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On January 20, federal health officials confirmed the first case of COVID-19 in Snohomish County, Washington, and by March 2, there were 80 confirmed cases in the US. On March 15, state governors started issuing public health orders to "shelter-in-place." In stunned reaction to this sudden economic freeze, the S&P500 Index declined from a record high of 3386 on February 19, to 2237 on March 23, the steepest sell-off in history (-34%). To counteract the virus, economic policymakers quickly responded with unprecedented monetary and fiscal stimulus; the S&P500 then soared over the next ten weeks, rising 44%, to 3230 on June 8, the fastest rise on record. The net result of this volatility in the first half was a decline of -3.1%, to 3100, still 8.5% below the record high.

The Federal Reserve plans to increase the money supply by $4 trillion this year; this compares to "only" $1.4 trillion in the first 2 ½ years of the last financial crisis. In addition, the Fed is supporting corporate and municipal bond markets and providing a lending facility for private businesses. Congress, in turn, enacted three stimulus packages worth $3 trillion, including relief checks (up to $3400 for an eligible family of four), payroll protection for employers, and higher unemployment benefits. Congress is now working on another $1-2 trillion package to help state and local governments and extend unemployment benefits, even though it has only spent half of the first $3 trillion!

Despite massive fiscal and monetary stimulus, the timing and strength of the re-opening of the economy remains uncertain. Large states like California, Texas, Arizona, and Florida are experiencing a surge in infections. Economic uncertainty is likely to persist until there is substantive progress on a vaccine. Several promising candidates are entering late-stage clinical trials this month; one or more could be available for emergency use before year-end.

This much economic uncertainty makes it difficult to assess market fundamentals. If S&P500 earnings decline 30% this year, as expected, then earnings would have to grow 40% to reach the record pre-COVID level in 2019. This may take two years, so the market looks expensive now. However, when interest rates decline to record lows, stock investors place more value on future earnings, and they are less inclined to buy fixed income. Low interest rates also support consumer spending on housing and autos and business investment.

Even after two months of strong job growth, total employment is 15 million (10%) less than it was before COVID-19. Paradoxically, under-employment is correlated with high stock market

returns, probably because there is ample labor to support economic expansion. Since 1974, during periods of at least 8% unemployment, the average annual return on common stocks was 25%. When unemployment was under 4.5%, the annual return was 8%. The current unemployment rate is 12%.

In the first half, the stock market was characterized by unevenness, as investors bought “COVID stocks” (such as online services and health care) and sold “re-opening stocks” (such as banks and industrials). We own a blend of both, but with a heavier weighting in the latter. Although our performance has lagged the S&P500, it compares favorably to an index more in-line with our strategy of investing in mid-capitalization stocks (such as the Russell 2500, as shown in your report). As the economy gains momentum in the second half, re-opening stocks (including midcaps) should outperform COVID stocks.

We included a client relationship summary (Form CRS) at the beginning of this report. Our Form CRS is a two-page summary of our services and fees. Please call us with questions or comments, or if there are changes to your financial goals, investment time horizon, or risk tolerance.