INVESTMENT LETTER **JULY – AUGUST 2020**

Global Stocks and the Economy

The news continues to be overwhelming and devastating. Deaths from Covid-19 in the United States have moved above the 135.000 people, nearly 50 million Americans have filed for unemployment insurance and the country is in state of grief and rage over racial injustice. It's getting easier to understand the skepticism associated with the perceived disconnect between real life pains on Main Street and the resilience of Wall Street.

The economy entered a recession in February and it dropped 5% in the first quarter. Industrial production and retail sales had the worst drops in 101 and 73 years, respectively. Unemployment is at levels not seen since the Great Depression when unemployment reached 26%.

It's expected to stay high. If so, it will reinforce that we are indeed in a depression or headed for one. This has resulted in unprecedented money creation. In fact, the Fed's balance sheet is now at a new record high of USD 7 trillion. This is an increase, which is already three times larger than the rise following the 2008 financial crisis. This in turn, will likely fuel inflation, sooner or later, probably following the recession. Some are calling for stagflation (slow economy and inflation). But whatever the outcome, the soaring cost of food to the highest levels in 46 years could be a sign of things to come.

For many years the US has depended on foreign investors to finance their deficit spending by buying US governments bonds, but now , with higher tensions, they have been selling their bonds by the most this century. This goes for China and Saudi Arabia to name just a few. This means, the Fed's going to have to raise interest rates to attract foreign buyers back to the fold. And if inflation perks up downstream, this will only add fuel to the fire because interest rates and inflation tend to rise together.

So , where are the stock markets going?

Monetary and fiscal stimulus, and more recently news on virus treatments/vaccines, have fueled an epic run up from the lows. Ultimately though, equity prices depend on economic conditions and corporate earnings. There is the risk that the stock market is not accurately reflecting second-order and longer-term economic impacts of the virus and attendant economic shutdown (including bankruptcies and temporary layoffs becoming permanent job losses). There is also a risk that the stock market is not accurately reflecting the weakness yet to be fully felt in corporate earnings.

That said, it's always wise to heed the market's messages. Fiscal and monetary support has been unpredecented and could ultimately overcome the damage to the economy. Our advice to investors trying to navigate these uncertain waters has been consistent this year: rely on tried-and-true disciplines like diversification and regular rebalancing. Keys to long-term investment success do not rely on the precise timing of market tops and bottoms. Investing is , and always has been, a process over time. It should never be about moments in time.

Stay tuned!

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