



Level Four Capital Management WEEKLY INSIGHT

MARKET COMMENTARY

As we begin the trading week, markets continue to digest a mountain of information related to the ongoing COVID-19 crisis gripping communities across the globe. Here in the U.S., residents are beginning to understand the drastic measures taken by other countries to slow the spread of the virus which consists of school and business closures, and in some cases, entire communities on lock-down. Indeed, most will likely agree that terms such as unprecedented and unsettling are fitting under these circumstances.

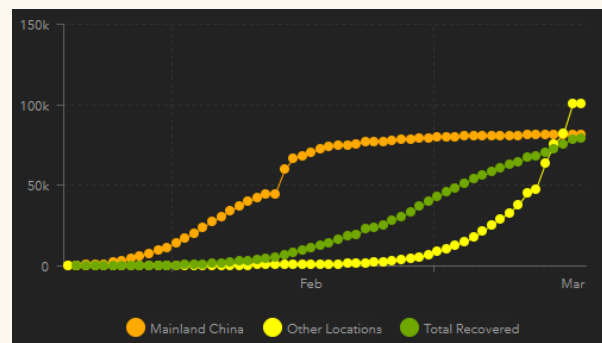
In this edition of the Weekly Insight, the Level Four Capital Management (LFCM) team will address a number of key themes impacting markets and provide our thoughts and observations, in addition to our routine recap of global markets. Below we address the following key themes: COVID-19 status, Fed and interest rates, and recession.

How does the COVID-19 Crisis compare to others?

For many investors, it is a struggle between Reality vs. Fear. Ultimately, no one knows the true extent of the damage caused by this crisis, both on the human and economic scale, and only time will tell. Unlike the Financial Crisis, this correction is event-driven and fueled by uncertainty and fear, versus a systemic issue.

While many of the headlines continue to stoke fear, resulting in unpredictable and emotional market reactions, we note a number of alternative views:

- South Korea reported no new virus deaths for the first time since February 15th.
- Active cases in China continues to moderate, and the number of **recovered** patients in the region continues to climb. (See chart at right)
- A potential Covid-19 vaccine moved into human testing Monday morning in Seattle with the first patient receiving the investigational vaccine which was developed by scientists at the National Institute of Allergy and Infectious Diseases in collaboration with biotechnology company Moderna.



Source: Bloomberg as of 03.17.2020

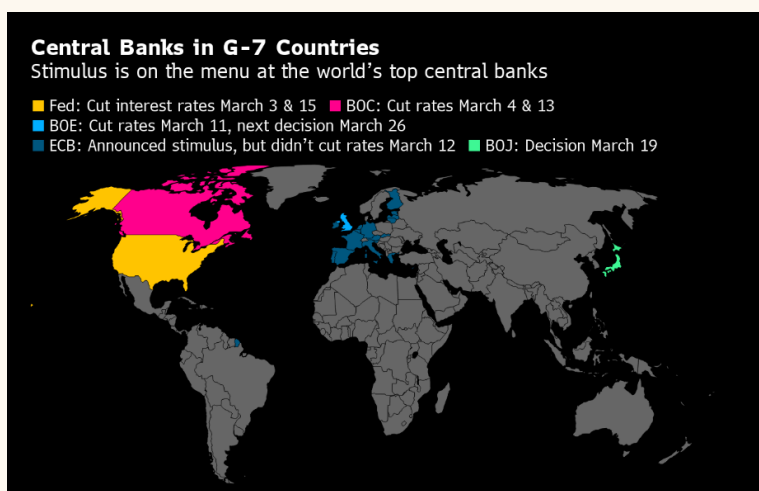
It is still too early to tell to the extent of which precautionary measures to slow the spread of COVID-19 across the U.S. and internationally have worked. However, officials rightfully so continue to urge people to adhere to social distancing and avoid public spaces in order to create less stress on our healthcare system. Simply put, it is easier for officials to manage a slow, steady, and prolonged health outbreak than it is for them to manage what is known as an “exponential curve”, one where the system would become overwhelmed due to lack immediate resources needed.

