TC Wealth Partners LLC
Trust Company of Illinois

MATTERS OF TRUST

From the desks of William M. Giffin, CEO (left) and Kevin Rice, Senior Investment Strategist (right)

IT'S NOT OVER YET

The first six months of 2020 altered the economic, policy and investing landscape more profoundly than any other half-year period in modern history.

The first half contained an all-time high for stocks, a global pandemic, the deepest recession since the 1930s and the sharpest bear market drop on record; that was followed by a market rally that included the fifth-strongest quarterly gain in the postwar era.

As we move into the second half of the year, the reopening of the economy has spurred hope that the worst economic news is in the rearview mirror, but the economic outlook remains highly uncertain given the nature of the underlying crisis.

COVID-19

The resurgence of COVID-19 cases in the U.S. is a reminder that the global economic recovery process is likely to be choppy, uneven and more drawn out than many expected. The recent rise in U.S. cases follows the widespread re-opening of the U.S. economy. States that never fully shut down have the highest case growth, which suggests that these states only partially flattened the curve and are now experiencing an intensification of the first wave of the pandemic (See Exhibit 1).

Conversely, states such as New York, New Jersey and Illinois, which mandated shutdowns and face coverings early on, are seeing declines in new daily cases. Case increases typically lead hospitalizations by one to two weeks, and hospitalizations lead deaths by three to four weeks. The U.S. is trending in the wrong direction.

▶ *Our View*

The reporting of new cases has been partially skewed by increased availability of testing over the past few months; however, we believe the recent rise in case numbers is real, and likely continues to undercount actual infected individuals. We expect volatility to remain a feature of the pandemic landscape as markets remain hypersensitive to COVID-19 news, both positive and negative.

We believe that the consumer, impacted by the news, will be the key determinant of the pace of the economic recovery. We expect consumer confidence to remain subdued until the threat of the virus diminishes materially. The more time it takes for consumers to regain confidence, the greater the toll on small businesses and other vulnerable sectors of the global economy.

FEDERAL RESERVE

The Federal Reserve (Fed) has moved aggressively in providing policy assistance during the ongoing COVID-19 crisis by setting up unconventional lending programs. At its June FOMC press conference, the Fed indicated that it is likely to stay on an easing path for the next few years. Since March, the Fed has cut the policy rate to zero and has expanded its balance sheet by nearly 75%: from four trillion dollars to seven trillion dollars. The federal deficit is now expected to rise to almost 20% of GDP on a monthly basis, or over 130% total debt outstanding, far surpassing anything since WWII.

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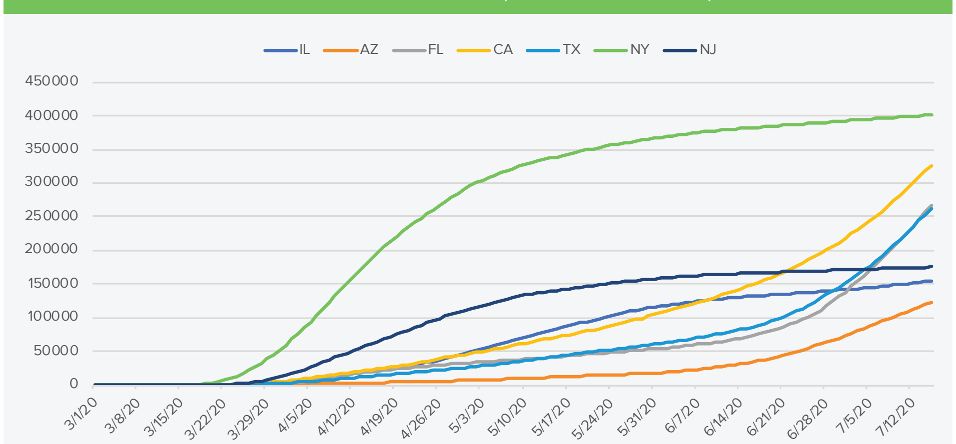
The Fed's lending facilities have succeeded in increasing the liquidity in markets and bringing yields down. To date, these facilities haven't been used very heavily (See Exhibit 2). They are meant to be a last resort for borrowers, so terms can be stringent.

