notes from the Assabet Vol. XVIII No. 1

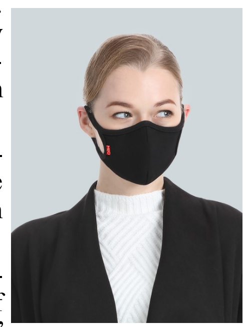
First Quarter, 2020

New Normal?

The concept of a "new normal" basically refers to a significant alteration in how things work. With the "new normal," owing to technological innovation, demographic transformation, political adjustments, or climate change, the normal way in which we have lived and behaved in the past has been transformed.

The term itself is attributed to Mohamed A El-Erian, PIMCO's CEO. In a 2010 speech, he used it in a discussion of the financial and economic crisis triggering the "Great Recession." He explained, "Our use of the term was an attempt to move beyond the notion that the crisis was a mere flesh wound….instead the crisis cut to the bone." In this statement, he defined "new normal" to systems and lifestyles which emerged from massive shocks to the prior systems, requiring extreme change. A new normal, he suggested, is one in which a return to "life as it was" is not possible. Certain implications of the crisis will be long-term.

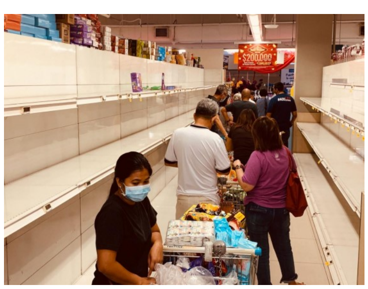
Also in 2010, "new normal" became associated scornfully with President Obama's use of the term identifying the period after the recession. Our country's rescue and recovery from the financial crisis of 2008-2009 involved extreme measures in monetary and fiscal response, plus attention to regulatory controls. Obama's intention was to set expectations for a period of slow growth, high unemployment and high debt, typical of times following a banking crisis. Critics saw his "new normal" as an excuse for such a disappointing environment.



Another notable use of "new normal" was by Xi Jin Ping, General Secretary of China's Communist Party. He was alerting the world to an economic slowdown in China, a departure from double-digit growth that would have global impact.

In all of these cases, "new normal" declarations followed difficult, usually surprising times. They made clear that concepts of "back to normal," "business as usual," "when this is over," wouldn't apply. How things would have to change, employing new systems and routines until the next "new normal." There is some chatter about a "new normal" for our country now, and certainly a lot of a yearning: "when this is over." However, we are in the midst of a crisis—an extremely difficult and surprising time, not the aftermath in which a new normal can be formed.

Americans have made incredible adjustments across the country in a short time, albeit irregularly. As of March 15, we talked about needing only 2 weeks worth of food in our homes. We hadn't quite cancelled vacation plans. Florida beaches hosted Spring Break celebrants. Massachusetts schools were still open, on the verge of closure. Articles written by investment management companies tended to focus on the gigantic stock market decline. They speculated how soon the COVID-19 crisis would be over so the market could recover, presumably continuing the long bull market, as generally predicted as recently as February. Continued page 2



WWW.ASSABETADVISORS.COM

Assabet Advisors LLC
customized investment solutions

Wayne Ushman

Robert Jacobsen

Assabet Advisors is an independent Massachusetts Registered Investment Adviser, seeking sound and customized investment solutions for high net worth individuals, businesses and foundations.

Focusing our business on larger portfolios, we are able to offer our clients highly flexible and personalized services.

We are among a limited group of fee-based advisors who are approved by Dimensional Fund Advisors for access to their funds.

1087 Main Street
Holden, MA 01520
Tel: 508-351-9666
Fax: 508-351-9689
wushman@assabetadvisors.com
rjacobsen@assabetadvisors.com

New Normal? continued

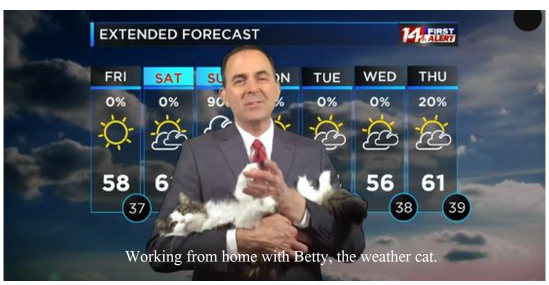
We didn't discuss the nature of a "new normal." We didn't anticipate one at all. Rather, we wondered when the crisis would be over. Meanwhile, as the coronavirus expanded, we experienced a daily "adjustment reaction" as we adapted to radical changes in our lifestyles. We all know these things, of course, but listing them gives us the full impact of what we've experienced. It also tells us how far we are from a "new normal."

