NovaPoint Capital LLC

Market Commentary

June 11, 2020

Down and Back

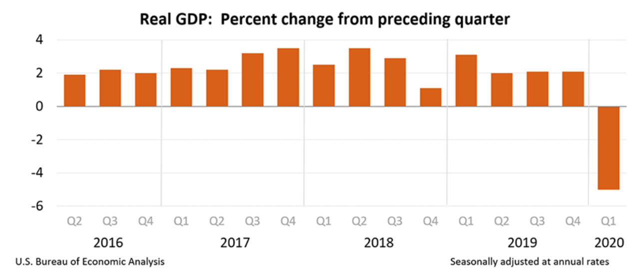
While the economy still has room for improvement, the stock market has staged an impressive recovery. Famed value investor Benjamin Graham once stated, “In the short run, the market is a voting machine but in the long run, it is a weighing machine”. In other words, near-term market prices are impacted by emotions and reactions to changes relative to expectations, while long-term value is determined by the financial results of the companies that comprise the market and relevant indices.

When faced with an event with an unknown range of potentially negative outcomes, the market declined swiftly because of the fear of the unknown. This is a similar pattern to what we have seen during events like the 9/11 attacks in 2001 and the collapse of Lehman Brothers in 2008.

When evidence emerged in February the COVID-19 pandemic could have a meaningful spread into the United States, the market started to waiver. By early March, the market voted that a severe crisis was at hand. The S&P 500 fell 35% from its February 19th peak to its trough on March 23rd. Cities were on lockdown. Daily cases, hospitalizations, and COVID-19 fatality numbers were rising, and fear has reached a potential peak.

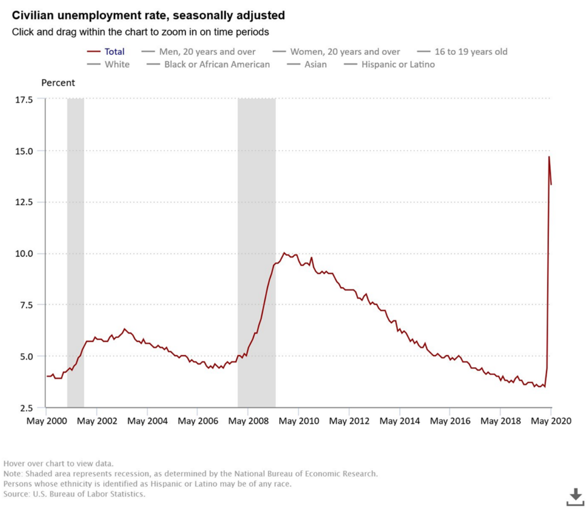
Since March 23rd, the S&P 500 Index has risen 45%, back near its January 1st starting levels. While the decline can be attributed to the COVID-19 induced shutdown of most of the economy and fear of the potential health and social impact of the virus, it may be harder to understand why the stock market has rebounded so quickly.

As parts of the U.S. went on quarantine and the need for social distancing was shutting down restaurants, retail, travel, and a long list of other activities, the economic calculation was that the economy was headed for a recession. A recession has traditionally been defined as two consecutive quarters of contracting (or negative) GDP growth, though the National Bureau of Economic Research has already declared a recession here in 2020. The first quarter of 2020 saw a contraction in GDP of 5.0% based on the current data from the Bureau of Economic Analysis (BEA). The economic impact of COVID-19 accelerated into April and early May. Second quarter GDP is currently indicated to decline by 35% which would confirm a recession.



If we look back at the 2008-2009 financial crisis, the fourth quarter of 2008 had a GDP decline of 7.2%, first quarter of 2009 GDP declined 4.5%, and second quarter of 2009 GDP declined 1.2%. During that recession, the stock market bottomed in March of 2009, before the first quarter of 2009 data was known. The stock market was taken by surprise by the Lehman bankruptcy in September 2008 and fell sharply in the fourth quarter of that year, but the market started rebounding before the first quarter GDP data was known to confirm the recession. The same pattern has emerged here in 2020. We can look out our doors and see that economic activity is lower than it was a year ago, but the stock market is forward looking and reacting to the data emerging indicating that, barring the return of a second wave of COVID-19 or another COVID-like event, the economy has bottoms and is currently improving each week. Third quarter GDP should see a significant positive sequential improvement.

Looking at the recent May employment report, there are not many times when some would be happy that the unemployment rate is 13.3%. Back in February 2020, the United States was at record low unemployment of 3.5%. Once COVID-19 hit and the economy shutdown, there was a wave of layoffs, furloughs, and business closures. Unemployment quickly ticked up to 4.4% by the end of March and to 14.7% by the end of April. Forecasts for May were predicting unemployment as high as 20%. The 13.3% figure released for May was welcomed news. The net 2.5 million jobs created in May versus over 20 million jobs lost in April was better than expected.



Another key factor supporting optimism in the stock market is the action by the Federal Reserve to maintain liquidity in the financial system. Looking back at the 2008-2009 financial crisis, excess financial leverage, bad loans, and the inter-related reliance on systemically important financial institutions caused the banking system to freeze up. Throughout the COVID-19 crisis Federal Reserve chairman Jerome Powell has asserted a consistent commitment that the Federal Reserve would use all the methods it could to maintain the liquidity and functioning of the banking system. The Fed lowered near-term interest rates to zero and has recently pledged to keep them there through 2022. The Fed has also been activity purchasing government and agency bonds, and other securities, in the open market. These are the two main ways the Federal Reserve acts, through setting interest rates which is known as monetary policy and buying and selling securities in the market which is known as open market operations. The Fed also worked with the Treasury Department to coordinate availability of funds for programs like the Paycheck Protection Program (PPP) and Economic Injury Disaster Loan (EIDL). These programs helped small businesses meet near-term financial obligations such as payroll and rent while they may have been temporarily closed.

