Trumbower Financial Advisors, LLC
2nd Quarter 2020
Investment Market Commentary

Unprecedented Events

The velocity of the Q1 financial market collapse was unprecedented as was the Q2 recovery trajectory. Congress and the Federal Reserve unleashed an unparalleled barrage of economic stimulus and stock markets roared back from late March lows in exceptional style. The S&P 500 enjoyed its biggest 50-day bounce in history and finished Q2 up 20.5% while Small Caps and the NASDAQ rebounded 25.4% and 31.0%. Markets overseas reclaimed 14% to 18%.

Interest rates followed the Fed's lead into rock bottom territory launching Fixed Income prices into outer space. Investment grade corporates and high yield bonds delivered windfalls of 9% and 10.2%. Despite concerns over solvency, municipals ticked up 2.7%. The Fed – for the first time ever – agreed to purchase a wide array of Fixed Income instruments including corporates and High Yield bond ETFs. Concerns over the demise of "investment-grade" status for scores of companies were assuaged by the Fed's infinite capacity to soak up the supply of "fallen angels".

Bargain basement rates proved irresistible to corporate treasurers who have borrowed $1.1 trillion. New issues were 70% ahead of the previous five-year average. What are they doing with the money? Cash rich tech and underleveraged companies are focused on stock buy backs and M&A because they can. Others are refunding higher cost issues and building a liquidity hedge against harder times ahead. Then there are those businesses who need the money to survive. In the meantime, 142 companies have cut or suspended dividends so far this year – more than in the previous 10 years combined.

Investors scampered in and out of stock markets in Q2 against a backdrop of COVID shutdowns and an appalling fall-off in economic activity. The latest estimates indicate a -5% decline in Q1 GDP and Q2 could be worse. Full year GDP projections from the Fed Board and bank presidents range from -10% to -4.2%. Unemployment predictions range from 7% to 14%. Enormous disparities in forecasts reflect the extreme level of uncertainty we face as communities struggle to reopen even as the Virus rages on.

No historical precedent exists. The brightest economists can't tell us if the recovery will be "L", "U", "V" or "W" shaped or if global financial conditions will ever return to normal – if such a thing exists.

Selected Benchmark and Category Average Total Returns

Large Cap Equity		
Benchmark Indx & Category Average*	**2nd Q 2020**	**12 Mos.**
S&P 500 Index	20.54	7.51
Large Cap Blnd Avg	19.72	3.70
S&P 500 Growth	26.23	17.75
Large Cap Gr Avg	28.30	19.29
S&P 500 Value	13.15	-4.50
Large Cap Val Avg	15.28	-8.07

Mid Cap Equity		
Benchmark Indx & Category Average*	**2nd Q 2020**	**12 Mos.**
S & P 400 Index	24.07	-6.70
Mid Cap Blnd Avg	21.14	-6.28
S&P MC 400 Growth	25.92	0.56
Mid Cap Gr Avg	31.25	12.17
S&P MC 400 Value	21.74	-14.75
Mid Cap Val Avg	19.93	-13.28

Small Cap Equity		
Benchmark Indx & Category Average*	**2nd Q 2020**	**12 Mos.**
Russell 2000	25.42	-6.63
Small Cap Blnd Avg	22.61	-12.61
Russell 2000 Growth	30.58	3.48
Small Cap Gr Avg	32.49	4.66
Russell 2000 Value	18.91	-17.48
Small Cap Val Avg	22.22	-17.71

International Equity		
Benchmark Indx & Category Average*	**2nd Q 2020**	**12 Mos.**
MSCI EAFE	14.88	-5.13
Intl Equity Avg	17.41	-3.09

* **Category average** calculated using *Morningstar Direct* . Fund universe screened to include funds that meet the following criteria:

- **A.** M-Star Category consistent with designated asset class and management st
- **B.** M-Star Style Box consistent with designated management style.
- **C.** Fund's Objective consistent with asset class.
- **D.** Excludes Index Funds.

We have not independently verified *Morningstar* data.

Unemployment peaked at 14.7% in April - reminiscent of the Great Depression that most of us only know from history books and grandparents. The June statistic dropped to 11.1% briefly energizing equity investors who may not appreciate underlying nuances. 40% of those re-employed work in bars, restaurants and other places particularly vulnerable to resurging Virus closures and the number of jobs lost permanently rose by 600K. There are 15 million more unemployed since the pandemic hit. Credit-cards and auto loans in hardship status have risen from .03%/.5% to 3%/3.5% reports TransUnion. Mortgage loans in forbearance have stabilized at around 8.5%. High income consumer spending is down -13% since January.

Before COVID the US was running a $1 trillion deficit projected to top $1.5 trillion over the next 10 years. June's deficit was a record breaking $864 billion – approaching 2019's total. Stimulus spending has ratcheted up the 2020 fiscal year deficit to a jaw dropping $2.74 trillion and more is on the way. The Fed's balance sheet has exploded to over $7 trillion since September – an unmatched increase in absolute terms and roughly in line with the rate of growth in 2008/2009. The Central Bank expects to pile on another $1 trillion in a best case and $7 trillion in a worst case recovery scenario. It is tough to predict the future impact of these extreme responses to an unprecedented crisis.

"Friedmanians" envision rampant inflation looming behind every aggressive monetary expansion. Those fears did not come to fruition as a decade of QE began to unwind. The inflation bullet may have been dodged because previous rounds of easing dribbled into the money supply gradually. Wages remained stubbornly low. Globalization and technological advances helped temper prices.

