



C.W. O'Conner Wealth Advisors, Inc.

Economic Update and Policy Response

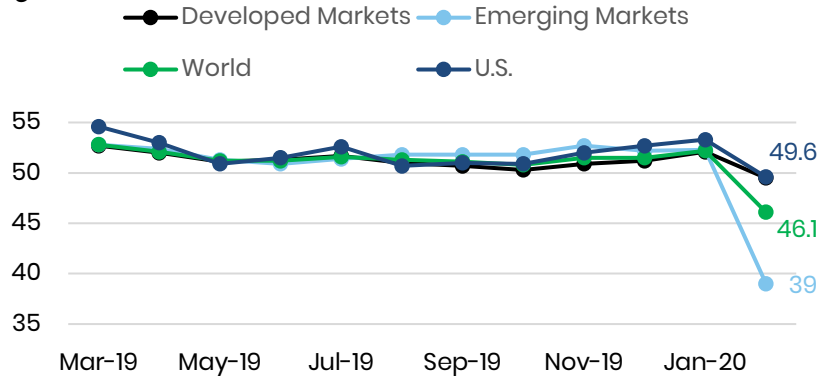
March 2020

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GLOBAL SLOWDOWN

PMI Composites: Developed Market Resiliency TBD

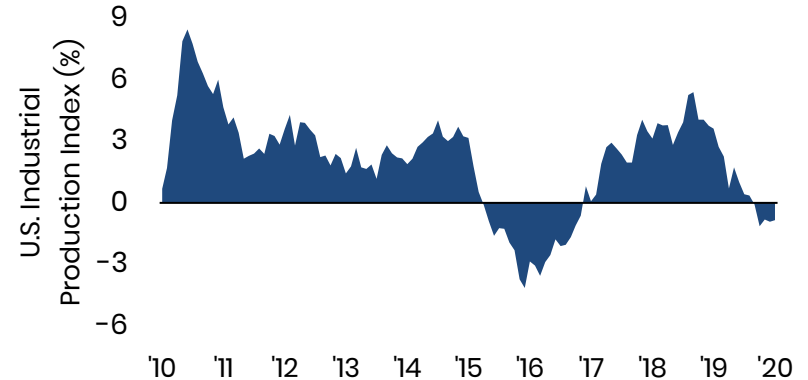
Emerging markets were hit hard in February as China grappled with the COVID-19 outbreak now permeating the globe.



Source: Federal Reserve Bank of New York

U.S. Industrial Production Signals Recession

Since 1920, the prior 17 recessions (and depression) coincided or followed every contractionary period except from 2015 – 2016.



Source: Federal Reserve Bank of St. Louis

Federal Reserve Bank of New York Recession Prediction Model, Next Twelve Months

While the probability remains under 50 percent, its worth observing that in 2010 the U.S. fell into a recession shortly after the model recorded a 40 percent probability. As of February 2020, the probability fell to 31 percent, but the probability likely rose in March.

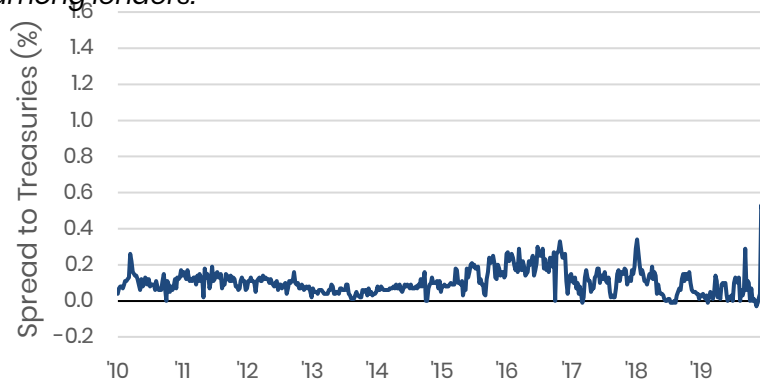


Source: Federal Reserve Bank of New York. Grey bars denote recessionary periods. The National Bureau of Economic Research (NBER) defines a recession as a recession is "a significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in real GDP, real income, employment, industrial production, and wholesale-retail sales." See <https://www.nber.org/cycles.html> for more information. Past performance does not indicate future performance.

U.S. FIXED INCOME SIGNALS

3-Month Nonfinancial Commercial Paper Spread

Corporations rely on short-term debt to meet short-term liabilities. Widening spreads reveal liquidity funding stress among lenders.