Nonetheless, the Fed has had success with these facilities. It appears that just by signaling its support for markets, the Fed has succeeded in increasing liquidity and bringing yields down. It also means these facilities have plenty of money left to combat the risks of renewed weakening in the economy or deflationary pressures.

▶ *Our View*

The soaring U.S. government deficit has raised questions about whether it will hinder our economic recovery. While the deficit is a long-run concern, we believe that low interest rates and Fed policies have enabled the government to undertake significant stimulus with little downside risk—for now. We expect support from the Fed to continue for some time, with its balance sheet continuing to grow into 2021. We do not believe the Fed has used all the tools in its toolkit just yet. It still has plenty of options – besides its lending facilities – that can be called upon to support the economy.

EXHIBIT 1: NEW DAILY COVID-19 CASES (7-DAY AVERAGE)

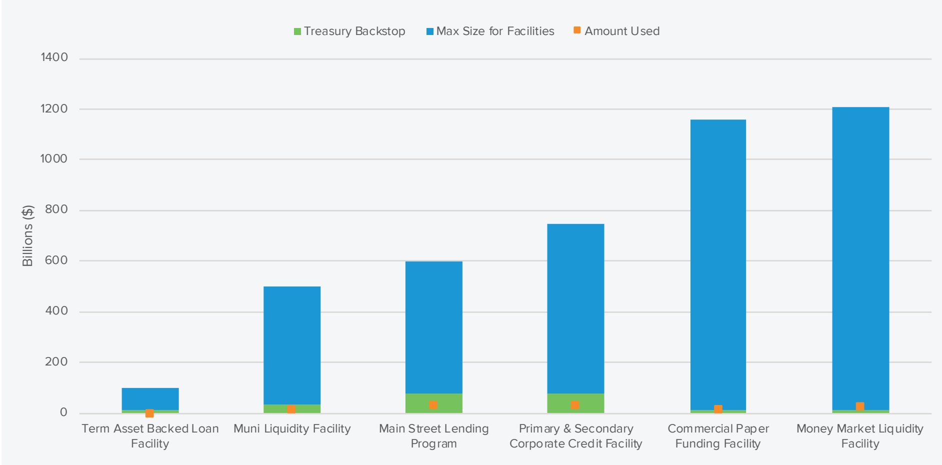


Source: TC Wealth Partners, Bloomberg (As of July 15, 2020).

EARNINGS

The release of second quarter earnings began on July 14, with some of the biggest U.S. banks reporting earnings. Analysts expect S&P 500 companies overall to report a -44.1%

EXHIBIT 2: FEDERAL RESERVE'S LENDING PROGRAMS



Source: TC Wealth Partners, Federal Reserve.

Current U.S. 12-month forward earnings show tentative signs of stabilizing, although we believe the upcoming second quarter results and guidance are biased downward.

decline in earnings for the second quarter, when the coronavirus likely took its biggest toll.

This is expected to be the low point for earnings this year and would be the second-biggest quarterly drop in earnings data since 1968. It would trail only 2008's fourth-quarter fall of 67%, when banks and other major lenders were hit at the height of the subprime mortgage crisis.

Third- and fourth-quarter 2020 earnings also look dire. Analysts see a -24.7% decline for the third quarter and a -13.1% fall in the fourth, while first-quarter 2021 earnings are expected to jump 12.1%.

Globally, earnings are expected to grow by 30% in 2021. For perspective, that is modestly stronger than the expected earnings rebound after the 2008-2009 downturn. As a reminder, it took more than three years for the level of 12-month forward-looking earnings to return to their prior peak following the Great Recession.