Unemployment and deflation remain present dangers, but the Government's cure for the infected economy could unleash hyperinflation into the post-pandemic world. Disrupted supply chains, tariffs and diminished mobility all impede global collaboration - a force largely credited with taming past inflationary pressures. Unlike the Financial Crisis the Government responded this time with a combination of massive monetary and fiscal relief that is landing directly in consumer and business accounts primed for spending - instead of trapped in financial institutions reluctant to lend. In other words, there has been a more immediate impact on the money supply evidenced by the 105% increase in seasonally adjusted M1 money supply over the three months ending May 31, 2020.

On the other hand, despite herculean efforts, we could be in for a prolonged arduous recuperation. An aging US population is expected to rein in growth. It will take time for businesses to adapt to new operating environments and heightened systemic leverage may alter the way super low interest rates affect economic activity. Over supply and refining capacity will restrain energy prices for some time to come. We addressed inflation anxiety in our June 2013 essay and, as unique as the present situation seems, there are similarities. We conclude, as we did then, that some good old-fashioned inflation will be welcome – hopefully with mechanisms to keep it in check.

The US is struggling to keep the Virus contained and nascent hints of recovery could be squashed by waves of reclosures. Jobs reports may be masking much deeper levels of unemployment and city streets have been plagued by unrest. Corporate bankruptcies abound but stock markets keep advancing perhaps disconnected from what is happening in life. Granted equities have recouped Q1 losses abundantly but not without drama. On the way up its 20% Q2 climb, there were multiple times when the S&P 500 dropped ~6%.

With nothing else to bet on and time on their hands, retail day traders emerged in swarms pumping up volume and volatility. Much like they did in the heydays of the dot com bubble, individual investors are gobbling up stocks – sometimes indiscriminately. A record number of accounts have been established through online brokers like Robinhood – a phone app where members can buy a fractional share and there are no commissions. Other discount shops have followed suit facilitating the feeding frenzy. Small lot buyers bid up prices for bankrupt companies like Hertz, Chesapeake Energy and Whiting Petroleum - corroborating the view that a surge in retail trading activity is a negative indicator.

The power of the public is also evident in the performance of a portfolio of popular retail stocks, up 61% since the trough, compared to the S&P 500, up 36% (as of mid-June). The flood of market participants showed up in recent earnings announcements by Goldman and Morgan Stanley. Both more than offset losses in other departments with record trading revenues. Another example of the baffling disconnection between economic and investment activity.

The Q2 rally has defied convention – at least temporarily – as stock markets typically thrive under times of muted uncertainty. Another key source of insecurity looms just four months from now when Americans take to the polls. Hopefully COVID won't impede voting logistics but the pandemic has taken a toll on the incumbent President's approval rating. Active managers are now thinking about how to position portfolios for a Biden victory. Themes include "green" energy, infrastructure and cannabis at the expense of big tech and pharmaceuticals. Historically, markets react favorably to one party control but if there is a Democratic sweep prospects for higher taxes and reregulation could temper the enthusiasm regardless of the state of the economy.

European Union leaders will be donning masks for an in person summit July 18th to negotiate a $2 trillion spending plan on top of the $3 trillion unveiled so far this year. The pandemic hit Europe early and hard. So far economies have been opening without spiking waves of infection. Early encouraging economic indicators, however, have proven overly optimistic and officials face a difficult debate over an extremely ambitious proposal. Median 2020 EU GDP forecasts range from -3 (Netherlands) to -11% (Italy, France and Spain). The disparity among member countries naturally exacerbates the potential for discord.

Singapore reported a 2nd quarter GDP contraction of -12.6%. Experiencing the highest rate of cases per capita in Southeast Asia, its radical response shut down construction, tourism and slashed retail spending. They have paid a hefty economic price but the entire city/state has reported under 30 Virus-related fatalities.

Ironically, the UK delayed lockdowns and started lifting restrictions in May but is on course to suffer an -11.5% decline in 2020 productivity. The downturn is expected to eclipse all other advanced economies and England has reported more COVID cases and deaths than any other European country.

It hardly seems fair, but the purported birthplace of the worst global health crisis in recent history seems to be on its way to a V-shaped recovery. China just announced a 2nd quarter year-over year growth rate of 3.2% avoiding technical recession. Official Chinese statistics are of questionable veracity, but there are confirmed indications that imports and exports are rebounding. The real estate boom in several Chinese megacities has escalated to US housing bubble dimensions. Retail sales and private investment are still weak but the Chinese economic recovery outshines progress made elsewhere.

China's advances will do little to stifle the tough talk coming from the White House. Still in the posturing stages, the Administration is considering a variety of new sanctions and restrictions including banning Communist Party leaders from traveling to the US and penalizing US companies who do business with China. Some of the rhetoric is undoubtedly intended to bolster the President's reputation with voters and will hopefully dissipate before it undermines trade deals that will ramp up US sales.

We are living through an extraordinary situation. The pandemic will continue to disrupt society and impose painful boundaries for an indeterminable time. Some businesses have and will reap windfalls and some will not survive. Others will adapt. What should we do to help our clients navigate uncharted waters? Please remember that these comments offer perspective and context when you consider your portfolio's performance. We do not believe generic advice is appropriate and we don't speculate for fear of making things worse. Unprecedented challenges will test the success of our mission - that being - implementing customized portfolios to accommodate needs during unforeseen adverse market conditions and reap profits when they emerge. We continuously review each client's position to be sure it reflects unique goals. We also understand the anxiety that comes with tumultuous financial markets and we welcome your questions, comments, concerns, ideas and if nothing else a comforting conversation.