IM&R Economic and Market Review Q1 2020

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Economic Review

The economy has come to an abrupt halt as much of the labor force has been required to shelter-in-place due to the impact of the spreading coronavirus. First quarter GDP is estimated to come in at 2.2% according to the latest Atlanta Fed GDPNow report, but all eyes are to the second quarter when GDP is expected to decline by 15-25% or more according to economists. The key questions are how long the virus will last and when will workers return to the job.

With a combined hit of both demand and supply side shock to the economy, a recession is expected ensue with a spiraling unemployment rate reaching well into the double digits. It is anticipated that the impact of the sharp downturn will be lessened and shortened with the help of unprecedented stimulus measures from both the Federal Reserve and Congress. If unemployment time averages under 6 months, the economy could return to prior spending levels within 12-18 months according to JPMorgan Chase Institute data.

A deluge of shocking economic data is forthcoming. Business activity contracted markedly in March with the IHS U.S. Markit PMI Report showing output dropping at the fastest rate in over a decade. The service sector has been especially affected, with consumer-facing industries such as restaurants, bars and hotels bearing the brunt of the social distancing measures, while travel and tourism has been decimated. Firms reduced their payrolls and capital expenditures expectations crumbled as business investment plans were scrapped across the U.S. Looking ahead, companies were generally optimistic that business activity would increase over the coming year. However, the degree of business confidence was by far the lowest ever recorded by the survey, as firms expressed concerns regarding the longevity of shutdowns and the ongoing impact of the coronavirus outbreak.

Consumer confidence plunged with the fourth largest one-month decline in almost a half century according to the March University of Michigan Survey of Consumers. The extent of additional declines in April will depend on the success in curtailing the spread of the virus and how quickly households receive funds to relieve their financial hardships. To avoid an extended recession, economic policies must quickly adapt to a new era that will reorder spending and saving priorities of consumers.

Financial Markets Review: Domestic Stock Market

With economic activity deliberately halted, U.S. equity markets fell from a mid-February all-time high to the worst quarter since the great recession. The impacts of the COVID-19 pandemic ripped through the markets resulting in the fastest correction in history, as the S&P 500 plunged 33.92% before recovering to end the quarter down 20.00%, to 2,584.59. Likewise, the Dow Jones Industrial Average finished down 23.20% to 21,917.16 and the Nasdaq composite fell 14.18% to 7,700.10.

All 11 S&P sectors were smashed in the quarter as there was nowhere to hide. The smallest losses were found in utilities (-9.88%), health care (-12.33%) and real estate sectors (-16.54%). The most dismal performing sectors were energy (-50.92%), financials (-29.62%), and industrials (-26.09%).

Growth stocks trounced value holdings for the quarter in both the large cap and small cap space with small caps hit particularly hard. Growth has considerably outperformed value over the past 1, 3, 5 and 10 years.

The best performing S&P 500 industries for the quarter were internet and catalog retail (+0.12%) software (-2.43%) and biotechnology (-2.60%). The poorest performing industries included energy and equipment services (-65.63%), airlines (-50.34%), and oil & gas (-48.75%).

The only holding in the Dow Jones Industrials Average that managed a positive return for the first quarter was Microsoft, gaining 0.33%. Rounding out the top three were Walmart down -3.94% and Intel slipping -9.02%. Stocks cratering the most were Boeing, falling -53.59%, Dow Inc. dropping -45.30% and Exxon declining -44.34%.

The election campaign has taken a back seat to the coronavirus, but will be ramping back up over the next quarter as the shutdown begins to abate.

While we absorb the current onslaught of damaging economic news, we remind investors that the markets are always forward looking. We recommend that investors stay calm, focus on their long-term goals and not let emotions get the best of them. Even though we expect a sobering number of new cases and deaths from the pandemic, mitigation efforts at the city, county, state, and national levels, rapid acceleration of vaccine testing and possible treatments, and our collective behavior will quicken the time until America returns to work. We believe that the markets will move in advance of these developments and will recover substantially in the coming quarters.