Source: Board of Governors of the Federal Reserve System (US)

(Corporate) Credit Check

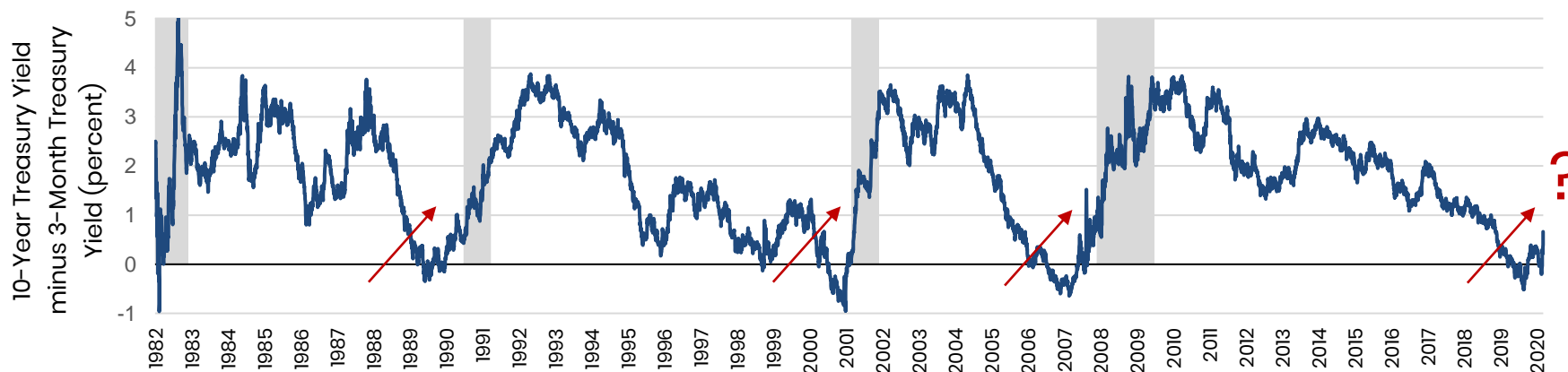
Corporate credit spreads (over Treasuries) moved sharply higher in March, weighing on core bond and high yield returns.



Source: ICE Data Indices, LLC, Federal Reserve Banks of St. Louis

Beware of the Yield Curve

Inverted yield curves offer a cautionary signal, but recessions often coincide with yield curve steepening as monetary policy pushes down short-term rates in an effort to extend the current cycle.



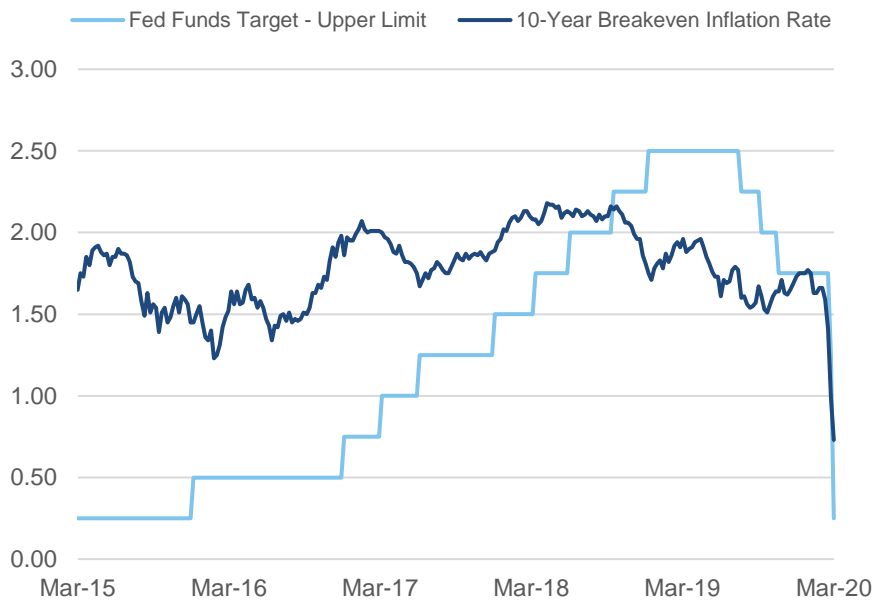
Source: Federal Reserve Bank of New York. Grey bars denote recessionary periods. Past performance does not indicate future performance..

