

Investment
Update

April, 2020

2020 First Quarter Update

Review: The S&P had started the year in positive territory before the impact of the coronavirus (COVID-19) pandemic took hold, resulting in a 19.6% decline for the quarter. In addition to a variety of programs intended to stabilize financial markets, the Federal Reserve stepped in with two emergency cuts to the Fed Funds Rate totaling 1.5%. As a result of these cuts and the flight to safety, US Treasury yields declined dramatically, resulting in a positive return for the Barclays Aggregate Index in the quarter.

Period	1Q20	4Q19	2019
S&P 500	-19.6%	9.1%	31.5%
MSCI EAFE ^{1,2}	-22.7%	8.2%	22.7%
MSCI Emerging Markets ²	-23.6%	11.9%	18.9%
Barclays U.S. Aggregate Bond	3.1%	0.2%	8.7%
Barclays Municipal Bond	-0.6%	0.7%	7.5%

¹ Europe, Australia, Far East

² MSCI returns are in U.S. Dollars

Increased Uncertainty Calls for Risk Management not Risk Avoidance

These are extraordinarily unusual times, as a global health crisis has caused major portions of the economy to shut down, leading to a significant amount of uncertainty. However, it is important to remember that there is always some amount of uncertainty in the market that requires investors to manage risk. Just in the last year and a half prior to the COVID-19 outbreak, investors have had to manage through US-China trade tension, *increases* in the Fed Funds Rate, and Brexit just to name a few. Although the cause(s) and magnitude of uncertainty change over time, the playbook on how to manage risk remains the same:

- **Asset allocation** – Is the mix of equity, fixed income, cash, and other asset classes appropriate given a client’s time horizon, risk profile, and investment objectives?
- **Sector and Industry exposure** – Do portfolios have exposure to secular growth trends (e.g. e-commerce) that are more insulated from economic cycles? Are there cyclical considerations that should be incorporated into positioning?
- **Individual stock selection** – Are current holdings the optimal picks relative to alternatives?
- **Scenario analysis** – How might portfolios perform under different conditions? How does this influence the other three bullet points above?

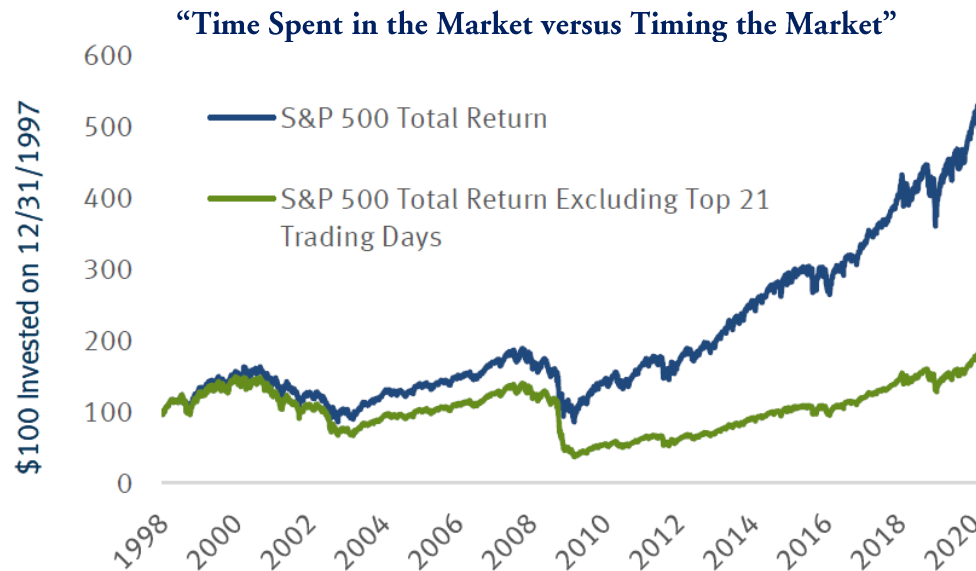
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With this in mind, the following chart taken from Stifel is a helpful reminder that staying invested in equities even during periods of uncertainty is critically important to long-term returns. From year-end 1997 through March 19, 2020, an investor in the S&P 500 would have realized a 252% return, 5.8% on an annualized basis. However, if an investor had missed just the top 21 trading days, the return would have been 0%.



Source: Stifel Investment Strategy via Bloomberg as of March 19, 2020; based on intra-day price

Outlook: Economic activity in the second quarter will clearly be negatively impacted by social distancing and shelter-in-place orders, and although the official determination will take some time, the US is in a recession or will be soon. In fact, we may see some of the worst readings on various metrics since the Great Depression. However, unlike the Great Depression, governments and central banks across the globe have been aggressive in implementing fiscal and monetary policies that should help support economies and financial markets during these uncertain times.

Unlike previous recessions, this recession was caused by a public health crisis. China and South Korea provide some insights about what a COVID-19 recovery period might look like. Not all parts of the economy will recover at the same time or by the same amount, but with improved monitoring and containment strategies, we should expect to see recovery over time. Additionally, unlike typical recessions, the service sector has been hit particularly hard rather than the manufacturing sector, and this also means that the recovery could be faster than usual.

Strategy: Volatility will likely remain elevated until we see a clear downtrend in the number of new COVID-19 cases, which in the US could be later this month if CDC projections are accurate. Given the recent selloff in equities, we believe the risk-reward in equities is much more favorable than fixed income when looking out ~6-12 months.