CMG Tactical All Asset Strategy
2020 Q2 Quarterly Update

The strategy began the quarter in an extremely conservative risk position with zero exposure to equities. During the market crash in the first quarter, the strategy moved entirely to fixed income and gold. As equity markets responded to fiscal and monetary stimulus, the strategy slowly added risk exposure over the quarter. In April, the strategy was primarily allocated to ultrashort duration bonds, long government bonds and gold. In May, the portfolio increased risk, rotating out of ultrashort duration bonds and into investment grade corporate bonds, mortgage backed securities and equities, specifically, healthcare and large caps. The strategy continued to add risk to the portfolio in June, further adding equity exposure. The portfolio held positions in technology and large caps. The fixed income allocations also reflected an increased appetite for risk, adding exposure to convertible bonds and longer duration government bonds at the expense of a reduction in ultrashort bonds. The strategy's holdings in technology funds and its position in gold have been strong contributors to positive performance, particularly at the end of the quarter and into July.

The strategy held the following allocations to equities, fixed income, commodities and cash at the end of April, May and June:

	Equities	Fixed Income	Commodities	Cash*
April	0.00%	39.85%	10.67%	49.48%
May	20.22%	50.64%	10.93%	18.22%
June	30.04%	58.88%	11.08%	0.00%

***Please note that cash holdings include cash equivalents such as ultra short duration bond positions.**

Market Commentary

Cassandra's Curse

Cassandra, the daughter of King Priam and Queen Hecuba of Troy, was cursed by the god Apollo. He sought to win her by giving her the divine power to see the future, but she reneged on her promises and her power was turned from a gift to a curse: the power to see the future and issue accurate prophecies but never to be believed. The many doctors and scientists on the front line of our battle with the novel coronavirus pandemic must sadly sympathize with her as the U.S. continues to struggle responding to the pandemic. Market commentators, prognosticators and professional money managers must feel the same way. Economic fundamentals and bond markets have diverged significantly from equity market valuations and those expressing caution over the past several months have been spurned like modern day Cassandras.

There are two main reasons for the immediate disconnect that together have helped propagate a false optimism: historic levels of monetary intervention from the Fed and fiscal stimulus from Congress. The Fed pulled out all the stops, taking a page out of Mario Draghi's, the former head of the ECB, playbook. The Fed quickly cut rates to zero, commenced a massive round of quantitative easing and rolled out a number of liquidity programs (domestic and international) to support credit markets. More controversially, for the first time ever, the Fed is buying ETFs that track the corporate bond market, including high yield bonds. Clearly, the Fed has learned its lesson from the financial and Eurozone crises, and in total has been very effective in calming financial markets.

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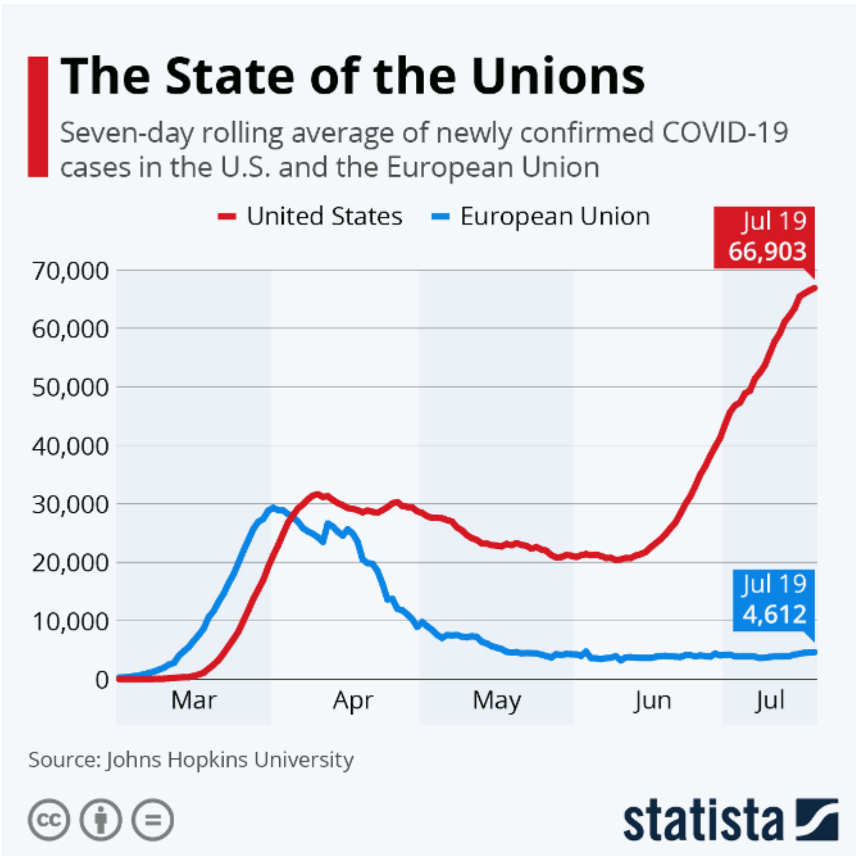
At the end of March, Congress passed the CARES Act (Coronavirus Aid, Relief, and Economic Security Act), a fiscal stimulus totaling $2.2 trillion that boosted unemployment benefits and suspended evictions and foreclosures. The massive injection of stimulus is historic, representing 10% of U.S. GDP, a much larger amount than during the financial crisis in 2009. The fiscal stimulus measures were expected to expire at the end of July with the hope that the epidemic would be contained and under control. It was mean to be a bridge and has been successful in limiting the economic pain for most Americans. Sadly, much less has been done to combat the pandemic itself. The U.S. accounts for about a quarter of the worldwide total of 16 million positive cases despite representing a fraction of the global population. A lack of leadership from the White House has been a contributing factor while state and local government has been uneven at best. Nothing epitomizes this dysfunction more that disdain shown for the CDC's reopening guidelines, which after rolled out, were promptly ignored by almost every level of government. As cases rise in the south and west of the country, smashing levels first seen in April (see below) at the start of the pandemic, one can't help but feel that we wasted four months. The only silver lining is that the mortality rate has declined as scientists and doctors have learned more about the virus and how to treat it. Testing capacity, while increased in aggregate across the country is lacking in hotspots where it is most needed. Turnaround times are still slow, limiting the ability of public officials to use that data effectively, in real time, and tracing, an important component of the response has barely gotten off the ground.