MONETARY POLICY RESPONSE

On March 15, the Fed issued an unscheduled press release outlining the following major policy actions:

- ✓ Set lower bound policy target rate to zero (range 0–0.25%)
- ✓ Reboot quantitative easing
- ✓ Expand repo market operations
- ✓ Make it easier for foreign developed banks to access U.S. dollars through swap lines

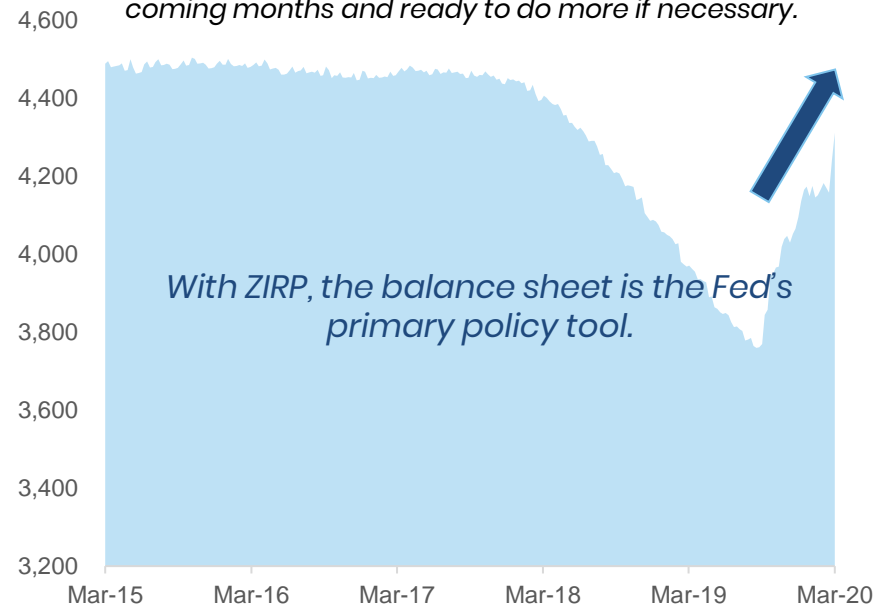
Zero Interest Rate Policy (ZIRP) Redux
Federal Reserve lowered interest rates to a range of 0–0.25% Sunday, March 15.



Source: Federal Reserve Bank of St. Louis 3/16/2020.
 Past performance does not indicate future performance.

Federal Reserve Balance Sheet (\$B)

Despite growing \$552 billion since August 2019, the Fed intends to grow its balance sheet another \$700 billion in coming months and ready to do more if necessary.



Source: Federal Reserve Bank of St. Louis 3/16/2020.

MONETARY POLICY RESPONSE (CONT.)

- ✓ March 17 – Established the **Commercial Paper Funding Facility (CPFF)** effective immediately
 - Intended to support the flow of credit to households and businesses by alleviating short-term funding stress.
 - Commercial paper markets finance a variety of economic activity and supply credit, and funding for auto loans, mortgages and liquidity to meet operational needs of companies.

- ✓ March 17 – Established **Primary Dealer Credit Facility (PDCF)** effective March 20
 - Intended to provide liquidity to credit markets using primary dealers (banks authorized to trade with the U.S. government).
 - Allows primary dealers to borrow from one to 90 days from the Fed
 - Primary dealers may collateralize loans with:
 - Investment grade debt
 - Commercial paper
 - Municipal bonds
 - Equity securities

MONETARY POLICY RESPONSE (CONT.)

- ✓ March 18 – Established the **Money Market Mutual Fund Liquidity Facility (MMLF)** effective immediately.
 - Intended to support the function of money market funds by making loans to eligible financial institutions secured by high-quality assets
 - Proceeds from loans should help money market funds meet redemption demands

- ✓ March 23 – The Fed announces it will begin purchasing commercial mortgage-backed securities (CMBS) in addition to Treasury and agency mortgage-backed securities (MBS).
 - This means the Fed will purchase as many Treasury, MBS and CMBS as necessary to support market function.
 - This action is incremental to the \$700 billion QE program announced on March 15

- ✓ March 23 – Established programs to support households and small businesses.
 - Provide up to \$300 billion in new financing available to employers, consumers and businesses. The Treasury Department, using the **Exchange Stabilization Fund (ESF)** will provide \$30 billion billion in equity to the Fed to make these loans.

MONETARY POLICY RESPONSE (CONT.)