"Essential" workers aside, we went home, either laid off, possibly to ponder the loss of income and health insurance, or to work from home. Restaurants were closed to eat-in patrons, stores not providing necessary goods were closed to walk-in shoppers, health care became concentrated on the virus, while most surgeries were postponed and doctors were consulted via telephone. Food shopping was a challenge, as consumers vacillated between entering a grocery store with bare shelves or purchasing pickup orders available in a few days. (And what can we even say about toilet paper?) Gyms, libraries, theaters and hotels were emptied. Government directives have altered almost daily while illness and fatalities have risen.

"Virtual" defines how most of our social involvement occurs. We worship via Facebook, have birthday parties through ZOOM, enjoy a glass of wine with friends on our iPads. Children are homeschooled. Creative and encouraging distractions for kids and adults appear regularly. Even without clear expectations or established instructions, we continue to adapt, often to lifestyles far from our former practices.

Discussion of the "new normal" in our future is premature. New normals *follow* crises, making change in order to eradicate the damage done. New normals in the past don't give us much guidance because they have concentrated on economic or financial renovation, as that was the source of crisis. New normals require a level of stability in government. So we aren't there. But those who study the possibilities offer some interesting projections. They suggest a new normal with far more breadth, encompassing our health system, of course, but also our economy.

Some pundits project a long and irregular transition as we move in and out of the need for social distancing. There remain critical questions not yet answered. We have to test, identify infection persons, isolate them and trace their contacts. And it will take time to provide inoculation and treatment. Also, Americans, known for individualism, can be impatient with containment efforts. However, this pandemic was a sudden and severe shock that hit all of us, showing no concession for people of privilege and status. Perhaps we will draw lessons from this unique experience and cooperate with a national plan for recuperation and ongoing safety. Hopefully we will be better prepared to respond to further threats.



Working from home with Betty, the weather cat.

What patterns from our weeks of social distancing might remain as a part of our "new normal" when we enjoy more freedom? How will heightened respect for health workers be evident? Now that more employers and workers have experienced working from home, will that be a greater percentage of the labor force? We've become more competent and comfortable with virtual meetings. Especially in a business setting, we've noticed the new efficiency of time and expense when avoiding flights. Will there be less travel? Many parents have enjoyed their greater informal exposure to their children. Will they be less willing to sacrifice family time or work/home balance than before the pandemic? And how about our recent restraint in interpersonal contact? Will we remain cautious about handshakes, casual embraces, and sexual freedom? How many times a day will we wash our hands? Will we miss those walks?

On a much more significant level, will our experience with coronavirus have taught us how things are connected? The lifestyle of people without access to healthcare coverage critically impacts that of those with greater protection. Climate change is linked to disease. Extreme wealth inequality hurts us all. Corporate strategies focusing exclusively on profits and markets rather than considering their affect on workers and communities, undercut their own long-term resiliency. Will our "new normal" recognize and incorporate what many individuals have noticed in this difficult chapter: we're all in this together? We are all stakeholders.

A. Winston, "Is the COVID-19 Outbreak a Black Swan or a New Normal?" Sloanreview.mit.edu, 3/16/20, M. DeWeaver, "This is the End: The Myth of a Return to Normal," seekingalpha.com 3/13/20, Lichfield, "We're Not Going Back to the New Normal," technologyreview.com, 3/17/20, J. Lanard & P. Sandman, "Past Time to Tell the Public: 'It Will Probably Go Pandemic'," virologydownunder.com, 2/23/20, E. Yong, "The New Normal. What to Expect From Our Economy," theatlantic.com, 3/25/20, CBSnews.com, 9/26/10, Ian Davis. "The New Normal," McKinsey.com, 2009 Commentary.

