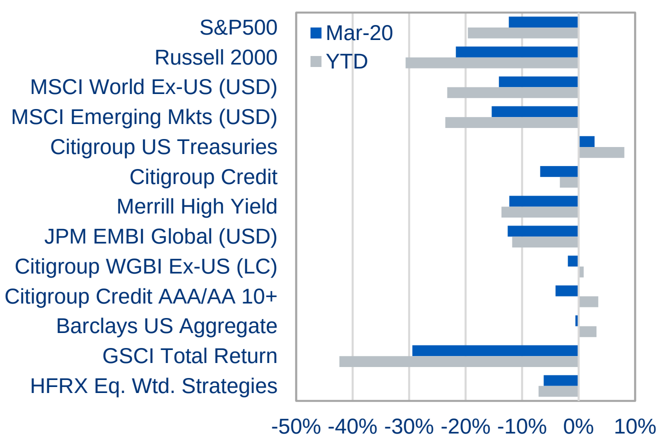
Global Market Review

Macro Summary

Measures to contain the Coronavirus have put the global economy in a medically induced coma. The suddenness of the collapse in employment and output is unprecedented. The longer the coma, the higher the economic cost. Uncertainty about the timing of the eventual economic revival and the speed with which activity can recover is roiling financial markets. Equity market volatility spiked to record levels in March. Global equity markets fell between 20-25% in the first quarter and commodity prices plummeted, led by a 66% fall in oil prices. Safe haven assets rose. U.S. Treasuries, especially at long maturities, gained as did the U.S. dollar, which appreciated particularly strongly against emerging market currencies.

Performance of Major Market Indices

Sources: S&P, MSCI, FTSE Russell, Barclays, Citigroup, Bank of America Merrill Lynch, J.P. Morgan, HFR, Bloomberg.



Coronavirus crisis triggers bear market.

Economies Shut Down for the Duration

The rapid spread of the Coronavirus and subsequent measures to contain the contagion roiled markets through March. Over a third of the world's population is currently under lockdown. The closure of non-essential businesses, travel restrictions, and other measures are taking a toll on output and employment. These measures are compounded by a sharp retrenchment in consumer spending and corporate investment induced both by fear and falling income. Major economies are at risk of a self-reinforcing downward economic spiral triggered by the interaction of demand shocks, supply shocks, and collapsing confidence. Recent economic indicators are worrisome. U.S. new unemployment claims rose in February at 4.5 times the previous most rapid pace. Coincident indicators of global economic activity also point to a sharp downturn. The OECD estimates that the median direct economic loss to advanced economy GDP is about 2% per month. Immeasurable indirect impacts would compound these declines. Emerging economies have been particularly hard hit by multiple shocks, including reduced export demand, collapsing commodity prices, a sudden stop of access to external financing, large capital outflows, and a strong dollar, as well as their own measures to contain contagion.

Global policymakers have rushed to respond to the crisis. The U.S. Congress passed a $2.2 trillion fiscal stimulus package providing funds to households, businesses, and the health care sector. The Fed slashed interest rates by 150 basis points to 0 – 25 bps, restarted its quantitative easing program, provided liquidity to poorly functioning domestic markets, eased access to dollar funding for foreign financial institutions, and initiated direct lending programs to U.S. corporations. Elsewhere, the ECB and Bank of Japan announced expansions to their asset purchase programs, while the Bank of England cut its benchmark interest rate by 0.5%. A wide range of European and Asian countries adopted fiscal stimulus packages. Governments around the globe are already planning additional extraordinary measures to keep the global economy on life support.

U.S. Equities Plunge into a Bear Market

U.S. equities took just 16 days to tumble 20% from their record high, easily eclipsing the previous record for swiftest fall into a bear market set in 1929 at 44 days (exhibit below). With losses of 10.9% in the month, the S&P 500 ended the quarter 19.6% lower. Amidst the rout, the VIX index of implied U.S. equity market volatility, also known as the fear gauge, soared to a record high in mid-March.