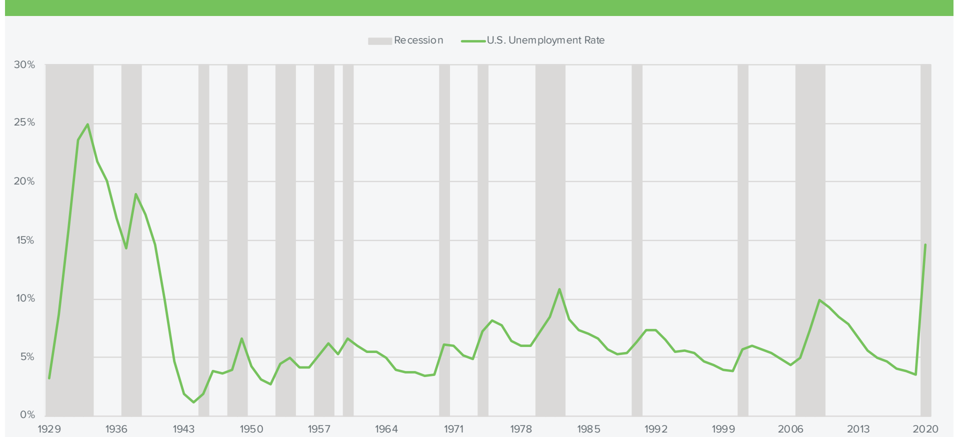
▶ *Our View*

We believe that investors have largely written off the earnings black hole in 2020 to focus entirely on the recovery that is forecasted to occur over the next 12-18 months as the economy rebounds. Current U.S. 12-month forward earnings show tentative signs of stabilizing, although we believe the upcoming second quarter results and guidance are biased downward. We believe the pandemic's earnings impact will remain with us for a while, and the earnings impact will not be uniformly distributed across all sectors, with technology and medical expected to perform reasonably well.

UNEMPLOYMENT

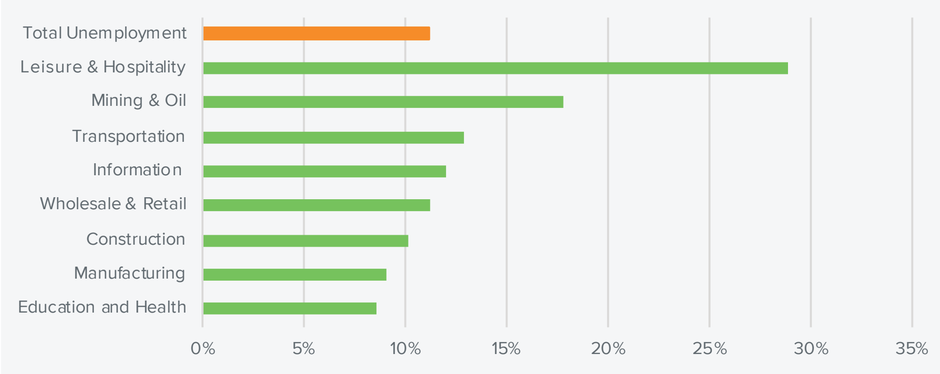
The national unemployment rate in the U.S. has fallen over the past two months from heights not seen since the Great Depression (See Exhibit 3). At its peak in April, unemployment reached a staggering 14.7%. It decreased to 13.3% percent in May and declined further to 11.2% percent

EXHIBIT 3: U.S. UNEMPLOYMENT RATE



Source: TC Wealth Partners, Bureau of Labor Statistics.

EXHIBIT 4: INDUSTRIES WITH THE HIGHEST RATE OF UNEMPLOYMENT



Source: TC Wealth Partners, Bureau of Labor Statistics.

in June. Hiring last month was supported by reopening businesses and government aid. Across the U.S., restaurants, gyms and salons, which shut down for several weeks to contain the virus's spread, began to open again. And small businesses that tapped federal loans through the Paycheck Protection Program have continued to recall workers.

Job gains in leisure and hospitality, a sector hard hit by the shutdowns (See Exhibit 4), accounted for about 40% of June's employment growth. But those sectors are particularly vulnerable to renewed layoffs as the recent rise in cases in several states is causing governors to halt or roll back re-openings.

Congress extended the Paycheck Protection Program until August 8th, which will hopefully allow small businesses in those sectors to retain employees and allow the labor market to continue to improve.

▶ ***Our View***

Given that 70% of GDP comes from consumer spending, improvement in the labor market will be critical to the economic recovery. We believe that the jump in payrolls over the past two months is an encouraging sign, but we still have a long way to go to recoup the nearly 14 million jobs lost since February.

The drop in temporary unemployment is a good sign that businesses are bringing back furloughed workers. However, in our view, this also signals that a bulk of the rehiring has occurred. The combination of this with the moderating pace of declines in weekly initial jobless claims suggests to us that the rate of hiring will slow in the second half of the year. We think the unemployment rate will trend lower toward the end of this year and contribute to the overall economic recovery.

