

Market Environment

Second Quarter 2020

Market Environment 2Q20: Global Economy

Following a brutal March and April, a handful of key economic measures rebounded in May and June, beating expectations and fueling optimism. However, most have yet to recoup the losses incurred and a high degree of uncertainty remains as to the path over the foreseeable future. Global fiscal and monetary stimulus was swift and massive, helping to bolster confidence and liquidity and fueling an appetite for riskier assets.

U.S.

- 1Q GDP contracted 5.0%, 2Q is expected to be far worse
 - 2Q estimates vary and are fluid, but range from –35% to –45% (annualized)
 - Initial 2Q GDP number to be released on July 30th
- Some measures rebounded, but have not fully recovered:
 - Retail sales grew a record 18% in May (-6% yoy)
 - Durable goods orders up 16% in May (-18% yoy)
 - Personal spending rose 8% in May (-9% yoy)
 - Hotels, restaurants, airlines and many small businesses were among the hardest-hit
- Unemployment (11.1% in June) remains elevated
 - Jobless claims, around 1.5 million per week, have decelerated
- Housing received a boost from relatively low mortgage rates
 - Pending home sales up 44% in May (down 5% yoy)
- Fed left rates close to 0% and expects to be on hold until at least 2022
- Speed and size of stimulus programs unprecedented
 - Stimulus programs approach \$3 trillion (about 14% of GDP)
 - Fed balance sheet roughly \$7 trillion
 - Fed budget deficit was \$2.7 tn in the first 9 mos of FY 2020, \$2 tn more than the same period last year (CBO estimates)
 - Most expect more as needed

Overseas

- Euro zone
 - 1Q GDP contracted 3.8%, largest quarterly drop on record
 - Economic activity showed improvement as Eurozone PMI for June rose to 47.3 (30.5 in May; 13.5 in April)
 - European Commission support included €750 bn recovery fund plus €540 bn rescue package
 - ECB expanded pandemic emergency purchase program to €1.35 trillion
- U.K. GDP sank 20% in April, most ever
 - Bank of England expanded its quantitative easing program; negative rates were under “active review”
 - Brexit returned to the agenda as the deadline passed for an extension of the transition period, which expires on 12/31/2020
- Japan’s economy shrank 4.4% in April
 - Bank of Japan increased its stimulus from \$700 billion to \$1 trillion in June
- China’s GDP fell 6.8% in Q1, first contraction in 28 yrs
 - Chinese government unveiled fiscal stimulus of US\$506 bn, bringing budget deficit to a record high of 3.6% of GDP
 - Growth is expected to be positive in 2Q
 - Geopolitical concerns increased as the US moved to end its special treatment of Hong Kong after China announced the imposition of a national security law in Hong Kong

Market Environment 2Q20: Global Equity

Following steep declines in the first quarter, global stock markets posted double-digit returns in the second quarter. The S&P Index notched its best quarter since 1998 with a 20.5% return. Outside of the U.S., developed and emerging market equity indices also posted returns approaching 20%. Growth vs. Value and Large vs. Small Cap returned differentials remain at extreme levels.

U.S. Equity

- S&P 500 Index returned +20.5% in 2Q; -3.1% ytd
 - Top sector performers were Consumer Discretionary (+32.9%), Information Technology (+30.5%), and Energy (+30.5%)
 - Defensive sectors: Utilities (+2.7%) and Consumer Staples (+8.1%) were among the worst performing sectors
 - Risk factors outperformed Quality factors for the quarter
 - Notably, over 40% of the S&P 500 companies pulled earnings guidance given uncertainty around the pandemic
- Growth significantly outperformed Value
 - R1000 Growth: (2Q:+27.8%; ytd:+9.8%)
 - R1000 Value: (2Q:+14.3%; ytd:-16.3%)
- Large caps trailed small caps, but outperformed YTD
 - R1000: (2Q:+21.8%; ytd:-2.8%)
 - R2000: (2Q:+25.4%; ytd:-13.0%)
- High-flying growth stocks “FAAMG” contributed nearly 30% to the S&P 500 return