Stocks across all sectors and market capitalizations suffered steep losses. The energy sector led declines, falling over 50% in the quarter as oil prices collapsed. Stocks in the financial sector lost about one third of their value. The healthcare sector outperformed others, falling 12.8% in the quarter. Small cap

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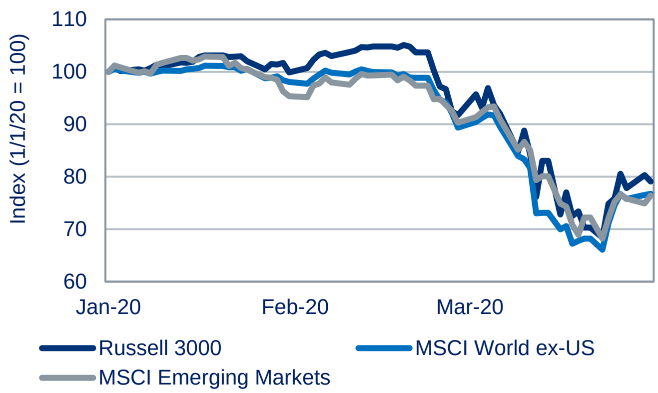
stocks struggled more than large, with the Russell 2000 index slipping 30.6% in the quarter, compared with the 20.2% decline of its large cap counterpart. Growth stocks (down 14.9%) outperformed value (down 27.3%).

Global Equities Plunge
Source: Bloomberg.



Global Equities Tumble

The selloff was even more pronounced in global equity markets. The MSCI World ex-U.S. index of developed market stocks fell 23.3% in the first quarter as economic activity ground to a halt and investor and consumer confidence collapsed. Both European and Japanese bourses lost about 24% as measures to contain the pandemic took their toll.

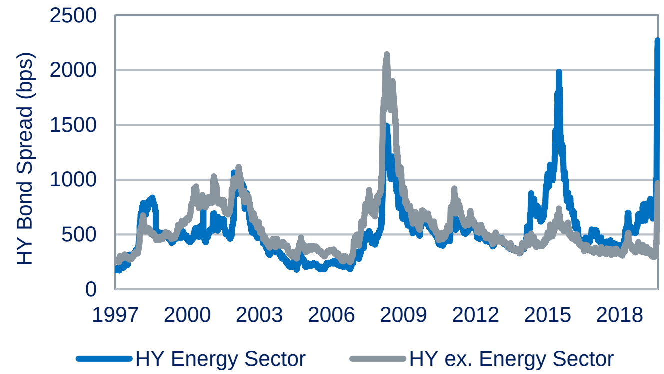
Emerging economies, especially those heavily reliant on short-term external financing appear vulnerable. The MSCI Emerging Markets index lost 23.6%, with bourses in Latin America (down 46%) leading the decline. Emerging market currencies, excluding China, fell to their weakest level since the 1990s as companies and investors rushed to build reserves in dollars in the face of diminishing access to external financing and a withdrawal of foreign capital. Russia's rouble has lost 23% of its value since January, while the South African rand and Mexican peso depreciated by 18% and 25%, respectively, over the same period. Chinese markets fared notably better than other emerging markets. The MSCI China index lost 10.7% in the quarter. Initial indicators suggest that China, the previous epicenter of the virus, has been able to contain its spread. The government is easing its quarantine measures, people are gradually going back to work, and output is picking up.

Fed Stabilizes Bond Markets

Amidst a flight to safety and fears of a sharp economic downturn, yields on safe haven assets hit all-time lows during the quarter. The yield on the 10-year U.S. Treasury note briefly touched 31 basis points intra-day, and the 10-year German bund yield fell to -55 basis points. Real yields on 10-year TIPS also reached record lows, reflecting the market's expectations for long-term disinflationary pressure from the downturn in economic activity. Inflation in the U.S. is now priced by the TIPS market to average less than 1% over the next 10 years, a post-GFC low.

