REDHAWK®
WEALTH ADVISORS

Redhawk Quarterly Commentary

March 31, 2020

Each quarter, Redhawk's Investment Committee provides a Quarterly Commentary. We look at what's going on in the investment landscape and provide our perspective on a variety of topics. These aren't predictions and it represents our perspective on important market and economic information designed to help make decisions affecting your long-term financial strategy. Our goal is to help you understand what is going on in the markets so you can more clearly define investment goals, diagnose unintended risks, and utilize portfolios that can achieve a better financial outcome.

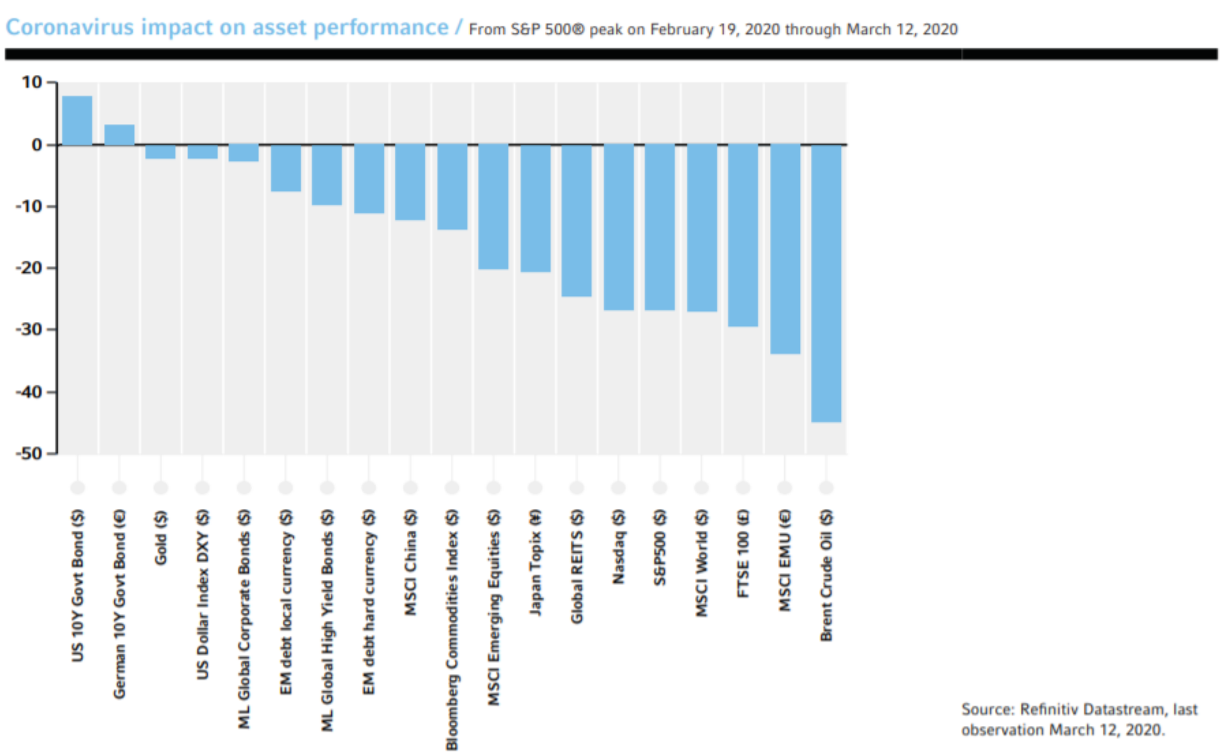
Market Commentary

We entered the new year with economic momentum fueled by global central bank rate cuts and an agreement on the first phase of the trade war. Global markets rallied until mid-January, at which point news of a virus outbreak in China emerged. Initially, the coronavirus was believed to be confined to China, and U.S. markets continued pushing forward as domestic economic data improved. Then it became clear the virus would not be confined, as infections rose in Italy, Iran and South Korea. Today, there are infections globally, with the U.S. leading the world in confirmed cases.