	2Q20	YTD
Facebook	+36.1	+10.6
Apple	+43.8	+24.9
Amazon	+41.5	+49.3
Microsoft	+29.4	+29.8
Google (Alphabet Class C)	+21.6	+5.7
Netflix	+21.2	+40.6

Non-U.S. Equity

- Non-U.S. developed markets also up sharply
 - EAFE: (2Q:+14.9%; ytd:-11.3%)
 - ACWI ex-U.S.: (2Q:+16.1%; ytd:-11.0%)
 - Top sector performers included Materials and IT
 - Value (2Q:+12.8%; ytd:-19.4%) trailed Growth (2Q:+19.1%; ytd:-2.6%)
 - Top country performers were Germany (+27%), Netherlands (+25%), Canada (+20%) and Sweden (+20%)
 - U.K. (+8%) and Japan (+12%) lagged
- U.S. dollar was mixed
 - USD depreciated against the euro (2Q:-2.4%;ytd:-0.1%), the Australian dollar (2Q:-12.5%; ytd:+2.1%) and the Canadian dollar (2Q:-4.5%; ytd:+4.8%)
 - USD posted flat returns versus yen (2Q: -0.1%; ytd:-0.7%) and British pound (2Q:+0.4%;ytd: +6.7%)
- Emerging markets recorded the strongest quarterly return in over a decade, with U.S. dollar weakness amplifying returns
 - MSCI EM: (2Q:+18.1%; ytd: -9.8%)
 - Most countries delivered double-digit returns
 - BRIC countries all performed well but most remain sharply down ytd. Brazil: (2Q:+23%; ytd:-39%); Russia: (2Q:+19%; ytd:-25%), China (2Q:+15%, ytd:+4%); India (2Q:+21%; ytd:-17%).

Market Environment 2Q20: Global Fixed Income

Fixed income markets saw a strong rebound in risk appetite amid strong support from the Fed and improvements in liquidity. Overseas, rates were lower, fueled by rate cuts across a broad swath of countries and strong performance from corporates. Emerging market debt posted lofty results but remain down single digits from the beginning of the year.

U.S. Fixed Income

- U.S. Treasury yields were range-bound in 2Q
 - 2-year U.S. Treasury Note declined 7 bps to close at 0.16%
 - 10-year U.S. Treasury yield closed the quarter at 0.66%; down only 4 bps from the end of Q1 but off far more sharply from the level at the start of the year of 1.92%
 - 30-year Treasury yield increased 6 bps and closed at 1.41%
- Bloomberg Barclays Aggregate (+2.9%; +6.1%) rose with non-Treasury sectors faring the best
 - Bloomberg Barclays Corporate: (2Q:+9.0%; ytd:+5.0%)
 - Bloomberg Barclays US Treasury: (2Q:+0.5%;ytd: +8.7%)
- TIPS outperformed nominal Treasuries
 - 10-year breakeven spread ended quarter at 1.34%, up from 0.87% at March 31 but down from 1.77% at December 31, 2019
 - Bloomberg Barclays TIPS Index: (2Q:+4.2%; ytd:+6.0%)
- High Yield posted sharp gains
 - Bloomberg Barclays High Yield Corp (2Q:+10.2%; ytd:-3.8%)
 - But default rate hit a 10-year high (6.2%)
- Municipal bonds also rebounded from relatively poor performance in Q1
 - Bloomberg Barclays Municipal Bond Index: (2Q:+2.7%; ytd: +2.1%)

