after January 1, 2000 came and went without incident, market forecasters expected a continued move higher since the Y2K crisis never materialized. What forecasters did not see was the lack of demand for computers and software after the crisis passed and the subsequent decline in the fortunes of many companies that benefited from this event. Unfortunately, the government failed to aid those companies affected.

Can we draw parallels between these two events? Naysayers are convinced that a bubble is forming again just like the late 90s when Chairman of the Fed referred to the market rally as "irrational exuberance" and that a crash in the stock market is only a matter of time. We believe that today's bull market is based on cash-rich companies that have taken advantage of the COVID crisis and are disrupting the normal way of doing business. These disruptors exist across all industries as opposed to only information technology companies that benefitted from the lead up to Y2K. While there will be a change in investors' strategy into the recovery, we do not envision an "us versus them" event where one sector will go up in price while another one falls. There will be periods when there are temporary corrections but that does not mean that the bull market is over.