ELECTION

With less than four months to go until the election, the race for the White House is heating up. History strongly favors the incumbent, as nearly three quarters of sitting presidents have been re-elected since 1900. However, only one has won re-election with a recession occurring sometime in the last two years of their first term. While the economic downturn could significantly diminish the chances of a Trump victory, the critical swing factor is likely to be public perception of the President's management of this crisis. Trump's approval ratings have declined over the course of the summer, ending June at their lowest level since February 2019.

In recent weeks, Joe Biden and the Democratic Party have seen a surge in the polls, against a backdrop of widespread protest against racial inequality and social justice issues, and a new wave of Covid-19 cases in the U.S. The next key event in this election will be the selection of Joe Biden's running mate - a decision that takes on more significance this year than in a normal election campaign because of Biden's refusal to commit to a second term as president.

▶ ***Our View***

Following the 2016 presidential election, the reliability of election

When looking at the impact of elections on the markets, historically they have tended to be short-term catalysts for volatility as opposed to a long-term determinant of market performance.

polls has been called into question. Therefore, we believe that national polls should not be treated as a wholly accurate forecast of who will become president, though they can be useful to gauge candidates' momentum. Similarly, betting odds can provide a helpful steer on the likelihood of different outcomes, but we believe they are also imperfect.

When looking at the impact of elections on the markets, historically they have tended to be short-term catalysts for volatility as opposed to a long-term determinant of market performance. That said, the polarized political environment seems likely to prompt episodes of volatility as we progress towards Election Day. We don't think the outcome will be a trigger for a market rally or sell-off, but we think it's likely the market will react to proposed policies from each candidate.

A Biden win would not immediately reverse all of President Trump's policies, but we do anticipate Biden to emphasize his differences with proposals related to corporate taxes and certain regulations. The market appears rather complacent on the election uncertainties for now, but we suspect one potential source of volatility will be the prospect for a party sweep across the White House and Congress; this could potentially lead to more aggressive, less obstructed policy actions.

MARKETS

DOMESTIC EQUITIES

Stocks rebounded in the second quarter, with the S&P 500 Index recording its best quarterly performance since 1998, while the Dow Jones Industrial Average jumped the most since 1987 (See Exhibit 6).

Within the S&P 500, consumer discretionary and technology companies performed the best with returns in excess of 30%. The Nasdaq reached record highs and easily outperformed the other benchmarks, and the Russell 1000 Growth Index nearly doubled the return of its value counterpart. Equity prices trended higher in the second quarter even as analysts revised their earnings expectations lower.

Progress in the battle against COVID-19 boosted markets early in the quarter, when infection rates, hospitalizations, and deaths began to decline in early April in New York and other hard-hit areas. On June 11, the S&P 500 suffered its biggest one day sell off since March 16, as investors reacted to reports of increasing numbers of cases in Arizona and Texas. Throughout the quarter, markets also reacted positively to reports of progress in developing treatments and a vaccine for COVID-19.

▶ *Our View*

During the quarter, stock prices and the economy moved in different directions. We believe this reflects not only the powerful policy support that markets have enjoyed since the COVID-19 crisis began, but also the optimism that has surrounded the economic reopening. It is no coincidence that the speed and magnitude of the fiscal and monetary policy response was matched by that of the market rebound.

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In our view, fiscal support has helped blunt the record drop in economic activity that has been brought on by the virus, while Fed programs have kept interest rates at record lows and aided credit flow to businesses. We believe that current equity valuations are expensive, but we recognize that you never want to fight the Fed.

