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> "Everything about recessions are easy to predict except the timing, location, duration, magnitude, and policy response." *- Morgan Housel*

As the threat of the coronavirus grew in the first quarter, there were a number of reports exploring the possibility that millions of Americans would pass away and that the U.S. healthcare system would be overwhelmed. In response to these reports, most states implemented stay-at-home orders effectively shutting down much of the U.S. economy. In this edition of Viewpointe, we discuss the economic impact of these shutdowns. We also explore what may lie ahead as states begin to reopen. In addition, we summarize recent developments in both the fixed income and equity markets. In the asset allocation section we discuss some recent changes on the portfolio strategy front as well as our thoughts for moving forward. We conclude with a summary of the ins and outs of participating in a Zoom meeting.

Economic Review -
The Grand Reopening

After roughly three months of staying at home, many Americans are ending social distancing in grand fashion. Perhaps one of the best economic indicators that demonstrated this point was the May retail sales report. This report demonstrated a strong rebound in all categories. Clothing was up 188% month over month. Sporting goods increased 88.2% and furniture showed an 89.7% gain. Notably restaurants rebounded 29.1%. In short, these increases in consumer spending indicated a decline in risk aversion and provided signs things were moving slowly back to normal. This was welcome news for an economy that had been pretty much mothballed.

While the second quarter provided some of the largest drops in economic indicators that we had ever seen, there are some welcome signs the worst may be behind us from an economic perspective. As states continue to proceed with their reopening strategies, governors are expected to avoid wide scale shutdowns going forward. While that is welcome news from an economic standpoint, we are not out of the woods yet in terms of the coronavirus.

Unfortunately, cases are beginning to trend up in the states that have reopened. In addition, it appears the warmer weather will not provide the relief that was initially anticipated as we are seeing the number of cases rise in the Sun Belt states.

While the number of cases in several other countries has risen to a peak and then gradually tapered off, in the U.S. we appear to be stuck on an extended plateau. To a large degree that is attributed to the use of more aggressive tactics by some other nations. Ironically, countries with authoritarian governments have been more effective in controlling the spread of the virus. Nations that conduct widespread population surveillance including door-to-door symptom checks combined with "mandatory" isolation procedures have been more successful in preventing the spread.

The U.S. on the other hand for the most part has been dependent upon people complying with "recommended" risk aversion techniques, or mandatory techniques implemented on a more localized level. While these less intrusive strategies proved effective when fear levels were elevated, the compliance level is significantly decreasing as people start to discount the risk. This appears to be leading to an increase in cases, which is resulting in anxiety regarding a "second wave" in the fall. While we believe a "second wave" is a distinct possibility, we expect governors to avoid statewide shutdowns unless absolutely necessary. In the alternative, we anticipate more localized shutdowns focused on locations where healthcare systems are overwhelmed. Local officials will be engaged in a balancing act between economic pressures on the one hand and the ability to provide medical care to those that need it on the other. We believe economic pressure will win out as long as a reasonable level of medical care can be provided.

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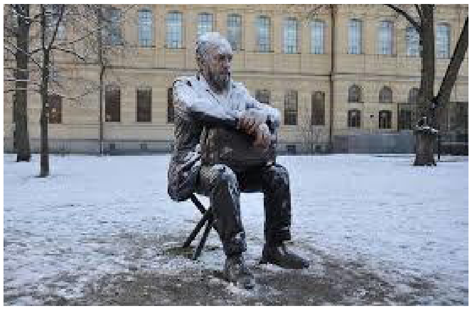
While from an economic perspective the worst may be behind us, it is important to note the National Bureau of Economic Research (NBER) declared an official end to the 11 year long U.S. economic expansion. According to the NBER, a recession officially started in February. While the average length of a recession is 11 months, as states reopen we are already seeing signs that we may be moving toward an early exit. With that said, it is important to note we are not saying we will reach beginning of the year growth levels quickly. With the long lasting impact the coronavirus will have on the U.S. economy, it will likely take more than a year to just get back up to where we were in January. In addition, it is important to note that trade tensions are once again building. Also general geopolitical tensions are growing as nations become stressed by the coronavirus and look for someone to blame for their plight. In short, it is unlikely we go back to open trade and economic cooperation on a global scale anytime soon. As a result, we see slower growth on the horizon for quite some time to come. Such slow growth increases the risk of slipping into another economic slump placing a lasting recovery at risk of failure.