After hitting an all-time high on February 19th, the S&P 500 plummeted by more than 35% from peak to trough. More impressive than the magnitude of the decline was the velocity. The S&P 500 entered a bear market (i.e., falling more than 20%) in just 16 trading days (see the chart to the right). In contrast, it took 188 trading days for the S&P 500 to decline that amount during the Global Financial Crisis.

With no vaccine and no scientifically proven treatments, countries implemented social distancing as a first line of defense against the virus. That, as we now know, has led to widespread business closures and quarantining. Viewing the economic slowdown from a different angle, Moody's Analytics noted that as of the final week of the quarter, 41 states had ordered some business shutdowns to stem the virus' growth. That caused daily output at the end of March to fall roughly 29 percent from the first week in March.

The chart below shows that the coronavirus impact was severe since the U.S. equity market peak on February 19.



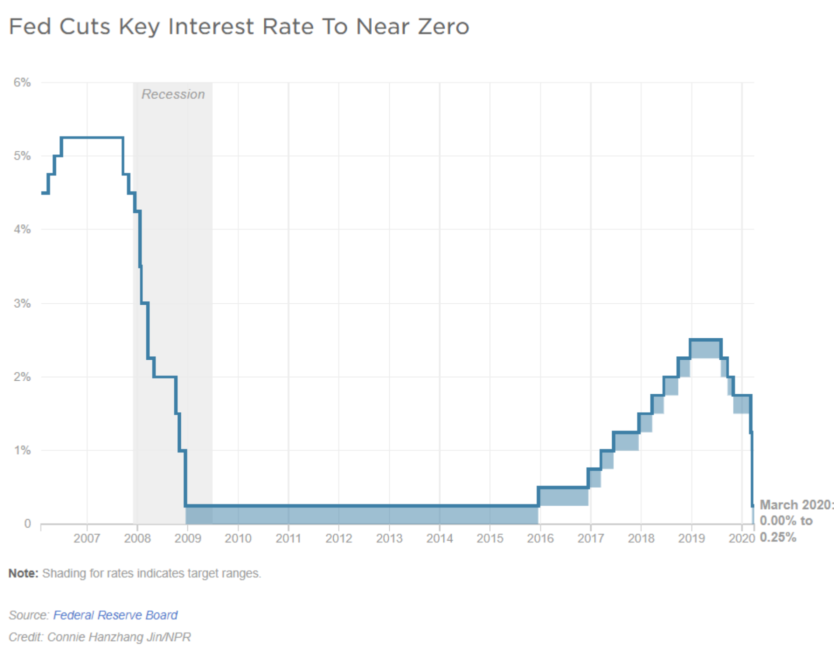
To say that the virus took the market and policymakers by surprise is an understatement. Now, economists are aggressively reducing economic forecasts and warning about the future of equity markets. Because we are in unchartered waters, take any economic forecasts with a grain of salt because we are dealing with a virus and no one knows for certain how it will progress or how long current shutdowns will endure.

U.S. Market

The longest bull market in U.S. history ended abruptly during the first quarter as the coronavirus spread across the globe. Investors braced for an economic recession by selling equities and cyclical commodities in favor of safer government bonds and gold. Within equities, growth protected more than value, large-cap outperformed small-cap companies, and the U.S. sold off less than international equities. Within fixed income markets, investors favored higher quality, longer-duration bonds. The 10-Year Treasury yield ended the quarter at 0.7%. West Texas Intermediate ("WTI") Crude Oil slumped 66.5% after Russia and Saudi Arabia increased production unexpectedly.