Elsewhere, credit spreads rose sharply, with spreads on high yield bonds in the energy sector reaching historical extremes (exhibit below). U.S. high yield bonds lost 13% in the quarter, and there were a record number of "fallen angels", formerly investment grade bonds downgraded to high yield. The Fed stepped in to help calm investors, taking the unprecedented step of announcing that it would begin to buy investment-grade corporate bonds as a means of ensuring orderly markets.

High Yield Spreads Soar
Source: Bloomberg.



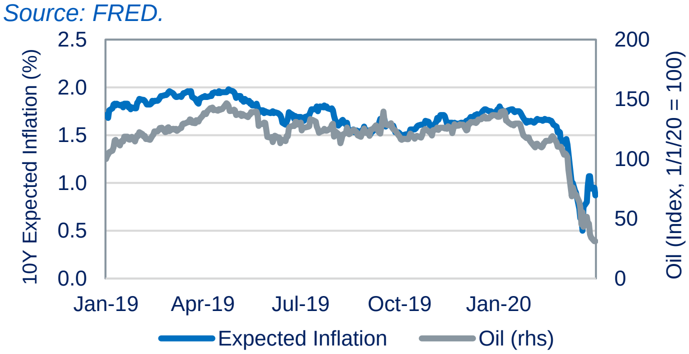
Equity Strategies Lead Hedge Funds Lower

The HFRX Equal Weighted Strategies Index fell 7.1% in the quarter, driven by weakness in directional equity and merger arbitrage strategies. Spreads on merger transactions widened considerably, reflecting heightened difficulty in financing and closing deals. Hedge fund managers have sharply reduced gross leverage to safeguard liquidity.

Oil Falls to 18-Year Lows

Oil prices crumbled from over $70/barrel in January to under $20/barrel in March as Russia and Saudi Arabia engaged in a bizarre version of Russian roulette in which all barrels are loaded and each player takes turn shooting himself in the foot. Their ill-timed price war flooded markets with supply just as demand tumbled on a sharp global economic decline. With oil prices down about two thirds, the GSCI commodity index fell 41% in the quarter.

Oil Slips on Slowing Demand and Surging Supply
Source: FRED.



Performance of Major Market Indices through 02-29-2020
Sources: MSCI, FTSE, Barclays, Citigroup, Bank of America Merrill Lynch, J.P. Morgan, S&P GSCI, HFR, Bloomberg.

	1-Month	QTD	YTD	1-Year	3-Year	5-Year
S&P500	-12.4%	-19.6%	-19.6%	-7.0%	5.1%	6.7%
Russell 2000	-21.7%	-30.6%	-30.6%	-24.0%	-4.6%	-0.2%
MSCI World Ex-US (USD)	-14.1%	-23.3%	-23.3%	-14.9%	-2.1%	-0.8%
MSCI Emerging Mkts (USD)	-15.4%	-23.6%	-23.6%	-17.7%	-1.6%	-0.4%
Citigroup US Treasuries	2.8%	8.1%	8.1%	13.1%	5.8%	3.6%
Citigroup Credit	-6.8%	-3.3%	-3.3%	4.9%	4.2%	3.3%
Merrill High Yield	-12.3%	-13.7%	-13.7%	-8.0%	0.3%	2.5%
JPM EMBI Global (USD)	-12.6%	-11.8%	-11.8%	-5.3%	0.4%	2.8%
Citigroup WGBI Ex-US (LC)	-1.9%	0.9%	0.9%	3.8%	2.9%	2.2%
Citigroup Credit AAA/AA 10+	-4.1%	3.5%	3.5%	16.6%	9.7%	6.5%
Barclays US Aggregate	-0.6%	3.1%	3.1%	8.9%	4.8%	3.4%
GSCI Total Return	-29.4%	-42.3%	-42.3%	-41.0%	-13.3%	-12.8%
HFRX Eq. Wtd. Strategies	-6.2%	-7.1%	-7.1%	-3.1%	-1.5%	-0.5%