Much of this could have been avoided (and was predicted by many experts) and could have been managed much better. Countries in Europe and Asia, while still seeing outbreaks are doing a significantly better job. Accordingly, the economic impact on these regions has been more subdued, with a smaller hit to growth, a lower spike in unemployment and a faster return to normal, or something close to it. At home, many indicators are turning negative, foreshadowing a more difficult period ahead. The unemployment rate is still over 11% and 18 million people (compared to 6 million before the recession) are unemployed. An additional worry is the coming wave of evictions and foreclosures that risks contagion of the housing and mortgage debt market. A survey by the Census Bureau showed that 16% of adults missed their rent or mortgage payment last month, adding another headache for the Fed to tackle.

Consequently, Congress is back to working on another round of stimulus ranging from $1-$3.5 trillion. While necessary to stop the economy from going into another coma, *The Economist* best summed up this approach in its recent edition: "This strategy of repeated enormous stimulus to cushion the blow of an ineffectual national strategy for containment resembles a hospital that invests mightily in palliative care while eliminating the oncology department."

Ten Cent Cotton and Forty Cent Meat

In the immediate outbreak of the pandemic in March and April, panic ensued at grocery stores as supply chains were stressed by shoppers hoarding everything from hand sanitizer and toilet paper to staples like milk and meat. As the virus spread to slaughterhouses and meat packing plants, Trump ordered those businesses to stay open due to the national emergency. Consequently, while inflation has been subdued, food inflation has skyrocketed pushing the CPI 0.6% higher in June, the biggest increase since 2012. The rebound in oil prices also contributed significantly to the uptick. Grocery prices, or what the government calls "food at home" have risen at a 5.6% annual rate, the highest since 2011.

At a time when so many Americans are out of work, food inflation adds another stress encapsulated by the song "Ten Cent Cotton and Forty Cent Meat," from the American epic, *The Grapes of Wrath*, and popularized by folk singer, Pete Seeger (cotton was seven cents in his version). Its first verse conveys the fragility of the country during this troubling time.

Seven cent cotton and a forty cent meat
How in the world can a poor man eat?
Flour up high and cotton down low
How in the world can we raise the dough?

If the pandemic is not contained soon, the economy will worsen, likely extending the duration of the current recession beyond best case scenarios from a couple months ago. Prospects in Europe and Asia look better than at home in direct correlation to the effectiveness of the pandemic response. As the country accumulates debt to fund fiscal stimulus, the U.S. is heading down the debt trajectory like Japan: high debt and low growth. The trade war with China in tandem with the pandemic will force a reconfiguration of global supply chains. Altogether there is a risk that the economy enters a painful period of stagflation like the 1970s.

