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STRATEGAS
insight
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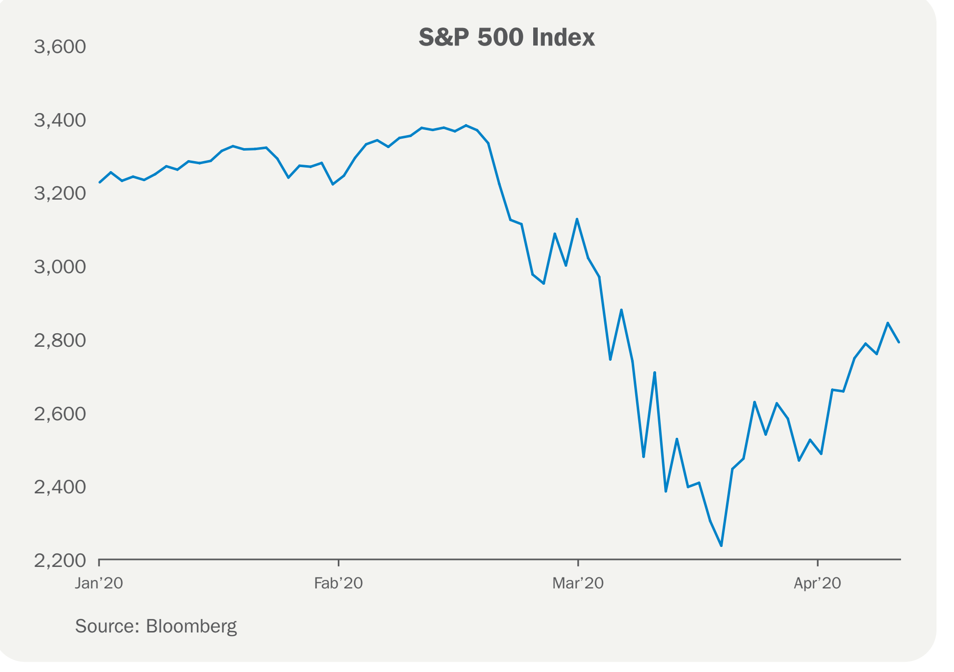
Vigilance and the Journey Ahead

The intersection of crisis and the human experience is fascinating. In isolation—*one person, one crisis*—a circumstance beyond our control can present seemingly insurmountable odds; lives are defined by these experiences. When universally experienced—*as with the current global health pandemic*—this intersection can reveal (and remind us of) the power collective energies and community spirit can have in overcoming any obstacle; generations are defined by such episodes. Although the nightly news has been peppered with the heroism of our frontline responders and the unselfish acts of our neighbors, we must acknowledge the difficulty so many of our friends will have (and already have had) in adjusting to the severity of changes in our social and economic norms. We are wise to remember that within the universal crisis are millions of crises felt in isolation. Without dismissing the real human health tragedy that the pandemic has wrought, the societal and economic costs of the cure have not yet been tabulated. Unfortunately, they are likely to be steep. In this, the growing divergence between the social and economic costs, on the one hand, and the capital markets, on the other, has become notable… and worrisome.

Investors seem to have latched on to modest gains and incremental improvements on the health front (i.e. flattening the curve and lowered worst-case projections) to drive shares off their late-March lows. If our recent conversations with clients are any guide,



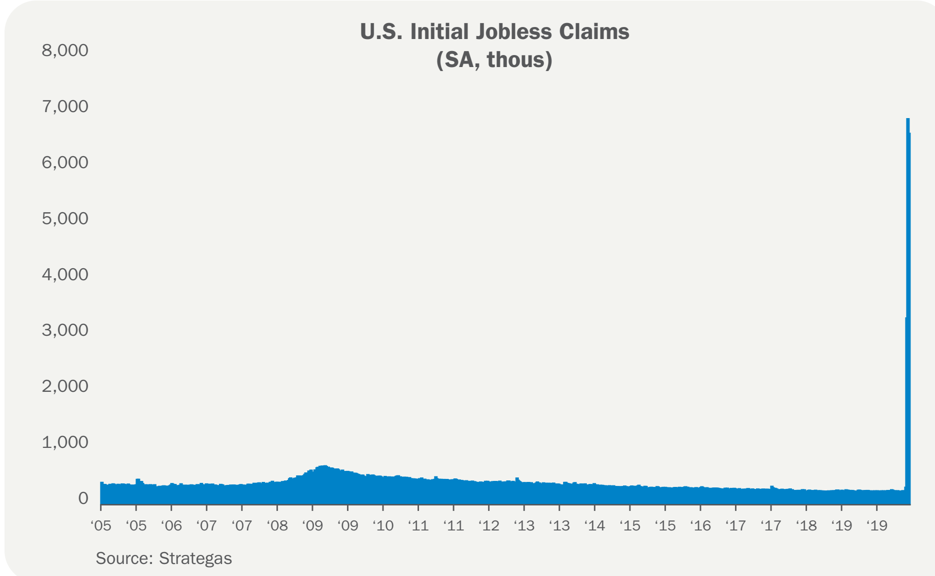
Source: Bloomberg

market psyche has quickly shifted from a pronounced concern about the potential for a new Depression to a general confidence in the durability of the recent price move.

The bedrock of this move is not formed on the improved human health outlook alone, but also by the timely and unprecedented action taken by policymakers—*both monetary and fiscal*—to backstop the economy. The combination appears to have moved the consensus to dismiss quickly the worst of 2020 and embrace the potential for the very best in 2021. That is what we all want, but want and hope are not, in our view, the right starting point. If the facts deliver the desired outcome, terrific. The potential for a "V-day" moment always remains, but this has, thus far, been absent.

