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MACRO MUSINGS

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FIRST HALF OF 2020 REVIEW: A TALE OF TWO MARKETS

SUMMARY

- **Improvement in the economic indicators is the primary driver pushing MACROCAST™ back into positive territory. While on an absolute basis the data remains mostly negative, it has improved substantially relative to the lows of April and May.**
- **Market performance in the second quarter mirrored the first quarter's big decline. Equity markets had one of the best quarters in history. In the past, when the market performed as well as it did in Q2, it registered further gains in the months ahead.**

WHAT WOULD CAUSE MACROCAST™ TO GO NEGATIVE AGAIN?

We have received inquiries from clients as to what must happen for MACROCAST™ to fall back into negative territory. While we can never predict how the model will behave, we have a clear idea of the categories that are most vulnerable to declining.

The Aggregate Economy and Technical Analysis categories contain the most indicators and carry the most weight. Together, they account for over 40% of the headline MACROCAST™ score:

- While Technicals remain mostly neutral, these faster moving signals could flip negative if the market were to pullback; however, this alone would not be enough to push the overall score below zero.
- A far greater concern is a downturn in the economy. A reversal to the downside in the months ahead would further weaken our Aggregate Economic Indicators, and that would be enough to tip MACROCAST™ into the red.

Unless we see significant deterioration in the broader economy, the Inflation and Liquidity categories should serve as a ballast, keeping the MACROCAST™'s score from getting too negative as Fed policy continues to be accommodative and inflation remains muted.

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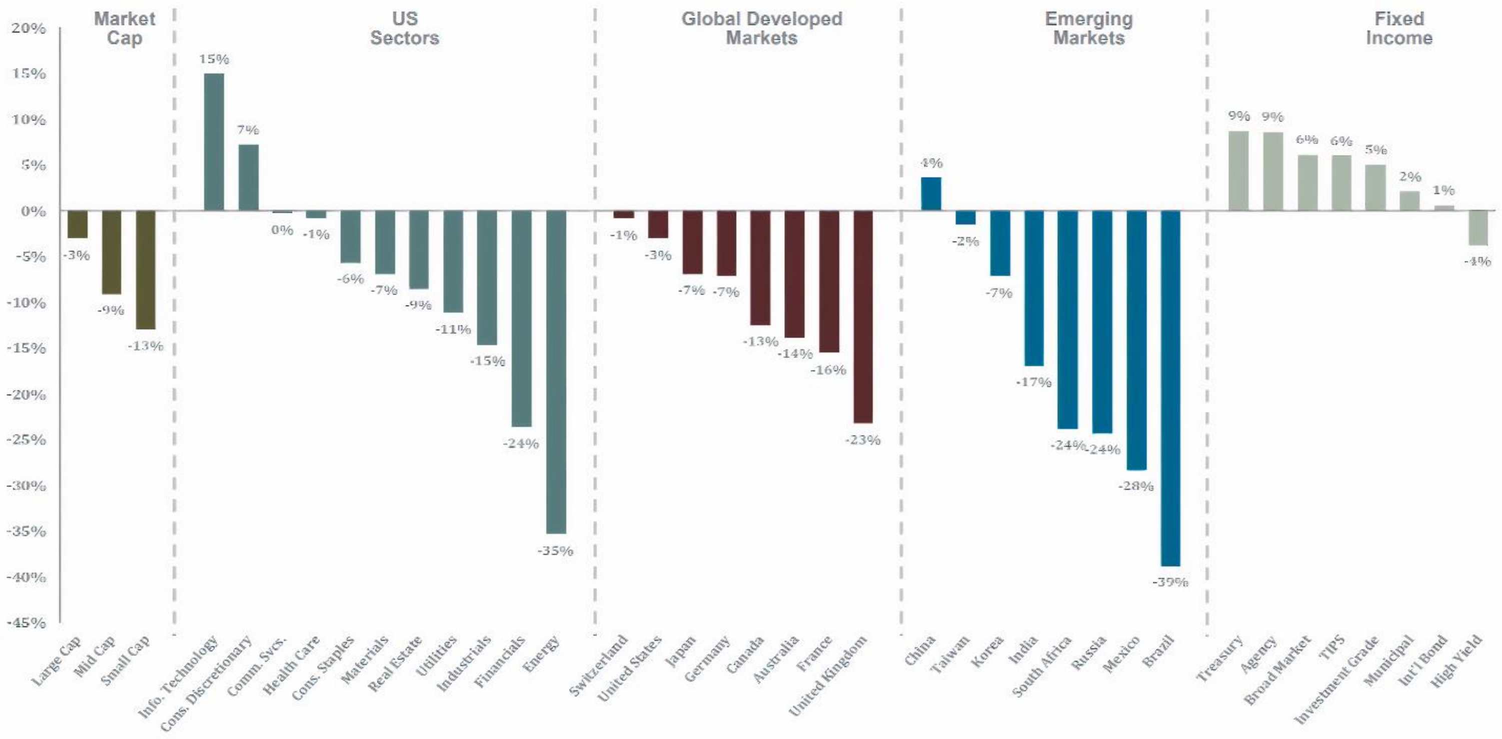
FIRST HALF ASSET CLASS REVIEW