Federal Reserve and Interest Rates

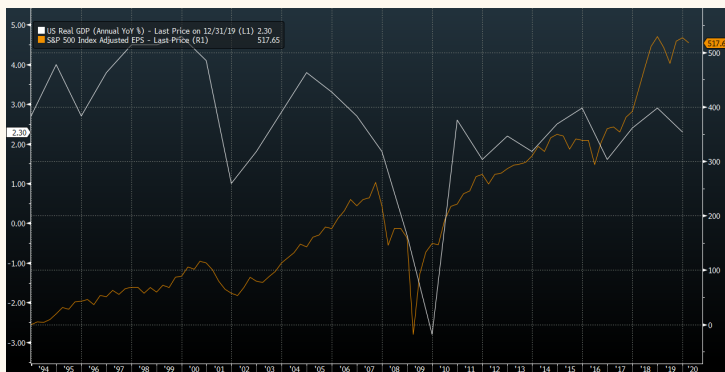
The Fed and central banks around the world continue to work in a coordinated effort in order to offset the negative economic effects of the Coronavirus. On Sunday, the Fed announced an emergency cut of 100bps to the Fed funds target rate, bringing the level to 0-0.25%. Additionally, they announced a large bond buying program of at least \$700B and said that banks are now allowed to borrow from the discount rate window for as long as 90 days. They also announced that the reserve ratio would be cut to 0%. These are significantly positive moves and we continue to see packages introduced as well as those still in discussion phases with very targeted objectives to aid individuals and businesses.

These coordinated efforts by central banks and governments around the world have resulted in the following proactive measures taken:

- The International Monetary Fund is ready to mobilize its \$1 trillion lending capacity to help nations counter the Coronavirus outbreak. As of Monday, the fund has \$50 billion in flexible and rapid-disbursing emergency funds for developing nations, with as much as \$10 billion available at zero interest rates. The fund also has about \$400 million in its Catastrophe Containment and Relief Trust to help poor countries with debt relief
- Central Banks continue to coordinate dollar liquidity around the world via swap lines
- Central Banks actions include: Bank of Japan (BOJ) buying for Japanese Government Bonds/ETFs, Reserve Bank of New Zealand (RBNZ) cut 25bps, Hong Kong cut 64bps, and Bank of Korea (BOK) cut 50bps



Source: Bloomberg as of 03.17.2020



Source: Bloomberg as of 03.17.2020

Will this crisis cause a recession?

Over the last few days, we've witnessed mounting speculation regarding the impact of the virus outbreak on earnings and GDP, and the increased probability of a recession. While the probability of a recession has indeed increased, this remains as a fluid environment and we have confidence that the event and its disruption will be relatively short-lived. If we look at the long-term correlation between the U.S. real GDP and S&P 500 adjusted Earnings Per Share (EPS) from 1994 to 2020, we see that the S&P 500 is a leading indicator and has roughly a four to six-month lead on the U.S. GDP. We believe that the market will functionally bottom before we see negative earnings. This means that by the time hard data comes out relating to the virus' impact, it will already be priced in.

Each day of this crisis brings a new round of information to digest and interpret. The LFCM team continues to proactively monitor client portfolios, balancing our disciplined investment process with our mosaic approach to research, aggregating a wide range of data points to help us arrive at strategic investment decisions. We will continue to provide our thoughts and insight throughout this process.

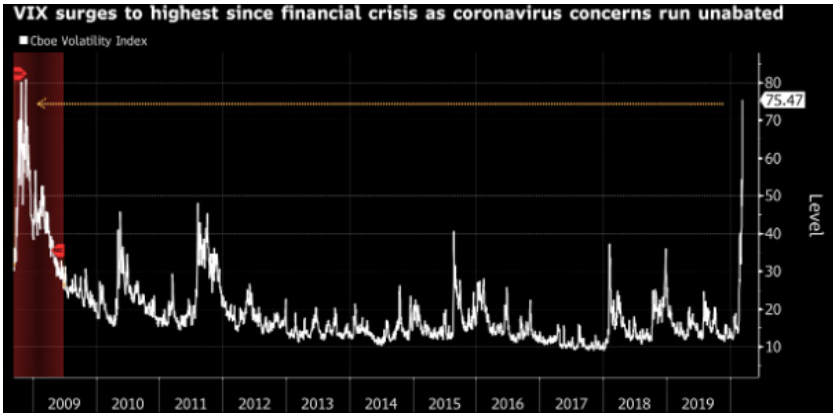
LAST WEEK MACRO RECAP

U.S. equities continued to come under pressure throughout the week led lower by Energy, Utilities, Materials, Industrials, Consumer Discretionary and Financials. The week's selloff did not discriminate as all 11 sectors closed lower. The energy sector fell 24% as Saudi Arabia and Russia engaged in a price war after the collapse of an OPEC+ deal while trying to agree on additional supply cuts in the wake slowing global demand. Utilities also lagged broader markets bringing into focus that even safe haven assets underperforming could be a sign of capitulation. Industrial names uninspired after a 35% pullback in industry leader BA and airlines continued to experience selling pressures hurting the space even further. Financials, and more specifically, Banks, continued their move lower after yields continued their collapse while insurers and asset managers were also hit as fears surrounding the Coronavirus grew. Despite finishing the week lower, Technology, Healthcare and Consumer Staples all outperformed. Golds status as a haven took a hit throughout the week as investors were seemingly forced to sell the asset in order to cover losses in other areas of the market. When all was said and done, gold fell 8.6% posting its largest one week drop since 1983. Bonds continued to surge higher with the risk-off trade as yields finished the week off as follows:

