Corona dislocation and alpha potential

In general, I've tried not to think much about macro over the past few years. I much preferred to think about micro (company specific) ideas. Obviously, Corona has thrown a lot of that into question: for a lot of companies, whether they're investable or not depends on how long the economic shutdown lasts. As an extreme example, if you thought we needed to fully lock the country down for five years in response to Corona (again, an extreme example), every single travel or restaurant related stock would be completely uninvestable because they'd all be bankrupt. In contrast, if you thought the shut down was fully ending this Friday because some miracle cure was coming, every travel or restaurant related stock would be a screaming buy because they are, across the board, discounting months and months of hugely depressed revenues. Again, those are super extreme examples, but sometimes extremes can be useful for highlighting a point!

Anyway, I've spent more time than I'm used to thinking about macro stuff, and the article "I'm struggling here" really spoke to me. It's really hard to look at the market and make sense of it.

On one hand, we're about to post the worth quarter of GDP in history. In a week, we're seeing unemployment numbers that exceed the totality of previous recessions. I know the market is a discounting machine and it's supposed to look through the near term, but it's really hard to look at numbers and an environment that bad and think the stock market (Down ~20% from all time highs) is properly reflecting those numbers.

On the other hand, a 20% decline in stocks is a really, really large drop. If you think fair value for the market is 15x earnings, a 20% decline is roughly the equivalent to the market just saying "earnings will be zero for the next 2-3 years and then return to normal." That's a pretty large drop; even with the economy in shambles for the next few months, the overall market will earn something, and a year from now most companies will be operating at something approaching normalcy and be earning some profit. So you could probably argue that, on the whole, the market has more than accounted for the earnings drop here.

I don't know the right answer, and my guess is that no one really "knows" the right answer. I'm sure people have strong opinions, and fortunes will be made betting one way or the other on those opinions, but at this point I think the market is largely aware of the Corona risks and its probably not possible to have a "Corona macro" edge. If forced to give my personal outlook, I would probably be a moderately bearish in the short term but still think that the current environment presents a good buying opportunity for the market overall and in particular for some individual stocks. I write this fully understanding that that sentence was the most "talking head / market pundit" thing I have ever written, so go ahead and take it with fifteen grains of salt.

I did want to point one thing out: my guess is this is the greatest environment we'll ever see for individual stock picking / alpha generation, and that's pretty exciting as an investor most interested in individual stock picking. My thinking here is simple: historical financials are basically meaningless right now (who cares if a restaurant company earned $5/share last year; all their stores are shut for the next six months and who knows what environment they reopen into). The range of outcomes for the environment we open into is insanely wide (what does everything opening look like? is it just flip a switch and we're back on, or is it 18 months of things are open but no more than 10 people can be in a restaurant at a time?), and when we do open, companies could gain or lose huge swaths of market share very quickly. Good management and businesses are going to have opportunities to create enormous amounts of value (buying out distressed competitors on the cheap, making good operating decisions that let them take share, etc.) or perhaps seriously impair their businesses (opening too early and being branded the company that exposed all their customers; restarting their cost centers too soon and destroying the balance sheet, etc.). And there are plenty of sectors where every company has been sold off roughly equally hard; picking a winner in those sectors could easily yield a multibagger (for example, picking a hotel company who has some type of unique exposure that lets their properties open and fill significantly quicker than their competitors). Having a "corona macro" edge is probably impossible now, but I fully think it's possible (indeed, likely) that there is some "corona micro" edge to be had where you can identify businesses that will inflect one way or the other because of corona where the market hasn't fully discounted it yet. All of those combine to create an environment ripe for good stock selection.... but also an environment that's particularly fraught for investors who aren't actively identifying new risks / the changing landscape / who are relying on stale financials instead of thinking about how the business is rapidly evolving (and yes, I do understand that sentence was pretty talking head / market pundit-y as well).

Perhaps nothing earth-shattering or new here, but it's something I've been thinking about a lot this weekend so I wanted to throw it out there.

The bottom line of this article: things are somewhere between scary to weird out there, but I'm pretty sure that there's never been a value creation / alpha opportunity like the present environment for good managers / businesses / stock analysts. That's a really exciting (and a little scary!) prospect.