Smith Group
ASSET MANAGEMENT

MARKET PERSPECTIVES

MARCH 27, 2020

Equity Market Summary

U.S. Equity Markets	Feb 19-Mar 26	YTD	Top/Bottom Sectors	Feb 19-Mar 26	YTD	Non-US Equity Markets (in USD)	Feb 19-Mar 26	YTD	Non-US Regions (in USD)	Feb 19-Mar 26	YTD
S&P 500	-22.2%	-18.2%	Technology	-19.5%	-9.7%	MSCI AC World Ex U.S.	-23.3%	-23.4%	Developed Americas	-28.9%	-26.6%
Russell 1000 Growth	-20.1%	-12.7%	Utilities	-20.4%	-13.5%	MSCI EAFE (Developed)	-22.6%	-23.0%	Developed Asia	-19.9%	-21.9%
Russell 1000 Value	-26.1%	-25.2%	Cons. Staples	-15.9%	-13.8%	MSCI Emerging Markets	-22.9%	-23.4%	Developed Europe	-23.7%	-23.5%
Russell 2000	-30.1%	-29.0%	Materials	-23.6%	-24.7%	MSCI China	-12.5%	-10.5%	Emerging Americas	-38.9%	-41.7%
Russell 2000 Growth	-27.9%	-24.3%	Financials	-29.7%	-28.9%	MSCI Japan	-15.5%	-18.9%	Emerging Asia	-19.0%	-18.8%
Russell 2000 Value	-32.6%	-34.0%	Energy	-43.0%	-48.0%	MSCI Italy	-29.9%	-27.4%	Emerging EMEA	-29.0%	-31.7%

What's changed since our last report (on Mar. 20, 2020):

- Coronavirus (CV-19) continues to spread rapidly around the globe with cases doubling and deaths doubling and the U.S. now reporting more cases than any other country. International borders remain closed and much of the Northern Hemisphere is in some form of government mandated or self-imposed quarantine. Financial markets continue to swing wildly although equity markets bounced significantly over the past several trading days.

Where are we now:

- CV-19: more than 550,000 cases and 25,000 deaths. Reported cases in most all United Nations recognized countries. China is experiencing a modest echo bounce but are only averaging double digit new cases per day and in South Korea new cases are on average rising by only 1% per day.

Economy:

- It's pretty clear the global economy entered recession in late February or early March.
- Jobless claims rose by a record 3.3 million this week exceeding the record of nearly 700,000 set in 1982. Look for this number to continue to rise as there are 17 million hotel and leisure workers in the U.S., a significant portion of whom have already been furloughed.
- Policy makers have four primary policy levers they can pull to stimulate (or slow) an economy: Monetary ; Tax/Spending; Regulatory and Trade. Thus far U.S. policy makers have pulled out the bazooka on the first two and relief on the last two could be on the way. The size and speed of the policy response to this crisis is un-precedented. While it would be naïve to say the chance of a Depression is zero; the policy response to this crisis stands in stark contrast to the policy errors post 1929 in which every possible wrong move was made.

Financial Markets:

- U.S. equity markets are coming off of a historic 3-day rally of 19.8% from the lows of Monday, Mar. 23. Prior to the rally the S&P 500 had declined 33.8% from the Feb. 19 high. The rally has been led by a 29% rise in Energy stocks and a 71% jump in the shares of Boeing.
- The Fed's balance sheet is now greater than $5 trillion and the impact on the credit markets is being felt as credit spreads have compressed over the past week. The $500 billion pool of commercial mortgage backed securities may be the best place to look for the next signs of stress.
- China equity markets continue to be among the top performing markets having fallen only half as much as global equity markets during the market sell-off and down only 10.5% year-to-date.

Earnings:

- Earnings expectations continue to be very slow to react as year-over-year earnings are still forecast to increase. To date we count approximately 5% of mid and large cap U.S. companies as having withdrawn 2020 earnings guidance.
- Over the past week 22 of 24 Industry Groups in the S&P 500 have seen more earnings downgrades than upgrades as analysts are dropping estimates at a nearly 4 to 1 ratio. Food & Staples Retailing and Household & Personal Products are the only two industry groups with net upgrades to earnings expectations.
- Reporting season is only a couple of weeks away so management and analysts may be delaying guidance and revisions until that time.