Prince Rupert's Drops

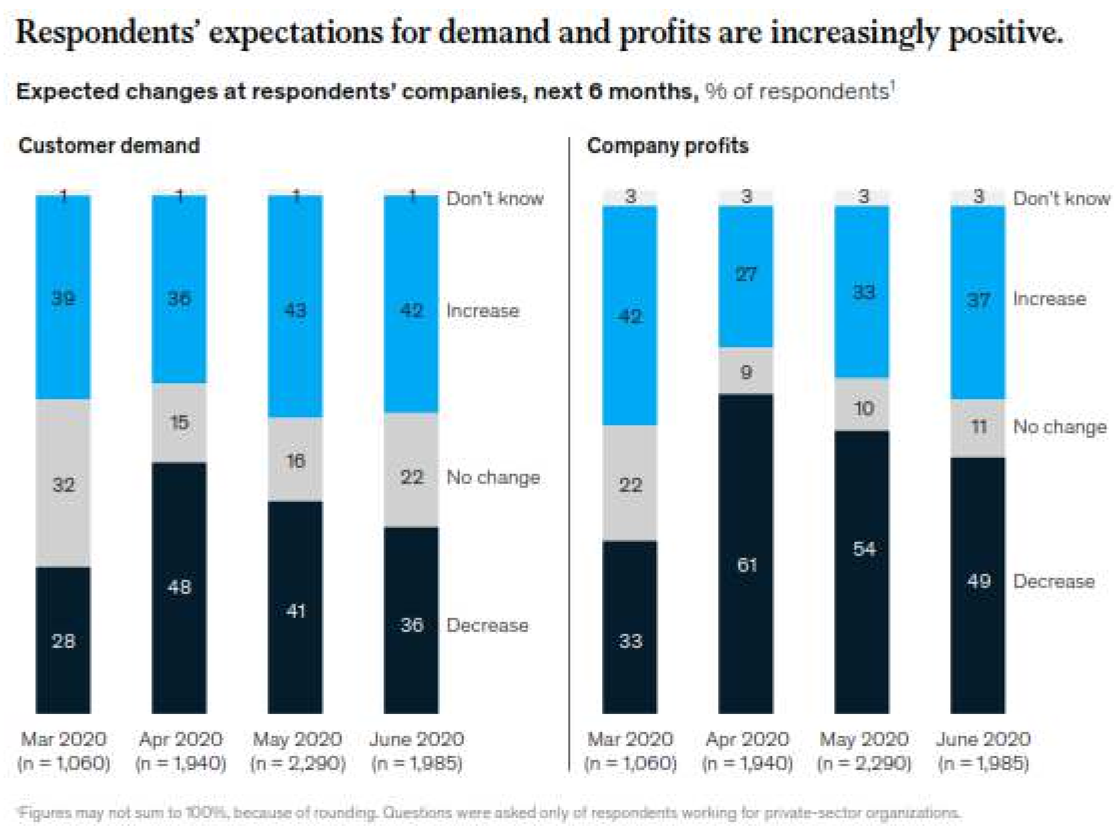
Batavian tears, also known as Prince Rupert's Drops, are a scientific curiosity brought to England for study in 1660. By dropping molten glass into cold water, the droplets solidify into a tadpole shape with properties that have interested scientists for hundreds of years. The drops have two very curious properties: the bulbous head can withstand impressive amounts of residual stress / pressure (>3,400 lbf and able to withstand a blow from a hammer), while the tail (comparable to a black swan market event), if just slightly damaged, can cause the drop to disintegrate into powder. The drops, like the economy and the market, exhibit extreme contradictory properties. Although we are a decade on from the financial crisis, many Americans have lived on a precarious personal fiscal cliff for much of that time despite strong macroeconomic readings of the economy. That feeling of anxiety at home and abroad contributed to the burst of global populism in over the past four years. The business community has been in a similar situation, seemingly resilient and growing but also dependent on ample liquidity and low interest rates to survive. For many, individuals and businesses alike, the pandemic will be a tipping point if we continue on the current path much longer.

In the business world, few sectors have been as hard hit as retail. For many companies like department stores, that have struggled to adapt to the growing e-commerce landscape, the pandemic is a death knell. Companies looking to restructure remain at great risk as rolling lockdowns limit their ability to liquidate and move forward. The chart below shows some of the casualties in the retail sector. Behind these names is a wave of more businesses that were hoping to push off difficult decisions in hope of a summer rebound.

The knock-on effects of carnage in retail on real estate and debt markets has been lurking below the surface and more adverse scenarios than a V-shaped recovery have not been priced into equity markets.

