Palisade
CAPITAL MANAGEMENT

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Dear Investor:

As the data below show, the first quarter of this year offered a grim counterpoint to the near-euphoric feeling that most stock and bond investors felt in 2019 – and as recently as six weeks ago.

	MARCH 31, 2020	DEC. 31, 2019	% CHANGE
S&P 500® Index	2,584.6	3,230.8	-20.0%
Dow Jones Industrial Average	21,917.2	28,538.4	-23.2%
NASDAQ Composite Index	7,700.1	8,972.6	-14.2%
Russell 2000® Index	2,865.8	4,146.6	-30.9%
VIX Volatility Index	59.3	13.8	+329.7%
Barclays Bond Index – ETF “AGG”	115.4	112.4	+2.7%
10-Year U.S. Treasury Yield	0.68%	1.92%	-64.6%
Baltic Dry Index – Spot	626	1090	-42.6%
Gold (ounce) – NY Spot	$1,591	$1,520	+4.7%
Oil (barrel – West Texas intermediate)	$20.10	$61.08	-67.1%
Bitcoin	$6,490	$7,220	-10.1%

Data Source: FactSet Data Systems

What a world! The March 19 cover of *The Economist* (left) pictured it perfectly: the planet’s social and commercial life has been laid low by a virus unknown to most of us just a few months ago. We have lived through other economic contractions, but this one is unique in its speed and severity. The normally sober-minded president of the St. Louis Federal Reserve, James Bullard, has predicted that unemployment in the U.S. could jump sharply, if temporarily, to 30% in the second quarter of 2020. The rapid spread and morbidity of the COVID-19 virus may touch everyone in its path, which is why cities and regions are in lockdown. But unlike other severe recessions, the exact cause of this contraction is well-known and likely to run its course in several quarters, even without intervention. Policymakers’ first concern is to keep citizens from spreading the virus socially, so as not to swamp healthcare systems and to “flatten the curve of infection”.

Policymakers’ other obsession is the country’s economic well-being. That battle is being fought on many fronts and contrasts sharply to the policy responses of the crises of the early-1930s or even the first months of the Great Financial Crisis of 2008-2009. The Federal Reserve Bank (the “FRB”) cut its key interest rate to 0.25% and revived and enlarged its aggressive bond purchase program of a decade ago by promising to buy nearly $1 trillion of treasury and mortgage-backed debt securities. The Fed aims to ensure the liquidity of the U.S. banking system as corporate borrowers take down credit lines. The program includes a first: the purchase of bond exchange traded funds (ETFs), a direct-to-market way of calming fixed income capital markets. Fed Chairman Jay Powell has made it clear that the FRB stands ready to do even more to calm markets, including the extension of dollar credit lines to *foreign* central banks on the collateral of their U.S. treasury bond holdings.

On the fiscal front, Congress last week passed the $2 trillion CARES (Coronavirus Aid, Relief, and Economic Security) Act, which the President quickly signed. CARES is designed to do several things, including: 1) provide direct cash payments to most Americans who earn less than $99,000 for single tax filers and $198,000 for married filers (limits are higher for those with children); 2) make loans or grants to all businesses that continue to employ their pre-crisis staffs; and 3) extend through July new federal unemployment benefits of $600 a week to each unemployed person – in addition to the person’s state unemployment benefits.

Will the CARES Act forestall widespread personal distress? That is certainly Congress's aim. And if CARES falls short of that aim, Congressional leaders have signaled their intention to reload the bazooka for another round (or rounds) of fiscal assistance.

What lies ahead for investors?

First, we do not believe the country's economy or financial markets will be permanently impaired. The COVID-19 pandemic came upon us suddenly, but the siege will lift. James Bullard of the St. Louis Fed, whose dire unemployment prediction we cited earlier, stated he believes employment will recover strongly by year-end. Epidemiologists also believe the virus will likely *not* re-infect those who have been previously exposed. And health care companies are racing to develop prophylactic vaccines to stop future coronavirus infections. So, the health outlook – while dire in the short-term – appears at least promising in the longer run. Until then, monetary and fiscal policymakers are determined to preserve our economic capacity.