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	Total Returns* (03/31/20)			Annualized Returns (03/31/20)		
Category/Style	**1st Quarter**	**Year-to-Date**	**One Year**	**Three Years**	**Five Years**	**Ten Years**
S&P 500	-19.60	-19.60	-6.98	5.10	6.73	10.53
S&P Midcap 400	-29.70	-29.70	-22.89	-4.09	0.56	7.88
S&P Small Cap 600	-32.64	-32.64	-25.89	-5.34	0.45	8.06
Russell 1000 Large Cap Growth	-14.10	-14.10	0.91	11.32	10.36	12.97
Russell 1000 Large Cap Value	-26.73	-26.73	-17.17	-2.18	1.90	7.67
Russell 2000 Small Cap Growth	-25.76	-25.76	-18.58	0.10	1.70	8.89
Russell 2000 Small Cap Value	-35.66	-35.66	-29.64	-9.51	-2.42	4.79

Source: Standard and Poor's, Frank Russell Company * returns include reinvested dividends

International Stock Markets

The global spread of coronavirus has led to the greatest downturn since the great recession. With the oil market crash and the coronavirus-induced global recession, world economies have suffered a sharp contraction in business activity. Tighter financial conditions and weaker global demand for commodities have severely hurt emerging market economies. On monetary policy, nearly all central banks have assessed the increased liquidity risks and delivered rate cuts along with quantitative easing measures. Still, we expect a sharp contraction in second quarter activity. The European region will probably experience a sharp and deep recession as domestic activity, global trade and supply chains face massive disruption. After a contraction in the first quarter, China's economy is beginning to recover. The question is how rapidly?

Looking to the markets, the MSCI EAFE Index of developed markets plunged -22.83% for the first quarter. Emerging markets worsened as the MSCI Emerging Markets Index dropped -23.60%, and the MSCI Frontier Markets Index plummeted -26.59%. In the Eurozone stock markets, the Euro Stoxx Index fell -24.94% for the quarter to 303.18. Among key Euro members, France's CAC-40 Index slid -26.46% (in local currency) to 4,396.12 and Germany's DAX Index sank -25.01% to 9,935.84. The United Kingdom's London FTSE 100 deteriorated -24.80% to 5,671.96 and UK Prime Minister Boris Johnson contracted COVID-19.

Asia-Pacific markets moved significantly lower in the first quarter. In developed markets, Japan's Nikkei stock index dove -20.03% to 18,917.01. In emerging markets, the China Shanghai Composite Index's drop to 2,750.30 for a -9.82% loss was a rising sun compared to all other countries. India's S&P BSE Sensex Index cratered 28.66% to 29,468.49.

The flight to the security of the U.S. dollar was reflected in a 4.59% rise against world currencies in the first quarter according to the WSJ Dollar Index. The dollar fell, however, 1.13% against the yen to 107.53 (JPY/USD). The dollar was 1.60% higher versus the euro at $1.1034 (USD/EUR).

World Bond Markets

The Fed's dramatic liquidity measures have once again brought rates to the zero bound. The yield curve widened in the first quarter with the 10-year/3-month Treasury spread at 0.59 basis points. The U.S. 10-year note yield crashed from 1.91% at year end to 0.70% and the 3-month yield stood at 0.11% from 1.56% a quarter earlier. As a result of the yield drop, bond prices proved to be a safe haven and the Barclays U.S. Aggregate Bond Index jumped 3.15% for the quarter. Reflecting the burden on state and local governments, the Barclays Municipal Index slipped 0.63%. The Barclays U.S. Treasury TIPS Index returned 1.69%. Money market yields were 0.46% and falling quickly at quarter end according to the Crane 100 Money Fund Index.

According to Value Line, yields on Japanese government bonds moved ever so slightly into positive territory at the end of the first quarter with the 10-year bond at 0.05%. Yields on German government bonds, on the other hand, moved further below zero from -0.24% at the end of the fourth quarter to -0.36% on the 10-year bond. Yields on United Kingdom 10-year government bonds were at 0.45% and Canadian 10-year government bonds were at 0.83% at quarter end.

Commodities

Commodities as a group crashed in the first quarter as global demand dried up. The DJ commodity index lost -27.15% to close at 467.93.

The oil war between Russia and Saudi Araba, and quarantine measures restricting business activity in most economies have led to the biggest decline of oil demand in history, with prices hitting an 18-year low and closing the quarter at $20.48/barrel, crashing -66.45% for the quarter. Analysts anticipate oil prices returning into the $40 range as business activity resumes.

Gold continued to shine, providing a defensive hedge and rising 4.21% to $15,583.40.

Mutual Funds/Exchange-Traded Funds

The explosion in passive investing has led to concerns of the impact the growing ETF market would have in a financial crisis. In the current environment these funds have demonstrated no significant dislocations to pricing as a result of large volume trading similar to past crises.

