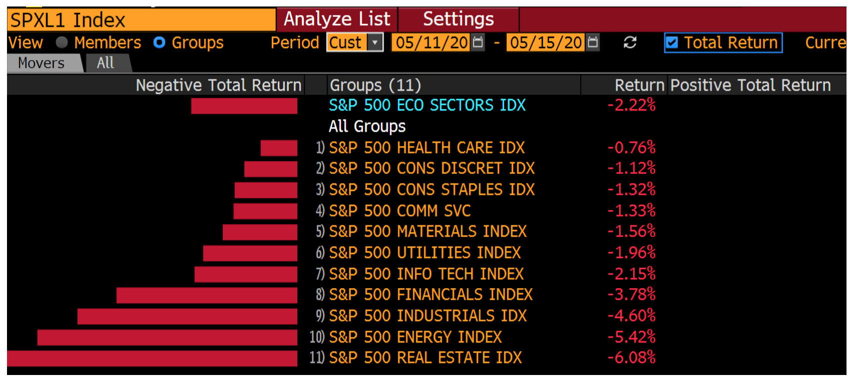
Level Four Capital Management

WEEKLY INSIGHT

MARKET COMMENTARY

LAST WEEK



Source: Bloomberg as of 05.19.2020

U.S. equities finished lower on the week and was led to the downside by Energy, Real Estate, Industrials, Financials, Materials and Utilities which all underperformed the broader market. Energy fared the worst despite WTI crude rising more than 19% on the week and pared gains after several weeks of rallying. REITs sold off sharply with the retail and hotel linked names coming under the most pressure, while Industrials lagged with another selloff in airlines. Financials continued their recent bout of underperformance with banks being the major lagging factor amid negative rate worries, as the Nasdaq Bank Index closed down 9.8% over the five days. Tech held up better than initially thought, however Semis were hit due to ongoing U.S.-China trade tensions. Healthcare was the only sector to finish higher with strength in biotech, big pharma and some managed care names. Treasuries were mostly stronger throughout the week with slight curve flattening as the Federal Reserve kicked off their Fixed Income ETF buying program. According to data published Thursday, the Central Bank bought $305 million worth of ETF's in the first two days of its historic intervention into U.S. corporate debt markets. Per the program's announcement, the Fed plans to make both direct purchases of corporate bonds, as well as ETFs invested in the asset class, including potentially some sub-investment grade debt.

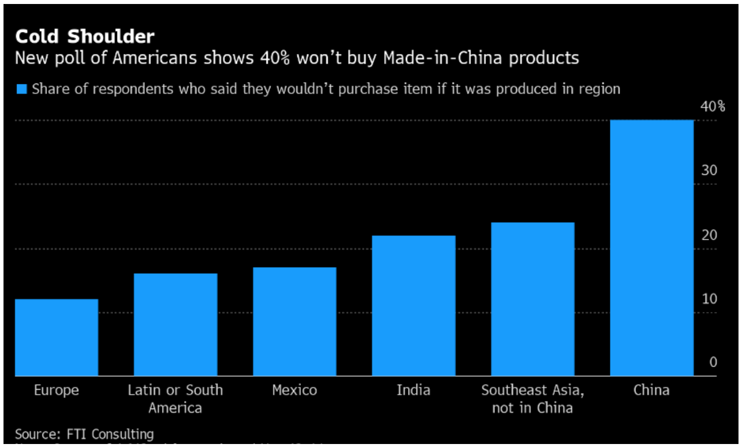
There was no specific catalyst behind the move lower, however, it came as various high-profile investors gave additional cautious comments and others continued to note the disconnect between the recent rally and the weak macro data being released. Weak economic data throughout the week included:

- A record 16.4% m/m decline in April retail sales
- A record 0.4% m/m decline in April core CPI
- An increase of 3 million initial claims from people pushing total job losses since the start of COVID-19 to ~36M

Most of the recent data and commentary continued to fit the theme surrounding skepticism of a V-shaped recovery and investors scrutiny on the quality of the rebound. However, even as uncertainty persists, the bull narrative continues to remain intact with many believing further moves to the upside are possible, citing:

- Unprecedented fiscal and monetary policy support
- Improved credit market functioning
- A fear-of-missing-out (FOMO) trade
- Signs of a bottoming in global economic activity
- A 2021 earnings rebound
- The ongoing reopening push by various states and countries

U.S.-China tensions flared up again this week as The White House continued to disapprove of China's handling of the Coronavirus outbreak. President Trump said he could scrap the whole U.S.-China relationship and save $500B. Additionally the President implemented new export restrictions on semiconductors, taking aim directly at Huawei, which many believed would only anger Chinese officials. Prior to adding the restrictions on the company, China announced they could activate their "unreliable entity list", restrict or investigate large U.S. companies such as Qualcomm, Cisco Systems, Apple, and even suspend purchases from Boeing.



