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Hilliard Lyons Trust Market Commentary

This Too Shall Pass



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March 12. The market continued sharply lower, reaching a 34% drawdown before ultimately closing 24% below the peak at the end of March.

Bear markets are nothing new, but they are always painful. Feelings of fear and uncertainty are natural, especially given the catalyst for this bear market is the COVID-19 pandemic. What looked like a small, regional outbreak in January quickly turned into a global pandemic that threatens all aspects of society. Beyond the serious health implications for both individuals and the doctors and nurses on the front line providing treatment, the fallout from the pandemic has put significant strain on global supply chains, markets and economies.

A Damaged Economy

While essential to slow the spread of the disease, widespread government actions are causing a serious economic crisis. In a matter of weeks, the U.S. transitioned from a robust economy with record low unemployment and surging consumer sentiment to one that is almost completely shut down. This is unprecedented in our nation's history, and the swift change

"Fear incites human action far more urgently than does the impressive weight of historical evidence."
– Jeremy Siegel

After 11 years, the longest bull market in history came to an end with a screeching halt in March. The S&P 500 reached an all-time high of 3,386 on February 19, and it took just 16 trading days to plunge into a bear market, closing down 27% by

is stunning. Even after 9/11 and during the Great Recession of 2008-2009, restaurants remained open, children attended school, and sports and entertainment events continued.

The economic impact will be devastating. During the last week of March, weekly initial jobless claims hit 3.28 million, a record high since tracking began in 1967. In fact, this figure is nearly five times higher than the worst week during the Great Recession. In the coming weeks, we anticipate the release of some of the worst economic data this country has ever seen. At this point, we believe a recession seems inevitable.

Lessons Learned from the Financial Crisis

Both the federal government and the Federal Reserve moved quickly to shore up the system and prevent this crisis from snowballing. The Fed swiftly cut rates to 0%, announced an expansion of bond buying (Quantitative Easing, or QE), and initiated lending facilities to large and small businesses. These moves aim to provide enough liquidity to the markets to avoid a credit crisis.

Additionally, Congress passed the CARES Act in late March to provide \$2 trillion in economic stimulus including direct cash payments for individuals, an expansion of unemployment benefits, and relief for student debt. It also provides emergency loans and grants to encourage both small and large businesses to keep employees on the payroll and avoid widespread bankruptcies. This massive and immediate response was largely possible due to lessons learned from the 2008-2009 financial crisis.

Wide Range of Potential Outcomes

No one can accurately predict how long the pandemic will last and what its ultimate impact on the economy will be. The range of potential outcomes is enormous. In a worst-case scenario, a multi-month complete economic shutdown will put tens of

millions out of work, see many businesses fail, and severely stress the financial system for years to come. In a best-case scenario, the spread of the virus is successfully stopped in a matter of weeks and the rebound is swift given the thriving economy prior to the onset of the pandemic. Both extremes are possible as well as everything in between. The only thing we can say with certainty is that the economy will eventually recover.

A Historic Bear Market

This extreme uncertainty triggered the fastest bear market ever – just 16 trading days. Market volatility has been record-breaking with the S&P 500 averaging a daily move of 5.0% up or down for the month, well above the previous record of 3.9% in November 1929. Furthermore, in mid-March the index moved up or down more than 4.0% for eight consecutive days – the longest streak in history. On March 16, the S&P 500 declined 12.0%, the third largest single-day decline in history, behind only the 20.5% decline on October 19, 1987, and the 12.3% decline on October 28, 1929.

Keeping Things In Perspective

Bear markets are actually more common than many suspect. Since 1928, the S&P 500 has experienced 12 declines greater than 30% and 20 declines greater than 20%. This means that, on average, declines of 30% happen every seven to eight years and declines of 20% happen every four to five years. The specific causes of bear markets are always different, but the commonality is immense uncertainty. This uncertainty raises doubts that a recovery is even possible.

The near-term economic future has never been more uncertain than it is today. As a result, stock prices are oscillating wildly as short-term Wall Street traders and computer-based algorithms react to the latest headlines and struggle to anticipate company earnings over the next few quarters.

As long-term investors, we know that the intrinsic value of a business is determined by its expected cash flows over many years, not the next several quarters. While many businesses will see their cash flows decline in the coming months, we believe long-term cash flows of strong businesses are unlikely to be meaningfully impacted. It is important to remember that underlying fundamental business values are far less volatile than the swings in share prices.

Our Process Is Built For These Environments

Our investment process, which has been tested by many market

conditions over decades, seeks to prepare client portfolios for market downturns before they actually happen. We do this by focusing only on the highest quality stocks and bonds. Because our clients' time horizons are generally long term, we must contemplate the ability to withstand a recession before purchasing any security. Our ultimate objective is to achieve attractive returns over full market cycles, which include both bull markets and bear markets.