- U.S. 3M: .24%
- U.S. 5Yr: 0.72%
- U.S. 30Yr: 1.52%
- U.S. 2Yr: .49%
- U.S. 10Yr: 0.96%

SPXL1 Index		Analyze List	Settings	Group Ranked Returns
View		Members	Groups	Period
Movers		All	Period	Cust
Negative Price Return		Groups (11)	Return	Positive Price Return
		S&P 500 ECO SECTORS IDX	-8.79%	
		All Groups		
1	S&P 500 INFO TECH IDX	-5.20%		
2	S&P 500 HEALTH CARE IDX	-6.65%		
3	S&P 500 COMM SVC	-6.70%		
4	S&P 500 CONS STAPLES IDX	-7.93%		
5	S&P 500 REAL ESTATE IDX	-8.57%		
6	S&P 500 FINANCIALS IDX	-9.83%		
7	S&P 500 CONS DISCRET IDX	-10.47%		
8	S&P 500 INDUSTRIALS IDX	-13.12%		
9	S&P 500 MATERIALS IDX	-13.21%		
10	S&P 500 UTILITIES IDX	-14.26%		
11	S&P 500 ENERGY IDX	-24.28%		

Source: Bloomberg as of 03.17.2020



Source: Bloomberg as of 03.17.2020

Date	Last Price	Net Change	% Change
Fr 03/13/20	2,711.02	+230.38	+9.29%
Th 03/12/20	2,480.64	-260.74	-9.51%
We 03/11/20	2,741.38	-140.85	-4.89%
Tu 03/10/20	2,882.23	+135.67	+4.94%
Mo 03/09/20	2,746.56	-225.81	-7.60%

Source: Bloomberg as of 03.17.2020

Investors continued to get whipsawed by the extremely volatile moves as the S&P 500 posted its most volatile week since October 1987. S&P futures had a high-low range of 19.5% throughout the five days and saw wild swings in either direction, sometimes in excess of 12% on a given day. Last Thursday, March 12th, the VIX surged closing just over 75, its highest level since 2008 as the S&P 500 posted its largest one-day loss since 1987, closing 9.51% lower on the session. The following day markets rebounded by 9.29%, gaining over 1K points in the final 30 minutes of trading as President Trump and CEO's of various healthcare companies addressed the nation regarding the current Coronavirus outbreak. Overall, bullish talking points remained limited and many of the headlines revolved around the volatile moves lower. Bank of America's Michael Hartnett mentioned various statistics in the firm's weekly Flow Show report, noting the 16 days from peak to U.S. equity bear market (decline of 20%) was the fastest ever and was comparable to the 1929 and 1987 declines. The report also noted that global market cap loss over the past three weeks has been \$16T. With the decline in equities on Thursday, P/E's fell to 17 from just above 22 last month, contracting close to 24%. According to strategists led by Gina Martin Adams, this is in line with the average fall of 24.5% during the past six growth scares.

The week was dominated by headlines surrounding:

- Travel restrictions
- Work closings
- Event cancellations
- Public gatherings
- School closings

Many of the measures taken are expected to continue and, in some cases, become even more restrictive in the coming days/weeks. The World Health Organization finally declared the Coronavirus a global Pandemic last week as President Trump announced travel restrictions from Europe to the U.S. for 30 days in a bid to help slow the spread. Furthermore, essentially all collegiate and professional sports were suspended until further notice while various states have decided to take even more restrictive measures closing down restaurants, bars and other non-essential businesses.

Central banks continued to step up their policy response's as:

- The Fed announced on Thursday that it would provide \$1.5T in temporary liquidity
- The Fed announced it would also be purchasing a wider range of maturities along the curve as part of their monthly purchases
- European Central Bank (ECB) left rates unchanged however raised their QE authorization by €120B through year-end
- Bank of England (BOE) announced a 50bps cut to 0.25% and a 100bps reduction in the counter-cyclical buffer for banks to 0%
- Bank of Japan (BOJ) announced they would buy ¥200B (\$1.9B) of Japanese Government Bonds with maturities of five to ten years while also injecting a ¥1.5T in two-week lending

Even as global central banks continue to approach the situation proactively, many investors are still awaiting the announcement of additional fiscal policy measures from the Trump administration to help offset the negative effects of the virus.

