GUGGENHEIM

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Global CIO Outlook
Shock and Awe Falls Short

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Where are we now?

- The Federal Reserve's (Fed) attempt to go for shock and awe seems to have been made with the idea that doing something unusual on Sunday night, after the market closed out strong on Friday, would be good for confidence.
- Of course, the market didn't take it that way.
- Instead of inspiring confidence, the market seemingly responded as if the Fed knows something we don't know and it's actually worse than we think.
- Monetary policy is not designed to deal with pandemics. Monetary policy is designed to provide adequate liquidity to the financial markets to keep them functioning, and I think the Fed is doing a pretty good job at this.
- The Fed still has a number of tools at its disposal that haven't yet been implemented. Probably the most important of these is Section 13(3) powers.
- Section 13(3) can only be invoked with the approval of the Treasury in the first phase. The second phase would allow for the establishment of programs like the Troubled Asset Relief Program (TARP) and the Term Asset-Backed Securities Loan Facility (TALF), only with the passage of legislation in Congress.
- Given the size of our economy relative to where it was 10–15 years ago, it would probably be appropriate for Congress to pass a TARP-style program of $2 trillion.
- Then on the back of that, the Fed would have the ability to introduce a TALF-style program again.
- So, it's going to take some major firepower to resolve the forthcoming problems or the slide will continue.

What is your economic outlook?

- My expectation is that there is no economic growth in the near term, that we've probably already entered a global recession.
- The Chinese, for the first quarter, will print a gross domestic product (GDP) number which will not truly reflect the economic damage to their economy. Our best estimates are that the Chinese economy is contracting in excess of 15 percent at an annualized rate, and I've seen numbers as big as negative 40 percent.

- Europe is probably already in a fairly severe recession at this moment.
- If the United States is not already in a recession, it will enter one shortly.
- While shutting down restaurants, schools, and major events, a lot of people are going to be without a paycheck—people who probably don't have $500 of savings in the bank—and they won't be able to cover next month's rent, their car payment, and their living expenses. Given this dynamic, I see this getting much worse.
- The risk is that for the first time since the 1930s we are facing the possibility of a downward spiral into something akin to a global depression.
- We have at least a 10–20 percent chance that that's the path we are on if policymakers don't act quickly.
- It depends on the policy response that we get out of Washington, D.C. We desperately need programs like TARP and TALF, that were used in the financial crisis to shore up failing industries. The idea that Congress can address one failing industry at a time—like the airlines now with the $50 billion proposed bailout package—is wrongminded.
- As the economy continues to slow, crisis will start to cascade through many industries, and the problems will come faster and faster.
- The Families First Coronavirus Response Act, the Coronavirus emergency funding bill currently in front of Congress demonstrates how long it takes to react to something. There really needs to be a dedicated pool of money that is available to step in and salvage viable companies that are struggling.
- And remember, TARP was a money-making exercise for the government. We should get away from the idea that we are bailing people out. With TARP, the U.S. government becomes a distressed investor, and also is helping to sustain the economy and the working class.
- This is the scenario that leads to global depression. Should policymakers fail to get these sorts of programs in place quickly, there is increasing risk that we could fall into a deep, dark spiral.

What are you seeing in the markets?

- We have yet to see wholesale panic.
- From a value standpoint high-yield bonds or investment-grade corporates have only been cheaper relative to Treasurys 15 percent of the time. But valuation is a poor tool for timing the market. We're not really seeing the kind of selling that you would see in a market capitulation. Selectively adding to risk is the prudent approach.
- We have maintained the discipline of our robust investment process which is based on the belief that investors simply have not been compensated for taking on credit risk.
- We believe our prudence leaves us positioned to deliver strong value for clients now and in the future by taking advantage of opportunities afforded to us in our position of strength.

- I'm more concerned about the stock market. In the worst-case scenario, we could go back to the old highs of the market prior to the financial crisis. This would put the S&P 500 in the 1600 ZIP code. I'm not saying we're going there, but it certainly makes me pause before I think about loading up on equities.
- It is worth keeping an eye on emerging markets where interest rates have increased significantly. The next domino to fall as a result of the butterfly effect may well be here.

What would you advise investors?

- At this stage it would be unwise to make a tactical play to reduce risk, then try to figure out where the bottom is, then get back in. For those types of investors, I think at this point you missed your chance to get out.
- Investors panic too often and try to do too many tactical trades rather than just sticking with their long-term view. The opportunity to sell risk assets has passed.