Fixed Income Commentary - Staying Put

The Federal Reserve (Fed) cut rates, expanded their liquidity programs and employed Quantitative Easing (QE) at a historic pace during the first half of the year. Using similar methods to those utilized during the Great Recession, the Fed launched QE4, purchasing more assets than all of the other QE programs combined. These Fed purchases provided needed liquidity in target markets. This avoided what could have easily become a credit crisis. While on the one hand the Fed's actions prevented large scale bankruptcies, on the other, the Fed selected the winners and the losers depending upon what they decided to purchase. For those that believe in free markets, it is hard to identify more blatant market manipulation.

Regardless of where you may stand on the issue of Fed intervention, at the present time the facts show the Fed is the dominant force within the fixed income markets. Interest rates are currently being driven primarily by Fed policy. With that said, the old saying "Don't fight the Fed" rings as true as ever. As a result, we monitor Fed statements very closely. In June, Fed Chairman Powell stated the Federal Reserve is not even thinking about raising rates. Powell made this statement shortly after the full Federal Open Market Committee indicated the Fed Funds rate is likely to stay near zero until 2022. These bold statements effectively provide forward guidance indicating the Fed Funds Rate will remain low based on a period of time rather than upon reaching defined economic milestones.

As a result, our base case calls for fixed income securities to trade in a relatively tight trading range for the time being. This significantly limits return prospects given yields are stuck near historic lows and there is little opportunity for market value appreciation. U.S. Treasury yields provide a good example of how stable yields have been over the last few months. Yields ranging between 1 month to 3-years remained within the upper and lower bound set by the effective Fed Funds Rate. This bound ranges between 5-25 (.05-.25%) basis points. While yields have crept up slightly further down the yield curve, yields in the 10 to 30 year part of the curve have not moved much either over the last few months.



Our base case anticipates interest rates to remain low for the remainder of the year with a high degree of price stability. While we anticipate some upward drift amongst intermediate and long-term rates, we do not anticipate significant movement. We feel this is the most likely outcome absent a positive surprise on the economic growth front, an unexpected rise in inflation or a change in Fed policy. At the present time we believe all three scenarios are unlikely. An alternative factor that may impact fixed income security prices is credit risk. At the present time the Fed is providing ample liquidity, thereby decreasing default risk. In the event this were to change we could experience a repricing of risk where investors demand more yield for the risk they are taking. This is an area that we are watching closely since many debt issuers are under financial pressure as a result of the coronavirus shutdowns.

Equity Commentary - A Lasting Recovery?

Dating back to 1948, the average bear market loss for the S&P 500 was 36% from its peak and lasted 16 months. At the low on March 23rd, the S&P had dropped 34%, placing the drop very close to the historic average. Following that low, the S&P 500 rebounded swiftly returning just under 40% as of the time of this writing. Most importantly, this recovery took place during a quarter in which we experienced some of the weakest economic readings most of us have ever seen. So, why the drastic disconnect between what is occurring on Wall Street versus Main Street? Well, first off, we need to look back at history. Prior to the recent recession, the U.S. experienced 12 recessions following World War II. The stock market has bottomed an average of 5 months before those 12 recessions officially ended.

This disconnect between economic conditions and market performance can be explained largely due to the fact that markets are forward looking. In other words, they do not price in where you are at that particular point in time, but rather where they believe things will be in the future. With that said, we have identified a handful of positive drivers that the equity markets appear focused on. First off, the markets seem to be betting on the introduction of a vaccine for the coronavirus as soon as year-end. This is viewed by many as the silver bullet solution. In the event an effective vaccine is introduced, we likely will be able to place the current coronavirus situation to rest. One only need to look back at some of the best return days of the second quarter to see that several were tied to positive vaccine announcements.