With respect to equities, we invest in businesses with sustainable competitive advantages that are led by intelligent management teams and trade at compelling prices. Our portfolio companies have strong balance sheets, robust cash flows, exemplary corporate cultures, and talented leaders, all of which will help them endure this economic chasm.

With respect to fixed income, we seek out short- and intermediate-duration bonds of high-quality companies that will stand the test of time. Our bond portfolios are conservative and are built to hold their value in times of stress. Our fixed income investment strategy helps to provide stabilization from sharply falling equity prices during down markets.

Looking Forward with Optimism

For a long-term investor, selling stocks in a bear market should be avoided. While the timing is unpredictable, every bear market eventually leads to the beginning of the next bull market. Your investment plans were created knowing that there will be periods of rough markets. The best course of action is generally to stick to the plan that was put in place before this market turmoil began.

Despite the current environment, we are optimistic. The Federal Reserve and Congress have moved quickly to provide support for the economy. We believe the long-term outlook for the businesses you own remains positive. While the headlines over the next month will almost certainly be bleak, we must remember the night is always darkest just before the dawn. We will get through this crisis, our lives will return to normal, and, if history is a guide, portfolio values will recover and realize new gains over the coming years.

We thank you deeply for your relationship with Hilliard Lyons Trust. We hope that each of you are healthy in body and spirit. During this stressful time, we want to assure you that we are here to serve your needs and help you build wealth over time.

Personal Care Documents



Chris Staples, J.D.

Director
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in the face of changing conditions will ultimately determine success. This lesson is as true with a family's financial and investment plan as it is for any military planner.

The true benefit of a well-thought-out plan is that it serves as a guiding light during stormy seas, financial or otherwise. It is during these times that many review their plans, specifically investment, estate and financial plans, to ensure the plan continues to reflect their current goals, circumstances and tolerances. These reviews are critical to ensure a plan matches the family's vision.

An important, and often overlooked, element to a complete financial and estate plan is a full set of personal care documents. These ensure someone is empowered to make decisions on your behalf if you are unable to due to incapacity or other circumstances. Like many things in life, people don't realize the importance of these documents until they are needed and it's too late.

The importance of having complete personal care documents has never been more evident than it is today, given the ever-changing landscape families face. These documents, including durable powers of attorney, health care surrogate

designations, and living wills, are often updated as part of an estate plan review. It is possible, though, that these documents don't garner the same level of attention as a will or trust that addresses the transfer of wealth to family members.

Without valid personal documents like these in place, it becomes difficult to manage the affairs and care for an incapacitated family member and it is difficult for your loved ones to care for you. Although each document serves a different purpose, having all of them in place is crucial.

- **Durable Power of Attorney:** This document appoints an individual or individuals to manage your personal affairs if you become incapacitated or if other circumstances keep you from being able to manage them yourself. The person, or persons, you name should certainly be someone you trust to make decisions in your best interest and is positioned to make decisions in your time of need.

Because these documents give control over your affairs, you should give careful consideration in naming your power of attorney. Many couples will choose their spouse or, in some cases, their children as power of attorney in these documents. It is also important to consider naming an alternative person in case your first choice can't assume the responsibility.

- **Health Care Surrogate Designation:** Like a financial power of attorney, this designation appoints someone to make health care decisions if you become incapacitated. The individual(s) you name in this document will have the ability to choose between competing health care options presented by your health care providers related to treatment or long-term care. You should select someone in this document who will have the ability to make decisions during an emotional time. As with the financial power of attorney, you should give careful consideration in selecting the individual whom you name in this document.

- Living Will or Advanced Directive: This document serves as your instruction to your family and care providers as to your end-of-life care wishes and whether you want to be kept alive via artificial means or not. Without this direction, it will be left to your family and health care providers to decide what is best. This can sometimes result in disagreements among family members or between family members and health professionals at a very emotional time. Clear guidance from you can help avoid these potential conflicts.

If you believe your personal care documents need a refresh, reach out to your attorney. Most attorneys are working remotely and can help with updates despite the various shelter-at-home orders and quarantines in place. Also, many states have begun enacting legislation that permits virtual execution and notarization of these types of documents, meaning your attorney may be able to guide you through executing documents without leaving the safety of their home. Also, it is always a good idea to furnish your health care providers copies of your health care documents to ensure they have them, and also to ensure they accept these documents as valid.

Consider that having these documents in place is a true gift for your family because it reduces the burden on them, as they now have your guidance to help them make decisions during what can be an extraordinarily emotional time. And, once you are confident your planning documents accurately reflect your wishes, you can then turn your attention to what matters most in your life, such as family, health, and community.

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