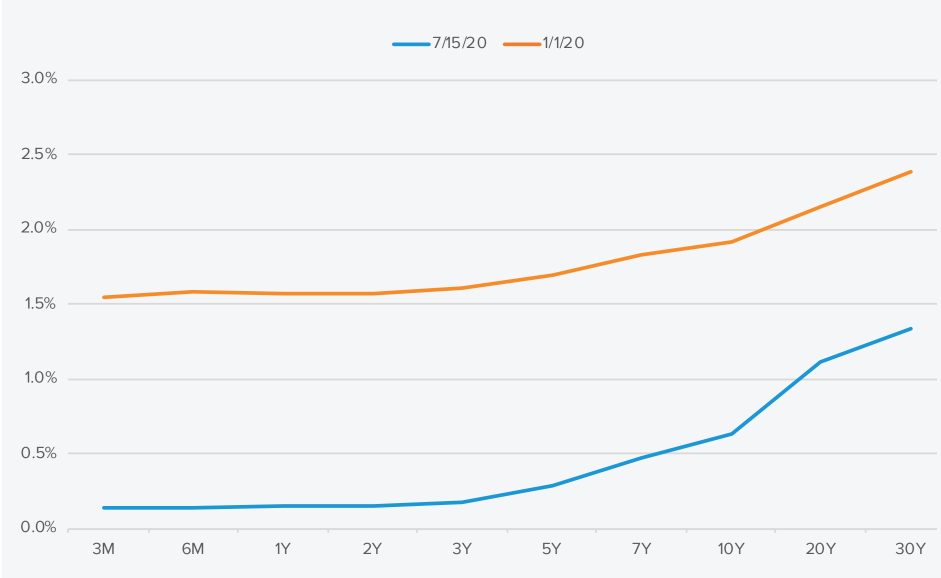
In our view, the low rate environment supports higher multiples, although we recognize that valuations are already at lofty starting levels.

INTERNATIONAL EQUITIES

Non-U.S. developed equities rallied 15-20% in the second quarter, but like the U.S., the economic picture is fairly bleak (See Exhibit 6). Europe has cautiously reopened its economy that was flatlining prior to the pandemic, and Japan was teetering on recession due to its recent sales tax hike.

The European Central Bank (ECB), the Bank of Japan (BOJ), and the Bank of England have all followed the Fed in ramping up or restarting asset purchases and rolling out various liquidity facilities, which should offer support to the markets. Emerging market (EM) equities also rallied, recording their strongest quarterly return in over a decade. This was

EXHIBIT 5: U.S. TREASURY YIELDS



Source: TC Wealth Partners, Bloomberg.

despite an acceleration in the number of new daily cases of Covid-19 in some EM countries.

▶ *Our View*

We continue to believe that economic uncertainty remains the greatest across Europe and Japan. Both entered this global crisis on weaker footing than the U.S. and the damage to economic growth and earnings is substantial. GDP is expected to decline 12% in 2020 for Europe/U.K. and 6.5% for Japan. Goldman Sachs forecasts earnings to decline by 45% in Europe and around 20% in Japan. While the ECB and BOJ have provided stimulus, they seem to regularly lag behind U.S. efforts in terms of support; therefore, we believe that their economies will take longer to recover.

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FIXED INCOME

Returns for most fixed-income sectors were positive during the quarter, helped largely by the Fed's efforts to add market liquidity and bring down yields (See Exhibit 6). Although returns were generally positive, yields swung widely as markets reacted to the sudden halt in economic growth, the Fed's rapid rate cuts and fiscal stimulus, followed by the gradual reopening of the economy.

With a rising budget deficit, Treasury issuance has shifted toward longer dated bonds, which has caused the yield curve to steepen (See Exhibit 5). Investors' search for yield and Fed support for the corporate debt market lifted the investment grade and high yield credit sectors to their best quarterly performance since 2009.

▶ *Our View*

Assuming the economy rebounds in the second half of the year, we expect longer-term yields to move slightly higher. In our view, signs of improving economic growth combined with an ever-increasing supply of Treasuries will likely result in moderately higher bond yields and a steeper yield curve.

OUR FINAL THOUGHTS

Please know that we are so appreciative to serve you through this unprecedented time in the history of this country and the world. As it pertains to our role, we will continue to keep you updated with our views as this crisis unfolds. We urge you to continue to keep a long-term perspective, review your financial plan, have conversations with your advisor, and work with them to plot your course. Please take care and be safe! ■

NOTEWORTHY

ATTENDED

SHANNON STEVENS
IICLE 2020 Estate Planning Course (Illinois Institute for Continuing Legal Education)
May 2020