- ✓ March 23 (cont.)
 - Establish **Primary Market Corporate Credit Facility (PMCCF)** for new bond and loan issuance and the **Secondary Market Corporate Credit Facility (SMCCF)** to provide liquidity for outstanding corporate bonds.
 - PMCCF will allow companies access to credit to maintain business operations during the pandemic. It is open to investment grade companies and will provide credit up to four years.
 - SMCCF will purchase investment-grade corporate bonds (issued by U.S. companies) and U.S. listed exchange traded funds that are (1) investment grade and (2) provide broad exposure to the market for U.S. investment-grade corporate bonds
 - Establish the **Term Asset-Backed Securities Loan Facility (TALF)** to support consumer and business access to credit. The TALF will enable issuance of asset-backed securities (ABS) backed by student loans, auto loans credit card loans and loans guaranteed by the Small Business Administration (SBA). Expand the MMLF to allow for a broader range of collateral in exchange for credit for municipalities. New collateral include certificates of deposit (CDs) and variable rate demand notes (VRDNs).

MONETARY POLICY RESPONSE (CONT.)

- ✓ March 23 (cont.)
 - Expand the CPFF to include high-quality, tax-exempt commercial paper as eligible securities to aid the flow to credit to municipalities. The price of the facility has also been reduced.
 - Announced establishment of a Main Street Business Lending Program (MSBLP) to support lending to eligible small- and medium-sized business to complement SBA efforts.

MONETARY POLICY RESPONSE (CONT.)

European Central Bank Policy Response

- ✓ March 18 – The European Central Bank (ECB) announces the following actions:
 - €750 billion **Pandemic Emergency Purchase Programme (PEPP)** to purchase public and private sector securities.
 - Expand the range of eligible assets under the **Corporate Sector Purchase Program (CSPP)** to include non-financial commercial paper (similar to the Fed's CPFF).
 - Ease collateral standards under the **Additional Credit Claims (ACC)** program to ensure counterparties can continue to use the Eurosystem's refinancing operations.

Our take on the monetary policy responses:

- *The Fed and ECB took several steps to alleviate mounting liquidity pressures on U.S. credit markets.*
- *Since the cumulative effects of these policy tools will take time to work through the economy, we continue to expect elevated volatility in fixed income assets.*
- *Therefore, we believe investors should stick to their long-term strategic allocation investment process and avoid tactical positioning.*

FISCAL POLICY RESPONSE

- ✓ March 18 – U.S. enacts the **Families First Coronavirus Response Act** (H.R. 6201) effective April 2, 2020, until December 31, 2020, to provide:
 - Emergency paid sick leave¹
 - Eligibility: All employees of employers with fewer than 500 employees, regardless of tenure with employer who meets the defined qualifications
 - Benefit: Full-time employees receive 80 hours of paid sick leave. Part-time employees receive the equivalent number of hours they would work during a two-week pay period.
 - Free coronavirus testing
 - Expanding food assistance and unemployment benefits
 - Requires employers to provide additional protections for health care workers

Source: Forbes, "Time to Hit Pause: What Employers Need To Know About Yesterday's Families First Coronavirus Response Act"

FISCAL POLICY RESPONSE (CONT.)

- Expansion of Family Medical Leave Act (FMLA)¹ to provide benefits to employees with school-aged children or children in daycare
 - Eligibility: While FMLA presently applies to employers with 50 or more employees and to employees who worked for at least one year or 1,250 hours, from April 2 through year-end, FMLA will apply to all employers with less than 500 employees who worked at least 30 days.
 - Qualification: Eligible employee may take up to 12 weeks of leave if he/she is unable to work (including telework) because he/she must care for his/her child under 18 years of age and whose school or place of care closed due to COVID-19.
 - Benefit: Qualified employee may take up to 12 weeks of leave, but the initial 10 days will be unpaid (unless the employee elects to use accrued PTO). After the initial 10-day period, the employee is entitled to receive two-thirds of normal wages, up to \$200/day. Total employee benefits under this provision are capped at \$10,000.

Source: Forbes, "Time to Hit Pause: What Employers Need To Know About Yesterday's Families First Coronavirus Response Act"

QUESTIONS? WE'RE HERE TO HELP.



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If you have questions about the topics covered in this material, please reach out to us directly at (770) 368-9919, or email Cliff at cliff@cwoconner.com or Kevin at kevin@cwoconner.com.

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