



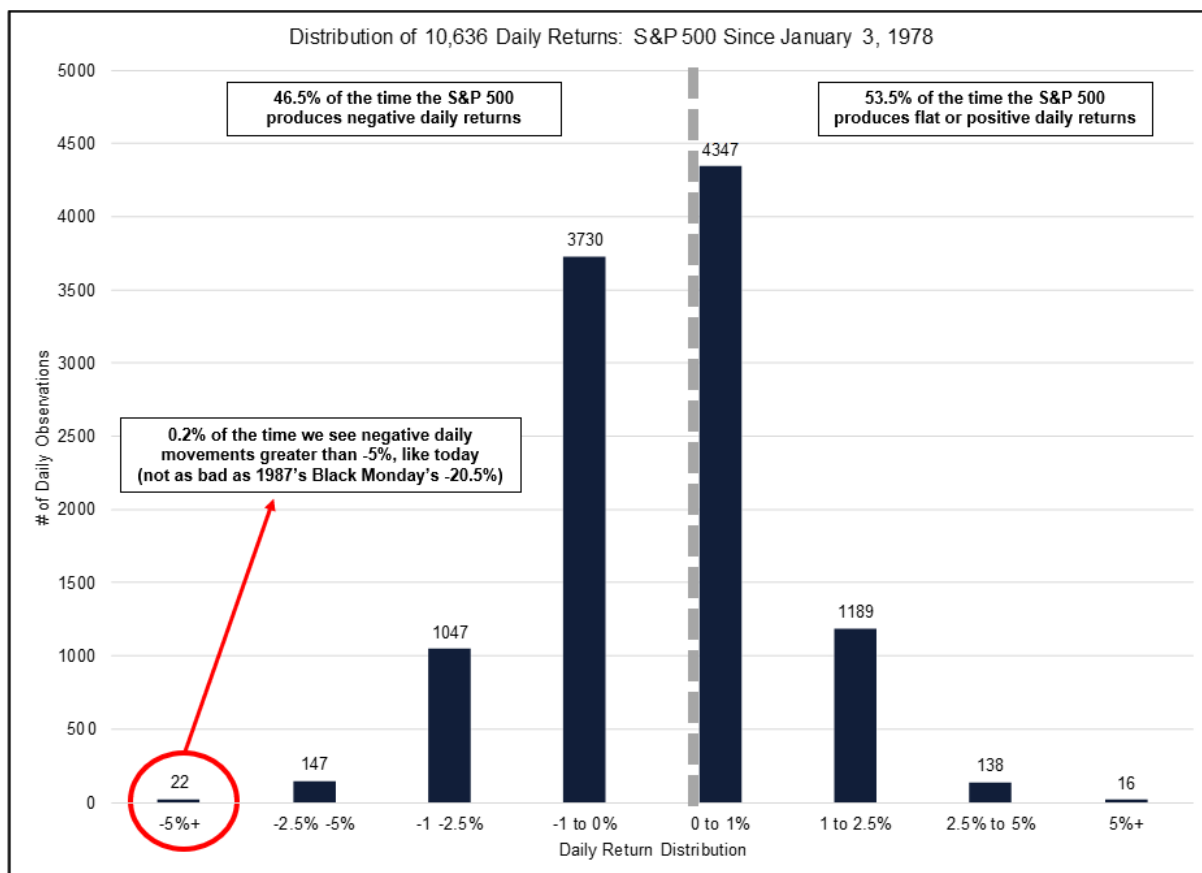
From Russia (and Riyadh) With Love.

The weekend's gratuitous knife fight between Putin and Mohammad Bin Salman, came at the absolute wrong time for a world already spooked by COVID-19. Obviously, no one was looking for either of these men to be helpful in the contemporary COVID-19 world (amazingly, [Russia](#), the apogee of global health, has reported only seven cases of COVID 19), but this weekend's standoff reaches a new low for two men whose lows were already subterranean.