Economic and Financial Overview

On February 12, with world equity markets already traumatizing investors, the Dow Jones Industrial Average (DJIA), S&P 500 and NASDAQ reached record highs, extending an extraordinary period of ups and downs. Equity markets worldwide had their largest weekly losses since 2008 in the final week of February. Severe volatility continued, reacting to news of the coronavirus, with help from an oil price war between Russia and OPEC nations. Early on, analysts, many of whom had forecast continued moderate growth in a wary market, tried to offer explanations and predictions related principally to the markets. Over time, however, dread of the pandemic's impact caused most economists to throw up their hands. In early April, Michael Antonelli, chief strategist at Baird spoke for most in saying, "Forecasts are all over the place - it's just outright throwing a dart." From that point, any hope of a V-shaped economic recovery is purely speculative.

The pandemic has been the cause of widespread economic damage. China, the world's foremost industrial provider, closed supply chains, causing a substantial turn in economies throughout the world. As the U.S. slowly began to fight the virus, shutting down all but "essential" jobs, and moving individuals into their homes, unemployment skyrocketed. Business profits tumbled and vulnerable companies faced failure. Even at the $2 trillion level, the coronavirus emergency funding proved insufficient in areas such as the Small Business Administration. Housing is in a slump. Buyers and sellers are quarantined. Construction has been paralyzed. With layoffs in the millions, consumers have lacked spending power, and there are far fewer places to spend. Although the economy will be "reopened" soon in some locations, the bounce back probably will not compensate for the massive losses.

No one can reasonably predict the behavior of the virus, or of the American people, or of the president, for that matter. We just know that our struggles won't abate quickly. Meanwhile, the basic infrastructure will progress as best it can, hopefully improving slowly. In the first quarter, large growth stocks fell by –14.1%, large value by –26.7%, small growth declined –25.8% and small value by –35.7%. Consumer staples, healthcare and utilities were the strongest performers while energy (-50.5%) financials (-31.9% and industrials (-27.0%) fell farthest. Wall Street economists are not promising a speedy recovery. Long Treasury bonds performed well in the quarter as the Fed kept interest rates close to zero. The Bloomberg Barclays

It Takes All Kinds

Difficult times offer opportunities for individuals to take personal advantage, or to be self-sacrificing. Suffering people, with limited options, are easy to defraud or bully. Greedy people can find ways to share in benefits intended for misfortunate people by public and private institutions. And there always are ways to be kind and offer help. With millions of people sick and dying, unemployed and destitute, these certainly are difficult times, presenting opportunities to be self-seeking or selfless. It's a choice that arises from personal character. Some people, with or without great wealth, tend to be generous through compassion, or perhaps from a sense of obligation. Some Americans realize that the $1,200 stimulus check they received was sent to offset personal economic loss, something they have not suffered themselves. Rather than spending the windfall on their own needs and pleasures, they contribute it to help those who are suffering. Some leave large tips for the people who risk themselves to deliver food orders. On the other hand, some Americans spot a way to make money at the expense of others.

Altruistic actions range from modest to considerable, while selfish acts extend from simply greedy to criminal. A Wall Street debate, fueled by an article in Bloomberg, deliberates that topic. Apparently, some hedge funds applied to receive bailouts from the SBA's Paycheck Protection Program (PPP), a first-come, first-serve program intended to cover payroll, rent and utilities for companies with 500 or fewer employees. Hedge fund eligibility is not clear, but certain firms figured that it was worth a try. Some in the money management community called it "morally corrupt" or "a complete abomination." Others offered a defense. The $349 billion set aside for the PPP loans was exhausted in two weeks. Especially in the hospitality and restaurant industries, money was distributed to the subsidiaries of very large companies with access to other sources of capital. Some examples display a selfish response. Yet Shake Shack decided to return their $10 million loan when they learned how many more needy restaurants received nothing. Congress will replenish the PPP loans, perhaps with better oversight.

S. Ruhle, A. Johnson, "Government Loans for Small Businesses Out of Money," Nbcnews.com, 4/20/20, M. DeCambre, "'It's a Complete Abomination'," Marketwatch, 4/15/20, J. Legum, "A Raw Deal," popularinformationsubstack.com, 4/20/20, K. Burton, J. Fineman, "Hedge Fund Managers are Claiming Bailout as Small Businesses," Bloomberg.com, 4/14/20

Modern or Magic?

