The Long Run

INVESTMENT LETTER | APRIL 2020

“Patience and fortitude conquer all things.”
- Ralph Waldo Emerson

Pulling the lens back to gain perspective can be particularly difficult when news is unfolding at such an extraordinary pace before our eyes. Add the reality that we are currently captive in a state of social distancing and economic suspension until the relentless wave of this deadly virus passes, and it becomes nearly impossible. But perspective and balance are critically important now, and we all need to step back on occasion to analyze this terrible event in a larger frame. We cannot let immediate fear – or the constant drumbeat of bad news during this acute period of crisis – push us into poor decisions, or drive us away from the fundamental disciplines that secure our financial foundations.

It seems so long ago now, but we entered 2020 on a high note. The S&P 500 was up nearly 30% in 2019. We had just finished “phase 1” of the China trade deal, and many economists were talking about how Europe, the United States, and China were all poised to begin a cycle of faster global growth. With earnings for S&P 500 companies growing at less than 1% in 2019, however, almost all the gains were predicated on expanding growth in 2020. The equity market legged up an additional 9% at the beginning of this year on the promise of good things to come. When the coronavirus entered the scene and showed its potential to erase global economic growth in 2020, therefore, we were not surprised to see the ferocity of the equity selloff. It took only 22 trading days for the S&P 500 to drop 30% from its February 19 high – the fastest such decline in history.

As Warren Buffet is fond of saying, “When the tide goes out, you find out who is wearing a bathing suit.” For many years, we have been expressing concern to clients about the impact of easy credit on everything from small businesses to private equity to commercial real estate. The rapid decline in equity prices in March, combined with the economic suppression needed to battle the virus, unmasked many areas of the economy deeply reliant on debt. It also waffled levered investors who suddenly faced margin calls as the value of their collateral dropped. As bills came due, a huge cohort of indebted enterprises and investors needed to sell assets to raise cash. In a normal bear market, people often will sell growth instruments, like stocks or real estate, to move to U.S. Treasury bonds or gold for safety. During many days in March, however, stocks, U.S. Treasuries, and gold all dropped in unison – demonstrating the enormous chase for cash and underscoring just how much leverage was in the system.

This point about leverage is important because it opened the door to a set of deeper concerns that dramatically accelerated last month’s market declines. As a crushing herd sold assets to raise cash, liquidity started to dry up – and credit markets began to lose their function. This was a frightening echo of the very same signals that ended up leading to the financial crisis in 2008. Once again, the credit markets looked to be the canary in the coal mine for a system so leveraged that it could seize. This is why the Federal Reserve stepped in with an extraordinary backstop to shore up credit markets on March 15. Utilizing tested playbooks from the financial crisis and Japan, the Federal Reserve dropped interest rates effectively to zero and became the buyer of last resort for credit markets, confirming that it would do “whatever it takes” to keep them open. This action provided the critical liquidity needed and calmed roiled credit markets. A week later, news came of the likely passage of the $2 trillion coronavirus relief bill in Congress. This powerful combination of policy responses helped to stop the precipitous declines in the equity market – and, in fact, contributed to a startling 20% upward bounce in the S&P 500 at the end of March. (We will reserve comment on the potential long-term impacts of such government largess for another day.)

As of this writing, the equity markets have given a bit of that month-end bounce back. While volatility is somewhat reduced, we suspect that we will test the market lows of March again as news and disquieting images emerge out of New York and other impacted areas. Despite all of the conversation about filling churches on Easter and opening the economy in April, it is now becoming clear to all that this crisis will be measured in months and not weeks. The economic reality of soaring unemployment and lost earnings cannot all be countered by government policy and, as the timeline extends, we will see more bankruptcies, more unemployment, and more lasting economic damage. The market is a leading measure and has discounted a great deal of this potential, but we will need to see more data on both health and economic fronts to know if equities have found a solid bottom quite yet.

