consequent capital management

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Capital Markets Review and Outlook

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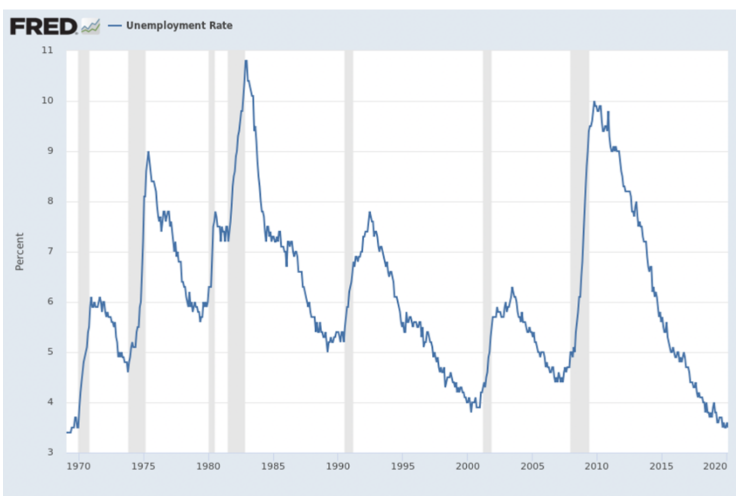
February 2020

Economy and Outlook

The rapid and relentless spread of the Covid-19 coronavirus has derailed the previously positive backdrop for world economic growth following the removal of major trade-related uncertainties at the end of last year. Although the rate of new infections and deaths from the virus have slowed in China, the global reverberations of the precipitous slowdown in the Chinese economy are profound. China accounts for around 1/3 of all global trade, which is 10 times greater than it was during the SARS epidemic almost 20 years ago. Manufacturers around the world are so inextricably tied to China's supply chains for a wide range of intermediate and finished goods that estimates from some economists for the world's lost output now exceed $1 trillion. The U.S. economy currently remains sturdy as reflected in the February employment report which showed job gains of 273,000 and upward revisions for January as well. The chart on the left highlights that the unemployment rate in the United States remains at its lowest levels in over half a century. However, there are mounting concerns about the future economic impact from the virus which is now present in many states across the country. While coronavirus containment efforts underway will slow the spread of the disease, they will also have a material negative effect on the economy, especially on small and medium-sized businesses which account for many jobs.



Governments and central banks across the world are moving swiftly and decisively to mitigate the damage from the coronavirus. For the first time since the Great Financial Crisis more than 10 years ago, the U.S. Federal Reserve acted outside a scheduled FOMC meeting and made an emergency cut in interest rates of 50 bp on March 3rd. Central banks in other countries have also cut official interest rates. Additionally,

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governments in several countries including China, South Korea, Japan, the United States and the European Union have started or are contemplating fiscal stimulus measures to combat the economic effects from the virus. Because much remains currently unknown about the coronavirus, especially its duration, uncertainty is high about the global economic impact. The key question is whether the effects of the virus could lead to a recession. If a global economic slowdown without a recession occurs, then we would expect a sharp economic recovery to follow a successful containment of the virus. The world, however, is the most interconnected it has ever been. As a result, it may be a challenge to successfully halt the spread of the virus until a vaccine is developed, which according to medical experts might take 12 to 18 months. The magnitude of the global coordinated monetary and fiscal actions that are being taken or are under consideration may, however, provide the interim measures to prevent a global recession.

Equity Markets

Equity market volatility spiked in February with the VIX index closing at 40, its highest level in 8 years as fears about the economic effects of the coronavirus weighed on investor sentiment. The broad domestic equity market represented by the Russell 3000 Index dropped sharply by -8.2% for the month which accounted for almost all of its year-to-date decline of -8.3%. Small Cap with a return of -8.4% was only 20 bp behind the performance of Large Cap in February. However, year-to-date, Large Cap is ahead by +330 bp. For the month, there was a marked differentiation by style. Growth outperformed Value across all capitalizations by +250 to +300 bp. Stock sector performance in February mirrored, for the most part, investors risk-off sentiment with Defensives outperforming Cyclicals. Energy and Financials were the worst performers with double digit losses for the month: -14.6% and -11.2% respectively. Energy was dragged down by the continued slide in oil prices as global demand declined due to the spreading coronavirus, while the sharp drop in interest rates weighed on banks. However, Technology, a Growth sector, was one of the better relative performers despite a decline of -7.3% in February as investors continued to favor growth names in the Technology space. Year-to-date, Technology was the best performing sector with a return of -3.6% compared to -8.3% for the broader S&P 500 index. Flight to quality and a stronger U.S. dollar weighed on international developed markets resulting in a return of -9% for the MSCI EAFE index. Emerging markets, however, outperformed following a dismal start to the year and were down about half as much with a return of -5.3%. Year-to-date, both developed and emerging markets underperformed the U.S. equity market by -260 and -140 bp respectively.