Secondly, equity markets are being supported by a massive amount of liquidity. In the first quarter edition of Viewpointe we mentioned how increases in the M2 money supply were providing support for risk assets. As a result of the government response to the coronavirus, the M2 money supply has significantly increased. At the same time the velocity of money, or the frequency that the money is spent, has decreased. This has resulted in more "savings" that oftentimes is being utilized to purchase assets such as stocks. Many investors anticipate this cycle to continue for quite some time to come.

Thirdly, equity investors are taking comfort that more fiscal stimulus will be enacted as needed. The combination of direct stimulus payments to taxpayers combined with enhanced unemployment insurance has provided needed financial support to those affected by the coronavirus. In fact, recent surveys indicate that roughly 60% of laid off workers have been made more than whole relative to their work based income prior to the pandemic. Many expect this "generous" support to be extended in the event workers are not able to return to work when the current program expires.

Lastly, investors are optimistic regarding a strong economic rebound now that states are reopening. Ironically, the "black swan event" was not the coronavirus as much as it was the economic closures that resulted from it. With the states reopening and the expectation that governors will be reluctant to implement state wide shutdowns going forward, many believe the worst of the economic pressure is now behind us.

With that said, there is no shortage of catalysts for a pullback. While the list is long, the top risks we have identified include a second wave of the virus in the fall, lasting economic impacts from the shutdown, lasting impact due to ongoing pathogen concerns, growing tensions between the U.S. and China, political dysfunction and civil unrest.

In conclusion, while equity markets have rebounded significantly, we do not assume smooth sailing from here. There are simply too many unanswered questions to make that assumption. We do not know when or if an effective vaccination will be introduced. We do not know when or if the coronavirus will experience a second wave. We do not know to what level the federal government will continue to implement fiscal stimulus. What we do know, however, is that sticking to your long term investment plan and not letting emotions hijack your better judgement is more likely to lead to a successful outcome. In short, we must hold the course and stay focused on the fact that history has shown Americans have always found ways to adapt to difficult situations. Sometimes it just takes a little bit more trial and error to get there.

Asset Allocation -

Lifted by the Rising Tide

We chose not to rebalance our Lakepointe Classic model portfolios during the second quarter. Going into the quarter we anticipated rebalancing back to our equity target, but instead we decided to hold off as stocks increased at a surprisingly rapid pace. We feared that we may simply be in the midst of a short-term bounce that could change direction abruptly. As equities continued to increase, we soon decided to just sit tight and see if the equity market momentum would bring us back to our equity target naturally. After all, large-cap U.S. stocks were our preference and we were already heavily weighted in that direction. Low and behold as the quarter comes to an end we find ourselves pretty much back in-line with our equity targets.

While in retrospect it would have been nice to add to our equity exposure back in April, hindsight is always 20/20. Frankly, we did not anticipate the equity rally that began in late March to last as long as it has or go up to the degree it did. At the time, there were a lot of potential pitfalls that could have changed equity market direction. Nevertheless, we are pleased with the fact we are pretty much back in-line with our equity target weights. After all, it is hard to complain too much about a positive surprise that benefitted portfolio performance.

While we are hopeful the equity market rally will continue, the majority of our research sources are pointing out the possibility of a potential pullback from current levels. In short, given the current backdrop, we would not be surprised if such a pullback were to take place during the third quarter. At the present time it is hard to have much confidence in sustained upward gains absent a resolution to some of the many obstacles that stand between us and a normalized corporate earnings environment. For the time being, with so many unanswered questions we feel the best approach is to hedge our bets and retain our current equity exposure, which currently lies on the lower end of our asset allocation ranges.

In mid-May, we rebalanced our Lakepointe Premier model portfolios. Similar to the reasoning laid out above, we were reluctant to add to our equity exposure given the significant equity market appreciation that had occurred by that time. As a result, we retained an equity target pretty much in-line with where the accounts sat at that time. In other words, if a balanced account was weighted 41% in equity we retained that weighting rather than bringing it up to the target of 44%. On the individual stock front we added two stocks to our political activism individual stock portfolio. These stocks were Illumina and Regeneron Pharmaceuticals. Both stocks fall within the healthcare sector and compliment the healthcare names that we already had. The stocks that were removed included Boeing and ViacomCBS. Boeing was removed in order to reduce exposure to air travel due to the long-term impact the coronavirus will likely have on this space. ViacomCBS was removed to reduce our exposure to traditional media which is under pressure due to a reduction in advertising dollars.

