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FIRST QUARTER COMMENTARY
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We hope all of our clients, friends and their families are healthy and weathering this crisis safely. These are unprecedented times. We are dealing with a health crisis which is causing severe economic problems. Business activity has declined precipitously and unemployment claims are at record levels. Our staff is working from our homes and we appreciate your patience as we strive to continue to provide the same high level of service. In the coming days you will be receiving a detailed summary of your quarterly results in place of the usual report.

The decline in stocks from their first quarter peak on February 19 was unprecedented. The broad market was up nearly 5% through that date. As more information about the coronavirus became available, the market decline picked up steam and hit its low on March 23 with the S&P 500 down over 30%. For the first quarter, the S&P 500 lost 19.6%. Large cap growth stocks performed best with the Russell 1000 growth index losing 14.1%, while small cap value stocks fared the worst losing 35.7%. In general, growth and large cap stocks lost the least. Foreign stocks lost over 22%.

Hedge funds had mixed results. Credit funds were forced to mark down values to what we believe are artificially low levels because of too few buyers late in the quarter.

Bond returns varied widely. Yields on Treasury securities declined to all-time lows as the Fed cut rates to near zero. Corporate and tax-free bonds had mixed returns as the spread on yields between Treasury securities and other bonds widened considerably. Most non-Treasury bond indices had slightly negative returns. Many high yield bond indices were down more than 10%.

The following are Treasury yields for various maturities:

MATURITY*	12/31/18	12/31/19	3/31/20
3 Month	2.45%	1.55%	0.10%
2 Year	2.50%	1.57%	0.20%
10 Year	2.68%	1.92%	0.68%
30 Year	3.01%	2.39%	1.32%

*Source: Factset

The COVID-19 outbreak triggered a liquidity crisis and extreme volatility in all financial markets. The Dow Jones Industrial Average moved +/- 1,000 points in 22 of the final 31 trading days of the quarter and averaged daily moves of more than 5% in March. Seemingly nonstop and unprecedented Federal Reserve intervention restored some order to the financial system by late March. Passage of the $2.2 trillion “rescue” legislation, hope of a coming virus “peak” in the US / plateau in Europe, and an unclogged financial system all led to a strong market rally the last week of the quarter.

The rally has continued into April as the Fed expanded its unprecedented support for the financial system. In addition, Congress is likely to pass another stimulus package. As of today, the S&P 500 is only 5% below where it was at the beginning of October 2019. In the meantime, millions have lost their jobs, the economy has stopped functioning normally, and people are locked in their homes, unable to socialize normally.

Projections of sickness and death have improved from more dire scenarios, but bad news will be forthcoming for many weeks or longer. In some places, the virus resumed its uptick of illnesses as countries attempted to normalize (Singapore, Hong Kong, Vietnam). Announcements of successful therapies and/or a vaccination will not only trigger short term rallies in financial markets, but may allow people to be more comfortable resuming their normal lives.

While the liquidity crisis appears to be behind us and the public healthcare emergency hopefully nears its peak, the economic fallout has just begun. The past three weeks have seen ~17 million in new unemployment claims. The St. Louis Federal Reserve President James Bullard predicted on March 22 the unemployment rate may hit 30% and annualized GDP may drop 50%. While such extreme forecasts were undoubtedly offered with the hope of getting Congress to pass legislation, they underscore the severity of the situation.

Economic activity will undoubtedly bounce after a sharp detraction in the second quarter, but it is anyone's guess how much damage will have been done in the meantime. Large companies may appear stable by tapping credit lines and furloughing workers, but we do not yet know the state of their customers nor how fast they will bring their workers back. New federal lending programs may be enough to save many small companies, but we do not know how effective they will be. When social distancing ends, will people be comfortable returning to pre-virus behaviors right away? How many visitors will Disney allow, and how many people will be comfortable going? When sports resumes, how many people will be allowed to attend, and how many will want to?

Compared to the 2007-2009 recession, there are many positives to weigh against the doom and gloom. Congress acted far more quickly and decisively than in 2008. The Federal Reserve and US Treasury aggressively intervened, supporting a potpourri of asset classes and financial service companies, effectively removing the risk of a banking crises in the near term. US Treasury interest rates will presumably stay low for the foreseeable future, supporting both equity and bond valuations once normalcy returns. The considerable resources of the US healthcare industry and intellectual horsepower of entrepreneurs give everyone hope. Still, this is a medical crisis, requires a medical solution, and all the actions by the Fed and Congress cannot change that fact.

Sharp market rallies often occur during bear markets. It is possible March 23 marked the low in the market. There is too much uncertainty for anyone to have confidence that we have seen the low for this cycle. We believe volatility will remain very high and, in this environment, we would rather err on the side of caution. Seemingly unlimited support from both Congress and the Federal Reserve gives comfort the current order will remain intact, but no one knows what the financial, economic, political, and institutional costs will be, nor how they will affect future valuations. Corporate earnings and cash flow, key determinants of valuation, are completely unknown for countless companies and cannot be known for some time. The rally in stocks from the bottom feels good, but may not be on solid ground given the high level of "known unknowns" on the other side of the virus' peak.

Having said all of this, we still are confident in the long-term outlook for stocks. This, too, shall pass, and we do not believe we need to make further changes to current portfolios. We have adequate non-stock holdings for clients as appropriate for each individual. Our investment team has been dually focused on how our investment plans and asset allocations should be optimized for what is unquestionably a new investment climate, while also speaking with our managers to see how they are analyzing their holdings given this new reality.

Our best wishes for good health and better days ahead! Happy Holidays!

The Portfolio Strategy Group

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