MUTUAL FUNDS OVERVIEW AS OF MARCH 31, 2020

	Total Returns		Annualized Returns			
Category	**1st Quarter**	**Year-to-Date**	**One Year**	**Three Years**	**Five Years**	**Ten Years**
Municipal Bond Interim-Term	-1.50	-1.50	2.49	3.00	2.37	3.16
Short-Term Taxable Bond	-2.14	-2.14	0.63	1.42	1.27	1.64
Interm.-Term Taxable Bond	1.54	1.54	6.65	3.97	2.87	3.73
Long-Term Taxable Bond	-0.67	-0.67	10.92	6.80	4.48	6.47
High Yield Bond	-12.60	-12.60	-7.56	-0.20	1.56	4.43
World Bond	-5.09	-5.09	-1.29	1.44	1.33	2.14
Small-Cap Blend	-32.48	-32.48	-26.55	-7.04	-2.08	5.50
Mid-Cap Blend	-28.42	-28.42	-20.94	-3.87	-0.59	6.31
Large-Cap Blend	-20.85	-20.85	-9.85	2.89	4.30	8.36
World Large Stock	-21.02	-21.02	-11.73	1.10	2.35	5.65
Foreign Large Blend	-23.32	-23.32	-15.54	-2.56	-1.17	2.18
Natural Resources	-33.55	-33.55	-31.60	-11.40	-7.03	-3.81
Real Estate	-26.41	-26.41	-19.30	-2.83	-0.62	6.78

Source: Morningstar Category Returns, Morningstar, Inc.

Important Definitions and Disclosures

The opinions and material presented are provided for informational purposes only. No person or system can predict the market. This material includes forward-looking statements that are subject to certain risks and uncertainties. Actual results, performance or achievements may differ materially from those expressed or implied. No predictions or forecasts can be guaranteed. Companies mentioned are for informational purposes only. It should not be considered a solicitation for the purchase or sale of the securities. Any investment should be consistent with your objectives, time frame and risk tolerance. Neither asset allocation nor diversification guarantee a profit or protect against a loss. All investments are subject to risk, including the risk of principal loss. There is no assurance that the investment goals and process described herein will consistently lead to successful investing. The investment return and principal value of an investment will fluctuate, and an investor's shares, when redeemed, may be worth more or less than their original cost. Funds that invest in stocks of small-cap or mid-cap companies involve additional risks. The securities of these companies may be more volatile and less liquid than the securities of larger companies. Funds that invest in international securities involve special additional risks. These risks include, but are not limited to, currency risk, political risk, and risk associated with varying accounting standards. Investment in emerging markets may accentuate these risks. Alternative strategies, including those used in mutual funds, have risks that may substantially increase the potential for loss. Bonds are subject to interest rate risk. Bonds have interest rate risk and credit risk. As interest rates rise, existing bond prices fall and can cause the value of an investment to decline. Changes in interest rates generally have a greater effect on bonds with longer maturities than on those with shorter maturities. Funds that hold bonds are subject to declines and increases in value due to general changes in interest rates. Credit risk refers to the possibility that the issuer of the bond will not be able to make principal and/or interest payments.

The information shown does not constitute investment advice and does not consider the investment objectives, risk tolerance or financial circumstances of any specific investor. The information provided is not intended to be a complete analysis of every material fact with respect to any portfolio, security, or strategy and has been presented for educational purposes only. Data obtained from the sources cited is believed to be reliable and accurate at the time of compilation. Nothing contained herein should be construed as a recommendation to buy or sell any individual securities. It should not be assumed that an investment in any of the securities identified was or will be profitable.

