

Delta Investment Management is a registered investment advisory firm. Delta welcomes discussions with individuals seeking investment advice and advisors seeking a new turnkey asset management solution.

Delta manages portfolios at TD Ameritrade and Schwab.

Please contact Delta at info@deltaim.com or 415-249-6337 to learn more.

February 28, 2020

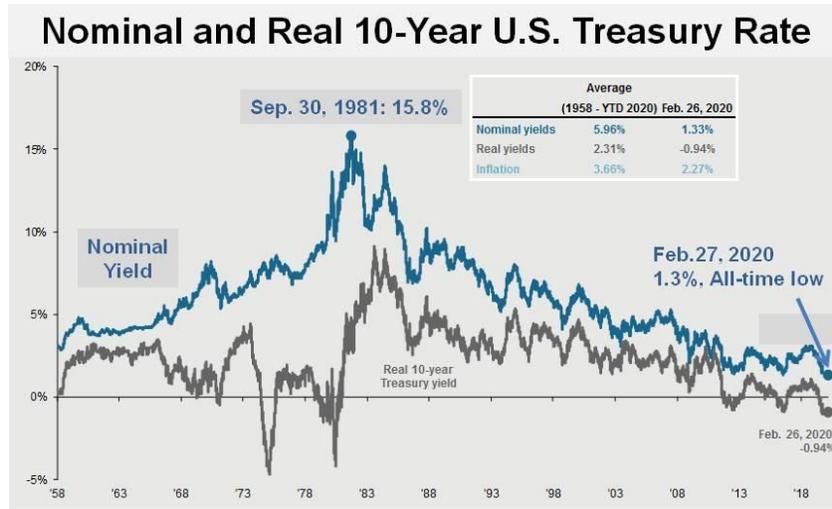
What If?

What if the current outbreak of coronavirus spreads significantly more than expected? This is the question the market is attempting to discount into stock prices.

On Thursday of this week, the S&P 500 traded down 2.6 standard deviations below its 50-day moving average. This is outside of what normally happens about 98% of the time.

Two of the largest companies in the world, Apple and Microsoft, reduced their earnings outlooks this week because of coronavirus. 2020 S&P 500 earnings estimates are being revised down. What if 2020 S&P 500 earnings show no growth year-over-year? What would be our expectation for the value of the S&P 500 in a no-growth earnings year?

The amount of forward earnings adjustment necessitated by the coronavirus is uncertain. What is certain is interest rates have fallen significantly. At the start of 2020, the 10-year treasury was at 1.9%. This week, the 10-year treasury reached an all-time low of about 1.3%.



Fed Funds futures are pricing in a 76.4% probability the Federal Reserve cuts the Fed Funds rate at their March 18 meeting. The probability of a rate reduction by June 10 is 95%. By the end of 2020, the expectation is that there will be at least two Fed rate cuts.

Investors own stocks because they want to enjoy the extra return earned over time for taking on risk above and beyond risk associated with owning a risk-free asset like a one-month U.S. treasury bond. As the stock market sells off, the expected forward return from owning stocks rises, all else being equal.

But, it is likely that not all else is equal. We expect 2020 S&P 500 earnings to be lower than the \$175 currently estimated. We also expect the risk-free interest rate to be lower.

If we assume the S&P 500 earnings for 2020 is roughly flat with 2019 earnings at about \$163, the Delta stock market valuation model shows the S&P 500 fairly valued at about 3,000. The index closed at the lows on Thursday at 2,978. If we assume the risk-free interest rate falls from about 1.5% to 1.25%, the Delta stock market valuation model shows the S&P 500 fairly valued at about 3,400, about where the market was on February 19. If the risk-free rate falls to 1.00%, the S&P 500 would be fairly valued 20% higher at 3,600.

2020 may be a replay of 2018. In 2018, the S&P 500 appreciated by 7.5% by January 28. It then lost 10% of its value by February 8. By late August, the S&P 500 was back at its old high. In 2020, the S&P 500 climbed 5% by February 19. By February 27, it was down 10%. As long as coronavirus does not take the U.S. and the rest of the world into recession, one might expect the market to recover its losses later this year.

Because of the depreciation in stock valuations this week, the Delta MSI has fallen below the bullish threshold of 50 but remains within the 3% dead-band zone. The Delta MSI is an intermediate term price-based trading signal that is currently indicating risk is elevated. Too many “what ifs” creates volatility.

Give Us a Call Today

We have unique and sophisticated investment methods that seek to capture the stock market’s gains while minimizing drawdowns in bear markets. If you would like to learn more about how we manage money, we invite you to give us a call at **(415) 249-6337**, visit www.deltaim.com or email us at info@deltaim.com.



“The market was volatile.”

Delta Stock Market Dashboard

MARKET SENTIMENT IS

BEARISH

THIS WEEK’S NUMBER IS

47.5

Our technical indicator decreased from 65.8 to 47.5 this week

INDICATOR STATISTICS

Consecutive Bearish Weeks:	1
Cycle Inception Date:	2/27/2020
Range:	NA
Mean:	47.5
Bullish Weeks YTD:	1
Bearish Weeks YTD:	0
*S&P 500	NA%
*DJIA	NA%
*NASDAQ	NA%

* Percentage change during current cycle

Delta Market Sentiment Indicator Over the Past Year



(Delta MSI is published every week in *Barron's*)

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