Performance displayed represents past performance, which is no guarantee of future results. The aforementioned indices are not available for direct investment. The index returns do not reflect any management fees, transaction costs or expenses. Index information is provided for illustrative purposes only and is not meant to represent the performance of a fund or strategy.

Here are our main takeaways from the first half of 2020:

1. ***Market & Asset Class performance matches reality on the ground.*** The market rally in the wake of the worst economic crisis since the Great Depression has left many investors scratching their heads, but looking at the asset class and sector performance reveals that performance has generally reflected the changes in market and economic conditions.
    a. **Large Cap stocks, representing the largest companies, have held up the best.** They were led by Technology stocks, which have benefited from work-from-home mandates. Since Tech stocks now make up almost a third of the overall index, the S&P 500 has outperformed other equity major equity markets year-to-date.
    b. **Energy, Financials, and Industrial sectors have performed the worst**. The companies in those sectors are among the most economically sensitive.
    c. **Looking to emerging markets, the countries that have handled the pandemic effectively are performing the best**. Those who have struggled to control the spread of the virus are among the worst performers.

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2. ***Bonds are universally positive.*** Every sector of the bond market is positive except high yield. The higher the perceived quality of the bond, the better that sector has performed. US Treasury bonds are the top performer, and fixed income has demonstrated once again that they are among the best performing asset classes during a market selloff.

THE MARKET REBOUNDED STRONGLY IN THE SECOND QUARTER

The market registered a 20% gain in the second quarter. Past periods of similarly strong performance led to further gains in the months ahead (table from LPL):

Best Quarter For The S&P 500 Index Since 1998

Big Quarterly Gains Historically See Continued Strength

Quarter	Quarterly Gain >15%	S&P 500 Index Return: Next Quarter	S&P 500 Index Return: Next Two Quarters	S&P 500 Index Return: Next Four Quarters
Q3 1970	15.8%	9.3%	19.1%	16.8%
Q1 1975	21.6%	14.2%	0.6%	23.3%
Q4 1982	16.8%	8.8%	19.5%	17.3%
Q4 1985	16.0%	13.1%	18.7%	14.6%
Q1 1987	20.5%	4.2%	10.3%	-11.2%
Q2 1997	16.9%	7.0%	9.6%	28.1%
Q4 1998	20.9%	4.6%	11.7%	19.5%
Q2 2009	15.2%	15.0%	21.3%	12.1%
Q2 2020	20.0%	?	?	?
	Average	9.5%	13.9%	15.1%
	Median	9.0%	15.2%	17.0%
	% Positive	100.0%	100.0%	87.5%

Source: LPL Research, FactSet 06/30/2020 (1950 - Current)
All indexes are unmanaged and cannot be invested into directly. Past performance is no guarantee of future results.

The following quarter was positive every time, and there was only a single instance where the market was lower one year later.

IN CASE YOU MISSED IT

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