The good news is that we are gaining traction in our efforts to fight this virus. Patience is necessary now if we are to conquer it. Patience permits us the time to let the danger pass. Patience allows us to understand, measure, and plan. Patience opens the door to science, discovery, and innovation. We are so inspired by the tireless work being done in many of our portfolio companies to build therapies, accelerate vaccines, and advance testing. We are thankful for the technological infrastructure that allows for communities to stay connected and for bills to be paid remotely so we can stay safe. We recognize that it is ultimately innovation and ingenuity that solves problems, and we are seeing extraordinary creative energy being unleashed as necessity now demands.

Patience, of course, also requires that we – and our enterprises – have the reserve and wherewithal to weather the darkest storms. For too long, it has been too easy for too many in our society to slip into unmanageable debt. Too many companies are focused on short-term gain and have relied on debt to operate when they should have been setting aside appropriate reserves for inevitable storms. This is why we hold on to our investment principals so devotedly. We invest in companies with the depth of reserves that allows them not only to get through the most devastating crises, but also to continue investing in innovation, to pay dividends, and even to buy up weakened competitors to extend their leadership positions. We invest in secure, liquid fixed-income reserves of short duration and the highest quality so clients have access to cash and cash equivalents in the worst scenarios – without having to sell discounted equities. In short, we seek the highest ground with all of our investments.

Over the last two years, we have been net sellers of equities in our universe of client accounts, harvesting gains in the sunshine of a roaring bull market and building cash and fixed-income reserves in balanced accounts. While accounts have seen significant equity declines with the indiscriminate selling of the last month, we can report that the Reynders, McVeigh Core Equity mutual fund (“ESGEX”), which is a fair reflection of our core equity discipline, was down 13.61% for the quarter vs. a loss of 21.05% for The MSCI World Index, our comparative global benchmark, and a loss of 19.60% for the S&P 500 over the same period. Just as was the case in 2008, our equities are holding up well in the face of global hardship.

All of us here at Reynders, McVeigh are thinking of our clients and their families through this tremendous challenge. We are here to support you and to serve you. We also recognize the extraordinary needs emerging for health care workers, those without food security, and so many others in these difficult times. We will continue to reach out to communities in need through company charitable initiatives and investments in leading community development financial institutions. Please let us know if you would like to learn more about this work. But above all else, be well.

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Index/Fund Performance (as of 3/31/2020)

			Cumulative						Annualized
Fund Name/Index	Inception Date	NAV	1 Mo	3 Mo	6 Mo	1 Yr	Calendar YTD	Since Inception	Since Inception
ESGEX	3/29/2019	$9.71	-9.42	-13.61	-4.78	-2.78	-13.61	-2.78	-2.77
MSCI World Index Net (USD)*			-13.23	-21.05	-14.30	-10.39	-21.05	-10.39	-10.34
S&P 500 Total Return Index			-12.35	-19.60	-12.31	-6.98	-19.60	-6.98	-6.94

Performance data quoted represents past performance and does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Investors may obtain performance data current to the most recent month end by calling 1-800-950-6868. The fund's gross expense ratio is 1.44%, and the net expense ratio after fee waivers contractual through 5/31/21 is 0.96%.

DISCLOSURE: Investing involves risk, including loss of principal. The fund may not achieve its investment objectives. The value of equity securities is influenced by a number of factors which may relate directly to the issuer of the equity securities or broader economic or market events including changes in interest rates. Movements in the stock market may adversely affect the securities held by the fund on a daily basis, and as a result, such movements may negatively affect the fund's net asset value and investment return.

Given the significant differences between separately managed accounts and mutual funds, investors should consider the differences in expenses, tax implications and the overall objectives between separately managed accounts and mutual funds before investing. Past performance of the strategy/separately managed account is not indicative of future performance of the fund.

Investors should carefully consider the investment objectives, risks, and charges and expenses of the fund before investing. The prospectus contains this and other information about the fund, and it should be read carefully before investing. Investors may obtain a copy of the prospectus by calling 1-800-950-6868.

Distributed by Ultimus Fund Distributors, LLC. 9954172-UFD-4/3/2020

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