FIORI FINANCIAL GROUP

FFG Market Pulse Newsletter

2Q April 2020 Edition

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Latest Developments

We want to say, first and foremost, our thoughts are with everyone and hope their families are healthy and safe. To say the world has changed since February would be the understatement of the century. The globe is in the depths of the virus pandemic that has shut down countries, economies, travel, schools and kept many people stuck in their homes. At time of this writing, world-wide cases total more than 2,072,228 and 137,666 deaths. In the U.S., more than 639,664 confirmed cases and 30,985 deaths both stats according to Johns Hopkins. Due to the prolonged necessity of social distancing, the likelihood of a quick V-shape recovery for the economy has been swept away as the realization sets in that it will take time for the country to get back to normal. The reopening our country will require either increasing public comfort with the virus in generally accepting its effects or making testing and treatments readily available. Depending on the effectiveness of mitigation efforts and the seasonality of the virus will ultimately determine when the country will start to open. It is impossible to predict when this normality will slowly start to take place, but most seem to be focusing in on some sort of timeframe from May to July. It will be a slow process but eventually we will get there. The quicker we can get readily available and abundant testing capacity, the quicker the recovery can start. Test, Test and then Test some more!

Turning to the recent monetary and fiscal stimulus packages. The Federal Reserve, US Treasury and Congress acted very quickly (especially for Washington DC standards) as policymakers have put forth several packages to support individuals & small and mid sizes businesses. There will be a time in the future to debate whether those packages are best being served by the most in need. However, that time isn't now. There needed to be swift and historic levels of stimulus and that has taken place. The Payroll Protection Program (PPP) which seeks to help small businesses cover overhead expenses and retain workers, has seen exorbitant demand. Separately, the Fed unveiled $2.3 trillion in additional programs to bolster the economy, including a lending program aimed to benefit businesses as well as state and local governments. They will also be large buyers of Treasury, Mortgage backed Securities, Corporate & Municipal Credits. The Fed acted very swiftly and has indicated they are not finished if other tools are necessary. The Federal Reserve has probably taken the worst-case scenario off the table. The worst-case scenario was a lack of liquidity and credit to accompany a health/employment crisis. With the Fed making historic levels of liquidity available the system is now flush with available capital. This capital now needs to get into the proper hands to be able float small and medium size business and individuals until the country can slowly start to re-open for business. Ultimately these steps were necessary. Policymakers have attempted to help consumers, businesses and governments weather the storm until the economy can return to some form of normality.

So what does this all mean from a portfolio perspective? More then ever having a plan and knowing what you own is paramount during this time. As many of you know, we are fanatical when it comes to the clarity of our holdings and having a plan with regards to hedging the portfolio. We also focus on owning high quality companies with very strong balances sheets and high barriers to entry and historically strong cash flows. These are the type of companies that survive and then thrive in this type of environment. In addition, since we know what we own, we had no exposure to the hardest hit areas of the market, i.e. Airlines, Cruises Lines, Transports, Oil & Gas, Financials. These are also the times where planning with hedging becomes incredibly important for example having a gold position, cash and market neutral strategies. These types of strategies assist with reducing these drastic drawdowns we saw back in March. Finally, by having "dry powder" on the side to be able to take advantage of opportunity is key cog in portfolio management in times of volatility. As a country, we will exit this time differently in many ways then we entered. Certain industries and companies will be apart of the "new normal" going forward and present opportunities for portfolio additions with that dry powder.

Whats Next?

We obviously will see some historic economic data points over the coming weeks and months. Over the past four weeks, 22 million people have filed jobless claims. We will probably see the highest level of unemployment since the 1930s. Earnings expectations for the remaining part of 2020 and into 2021 will be reduced drastically. What remains to be seen is to how long these conditions will last. The markets priced in a steep, sharp recession in March given the unknown of the virus and its aftermath. In April, the markets have recently rallied on optimism that the data is peaking and on the enormous level of monetary and fiscal response.

There will be many industries that will take some time to recover. If we look back at past events it can give us some sort of guideline. U.S. air travel was shut down for three days after the Sept. 11, 2001, attacks. It took three years for the industry to recover despite toughened passenger screening and the creation of a new agency devoted to transportation security (The TSA). When home construction started tumbling in 2006, ahead of the financial crisis and recession, it was a full five years before the balance between builders and buyers was healthy enough to allow construction to start growing again. Certain industries will absolutely thrive in the new environment while some will take many years or may never get back to pre virus levels.

So what do we need to see for the country to open? Here is a listing of items that need to happen to have a chance to really start to move forward with opening of our economy.