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Fixed Income Markets

February's flight-to-quality drove Treasury yields sharply lower as interest rates dropped by 20 to 47 bp across the curve. The yield on the 5-year Treasury broke below 1% for the first time in almost 7 years ending the month at 0.9%. The Treasury coupon curve steepened with the 2-year/10-year spread differential widening by 9 bp to end the month at +27 bp. However, the 3-month TBill/10-year spread, which is sensitive to market expectations for Fed policy changes, inverted further to -14 bp as the yield on the 3-month Treasury Bill closed the month at 1.27% compared to 1.13% for the 10-year Treasury Note. In contrast, at the end of 2019, this spread was +37 bp. In line with the steep decline in equity markets, corporate bond spreads widened sharply in February with the overall Investment grade credit index widening by +26 bp which led to -175 bp of underperformance compared to Treasuries. As is typically seen in times of flight-to-quality, the credit curve and the quality curve both steepened in February, as short and intermediate maturity corporate bonds outperformed longer maturity bonds, and Single-A rated and higher bonds outperformed BBB-rated issues. Sector relative performance was similar to equities with Energy the worst performing Investment Grade Sector as spreads widened 42 bp resulting in an underperformance of -342 bp. REITs was the best performing corporate sector with a spread widening of only 11 bp. The High Yield sector was hit hard in February with spreads widening by over +100 bp. While investment grade spreads also widened in February, this was offset by the sharp decline in Treasury yields and coupon yield. So, on a total return basis, the Investment Grade sector had a positive total return of +1.3% in February despite the +26 bp in spread widening. On the other hand, the High Yield sector had a negative total return for the month of -1.4%. Similar to other risk asset classes, Energy was the worst performer in the High Yield bond sector. While non-dollar government bond yields also declined as investors globally moved out of stocks and into the safety of government bonds, the yield declines, especially in developed markets were significantly less than the decline in U.S. Treasury yields. Additionally, the rise in the U.S. dollar was a headwind for non-dollar bonds. As a result, the non-dollar government bond market's return of -0.1% significantly lagged the +2.6% return for the U.S. Government bond market.

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		Returns as of 2/28/20 (In %)				
		Month	YTD	1 Year	3 Years	5 Years
Russell 3000®	US AllCap Equity	-8.2	-8.3	6.9	9.3	8.7
Russell 1000®	US Large Cap Equity	-8.2	-8.1	7.8	9.7	9.0
Russell 1000® Growth	US Large Cap Growth	-6.8	-4.7	15.1	15.7	12.4
Russell 1000® Value	US Large Cap Value	-9.7	-11.6	0.5	3.8	5.5
Russell Midcap®	US Mid Cap Equity	-8.7	-9.4	2.3	6.6	6.4
Russell Midcap® Growth	US Mid Cap Growth	-6.9	-6.0	7.9	12.6	9.1
Russell Midcap® Value	US Mid Cap Value	-9.9	-11.7	-1.4	2.2	4.4
Russell 2000®	US Small Cap Equity	-8.4	-11.4	-4.9	3.5	5.1
Russell 2000® Growth	US Small Cap Growth	-7.2	-8.2	-0.7	7.9	6.5
Russell 2000® Value	US Small Cap Value	-9.7	-14.6	-9.3	-0.8	3.6
MSCI ACWI ex-US	Global Equity ex-US	-7.9	-10.4	-0.7	4.2	2.2
MSCI EAFE	Global Developed Mkts Equity	-9.0	-10.9	-0.6	3.9	2.0
MSCI EM	Emerging Mkts Equity	-5.3	-9.7	-1.9	4.9	2.7
Bloomberg/Barclays US Agg	US Core Fixed Income	1.8	3.8	11.7	5.0	3.6
Bloomberg/Barclays US Interm. Agg	US Intermediate Fixed Income	1.3	2.5	8.4	3.9	2.9
Bloomberg/Barclays US Credit	US Corporate Bonds	1.4	3.7	15.3	6.5	4.8
Bloomberg/Barclays US MBS	US Mortgage Backed Securities	1.0	1.7	7.5	3.7	2.8
Bloomberg/Barclays US Corp HY	US High Yield	-1.4	-1.4	6.1	4.9	5.2
FTSE Non-US WGBI	Global Fixed Income ex-US	-0.1	1.0	5.7	4.2	2.6