Second, we do not believe investment life will immediately return to its *status quo ante.* The epidemic has exposed everyday strengths and fissures. For those of us who have worked remotely in the past few weeks, **technology has become our new best friend**. We have depended on tech to communicate, remotely collaborate with colleagues, order essential products, and blow off stress (who hasn't binge watched a TV series in the last week?). The Internet and wireless connectivity are as vital to 21st century America as electricity and superhighways became to our grandparents to the 20th century. Similarly, **a modern economy cannot function without a strong, well-funded, and ubiquitous health care system. The same is true of the country's financial system – it must be government supported and properly regulated to ensure its vitality.** But what of other industries? What of brick-and-mortar retailing, commercial real estate, and social industries like hotels, cruise ships, and movie theaters? Those industries will all survive, of course, but they may recover late and, even then, are likely to look different than they did before the pandemic.

Socialized obligations like federal debt may soon swell from 100% of U.S. GDP to perhaps 150% ($30 trillion). But one should not conclude higher inflation and interest rates flow inevitably from a sharp jump in the national debt. There are examples of developed countries that have high debt/GDP ratios but little or no inflation. Japan's national debt to GDP stands at 234%, and that country has been battling price *deflation* for years. Americans are likely to absorb the country's debt binge through higher savings rates, which often happens after economic shocks. The personal savings rate was just 3.6% on the eve of the last financial crisis (December 2007) but has climbed steadily since; it stood at 8.2% in February of this year. That falls short of the 60-year high savings rate of 17.3% in May 1975. Our point is that Americans' rising propensity to save might neatly complement the country's need to fund trillions of new federal debts. The interest rate on these savings instruments will likely be low, but the trade-off for savers will be comfort in the full faith and credit of the federal government.

Investment capital will surely return to the common stocks of financially secure, well-managed companies that provide essential products and services. Throughout American economic history, common stocks have proved to be reliable creators of wealth, though not in an unbroken path. Consider that from 1928 to 2019, the S&P 500® index returned 9.9% per year, so that $10,000 invested then would have grown to $54 million by the end of 2019. And that 91-year period included the Depression, the second world war, several regional wars, an oil crisis, "stagflation", recessions, the 9/11 terror attacks, and a mortgage crisis that nearly brought down the U.S. financial system. We will survive this period and come out stronger on the other side.

Soon we will see "open" signs again.

Thank you for allowing us to manage your investments. We aim to reward your faith in us with creativity, diligence, and good results. That is our only business model.

Sincerely,
Palisade Capital Management

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Past performance is not a guarantee of future results.

Please note that each client account has different characteristics and other accounts with the same strategy may have materially different results. The actual characteristics of any particular account will vary based on a number of factors including, but not limited to (i) the size of the account; (ii) the timing of investment; (iii) investment restrictions applicable to the account, if any; and (iv) market exigencies at the time of investment.

The S&P 500® Index is an unmanaged index that is widely recognized as an indicator of general market performance. The S&P 500® Index does not have a defined investment objective, unlike the indices above, nor does it charge fees and expenses.

The Dow Jones Industrial Average is a price weighted index comprised of 30 of the largest and most widely held public companies in the United States.

The NASDAQ Composite Index measures all NASDAQ domestic and international based common type stocks listed on The NASDAQ Stock Market.

The Russell 2000® Index measures the performance of the small-cap segment of the U.S. equity universe. It consists of approximately 2,000 of the smallest securities based on a combination of their market cap and current index membership. Source: London Stock Exchange Group plc and its group undertakings (collectively, the "LSE Group"). © LSE Group 2020. FTSE Russell is a trading name of certain of the LSE Group companies. "Russell®" is a trade mark of the relevant LSE Group companies and is used by any other LSE Group company under license. All rights in the FTSE Russell indexes or data vest in the relevant LSE Group company which owns the index or the data. Neither LSE Group nor its licensors accept any liability for any errors or omissions in the indexes or data and no party may rely on any indexes or data contained in this communication. No further distribution of data from the LSE Group is permitted without the relevant LSE Group company's express written consent. The LSE Group does not promote, sponsor, or endorse the content of this communication.

VIX is the ticker symbol for the Chicago Board Options Exchange (CBOE) Volatility Index, which shows the market's expectation of 30-day volatility. It is constructed using the implied volatilities of a wide range of S&P 500® Index options.

The Barclays Bond Index – ETF "AGG" tracks an index of US investment-grade bonds. The market-weighted index includes Treasuries, agencies, CMBS, ABS and investment-grade corporates.

The Baltic Dry Index (BDI), is issued daily by the London-based Baltic Exchange. The BDI is a composite of the Capesize, Panamax, and Supramax Timecharter Averages. It is reported around the world as a proxy for dry bulk shipping stocks as well as a general shipping market bellwether.

West Texas Intermediate (WTI) is a grade of crude oil used as a benchmark in oil pricing and is the underlying commodity of the New York Mercantile Exchange's oil futures contracts.