Reasons for Stay at Home Orders	Status
Is Virus Peaking?	Not Yet but encouraging
Has Sentiment Bottomed?	Looks highly likely
Testing Capacity?	Limited at best
Monetary Response?	Yes, Fed is all in
Fiscal Response?	Yes, but not 100% complete
Protection Equipment Shortage?	Some progress but still limited
Hospital Capacity?	Better and improving

Phases of Sell Offs & Rebounds

History doesn't repeat itself, but it often rhymes. Looking back at the other historical sharp selloffs such as in the 1930s, 1987, 2000-2001 and 2008, all of them go through as a series of usually 3 phases. Those phases consist of:

Phase #1 – The sharp and swift decline caused by some drastic change in sentiment. In this case it was the very rapid of intensification of Covid-19 cases here domestically starting in late February and then Saudi Arabia and Russia tanked oil prices with continued supply to go along with the deterioration of demand. This is the phase where the trademark is indiscriminate selling. Selling pressure becomes incredibly extreme and volatility spikes to historic levels. In other words, everything is sold no matter how high the quality or the asset class. Phase #1 lasted almost 4 weeks and appears to have ultimately concluded at the low of the S&P on 3/23.

Phase #2 – Once Phase #1 exhausts itself, there is an oversold bounce that retraces a portion of that decline in phase #1. This is the Relief stage. There is a realization that the world isn't coming to an end and oversold conditions drive a reversal. This can last for days to weeks. As of this writing, we are probably towards the end of phase #2 or now entering the next phase.

Phase #3 – This is the realization phase. Once the bounce in Phase #2 slows, the markets must rationalize between long term optimism and short term economic and earnings data that will obviously be on the negative side. This is usually the longest phase in terms of time and comes with continued back and forth as weeks will trade between positivity and negativity. This is usually the stage where a re-test of the market lows is seen. However, in today's market, chances are we will not revisit those extreme lows of March because of the historic Federal Reserve intervention. However, we still have to deal with the uncertainty of the consumer as it will take some time to regain a normalized level of employment.