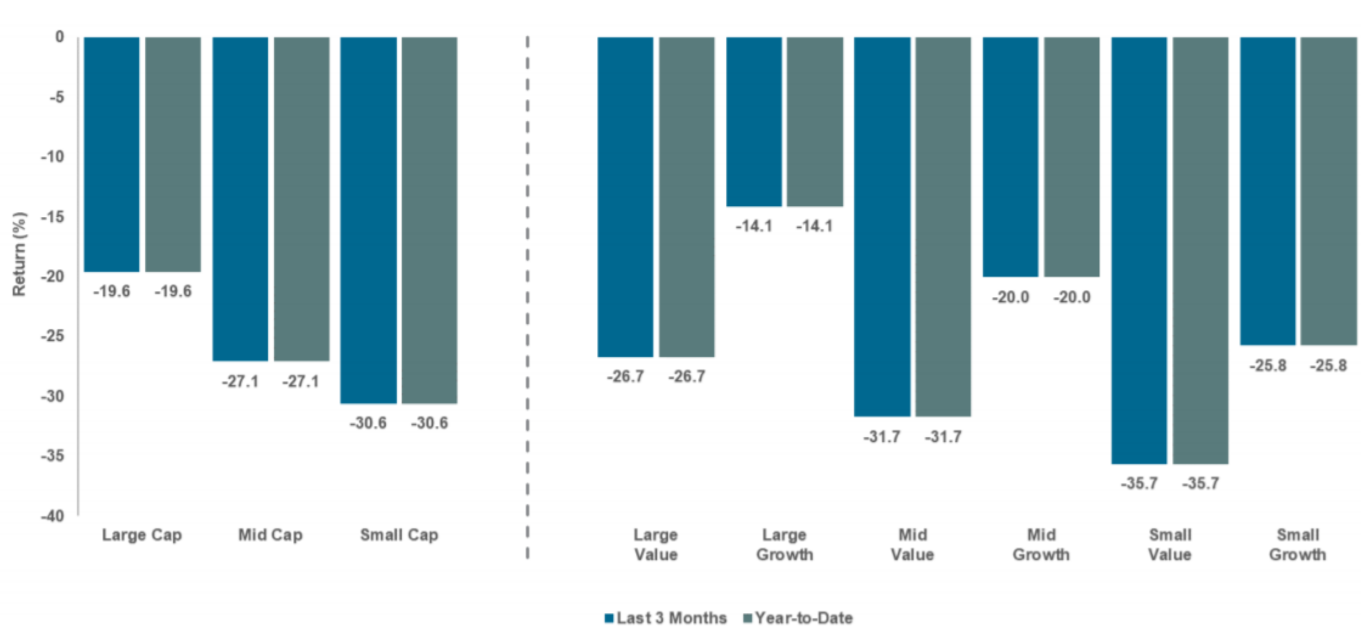
The state of the economy has changed drastically since the last quarter end. Consensus among economists is that a recession is imminent with a potential double-digit gross domestic product ("GDP") contraction in Q2. The St. Louis district of the Federal Reserve is predicting the worst of the economic damage from the coronavirus outbreak will result in a higher unemployment rate than at the worst point in the Depression. Economists at the Fed's St. Louis district said in a recent analysis that the U.S. will lose 47 million jobs, resulting in an unemployment rate of 32.1%, a considerable increase from the 24.9% unemployment rate during the worst point of the Great Depression. Policymakers have acted swiftly to combat the economic hardships. The $2 trillion relief bill is expected to provide stimulus payments to individuals, broader unemployment benefits, and loans to small businesses. Additional support could be on the horizon.

During the quarter, the Federal Reserve responded quickly to liquidity concerns and economic fears by lowering interest rates a total of 1.5% to a target range of 0.0% to 0.25% (see the chart to the right). Additionally, the Fed enacted emergency lending programs to keep credit flowing in the economy. The Fed expanded its asset purchasing program to include municipal bonds in addition to U.S. Treasuries and mortgage-backed securities.



During the quarter, growth protected by more than 12% over value as the Russell 3000 Growth returned -14.9% while the Russell 3000 Value Index lost 27.0%. Investors favored large-cap (-20.2%) over riskier small-cap (-30.6%). The worst performing style was small-cap value, which fell 35.7% while large-cap growth protected the most during the downturn, with a return of -14.1% (see the chart below).