The Bureau of Economic Analysis (BEA) of the United States Department of Commerce is a U.S. government agency that provides official macroeconomic and industry statistics, most notably reports about the gross domestic product (GDP) of the United States and its various units such as states, cities, towns, townships, and villages. **Gross Domestic Product** (GDP) is a measure of output from U.S factories and related consumption in the United States. It does not include products made by U.S. companies in foreign markets. **Real Gross Domestic Product** (real GDP) is a macroeconomic measure of the value of economic output adjusted for price changes (i.e., inflation or deflation). The **Atlanta Fed GDPNow** estimate is a model-based projection not subject to judgmental adjustments. It is not an official forecast of the Atlanta Fed, its president, the Federal Reserve System, or the Federal Open Market Committee. **Purchasing Managers' Index™ (PMI™)** is a survey-based economic indicator designed to provide a timely insight into business conditions. **The Conference Board Leading Economic Index® (LEI)** for the U.S. are the key elements in an analytic system designed to signal peaks and troughs in the business cycle. The leading, coincident, and lagging economic indexes are essentially composite averages of several individual leading, coincident, or lagging indicators. They are constructed to summarize and reveal common turning point patterns in economic data in a clearer and more convincing manner than any individual component – primarily because they smooth out some of the volatility of individual components. **Personal Consumption Expenditures** (PCE) is a measure of price changes in consumer goods and services and consist of the actual and imputed expenditures of households; the measure includes data pertaining to durables, non-durables and services. The **ISM Manufacturing Index** is based on surveys of more than 300 manufacturing firms by the Institute for Supply Management (ISM). The ISM Manufacturing Index monitors employment, production, inventories, new orders and supplier deliveries. A composite diffusion index monitors conditions in national manufacturing and is based on the data from these surveys. The **Federal Reserve System** (also known as the Federal Reserve, and informally as the Fed) is the central banking system of the United States. The Federal Reserve System is composed of 12 regional Reserve banks which supervise state member banks. The Federal Reserve System controls the Federal Funds Rate (aka Fed Rate), an important benchmark in financial markets used to influence the supply of money in the U.S. economy. The **Federal Open Market Committee** (FOMC), a committee within the Federal Reserve System is charged under United States law with overseeing the nation's open market operations (i.e., the Fed's buying and selling of United States Treasury securities). The **unemployment rate** percentage of total workforce who are unemployed and are looking for a paid job. Unemployment rate is one of the most closely watched statistics because a rising rate is seen as a sign of weakening economy that may call for cut in interest rate. A falling rate, similarly, indicates a growing economy which is usually accompanied by higher inflation rate and may call for increase in interest rates. Labor force participation rate is the percentage of working age population that is part of the labor force. It is a measure of what proportion of a country's population is employed or actively looking for employment. The index of leading economic indicators is intended to predict future economic activity. Typically, three consecutive monthly LEI changes in the same direction suggest a turning point in the economy. **Inflation** is the rise in the prices of goods and services, as happens when spending increases relative to the supply of goods on the market. Moderate inflation is a common result of economic growth. Hyperinflation, with prices rising at 100% a year or more, causes people to lose confidence in the currency and put their assets in hard assets like real estate or gold, which usually retain their value in inflationary times. **Treasury Yield Curve** is a line that plots the interest rates, at a set point in time, of bonds having equal credit quality, but differing maturity dates. The most frequently reported yield curve compares the three-month, two-year, five-year and 30-year U.S. Treasury debt. **The Michigan Consumer Sentiment Index** was created in the 1940s is conducted by the Survey Research Center and consists of at least 500 telephone interviews posed to a different cross-section of consumers in the continental U.S. each month. The survey questions consumers on their views of their own personal finances, as well as the short-term and long-term state of the U.S. economy. The **International Monetary Fund (IMF)** is an international organization that was initiated in 1944 at the Bretton Woods Conference and formally created in 1945 by 29 member countries. Each survey contains approximately 50 core questions, and each respondent is contacted again for another survey six months after completing the first one. The answers to these questions form the basis of the index. An **exchange-traded fund (ETF)** is a security that tracks an index, a commodity or a basket of assets like an index fund, but trades like a stock on an exchange. Indexes are unmanaged and investors cannot invest directly in an index.

Morningstar Category Returns are composed of the average return for the funds in each Morningstar category over the indicated time period. Categories are defined by Morningstar based on holdings statistics. The category returns are adjusted for survivorship bias, meaning they include all investments even if liquidated, merged or otherwise now obsolete. The returns also include funds that were in a given Morningstar category, but have since changed to another category.