Source: Bloomberg as of 05.19.2020

Despite tensions ratcheting up in recent weeks, many believe the current environment will remain just a war of words. Abandoning the phase one trade deal could ultimately jeopardize any global economic recovery, and would inflict more harm than good going into the election later this year. Tensions are expected to stay elevated, causing the potential for further investor uncertainty and volatility as the country remains a high-profile target on the world stage for their involvement in the global pandemic. According to a recent Bloomberg report almost 40% of Americans said they will not buy products from China citing a survey of 1,012 adults conducted May 12-14th by Washington-based FTI Consulting firm. The next closest was India (22%), Mexico (17%) and Europe (12%), while 78% of respondents said they would be willing to pay more for the products if the production was shifted out of China.

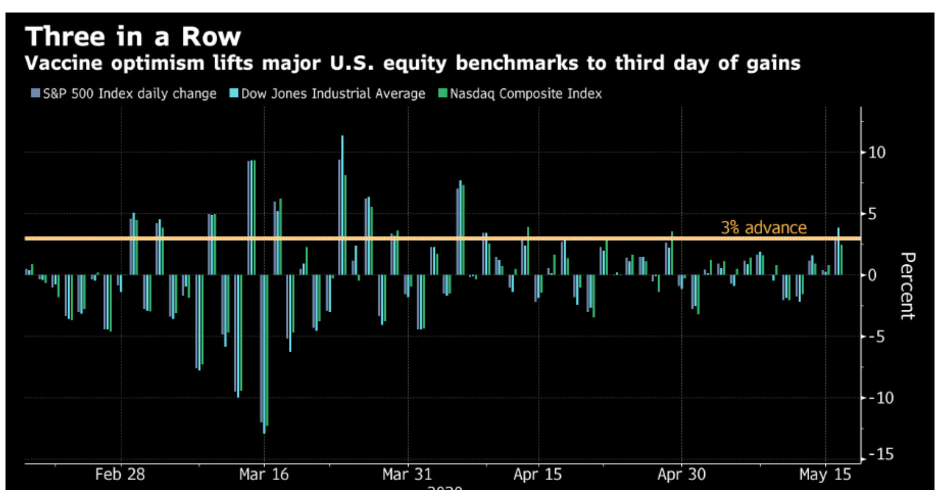
Reopening headlines continued to dominate news; however, the vast measures being taken continued to vary. Los Angeles, New York City, Germany, and China all saw further lockdown measures being extended, while the Wisconsin Supreme Court struck down the governor's latest stay at home order, and Georgia continued to push forward overcoming the initial worries of reopening too fast too soon. It was a very busy week of Fed-speak, however it did little to move markets. The most notable comments came from Fed Chairman Powell who pushed back against negative rates and lobbied for additional fiscal policy support. House Democrats continued to push forward with a fifth Coronavirus stimulus package which would encompass nearly $3T in additional aid. However, the lack of bipartisan support made it evident there was never really a chance the bill would pass the Senate.

Additional color from one of our trade desk partners showed the following trends for last week:

- Industrials and financials were net neutral for the week, while all other sectors were net sellers
- Tech, Financials and Healthcare made up 50% of all trading volumes on the desk last week
- Market volume picked up week over week, with the daily average climbing back above 11.5B shares
- Off exchange volumes remain elevated in the 40-45% range just as we have seen the past few weeks

THIS WEEK

U.S. Equities finished notably higher on Monday after experiencing their largest weekly percentage decline in almost two months last week. The move higher marks the third straight session where the S&P, Dow Jones, and Nasdaq all finished higher. The S&P finished higher by 3.15%, posting its best day since April 8th and closed at its highest levels since March 6th. All 11 sectors in the S&P finished in the green led by Energy, Industrials, Financials, Real Estate, Materials and Utilities, which all finished up over 4% on the day, while the average move across S&P members was 5.5%. The Dow Jones closed up 3.85% led by heavyweight Boeing which finished up by 12.87%.