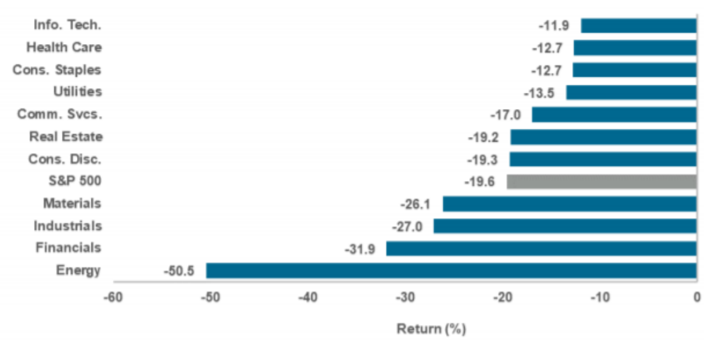
Performance by Market Cap and Style



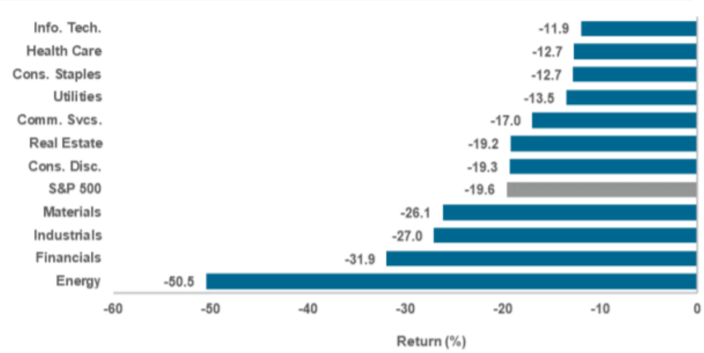
Source: Factset Asset classes are represented by the following benchmarks: S&P 500 (Large Cap), Russell Midcap® (Mid Cap), Russell 2000® (Small Cap), Russell 1000 Value® (Large Value), Russell 1000 Growth® (Large Growth), Russell Midcap Value® (Mid Value), Russell Midcap Growth® (Mid Growth), Russell 2000 Value® (Small Value), and Russell 2000 Growth® (Small Growth). See important disclosures and definitions included with this publication.

Defensive sectors outperformed cyclicals. The economy-sensitive sectors of financials, industrials, and materials fell between 25-35% while energy slumped over 50%. Energy companies faced significant pressure given Saudi Arabia's and Russia's decision to rapidly increase oil production while demand remained weak. Information tech, health care, consumer staples, and utilities protected on the downside, dropping between 12% and 14%, as demand for these products and services continued in the wake of social distancing (see the charts below).

S&P 500 Index: Performance by Sector (Latest Quarter)



S&P 500 Index: Performance by Sector (YTD)



S&P 500 Sector Statistics

	P/E Ratio (TTM)	P/E Ratio (NTM)	Dividend Yield (%)	EPS Growth (%)
S&P 500 Index	17.7	15.5	2.1	(0.9)
Communications Services	18.9	15.8	1.3	4.1
Consumer Discretionary	23.0	20.5	1.4	3.9
Consumer Staples	19.3	17.8	2.9	(5.7)
Energy	25.8	44.5	5.8	(49.1)
Financials	11.2	8.9	2.7	9.1
Health Care	15.4	13.9	1.8	18.2
Industrials	17.2	15.0	2.2	(9.0)
Info. Tech.	21.7	18.5	1.4	(1.1)
Materials	17.3	15.2	2.5	(33.0)
Real Estate	19.0	16.1	3.4	12.8
Utilities	18.9	16.9	3.3	4.0

Source: Factset. Performance greater than one year is annualized. Performance is represented by the benchmark listed in the "representative benchmark" column. See important disclosures and definitions included with this publication.

International Markets

Fears of the COVID-19 impact on global economic growth sent international equity markets lower. Riskier emerging market equities fell 23.6% and developed international equities fell 22.8%. Growth held up better than value across international markets. Within developed markets, Switzerland (-11.5%) and Japan (-17.2%) fared better than commodity-oriented Australia (-23.3%) and virus-affected countries, like Spain (-28.1%) and Italy (-29%). Within emerging markets ("EM"), the worst performing countries were also commodity exporters: Brazil (-35.8%), South Africa (-23.8%), and Russia (-21.8%). In contrast, China was the best performing country having only fallen 10.3% during the quarter despite its central role in the global crisis.

The country year-to-date returns are shown below.

Year-to-Date Performance

Source: Factset; Standards & Poor's (S&P 500); MSCI benchmarks (country returns). See important disclosures and definitions included with this publication.