Non-U.S. Fixed Income

- Non-U.S. returns were also positive
 - Rate cuts were widespread and US dollar performance was mixed
 - Bloomberg Barclays Global Agg ex-U.S. (unhedged): (2Q:+3.4%; ytd:+0.6%)
 - Bloomberg Barclays Global Agg ex-U.S. (hedged): (2Q:+1.8%; ytd:+2.3%)
 - The UK 2-year yield dropped below zero for the first time, finishing at -0.08%, as the central bank discussed the possibility of negative interest rates
- Emerging market debt up sharply but down ytd
 - The U.S. dollar-denominated JPM EMBI Global Diversified Index gained ground in second quarter. (2Q:+12.3%; ytd: -2.8%)
 - EM currency performance was mixed, but generally underperformed other risk assets
 - Local emerging market debt, as measured by the JPM GBI-EM Global Diversified also posted positive results: (2Q:+9.8%; ytd:-6.9%)
 - Turkey: (2Q:+5.2%; ytd:-5.4%)
 - Brazil: (2Q:-1.1%;ytd: -22.4%)
 - Mexico: (2Q:+10.3%; ytd:-11.0%)
 - Russia: (2Q:+17.2%; ytd:-7.5%)

Market Environment 2Q20: Real Assets

Real assets saw improved performance during the quarter. Commodities posted solid gains, led by the energy component as OPEC and Russia agreed to make temporary production cuts. MLPs rose over 50% in Q2 but not enough to recover the losses in Q1. TIPS outperformed nominal U.S. Treasuries as inflation expectations rose.

- Brent crude oil prices rallied from \$20.48/barrel (3/31) to \$39.27/barrel (6/30)
 - S&P 1200 Energy: (2Q:+16.5%; ytd:-35.2%)
 - Alerian MLP Index: (2Q:+50.2%; ytd:-35.7%)
- Commodities gained
 - Bloomberg Commodity TR Index: (2Q:+5.1%;ytd: -19.4%)
 - S&P GSCI Commodity Index: (2Q:+10.5%; ytd:-36.3%)
 - S&P Gold Spot Price Index: (2Q:+12.8%; ytd:+18.2%)
 - The exception: Agriculture (-4.9%) and Livestock (-8.6%) commodities continued their downward trajectory during the quarter.
- Listed Infrastructure also rebounded
 - DJ-Brookfield Global Infrastructure Index: (2Q:+11.6%; ytd:-11.8%)
 - FTSE NAREIT: (2Q:+11.8%; ytd:-18.7%)
 - FTSE EPRA/NAREIT Global: (2Q:+9.9%; ytd:-21.5%)
- Breakeven spreads for TIPS rose but remain low
 - 10-year breakeven spread ended quarter at 1.34%, up from 0.87% at March 31 but down from 1.77% at December 31, 2019
 - Bloomberg Barclays TIPS Index: (2Q:+4.2%; ytd:+6.0%)