Benchmark Definitions

The **S&P 500 Index** is an index of 500 of the largest exchange-traded stocks in the U.S. from a broad range of industries whose collective performance mirrors the overall stock market. The **Dow Jones Industrial Average** is a widely watched index of 30 American stocks thought to represent the pulse of the American economy and markets. The **NASDAQ** is an index that tracks the cumulative results on a market capitalization basis of all stocks trading in the NASDAQ system. An investment concentrated in sectors and industries may involve greater risk and volatility than a more diversified investment. The **S&P Small Cap 600 Index** (S&P600) covers roughly the small-cap range of U.S. stocks, using a capitalization-weighted index. The index covers roughly three percent of the total U.S. Stock market. The **S&P Midcap 400 Index** (S&P400) is a stock market index from S&P Dow Jones Indices. The index serves as a barometer for the U.S. mid-cap equities sector and is the most widely followed mid-cap index in existence. To be included in the index, a stock must have a total market capitalization that ranges from roughly $750 million to $3.3 billion. The **Russell 1000 Index** is a capitalization-weighted price-only index, which is comprised of 1000 of the largest capitalized U.S.-domiciled companies whose common stock trade in the United States on the New York Stock Exchange, American Stock Exchange and NASDAQ which are included in the Russell 3000 Index. This large cap market-oriented Index is highly correlated with the S&P 500 Index. **Russell 2000 Index** is a market-value-weighted index representing the 2,000 smallest companies in the Russell 3000 index, representative of the U.S. small capitalization securities market. **NAREIT Equity Index** is comprised of real estate investment trusts which own or have an equity interest in rental real estate (rather than making loans secured by real estate collateral). REITs involve risk, including the loss of principal and the possible lack of liquidity. **Morgan Stanley Capital International** (MSCI) All Country World Index (ACWI) is a market capitalization weighted index designed to provide a broad measure of equity-market performance throughout the world. **MSCI EAFE Index** is a market capitalization-weighted index of the leading stocks in Europe, Australasia and Far East. Membership of the index is selected by MSCI and designed for leading stocks roughly to match market sector weights. The **MSCI Emerging Markets Index** is an index created by Morgan Stanley Capital International (MSCI) that is designed to measure equity market performance in global emerging markets. It is a float-adjusted market capitalization index that consists of indices in 21 emerging economies: Brazil, Chile, China, Colombia, Czech Republic, Egypt, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Russia, South Africa, Taiwan, Thailand, and Turkey. The **MSCI Frontier Markets Index** provides broad representation of the equity opportunity set while taking investability requirements into consideration within each market. MSCI classifies 34 countries as Frontier Markets, 26 of which are included in the MSCI Frontier Markets Index. The **STOXX Europe 600 Index** is derived from the STOXX Europe Total Market Index (TMI) and is a subset of the STOXX Global 1800 Index. The **CAC 40 Index** is a benchmark French stock market index. The index represents a capitalization-weighted measure of the 40 most significant values among the 100 highest market caps on the Paris Bourse (now Euronext Paris). The **DAX Index** is a blue chip stock market index consisting of the 30 major German companies trading on the Frankfurt Stock Exchange. The **FTSE 100** is a share index of the 100 companies listed on the London Stock Exchange with the highest market capitalization. The **DJ Asia-Pacific Index** represents the leading stocks by dividend yield traded in the Asia/Pacific region. The **Nikkei Index** is a stock market index for the Tokyo Stock Exchange (TSE). The **Shanghai Composite Index** is a stock market index of all stocks (A shares and B shares) that are traded at the Shanghai Stock Exchange. **S&P BSE Sensex index**, is the benchmark index of the Bombay Stock Exchange (BSE). It is composed of 30 of the largest and most actively-traded stocks on the BSE, providing an accurate gauge of India's economy. The **S&P Global BMI (Broad Market Index)** comprises the S&P Developed BMI and S&P Emerging BMI, is a comprehensive, rules-based index measuring global stock market performance. **Barclays Aggregate Bond Index** is made up of the Lehman Brothers Government/Corporate Bond Index, Mortgage-Backed Securities Index, and Asset-Based Securities Index, including securities that are of investment grade quality or better, have at least one year to maturity, and have an outstanding par value of at least $100 million. The **Barclays Municipal Bond Index** is a market value weighted index of investment grade municipal bonds with maturities of one year or more. The **Barclays Capital U.S. Government Inflation-Linked Bond Index** (U.S. TIPS) measures the performance of the TIPS market. TIPS form the largest component of the Barclays Capital Global Inflation-Linked Bond Index. Inflation-linked indices include only capital indexed bonds with a remaining maturity of one year or more. Treasury notes (T-notes) are intermediate securities with maturities of 1 to 10 years. Denominations range from $1000 to $1 million or more. The notes are sold by cash subscriptions, in exchange for outstanding or maturing government issues, or at auction. The **Crane 100 Money Fund Index** measures the average yield of the 100 largest taxable money market funds. **Barclays Capital Global Aggregate ex-U.S. Index** measures the performance of the global bond market, excluding U.S. securities. **The Dow Jones Commodity Index**℠ is a broadly diversified index that allows investors to track commodity futures through a single, simple measure. The index is designed to minimize concentration in any one commodity or sector. Due to market fluctuation, the commodities represented by this index may experience loss of invested principal and are subject to investment risk.