Fixed Income Markets

The broad U.S. bond market, as measured by the Bloomberg Barclays US Aggregate Index, went on a wild rollercoaster ride during the quarter, and ultimately delivered a return of 3.2%. The sudden economic stop resulting from COVID-19 restrictions led to a rush for liquidity. Investors across financial markets preferred holding cash-like securities, which prompted massive redemptions, particularly within short-dated fixed income assets. As panic spread through the markets, investors de-risked in rapid fashion and sold everything they could rather than what they wanted to.

During the quarter, fixed income spiked to positive territory. A significant drawdown occurred as credit spreads widened and liquidity evaporated. In anticipation of economic deterioration and market uncertainty, the Fed acted swiftly. The Fed lowered the Federal Funds rate to a target range of 0% to 0.25%, vowed to provide “unlimited” quantitative easing, and enhanced the market liquidity. The Fed’s actions served as a powerful force pulling yields across the U.S. Treasuries curve down to record levels. The bellwether 10 Year U.S. Treasury yield finished Q1 at 0.70% after starting the year at 1.92%.

Investors benefited from an allocation to U.S. Treasuries, which returned 8.2% in Q1. In contrast, corporate credit experienced dramatic downside pressure. Corporate issuers experienced a material repricing during the quarter. Concerns rose about the ability of corporations to service large debt burdens in the coming quarters. Given low interest rates, corporations increased debt loads in part to buy back shares of stock and this action led to rating agencies to consider prospects for future growth in their ratings. Quick monetary and fiscal action may provide the necessary support to highly levered issuers. However, investors took no comfort in the sector. Investment grade corporate bonds fell 3.6% and high yield corporates dropped 12.7% during the quarter (see the chart on the next page).

The chart below shows the returns for various fixed income instruments.

Bond Types	Characteristics		Trailing Returns (%)						Annual Returns (%)			Benchmark
	Yield (%)	Duration	Last Qtr	YTD	1-Year	3-Year	5-Year	10-Year	2019	2018	2017	
Broad Developed Markets												
U.S. Taxable Bonds	1.6	5.7	3.1	3.1	8.9	4.8	3.4	3.9	8.7	0.0	3.5	*BBgBarc US Aggregate Bond*
U.S. Municipal Bonds	2.0	5.4	(0.6)	(0.6)	3.8	4.0	3.2	4.1	7.5	1.3	5.4	*BBgBarc Municipal Bond*
Global Bonds	0.8	8.2	(2.7)	(2.7)	0.7	2.6	2.0	1.4	5.1	(2.1)	10.5	*BBgBarc Glbl Agg. Bond*
Broad Emerging Markets												
Emerging Market Bonds	7.2	5.9	(9.5)	(9.5)	(2.9)	1.5	3.3	5.1	13.1	(2.5)	8.2	*BBgBarc Emerging Markets*
Taxable Bond Categories												
Treasuries	0.6	7.0	8.2	8.2	13.2	5.8	3.6	3.8	6.9	0.9	2.3	*BBgBarc US Treasury*
Agencies	0.6	6.9	8.1	8.1	13.1	5.8	3.6	3.7	6.8	0.9	2.3	*BBgBarc US Government*
Mortgage-Backed	1.3	1.7	2.8	2.8	7.0	4.0	2.9	3.3	6.4	1.0	2.5	*BBgBarc US MBS*
Inv-Grade Corporate	3.4	8.0	(3.6)	(3.6)	5.0	4.2	3.4	4.9	14.5	(2.5)	6.4	*BBgBarc US Corporate IG*
High Yield Corporate	9.5	4.1	(12.7)	(12.7)	(6.9)	0.8	2.8	5.6	14.3	(2.1)	7.5	*BBgBarc US Corporate HY*
Municipal Bond Categories												
Insured	2.9	5.0	0.1	0.1	5.1	4.9	4.0	4.8	8.3	2.3	5.6	*S&P Municipal Bond Insured*
State GO	1.7	4.6	(0.0)	(0.0)	4.1	3.7	2.9	3.8	6.8	1.4	4.7	*BBgBarc Municipal State GO*
Local GO	1.8	5.6	0.2	0.2	5.0	4.4	3.4	4.2	7.9	1.2	5.9	*BBgBarc Municipal Local GO*
Revenue	2.2	5.7	(1.0)	(1.0)	3.7	4.1	3.4	4.4	7.9	1.2	6.0	*BBgBarc Municipal Revenue*
High Yield	5.2	10.0	(6.9)	(6.9)	(0.7)	4.4	4.2	6.0	10.7	4.8	9.7	*BBgBarc High Yield Muni*