We mentioned that the economy still has room for improvement, and we believe, barring another COVID-like event, that economic and corporate earnings growth in 2021 should be substantially above 2020. The stock market has already anticipated this return to growth which has been the main driver of the recovery since late March. There are, however, a few gates to pass through to confirm that positive trajectory.

There is still a high degree of job dislocation across the country. These workers will need to be brought back to their jobs or transition into other jobs. Despite the government funded Paycheck Protection Program (PPP) and Economic Injury Disaster Loan (EIDL) programs, there are business that have already closed and more will likely close this year.

The dispute between the U.S. and China over the origin of COVID-19 and how each country handled the outbreak have caused a rift in U.S. – China relations. The first phase of a trade deal was scheduled to start just as the virus outbreak began. An on-going animosity between the U.S. and China is likely to continue as China vies for economic power globally. The upshot to this for the U.S. is a potential return of manufacturing, especially in areas such as pharmaceuticals and technology, where supply chain security cleared showed vulnerability during the COVID event.

The possibility for a second wave of COVID has been widely debated. Absent a viable vaccine, a return of COVID in the fall could impact vulnerable members of the population as we saw during the initial outbreak. While this is not likely to cause widespread closure of the economy again, it could impact the healthcare system, as well as undermine consumer confidence.

The lasting effects of the increased government debt increases required to bridge the economic gap during the crisis will be felt for years to come. The U.S. Dollar remains a strong currency globally because other countries have also needed to assume large amounts of debt to fund similar economic support programs.

Lastly, we believe is an important factor for the direction of the economy in 2021 is the result of the upcoming election. Along with the Presidency, the House of Representatives and one-third of the Senate are open for election. The balance of power could shift either way and that often brings potential policy changes which can impact multiple industries and sectors of the economy.

Market timing is tough. A strong 2019 performance and a strong economy had investors optimistic in January. COVID created a fear-induced run for the exits in March, and now we are seeing optimism about a recovery as well as a “fear of missing out (FOMO)” sentiment. Volatility likely stays elevated as the market votes on daily news headlines and their potential impact. We have never advocated an “all-in / all-out” market timing approach and prefer to make incremental decisions as we absorb and analyze data. Our preferred method of execution has been to make gradual adjustments against a well-research portfolio of stocks which possess, in our opinion, the durability to withstand the volatility of market cycles.

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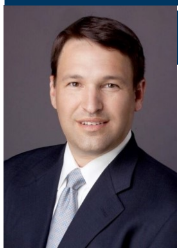

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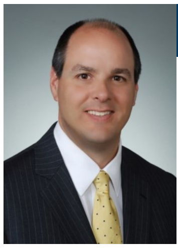
Joe has over 20 years of experience in the investment management industry. Prior to founding NovaPoint, he was a portfolio manager at Spectrum Advisory Services and GMT Capital in Atlanta, and Epoch Investment Partners in New York. He has also worked as an equity research analyst at Merrill Lynch and ABN Amro. Before beginning his investment career, Joe was an Infantry officer in the U.S. Army. Joe holds a BS from the U.S. Military Academy at West Point and an MBA from the University of Chicago. He is both a Chartered Financial Analyst (CFA) and a Chartered Market Technician (CMT).



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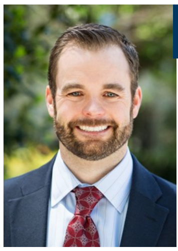
Alan has over 20 years of experience in the investment management industry. Prior to founding NovaPoint, he was a fixed income manager at both Spectrum Advisory Services and a private family office. Alan was also with the Bank Group division of Countrywide Capital Markets where he developed balance sheet strategies for depository institutions. He holds a BS in Banking and an MBA in Finance from Nova Southeastern University. Alan is an endurance athlete and three-time IRONMAN finisher.



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Jeff has 10 years of industry experience. Prior to joining NovaPoint, Jeff was a Vice President in the Private Banking and Investment Group at Merrill Lynch. Jeff also worked at Booz Allen Hamilton and the Department of Defense. Prior to his private sector career, Jeff was a Field Artillery officer in the U.S. Army. He holds a BA from the University of Texas and an MBA from the University of Maryland. Jeff is Chartered Financial Analyst (CFA).

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Frederick has over 25 years of experience in the investment management industry. Prior to joining NovaPoint, Frederick was a Partner and Investment Advisor at Brightworth where he advised high net worth investors. Frederick began his investment career in 1991 at Balentine & Co where he rose to Partner. He also co-founded and served as Chief Investment Officer at Wright Investment Management and at Smith & Howard Wealth Management . Prior to beginning his investment career, Frederick served as an Engineer officer in the U.S. Army. He holds a BS from the U.S. Military Academy at West Point and an MBA from Emory University. Frederick is a Chartered Financial Analyst (CFA).

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Christina has 25 year of accounting experience. She earned her CPA license in 1998 while working as a Senior Accountant for Bennett Thrasher PC. She has also worked in accounting roles in the financial services, public relations, and manufacturing industries. She earned her BS in Accounting at Miami University in Oxford, Ohio magna cum laude. She is a member of the American Institute of Certified Public Accountants (AICPA) and a member of the Georgia Society of CPAs.