Schroeder | Capital Management, LLC

Global Investment

# Investment Review and Outlook – Spring 2020

## The COVID-19 Challenge and Recent Positive Developments:

Daily reports on the COVID-19 global pandemic infection rate and casualties are becoming more encouraging in the U.S relative to "flattening the curve", especially in New York, the epicenter of this disease. While the death toll remains staggering, but declining, hospitalizations are slowing in New York and hopefully across the country, affirming the effectiveness of social distancing, testing and other preventive measures. However, it will be some time before the virus is safely contained.

On April 16, the Federal government unveiled 3-phase guidelines for reopening the country, after at least a month of sheltering in place for most U.S citizens. At a briefing with state governors, it was made clear that they were responsible for deciding when it is safe to lift restrictions in their states.

The first phase of the guidelines will ease restrictions where there has been low transmission of the coronavirus while maintaining strict preventive measures in states severely impacted and where progress against the virus is still needed. Phase one calls for strict social distancing, only gatherings of less than 10 people, discouraging nonessential travel and teleworking where possible as workers return in phases. After evaluating the impact of these easing restrictions for 30 days, some parts of the country could see the resumption in relatively "normal" business activity and social gatherings. In other parts of the country, or if virus cases pick up again, it could take longer to return to normalcy.

## The Current State of the U.S. Economy:

The economic backdrop is unsettling and unprecedented, starting in mid-March with varying degrees of weakness. Economic activity, as we know it, has been temporarily held in limbo across much of the U.S, although this is about to change for the better with the recent federal plan to gradually reopen the economy and get people back to work. The administration has recently focused on "helicoptering" money across the U.S. for financial assistance to both large and small businesses and individuals. Employer incentives to maintain their employment levels were put in place to qualify for loan forgiveness. The rapidly growing number of individuals seeking unemployment assistance is very troubling. However, the government stimulation programs that are now in place along with workers that will be returning to work in some states will eventually turn these numbers around.

Overall economic news is likely to worsen for a while. A sharp falloff in GDP and a sizable decline in corporate profits is expected in the current quarter, ending June 30th. Business activity for April will be significantly weaker than for March and prospects for May will be even more difficult, as our country navigates through a widespread lockdown. As a result, GDP will decline sharply for the current quarter. As we see a further flattening in the infection curve of COVID-19 and America gradually returns to a sense of normalcy, we expect an economic recovery during Q3 2020.

## The Current Posture of the Federal Reserve:

The response by the Federal Reserve to the broad-based national shutdown has been unprecedented financial stimulus, cutting interest rates to near zero and buying Treasuries and mortgage debt. The

Fed, along with Congress, despite their political differences, will eventually work together to ensure the economy regains its health and that individuals, businesses, healthcare workers, our institutions and the states are given financial assistance they need as a result of the COVID-19 fallout. It is also reasonable to assume that there will be additional fiscal and monetary stimulus measures put in place in the future to support the gradual reopening of the American economy. While the impact of the foregoing financial assistance will ultimately have consequences for both the federal government and states' balance sheets, the U.S. economy had very broad-based, positive underpinnings prior to the devastation of this virus. This will likely support a more rapid recovery. Ultimately, the financial strength of the U.S should be well-poised to regain the leadership position it had previously enjoyed on the global stage.

## Wall Street and the Markets:

For now, at least, investors who have "stayed the course" have been rewarded. However, the market's rebound should not obscure the fact that many dark days may lie ahead, even though the darkest hour for Wall Street may have passed. The stock market has recovered significantly from the dramatic decline during March, recouping over 30% from the March 23 low. Investors have anticipated an improvement over COVID-19 and flattening of the disease curve along with anticipation of a partial re-opening of the U.S. economy, relatively soon.

Historically, the stock market has been a leading indicator after past shocks and history could be repeating itself. Despite the drum roll of dour economic releases, reduced profit estimates and guidance suspensions by companies along with expected dividend cuts, markets look beyond all of this. History teaches us that financial markets typically establish a sustainable bottom well before the cycle of bad news runs its course, 6-9 months prior. That also occurred in the deep bear markets of 1973-1974 and 2008-2009.

## Investment Strategy:

In the short run, we anticipate a continuation of market volatility as efforts to bring the coronavirus under control continue and weak economic reports are released. However, it is also important to underscore the dramatic improvement from the dire COVID-19 infection and death forecasts only a couple weeks ago. This offers confidence that as a nation we are being successful in addressing the threat of this very difficult health situation and are seeing signs of a potential reversal.

We have favored U.S. securities over international since early 2019, as part of our overall investment strategy to reduce overseas portfolio exposure. We are also positioning accounts for the intermediate-to-longer term in light of current events with quality issues that have well-defined sustainable prospects. We have been emphasizing the healthcare and pharmaceutical sectors with additions of Abbott Labs (significant testing), Medtronic (ventilators), and 3M (N95 masks). Other existing pharmaceutical holdings including Roche, GlaxoSmithKline, Merck and Eli Lilly are acting in concert with the new positions we have added and are current and potential problem solvers of the pandemic.

We are continuously monitoring domestic and global economic developments along with a daily review of client portfolios and the COVID-19 updates. We are very focused on preserving client capital as we conduct research to identify high-quality investment opportunities for the future.

G. Frederick Schroeder, CFA
President and Chief Investment Officer

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