We tend to be consumed these days with circumstances caused by the pandemic. Some of us are working from home, which is difficult enough, but also are managing home schooling. Those living alone long for a human presence. We all are trying to figure out how best to handle what used to be the simple details of our lives: purchasing food, arranging social encounters, caring for independent seniors, and so on. But although our focus is on the immediate challenges of life, most of us are aware of the looming threat to our economy. Sooner or later, we will have to pick up the mess left behind.

In a crisis, things have to move quickly. 701,000 jobs were lost in March, schools were shut and small businesses faced closure. The federal government had to provide support. In rapid pace, the Congress passed the CARES Act, a roughly $2 trillion Coronavirus aid package, with help for big corporations, individuals, small businesses, states and local governments, public health, and education. We'll be saddled with an exorbitant debt. Governments at state and federal levels may suffer a significant drop in tax revenue. Consumer spending will decline in response to lower employment and stock market losses.

The budget deficit amassed by these expenses, comes on top of an already substantial deficit. For purposes of this discussion, it's useful to remember that despite the fact that both political parties espouse an aversion to high federal deficits, administrations on both sides have consistently run large deficits. Democrats have tended to be the more conservative party, concerned that high debt will have to be paid for by tax hikes. Ironically, the GOP, the standard bearer for federal debt control, has since Reagan, at least, built up high deficits for Democratic administrations to cut down. The U.S. ended 2019 with a deficit at nearly $1 trillion. And now this. As a country, we simultaneously criticize and generate healthy deficits. It will be interesting to see how we approach our growing debt burden.

One macroeconomic policy that has been around on the fringes for a while, but recently is attracting more public attention, is Modern Monetary Theory. "MMT" is ridiculed as "utopian thinking" by some, but defended by others as an innovative response to an outdated model. Both its support and its disparagement stem from its challenge to our longstanding principle that high deficits are inflationary and must be removed: that debt must be paid by 1) taxes, or 2) borrowing money by selling bonds to investors. MMT disciples call that an unnecessary regression to gold-standard thinking in which the value of money had to be backed by a fixed asset. With fiat currency (introduced in 1971), they argue, countries that issue their own currency can never run out of money. This does not mean that we don't have to pay our bills. Rather, MMT lays out a system that handles federal money management differently than our standard policy. Here are a few nuggets, not enough to explain the logic of MMT but sufficient to give a sense of how different it is. You may recognize these concepts when following political debates, perhaps the nuggets will excite your interest. (Note: MMT enthusiasts are not always uniform in their thinking.)

1. All money systems seek to achieve full employment and keep a lid on inflation, maintaining price stability. While our current system depends upon *monetary* policy to manipulate interest rates in order to make economic adjustments, MMT uses *fiscal* policy, government spending and taxation, to do so. According to MMT, interest rates should remain stable at 0, and bond sales should not be required.

2. While conventional policy says that high deficits lead to higher interest rates, MMT argues that as the government spends more, the private sector gets more money which is put into the banking system causing rates to fall.

3. MMT: spending "too much" raises inflation only when both public and private spend too much at the same time. In this event, the government uses taxation as a policy tool to reduce aggregate demand, not to fund government expenses.

4. MMT believes that the federal government should fund a Job Guarantee, locally administered, making low wage jobs available to all who need them during economic slumps, ensuring full employment.

MMT is controversial, even called the "Magic Money Tree," yet often misrepresented by detractors. But it has been given notice, particularly in the current political discord.

C. Roche, "You Can't Debunk MMT," pragcap.com, 1/10/19, M. Kilcoyne, "Modern Monetary Theory is no Magic Money, Tree," adamsmith.org, 5/20/19, P. Coy, K. Dimitrieva, M. Boester, Modern Monetary Theory: the Beginners Guide," Bloomberg.com, 3/21/19, R.Murphy, "The Upside-down World of MMT," Libertarianinstitute.org, 1/25/19, D. Matthew, "Modern Monetary Theory Explained, vox.com, 4/16/19, K. Snell, "What's Inside the Senate's $2 Trillion Coronavirus Aid Package, npr.org, 3/26/20