We continue to circle the same set of prerequisites we laid out roughly a month ago. Principal among these, of course, is the containment and cure of the virus. As we have seen, seven hopeful signs of improvement on this front will move the market. But although containment—*i.e., the flattening of the metro-area curves, particularly in and around New York City*—has been welcomed relief, it is not one size fits all. Other important metro areas, lest we forget, are just beginning to see the impact of the virus manifest. And although a cure—*i.e. the development of therapeutics*—could serve as violent upside catalyst, the timetable appears hopeful, approximate, and long-dated. By our lights, the burden of proof rests on four critical pieces of information: first, a measure of the trough level of activity resulting from mandating the global economy to a subsistence crawl; second, a timeline for "reopening" the economy; third, an estimate of the normalized forward demand curve (i.e., V, U, W, L, etc.) when we do; and fourth, a growth catalyst.

The consensus among investors seems pinned to the notion that the recovery in economic activity will be more "U-shaped," despite health professionals' concern that a second wave of the virus could break out later in the year should we relax social distancing too quickly. This would seem, at a minimum, to support greater consideration for either a "W-shaped" or "square root-shaped" outcome. This tension between the safest course, as defined by health protocols, and the desired course, as defined by economic considerations—which may not be mutually exclusive given the balance of risks—makes an understanding of the reopening timeline critical. Consider that although the Federal Reserve (in partnership with the Treasury) appears to have achieved its desired outcome—*ensuring investors of adequate liquidity and the continued orderly function of the capital markets*—the fiscal policy initiatives prescribed by Congress and signed by the President represent neither a full reimbursement of furloughed economic activity nor remain available indefinitely. It stands to reason that if the Administration and Congress find the need to go back to the well, the more frequently they do, the softer the slope of the recovery.



Given the strength of the crisis's global grip and the abrupt nature of its associated declines, most portfolios did not play through the traditional, increasingly defensive, prerecession sequence, and remained positioned for continued late-cycle economic reacceleration and a market driven by flows (as opposed to fundamentals). We believe portfolio repositioning following the recent decline (and retracement) should start from an assessment of terminal activity. If, for example, investors subscribe to the notion that economic activity will return to normal more quickly, then their portfolio adjustments might focus on the assets, industries, and companies that sold off the hardest, because the discount is likely steepest and the prospects for outperformance the highest. That said, this "trade" would exhaust most likely (and may have already). If, however, investors subscribe to the thesis that the timing and pace of a recovery remain unknown and, more likely than not, longer than the consensus expects, it would seem prudent to embrace disaggregated pockets of strength against risk-adjusted time horizons. We believe this likely will result in greater dispersion between winners and losers in the longer term (12+ months) and an erosion of the passive asset stack in favor of greater allocation to actively managed strategies.

Strategas Recommended Asset Allocation (Apr'20)

	Equities	Bonds
Overweight	Dev AC Core EM AC Core	IG Corporates TIPS
Neutral	US LC Value US LC Core US LC Growth US MC Value US MC Core US MC Growth US SC Core	Agencies ABS/CMBS US Dollar EMD Local EMD High Yield Convertibles Bank Loans
Underweight		US MBS U.S. Treasuries

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Index Overview & Key Definitions
Fed, The Fed or FED refers to the Federal Reserve System, the central bank of the United States. **Fed Funds Rate**, the interest rate at which a depository institution lends funds maintained at the Federal Reserve to another depository institution overnight. The **Gross Domestic Product (GDP)** rate is a measurement of the output of goods and services produced by labor and property located in the United States. **Real Gross Domestic Product (GDP)** is an inflation-adjusted measure that reflects the value of all goods and services produced by an economy in a given year. **Nominal Gross Domestic Product** is gross domestic product (GDP) evaluated at current market prices. The **S&P 500 Index** is an unmanaged index comprised of 500 widely held securities considered to be representative of the stock market in general. The **Russell 1000 Index** is a market capitalization weighted benchmark index made up of the 1000 largest U.S. companies in the Russell 3000 Index. The **Russell 2000 Index** is an unmanaged index considered representative of small-cap stocks. The **PCE (Personal Consumption Expenditure) Index** of Prices is a US-wide indicator of the average increase in prices for all domestic personal consumption. Using a variety of data including U.S. Consumer Price Index and Producer Price Index prices, it is derived from personal consumption expenditures; essentially a measure of goods and services targeted towards individuals and consumed by individuals. The **Producer Price Index (PPI)** program measures the average change over time in the selling prices received by domestic producers for their output. The prices included in the PPI are from the first commercial transaction for many products and some services. **FAANG** is an acronym for the five of the market's most popular tech stocks, namely Facebook, Apple, Amazon, Netflix and Alphabet's Google. The **North American Free Trade Agreement (NAFTA)** is an agreement signed by Canada, Mexico, and the United States, creating a trilateral trade bloc in North America. The **Seasonally Adjusted Annual Rate (SAAR)** is a rate that is adjusted to take into account typical seasonal fluctuations in data and is expressed as an annual total. SAARs are used for data affected by seasonality, when it could be misleading to directly compare different times of the year. The **Atlanta Fed GDPNow** forecasting model provides a "nowcast" of the official estimate prior to its release by estimating GDP growth using a methodology similar to the one used by the U.S. Bureau of Economic Analysis. GDPNow is not an official forecast of the Atlanta Fed. Rather, it is best viewed as a running estimate of real GDP growth based on available data for the current measured quarter.

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