Source: Bloomberg as of 05.19.2020

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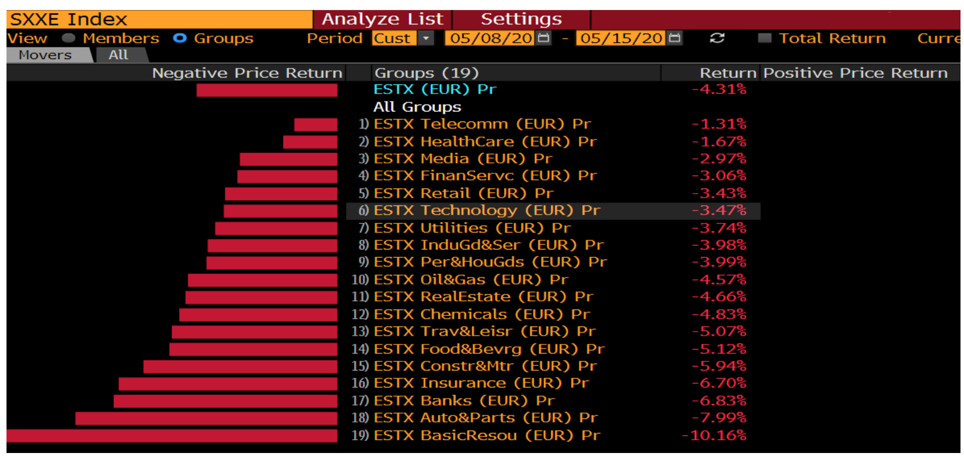
Value was a big performer relative to growth on Monday, outperforming by 1.67%. Despite the outperformance over the course of the day, valuations for U.S. growth stocks continue to show a large spread over value stocks, based on rolling relative price-to-earnings ratios for next year, illustrating that investors have yet to shy away from growthier names in the current market environment.

The move higher in markets came as Fed Chairman Powell gave an interview on 60 Minutes Sunday night. The Central Bank governor gave investors a reason to be optimistic stating the Fed has not exhausted their options and that there is no limit to what the Central Bank can do within their lending programs. Additionally, he said "in the long run, and even in the medium run, you wouldn't want to bet against the American economy. This economy will recover. And that means people will go back to work. Unemployment will get back down. We'll get through this." The comments pared with Moderna, Inc's (MRNA) positive Coronavirus vaccine trial data, which showed their treatment produced COVID-19 antibodies in all 45 participants and that the vaccine was generally safe and well-tolerated, helped renew global optimism. According to the New York Times, Moderna's Chief Medical Officer said if trials continue to go well, the vaccine could be in widespread use by end of 2020 or early 2021.

THIS WEEK INTERNATIONAL

Europe - The Euro STOXX Index was down 4.31% last week. Auto & parts and banks decreased 7.99% and 6.83% respectively.

Christine Lagarde wrote a letter last week to members of the EU parliament regarding monetary policy. She reiterated that the European Central Bank's (ECB) commitment is to continue "purchasing public and private sector bonds in large volumes via the Pandemic Emergency Purchase Programme (PEPP)." She also added that ECB's "new targeted lending facility provides up to €3 trillion in liquidity to banks at a negative rate, which can be as low as -1%, the lowest rate the ECB has ever offered."



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France and Germany proposed a €500 billion rescue fund to foster a fast recovery from COVID-19 in the European Union. According to the proposal, the most heavily impacted industries and regions will be able to apply for grants. Angela Merkel said that the plan was a short-term solution and that a long-term solution will be discussed later.

In the UK, Transport Secretary Grant Shapps announced that £2 billion will be deployed to restore infrastructure and build a network of fast charging stations for electric cars. The FTSE 350 Index decreased 2.51% last week, dragged by REITs down 8.23% and Insurance, down 7.76%. According to the latest Yougov poll, 46% of Brits believe Prime Minister Boris Johnson has gone too far with lockdown easing, while 10% think the steps do not go far enough.

APAC - In China, the Shanghai Composite Index decreased 0.93% last week, dragged by Real Estate and Utilities, down 2.11% and 2.02% respectively. The Chinese Yuan lost three cents on the U.S. dollar last week and closed the week at ¥7.10 CNY. The 10-year government bond yield ended the week at 2.65%, up from 2.61% a week earlier.

In Japan, the Nikkei 225 Index was down 0.70% last week, dragged by banks and industrials. The Japanese Money Supply M1 increased 7% year-over-year in April, while M2 increased 3.7% during the same period. Bank of Japan's governor Haruhiko Kuroda said that the central bank will keep focus on providing liquidity to corporations. He added that there is no current need to start purchasing municipal bonds.

In South Korea, the KOSPI Index was down 0.95% last week. Transport & Storage decreased 4.15% while Iron & Metals decreased 4.75%. Exports of semiconductors dropped 14.95% year-over-year in April.

South Korea's government is encouraging farmers in rural areas to adopt smart farm technologies to cope with the shortage of manpower.

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