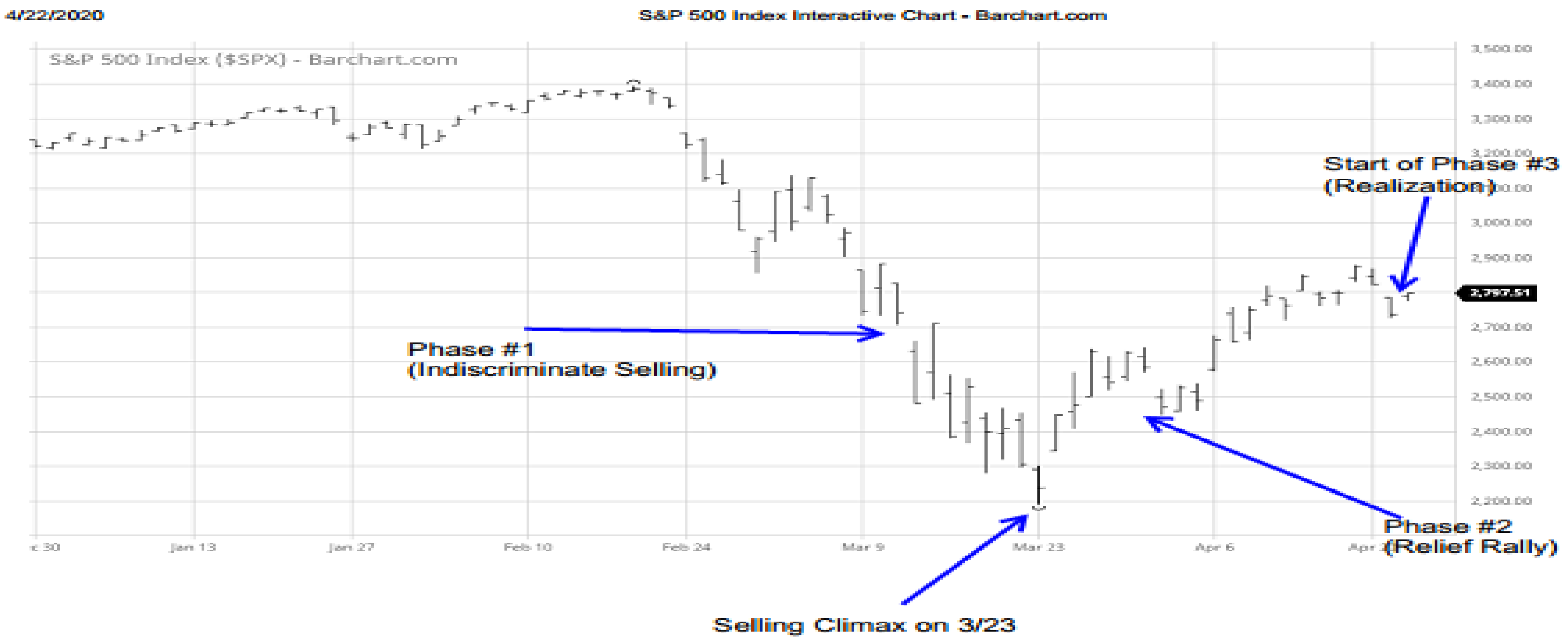
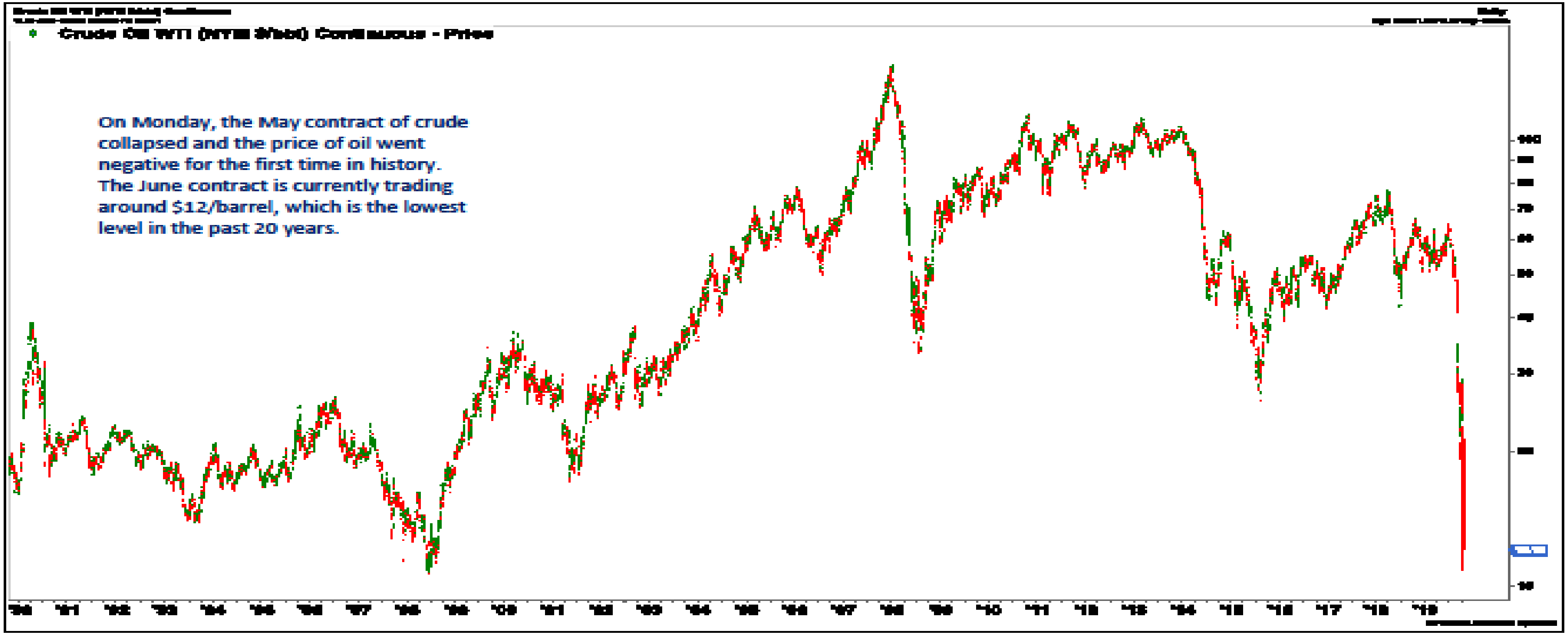


Chart of the Month

This week the price of the May Futures Contract for WTI Crude Oil(West Texas) traded negative. In other words, futures traders were willing to pay someone to take the oil off their hands. This is because in the futures market you must take physical delivery of the commodity once you reach a certain point at the end of the month. In normal times, industries like airlines or industrials would take the physical delivery and use the oil for the demand needs. However, since most planes aren't flying, and cars are for the most part off the road there is such a distortion in supply and demand that storage facilities of oil are filled to the brim. There is an extraordinary amount of supply and no demand to speak of.

Crude Collapse



Source: FactSet, Raymond James Equity Portfolio & Technical Strategy