With so much uncertainty and so little visibility, confidence among consumers and business leaders, remains weak. Despite the rally in stocks, market leadership is narrow, concentrated in a handful of stocks that have done well during the pandemic. It would take only one or two to stumble for investors to lose confidence, leading to a market correction. The June McKinsey & Company executive survey of economic conditions illustrates how fickle confidence has been over the past six months. However, despite a lot of negative sentiments, there is some good news as indicated by the last two charts showing profit expectations and recovery scenarios for the global economy.

- Nearly nine in ten executives say economic conditions in their home economies are worse than six months ago. It is the largest share since April 2009. If the pandemic is contained this could be a countertrend indicator.
- 52 percent of respondents report substantially worse conditions, up from 10 percent in March.
- Outside of China, more than 90% of respondents say conditions have worsened.
- Only 11 percent of executives say their companies are fully operational again further suggesting that a recovery will be slow going. Over half say it will take until 2021 to be fully operational.
- 39 percent expect their workforce size to decline over the next 6 months.



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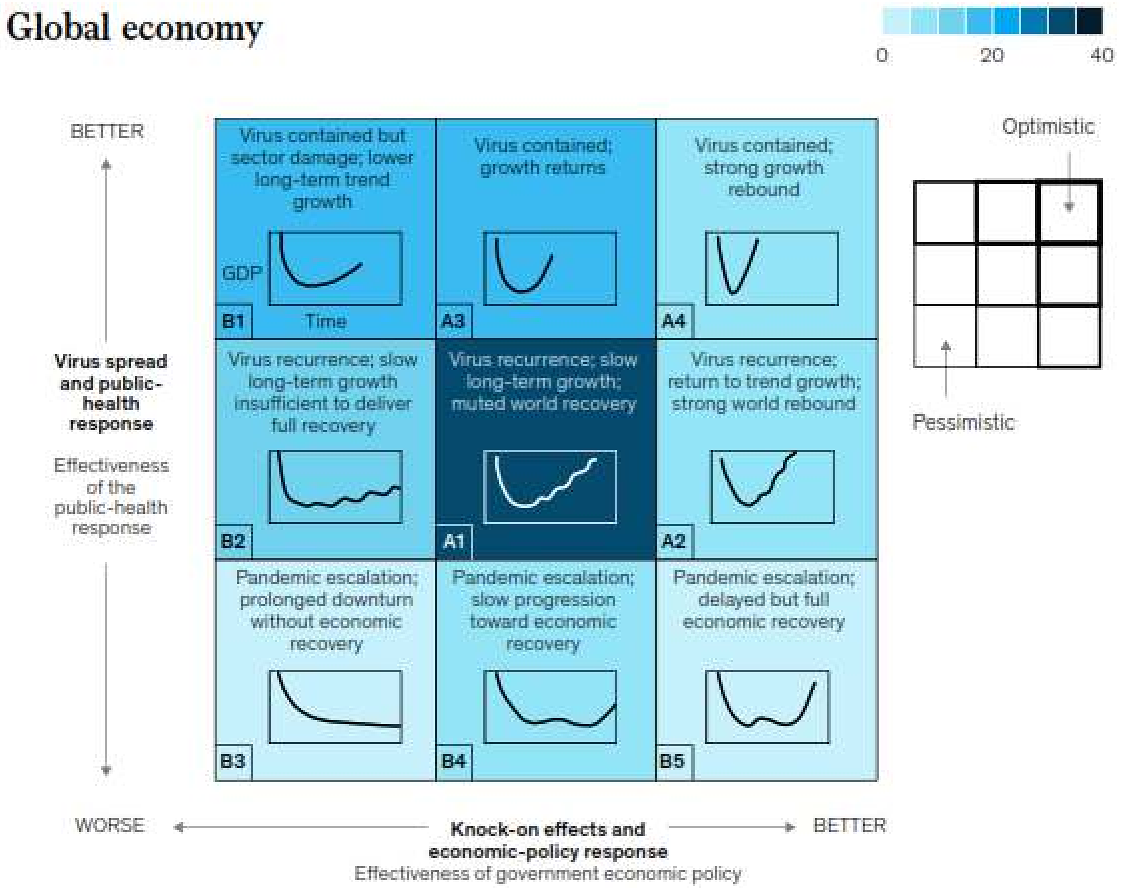
When asked about COVID-19 scenarios, respondents expect more positive outcomes for their own countries than the global economy.

Most likely scenario for COVID-19's impact on GDP, % of respondents (n = 2,174)



While there are some reasons for optimism, overall, current conditions warrant caution for equity markets. We believe that strategies that are flexible, unconstrained by asset classes or strict mandates have a better opportunity to navigate the market over the next several quarters than those that do not. The bond market and gold prices are just two market indicators suggesting a difficult, bumpy ride is ahead.

Kindest regards,

PJ Grzywacz
President

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