Returns for Various Periods – June 30, 2020

		April	May	June	Last Quarter	Year to Date	Last Year	Last 3 Years	Last 5 Years	Last 10 Years	Last 15 Years
EQUITY	1 Russell:3000 Index	13.24	5.35	2.29	22.03	(3.48)	6.53	10.04	10.03	13.72	8.78
	2 Russell:1000 Index	13.21	5.28	2.21	21.82	(2.81)	7.48	10.64	10.47	13.97	8.91
	3 Russell:1000 Growth	14.80	6.71	4.35	27.84	9.81	23.28	18.99	15.89	17.23	11.32
	4 Russell:1000 Value	11.24	3.43	(0.66)	14.29	(16.26)	(8.84)	1.82	4.64	10.41	6.24
	5 Russell:Midcap Index	14.36	7.03	1.80	24.61	(9.13)	(2.24)	5.79	6.76	12.35	8.51
	6 Russell:Midcap Growth	15.66	10.05	2.34	30.26	4.16	11.91	14.76	11.60	15.09	10.32
	7 Russell:Midcap Value	13.35	4.64	1.13	19.95	(18.09)	(11.81)	(0.54)	3.32	10.29	7.00
	8 Russell:2500 Index	14.55	7.39	2.89	26.56	(11.05)	(4.70)	4.08	5.41	11.46	7.85
	9 Russell:2500 Growth	16.03	10.44	3.68	32.87	2.02	9.21	12.10	9.57	14.45	10.07
	10 Russell:2500 Value	13.22	4.57	1.86	20.60	(21.18)	(15.50)	(2.60)	1.85	8.81	5.76
	11 Russell:2000 Index	13.74	6.51	3.53	25.42	(12.98)	(6.63)	2.01	4.29	10.50	7.01
	12 Russell:2000 Growth	14.89	9.45	3.84	30.58	(3.06)	3.48	7.86	6.86	12.92	8.85
	13 Russell:2000 Value	12.34	2.87	2.90	18.91	(23.50)	(17.48)	(4.35)	1.26	7.82	4.97
	14 S&P:500	12.82	4.76	1.99	20.54	(3.08)	7.51	10.73	10.73	13.99	8.83
	15 S&P:400 Mid Cap	14.18	7.31	1.26	24.07	(12.78)	(6.70)	2.39	5.22	11.34	8.21
	16 S&P:600 Small Cap	12.70	4.31	3.74	21.94	(17.85)	(11.29)	0.56	4.48	11.24	7.65
	17 MSCI:ACWI ex US	7.58	3.27	4.52	16.12	(11.00)	(4.80)	1.14	2.26	4.97	4.44
	18 MSCI:EAFE	6.46	4.35	3.40	14.88	(11.34)	(5.13)	0.81	2.05	5.73	4.09
	19 MSCI:EM	9.16	0.77	7.35	18.08	(9.78)	(3.39)	1.90	2.86	3.27	6.33
	20 MSCI:ACWI	10.71	4.35	3.20	19.22	(6.25)	2.11	6.14	6.46	9.16	6.42
FIXED INCOME	21 Blmbg:Aggregate	1.78	0.47	0.63	2.90	6.14	8.74	5.32	4.30	3.82	4.39
	22 Blmbg:Gov/Credit	2.23	0.58	0.87	3.71	7.21	10.02	5.87	4.74	4.13	4.50
	23 Blmbg:Credit	4.58	1.63	1.83	8.22	4.82	9.07	6.14	5.54	5.24	5.26
	24 Blmbg:Corporate High Yld	4.51	4.41	0.98	10.18	(3.80)	0.03	3.33	4.79	6.68	6.84
	25 Blmbg:Municipal Bond	(1.26)	3.18	0.82	2.72	2.08	4.45	4.22	3.93	4.22	4.28
	26 Blmbg:US TIPS	2.78	0.30	1.12	4.24	6.01	8.28	5.05	3.75	3.52	4.00
	27 Blmbg:Glob Agg ex USD	2.04	0.30	1.01	3.38	0.61	0.71	2.52	2.89	1.98	2.85
	28 S&P:LSTA Levlg Loan	4.50	3.80	1.14	9.70	(4.61)	(1.99)	2.07	2.89	4.16	4.28
	29 ML:US Treasuries 1-3 Yrs	0.04	0.07	0.03	0.13	2.94	4.07	2.69	1.84	1.33	2.29
	30 LIBOR - 3 Month	0.06	0.03	0.02	0.11	0.52	1.57	1.97	1.48	0.90	1.72
	31 3 Month T-Bill	0.01	0.00	0.01	0.02	0.60	1.63	1.77	1.19	0.64	1.34
REAL ASSETS	32 Blmbg:Commodity TR Idx	(1.54)	4.34	2.28	5.08	(19.40)	(17.38)	(6.14)	(7.69)	(5.82)	(4.34)
	33 GS Commodity Index	(9.67)	16.37	5.09	10.47	(36.31)	(33.90)	(8.71)	(12.54)	(8.53)	(8.40)
	34 MSCI:US REIT Index	8.24	0.18	3.02	11.70	(18.45)	(12.87)	0.08	4.08	9.06	5.99
	35 Alerian:MLP Index	49.62	8.95	(7.87)	50.18	(35.71)	(41.43)	(16.79)	(12.85)	(1.41)	2.64
	36 DJB:Gbl Infrastructure	8.33	4.37	(1.34)	11.55	(11.81)	(5.99)	2.79	3.90	9.69	8.19
	37 US DOL:CPI All Urban Cons	(0.67)	0.00	0.55	(0.12)	0.32	0.65	1.72	1.56	1.69	1.90