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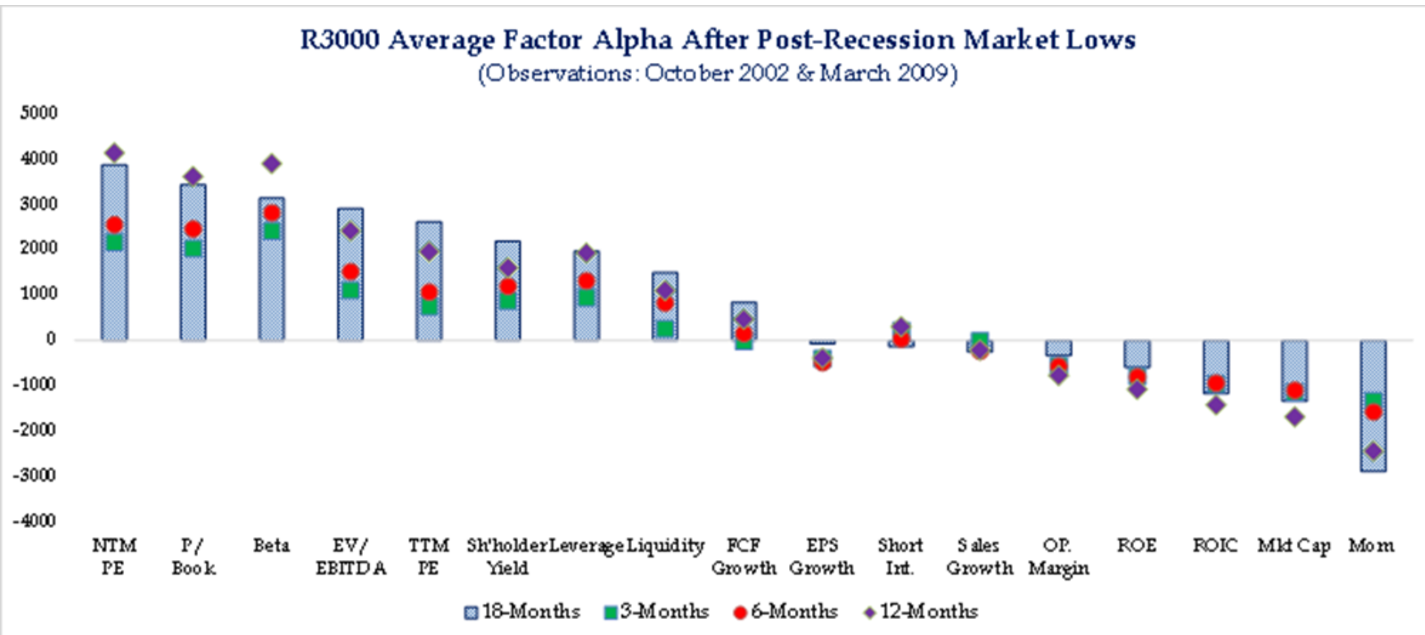
Summary:

The human costs of CV-19 continue to mount at a staggering pace and the global healthcare system is being stressed in ways that even the most aggressive of plans would have likely not forecast. The monetary and fiscal response to the crisis has been swift and staggering in its proportion but is also likely to prove to be not enough and further action will be required. Fiscal policy at this time is targeted to replace the fall off in private sector demand with public sector dollars. We continue to believe it will likely be a matter of months not weeks before the global economy begins to stabilize, but financial markets are always forward looking and are already beginning to look across the valley to what companies and industries rebound the most quickly and benefit the most from policy actions. The clear and direct beneficiaries of the first round of stimulus are hospitals, life sciences tools, restaurants, financial sector, airlines and many more. It is likely these groups will lead the markets in the initial phases of the recovery but portfolio decisions need to be balanced against what will be the long-term price to shareholders from dilutions or limitations on capital allocations that may be required if government aid is accepted.



Source: Strategas Research Partners

Where to Invest Off Market Lows

Strategas Research Partners published the above chart to look at the investment factors that drive stock returns off market bottoms. Off the market lows of Mar. 9, 2009, bank stocks rallied 125% thru year end, but then went on to underperform for an extended period. The same was true for technology stocks following the market lows of 2002, a strong bounce off the bottom then an extended period of underperformance. But the bounce off the bottom can be dramatic and powerful and if a portfolio is not correctly positioned to capture the risk factors and industries that bounce then significant return can be sacrificed. At this time, Smith Group is looking to remain as neutral as possible to significant risk factors such as beta and momentum in order to be well positioned for a market bounce or further market sell-off. While at the same time continuing to invest in businesses with high quality earnings streams that we believe are well positioned to exceed growth expectations over the long-term.

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