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On the fixed income front we made no changes to our mutual fund lineup. While our model fund lineup underperformed the Barclays Aggregate bond index during the first quarter, it was hard to fault them too much since it was unreasonable to expect them to be positioned for a pandemic and the resulting flight to quality that followed. Fortunately, they have made progress catching up now that they had the opportunity to reposition for the new investment environment. On the individual fixed income front finding attractive short to intermediate bonds has become extremely difficult. In addition, one year certificates of deposit are paying right around .25%. As a result, we find ourselves moving toward mutual funds in many instances.

Financial Planning -

Keeping In Touch Via Zoom

As we continue to cope with the coronavirus, we have had to adapt the way we conduct day-to-day business. In the wealth management field we recognize the importance of building a relationship with our clients. This relationship is more often than not built upon routine face-to-face meetings. During the current era of social distancing and stay-at-home orders, communication methods have had to change. While in many cases we have reverted to phone calls, our method of choice has been Zoom.

Zoom is an online meeting application where you can organize meetings that feature both audio and video functionality. More importantly, they offer the ability for participants to share their screen with the other participants on the call. This proves extremely beneficial when conducting investment portfolio reviews. As more and more clients show interest in meeting via Zoom, we wanted to take this opportunity to introduce you to the functions offered by Zoom as well as the basics of how to join a Zoom meeting.

To access Zoom go to www.zoom.us. Once there, you can select the “Support” tab at the bottom of the page where you can gain access to tutorials on a wide range of topics. Under “Support Topics” the “Meetings and Webinars” tab is where you can go to learn how to join and host meetings. For this illustration we will assume that you have been sent an invitation for a Zoom meeting. The appointment will contain the link to join the meeting. If you have not already participated in a Zoom meeting, you will want to go into Zoom in advance of the scheduled meeting. If you do not, you will be prompted to download and install Zoom prior to joining your first meeting.

We find that the best way to familiarize yourself with Zoom is to set up a free account and go in to join a test meeting prior to your initial meeting. Once you set up an account, there is a “Test Zoom” link that shows up on various pages within Zoom’s website. This “Test Zoom” link is usually located at the bottom of the page under the “Support” link. By joining a test meeting, it takes you through a series of tests to ensure that the various functionality is working and to familiarize you with the layout of the meeting screen. We find that people that set up an account, conduct a test meeting and participate in some of the tutorials are a lot more successful in engaging in their first real meeting.

Assuming that you have taken these preliminary steps, on the meeting day you should simply have to click on the “Meeting” link provided in the appointment. That should bring you to a prompt where you will need to select “Join a Meeting.” Shortly thereafter, you will be asked to provide the meeting id number and/or passcode that was provided in the appointment. Once you do, you should be on the meeting screen. Once here, you will be asked whether you plan on calling in or utilizing the computer audio. It is important to note that when you scroll over the meeting screen an information bar will appear on the bottom. This bar is where you can mute or unmute your speaker as well as select whether you want the video on or not. It also lists the individuals that are participating in the meeting and allows you to share your screen. Lastly, it provides the link to leave the meeting.

Many articles have been written about the security of Zoom meetings. Our security team has reviewed all of the features of Zoom and believes a meeting setup with a passcode is as secure as any virtual meeting application can be. The security rests on not sharing the passcode with people who should not be attending, and also not reusing meeting ID’s. It is simple to create a new meeting with a new ID and Passcode, so reuse is not necessary. For high-risk meetings, we also employ the Zoom waiting room feature. This pushes all participants into an isolated connection until they are admitted by the host. These practices mitigate the many incidents the news media has highlighted.

While we utilized Zoom prior to the pandemic, we now find ourselves using it much more. We find the more we utilize it the more effective it becomes. While we hope that we will be able to move back to face-to-face meetings before too long, we are thankful that applications such as Zoom still provide us with a vehicle to have virtual meetings with our clients.