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ASSET MANAGEMENT

October 16, 2020

In this month's Insight, Nicholas Bohnsack addresses the signposts we've used since the onset of the pandemic to better understand the depths of the decline, breadth, and durability of the ensuing recovery.

Nicholas Bohnsack is the President & Chief Executive Officer of Strategas Asset Management and a Managing Director of Baird.

No Rest For Investors

We've written at length on the vagaries of 2020, but the last month has been notable for the volume and disparity of incoming that investors have had to process. While the broad market reaction in March and April was certainly more acute, understanding why and the implications of why was far easier. Six months on, investors appear to increasingly have a "handle" on the virus. This is not to suggest that the virus is no longer an issue (it is) or that the necessary amount of point-of-care testing is available (it isn't). It is certainly not meant in any way to diminish the very real loss so many people have experienced at the hands of Covid-19. It is only to posit the notion that as society learns to live with the virus, however unpleasant, the impact that its ebb and flow has had on the markets – specifically, the equity market – has diminished. In its place is a menu of important issues, any one of which investors would typically digest with exhaustive care away from the Sturm und Drang of the capital markets. Increasingly, they just don't have the time before another substantive issue comes into view.

You could argue that, in it's simplest form, the endgame for investors is to keep their financial goals in sight and to react appropriately to the time ladder of risks to ensure they remain on track. At no point in the cycle is this trickier than at the top, which generally comes without warning inasmuch as we're blind to deteriorating economic conditions, as well as off the bottom. This second inflection point, "off the bottom," is what investors are grappling with today. In a typical business cycle, the variance between "trailing data," reflecting the period just passed, and the "forward data," reflecting expectations for future periods, is never wider than during the recession-to-recovery transition. Put simply; it is the point in the cycle at which the trailing data are at their worst and the outlook – at least relatively – is at its strongest. Anecdotally, we see this when our conversations with clients turn from interpreting events and data in their moment (as was the case in March and April) towards interrogating the merit of the assumptions propping up the longer end of the forecast curve as it steepens – even if it's a year or two ahead. A shorter field of vision generally accompanies uncertainty; a longer field of vision is generally accompanied by optimism.

So, inasmuch as the equity market remains a discounting mechanism of expected risk-adjusted returns and, given that uncertainty about the virus and its impact on the markets appears to be easing on the one hand while signs the economy continues to gather momentum intensify on the other, it is interesting that investors have not become more universally bullish. What is holding the market back?

One answer would seem to be the firm grasp that competing all-or-nothing political outcomes have on investors' mindshare. Without wading too far into the political, if there was one takeaway from the debate several weeks ago between President Trump and former Vice President Biden, it is simply that everything has become politicized. And while it is perhaps obvious that the volume of political vitriol and associated legislative jockeying would increase in an election year, the fact that neither party seems willing to concede an inch in the obvious service of the common good leaves us with little hope that the election itself – regardless the outcome – will foster timely reconciliation on the pressing points of policy being debated. This is particularly notable in two key areas that will likely have implications for the recovery well beyond Election Day, specifically the natural tension inherent in weighting freedom vs. safety as it relates to municipal lockdown and reopening, as well as the size and target of additional fiscal stimulus. This strikes us as important, given the economy's arguable reliance on reopening and the provision of additional fiscal stimulus to recover more robustly.

Readers of our work will recall the list of four signposts we've used since the onset of the pandemic to better understand the depths of the decline, breadth, and durability of the ensuing recovery: 1) containment of and a cure for the virus; 2) an understanding of trough levels of activity and areas of acute dislocation; 3) a reasonable forecast for the slope of the normalized forward demand curve; and, 4) the driver (or drivers) of organic growth available to transition the economy from recovery to expansion. Of the four, it seems that only the second marker, "an understanding of trough levels of activity and areas of acute dislocation," can be checked-off. So, where does that leave us? While it may seem stale, readers of these pages will know that we remain comfortable maintaining both an above-benchmark allocation to Equities (64% vs. 60%) and Cash (9% to 2%). If

market action in September is any indication, there is no incentive to position portfolios decidedly in one direction (i.e., bullish) or the other (i.e., bearish). The economic backdrop appears to be improving, albeit in fits and starts, given the two governing issues we noted above (reopening and stimulus). This should be taken as a positive, but it is likely, in our view, that the easier part of the recovery is behind us. This invites a degree of caution.

The question we're most frequently asked by investors in our tactical portfolios is for our views on Growth vs. Value. In short, we continue to favor Growth over Value. This is due, in part, to the persistent unevenness of the recovery inasmuch as it is an acknowledgement of the dominant weights in the composition of the benchmark indices. Should the normalized forward demand curve (#3 on our list of signposts) steepen, particularly with support of organic drivers of growth to aid in the economy's transition from recovery to expansion (#4 on our list), then it's reasonable to reorient the portfolio towards Value. In the meantime, we're willing to wait.

Stay healthy. Stay focused.

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