APAC - The SSE Composite Index closed the week down 4.8%. Industrials slid 5.4%, followed by conglomerates, down 4.6%. Defensive sectors that recently performed well were also impacted by the sell-off. Indeed, utilities finished the week down 3.9% and real estate tumbled 3.9%.

China's National Health Commission said during a press briefing that the peak of the Covid-19 epidemic has passed. Meanwhile, Shanghai government has decided that all travelers from Italy, France, Germany, Spain, Iran, South Korea and Japan must self-quarantine for 14 days upon their arrival. Limiting imported cases is one of the government's plan to contain the epidemic.

In an emergency meeting, the People's Bank of China (PBOC) announced its decision to cut the required reserve ratio (RRR) for some banks last week, in a move projected to inject \$79 billion in the economy. Qualified banks must meet inclusive financial targets set by the PBOC to take advantage of this liquidity boost.

In Japan, the prime minister said that the government will work closely with the BOJ to take "bold, unprecedented" measures to respond to the epidemic crisis. The BOJ moved its meeting initially scheduled for March 18th to March 16th. The Nikkei 225 finished the week down 15.99%.

South Korea is seeing a stabilizing trend with a double-digit decline of new cases over the last two weeks according to the Korea Centers for Disease Control and Prevention. Extensive testing combined with the use of technology were the catalysts to get the epidemic under control. General election to elect members of the National Assembly are expected to take place next month despite the outbreak. The Kospi index was down 13% last week, dragged by industrials, materials and financials.

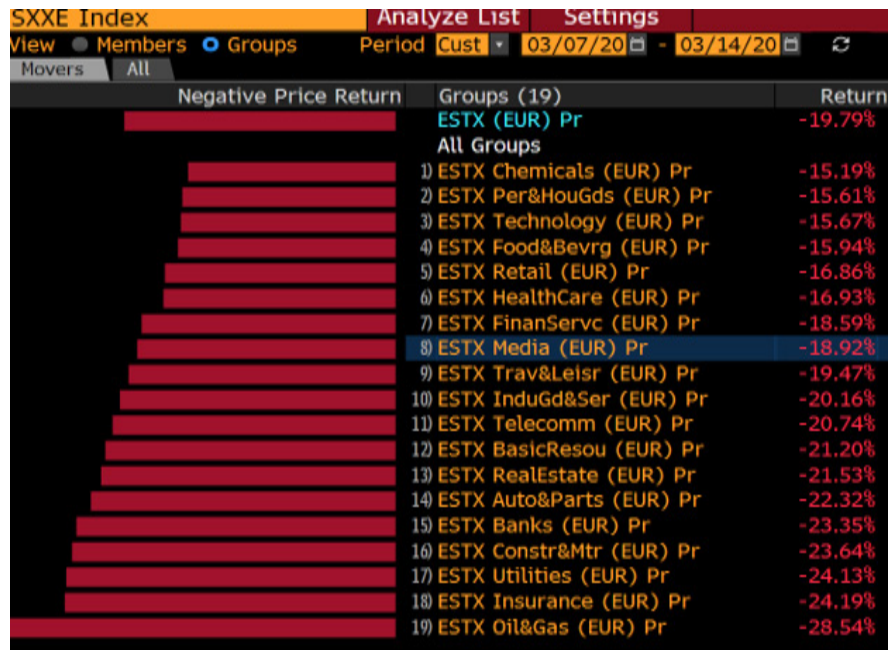
Europe - The Euro STOXX index plummeted 18.44% last week led by massive liquidation of energy stocks, down 29%, travel & leisure, down 25% and insurance stocks, down 23%. Surprisingly, utilities and telecommunication also performed poorly last week, losing 22% and 20% respectively.

The ECB decided to leave rates unchanged at -0.5%, despite expectations of 10bps cut. However, Christine Lagarde announced a stimulus package of \$135 billion through their asset purchase program to boost bank lending.

In Italy, the government is preparing a \$16.7 billion stimulus package to help businesses and populations affected by the virus. The country is still on lockdown and is the largest epicenter of the virus outside of China. According to the Italian Civil Protection Department, the total number of confirmed cases climbed to at least 20,603 on Sunday.

France has decided to close all non-essential locations such as restaurants, shops, cinemas, and nightclubs and told people to stay home in a move to contain the virus. The prime minister said that he expects companies to quickly accommodate employees so that they can work from home.

Spain has also decided to tackle the exponential growth of the virus by announcing a lockdown. All schools and universities are closed, along with restaurants, shops, and non-essential retail businesses.



Source: Bloomberg as of 03.17.2020

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