CONGRATULATIONS

KEVIN RICE
Senior Investment Strategist
June 2020

EXHIBIT 6: MARKET PERFORMANCE

S&P 500 SECTORS	Q2-2020	YTD	1Yr	3Yr	5Yr	10Yr
Utilities	2.74%	-11.14%	-2.11%	6.41%	10.16%	11.31%
Real Estate	13.21%	-8.53%	-2.02%	6.32%	7.14%	9.60%
Materials	26.01%	-6.92%	-1.11%	3.90%	5.43%	9.84%
Information Technology	30.53%	14.95%	35.90%	26.80%	23.38%	20.46%
Industrials	17.01%	-14.64%	-9.05%	1.88%	6.70%	11.73%
Health Care	13.59%	-0.81%	10.90%	10.30%	8.13%	15.71%
Financials	12.20%	-23.65%	-13.98%	0.08%	5.37%	9.64%
Energy	30.51%	-35.34%	-36.09%	-12.45%	-9.17%	0.20%
Consumer Staples	8.12%	-5.66%	3.62%	5.03%	7.21%	11.78%
Consumer Discretionary	32.86%	7.23%	12.59%	15.27%	13.19%	18.17%
Communication Services	20.04%	-0.31%	11.08%	8.57%	7.17%	10.57%
DOMESTIC EQUITY INDEXES	**Q2-2020**	**YTD**	**1Yr**	**3Yr**	**5Yr**	**10Yr**
Russell 3000	22.03%	-3.48%	6.52%	10.02%	10.01%	13.71%
Russell Midcap	24.61%	-9.12%	-2.25%	5.77%	6.74%	12.33%
Russell 1000 Growth	27.84%	9.81%	23.28%	18.98%	15.87%	17.22%
Russell 1000 Value	14.29%	-16.26%	-8.85%	1.81%	4.62%	10.40%
NASDAQ	30.95%	12.74%	27.05%	19.18%	16.42%	18.34%
S&P 500	20.54%	-3.09%	7.49%	10.71%	10.71%	13.97%
FIXED INCOME INDEXES	**Q2-2020**	**YTD**	**1Yr**	**3Yr**	**5Yr**	**10Yr**
Global Aggregate ex. US	3.38%	0.61%	0.71%	2.52%	2.89%	1.98%
US Aggregate	2.90%	6.14%	8.74%	5.32%	4.30%	3.82%
Treasury	0.48%	8.71%	10.45%	5.57%	4.07%	3.40%
High Yield	10.18%	-3.80%	0.03%	3.33%	4.78%	6.68%
TIPs	4.24%	6.01%	8.28%	5.04%	3.74%	3.52%
Municipals	2.72%	2.08%	4.45%	4.21%	3.93%	4.21%
Asset Backed Securities	3.54%	3.32%	4.68%	3.34%	2.67%	2.57%
Mortgage Backed Securities	0.67%	3.50%	5.67%	3.97%	3.22%	3.06%
Commercial Mortgage Backed Securities	3.82%	4.30%	5.94%	4.89%	4.14%	4.98%
INTERNATIONAL EQUITY MARKETS	**Q2-2020**	**YTD**	**1Yr**	**3Yr**	**5Yr**	**10Yr**
MSCI World	19.57%	-5.47%	3.43%	7.32%	7.53%	10.60%
MSCI ACWI	19.41%	-5.98%	2.66%	6.72%	7.06%	9.77%
MSCI ACWI ex US	16.33%	-10.74%	-4.34%	1.66%	2.80%	5.51%
MSCI EAFE	15.15%	-11.03%	-4.63%	1.38%	2.63%	6.31%
MSCI EM	17.43%	-11.93%	-4.92%	0.66%	2.74%	7.11%
MSCI Europe	13.02%	-12.46%	-4.97%	1.08%	1.87%	7.15%
MSCI Asia Pacific	15.97%	-6.27%	1.44%	3.65%	4.50%	6.52%
MSCI North America	21.70%	-2.69%	7.58%	10.54%	10.29%	13.36%
MSCI EM Asia	17.86%	-3.42%	5.14%	4.40%	5.15%	6.14%
MSCI EM Latin America	19.20%	-35.13%	-32.26%	-6.90%	-2.91%	-3.55%
MSCI EM Europe & ME	19.09%	-21.27%	-19.30%	-2.73%	-2.07%	0.00%

Source: TC Wealth Partners, Bloomberg.