Source: Factset; Barclays benchmarks. Individual security types are subsets of either the Barclays U.S. Aggregate or Municipal Bond benchmarks. Duration, measured in years, is a relative term that expresses the price sensitivity of an investment/benchmark to changes in interest rates. All else equal, the lower the duration, the less price sensitivity to interest rate changes. See important disclosures and definitions included with this publication.

Economic Outlook

Social distancing measures and expanded testing capacity give reason for optimism but expect volatility to remain elevated through the coming quarter as uncertainty is at an all-time high. Projections for the "reopening" of the U.S. economy are wide ranging, with major disagreements on a plan of action at even the highest levels of government. The world will closely monitor locations that are easing lockdown restrictions. Even positive scenarios assume weeks to months of continuous isolation efforts and prolonging economic strain. Additional stimulus from the Fed and the U.S. Government is likely. Many are forecasting a 20% or higher decline in 2Q GDP, while unemployment figures seem likely to skyrocket. Tremendous economic uncertainty will persist well into the summer.

The government's virus containment measures mean a technical recession is probable, which is negative GDP growth in Q1 and Q2. As of March 19, the S&P 500® Index has declined 29% from its 2020 peak, which is on par with a moderate economic recession. A reasonable amount of economic pain is already priced in the markets. A risk is that the sharp plunge in cash flows causes highly indebted companies to default, triggering a credit-crunch in the broader economy. This threat should be lessened by the Fed's 1.50% of emergency easing, asset purchases, and the resumption of liquidity management.

Fiscal policy will be important in offsetting the recession. The nature of the COVID-19 shock should force bipartisan agreement on large stimulus measures. More immediately, though, Congress and the U.S. Treasury can put emergency funding channels in place for stressed industries facing liquidity pressures. Tailwinds from monetary and fiscal policy should eventually promote stronger economic conditions when the virus disruption has cleared. The upside risk is that the number of new virus cases should begin to decline in Q2, and the subsequent recovery will be boosted by the strongest stimulus measures in more than a decade.

Global GDP growth will probably be negative for the first quarter, and the shutdown in economic activity from the virus containment measures assures negative growth in the second quarter. The number of virus cases is likely to increase, which means more drastic containment measures may continue to be implemented. It is also possible that stresses in credit markets create a wave of defaults and liquidity issues that cascade across investment markets. China's experience shows it is possible to contain the virus. Outside the stricken Hubei province, there has been an average of only 10 new cases per day in China during the first 18 days of March. South Korea is likewise having success in containing the outbreak. The fatality rate from the virus also seems lower than originally feared, with many estimates now placing it below 1%. Most deaths so far have been confined to the elderly and those with pre-existing respiratory conditions. Provided the virus is transitory and contained in the second quarter, the global economy should be poised to start recovering in the second half of 2020. There were signs of recovery in global economic indicators before the virus escalated in China during February. In addition, 2019 had seen the largest easing in monetary policy by global central banks since the 2008 financial crisis

It is not enough to own a portfolio personalized for your situation, based on your comfort with risk and long-term financial goals. You must be patient and disciplined, too. With our risk management process, our investment committee is reviewing the market conditions and underlying investments on a weekly basis. Please contact your Redhawk advisor to learn more.

Redhawk Wealth Advisors, Inc. is an SEC registered investment advisor (RIA) that provides comprehensive retirement plan and financial planning tools and critical back-office support for advisors nationwide. Redhawk's focus is to enable advisors create, grow and manage wealth through a broad range of financial products and services that promotes the economic well-being of our select group of clients and advisors.

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