Quick summary: Today was really bad. A blowout (Does Rachel Maddow get a royalty?). The indices listed below are all large, and their bad performance today represents a serious unrealized loss of capital globally.

US: The Dow Jones: -7.79%
US: NASDAQ: -7.29%
US: S&P500: -7.60%
EU: Euro Stoxx 50: -8.45%
UK: FTSE 100: -7.69%
Germany: DAX: -7.94%
France: CAC: -8.39%
Denmark: OMX Copenhagen All shares: -5.14%
Japan: Nikkei 225: -5.07%
Japan: Topix Index: -5.61%
Hong Kong: Hang Seng Index: -4.23%
China: CSI 300: -3.42% -- China appears the bright spot.
Australia: S&P/ASX 200 Index: -7.33%

For perspective, there have been 10,636 trading days in the S&P 500 since January 3, 1978, only 38 times have we seen movements greater than +/- 5% in a day (22 negative, 16 positive). Volatility begets volatility, in the 38 times we have seen +/- 5% moves in a day, 20 of those times occurred within 15 calendar days of one another, oftentimes these negative days saw equally violent moves to the upside shortly thereafter. Moves greater than +/- 1% on a given day are more frequent, occurring 24% of all trading days, however, days like today feel particularly painful in context of the bull market which began March 9, 2009 where less than 6% of trading days have seen daily moves +/- 1%.



Were any stocks up today? Yes. Traders dusted off their 2008 playbooks to buy the auto part retailers: AutoZone (AZO, +4.75%), Advanced Auto Parts (AAP, +1.96%), O'Reilly Automotive (ORLY, +1.51%) and the classic inferior good store: Dollar Tree (DLTR, +4.08%). We look forward to Trump announcing, "Cash for Clunkers." Predicted Trump quote: "I thought of the name long before Obama, I told him to use it. It's a beautiful name, perfect."

What happened: In very simple terms, the markets closed Friday worried about COVID-19. No good news about this serious epidemic came out this weekend. Instead, fears about the virus and its knock-on effects increased - organizers cancelled more events than could be counted. In certain countries, (read the US) policymakers seem completely unable to provide a cohesive, helpful message. Within the backdrop of COVID-19, the Russian disagreement with Saudi Arabia over supplies left the already vulnerable oil/energy markets drenched with over supply. Immediately, over the US weekend, oil prices dropped over 30%! This was on the back of significant oil demand destruction after COVID-19 caused millions of travelers to cancel trips. In the always helpful framework of supply v demand: Supply is way up! Demand is way down! Prices have one way move: down.

Shouldn't cheap oil help the economy? Yes...it is a question of when. Ryan's son, who tracks airline earnings like the savant he is, noted immediately, "only JetBlue does not hedge [its fuel prices.]" While Ryan's young analyst is partially wrong, he is partially right,



many airlines have oil price hedges in place, and it will take them months to realize the power of today's low prices. The US consumer should also benefit, in some ways, from lower oil prices. This is the old gas pump analogy/propaganda, "less money spent at the pump is more money to be spent

elsewhere." But these consumer benefits are offset partially (maybe entirely) by the fact that many companies along the Oil/Gas production stream are highly levered. Simply: lots of leverage, with a plummeting product price = increased chance for bankruptcy. The thread here is that while gas prices declining does help, they help substantially less if you lose your job. We know next to nothing about the amount of leverage in the US oil industry, in the fall of 2018, we read Bethanie McLean's book and [article](#) on the topic, and grew wary. We did not stay far enough away from the "value" sirens of dividends and distributions (many of which will be cut!).

To understand US Oil and Gas readers must understand that many of these companies thrive on debt. The lenders of this debt, like US banks, were pounded today! The fear here is that with less revenue, the oil companies won't be able to pay back banks (and investors) as originally planned. The financials ETF, XLF, tumbled 10.72% today. This is not an index of silly banks you have never heard of! XLF components: Bank of America fell 14.70%! J.P. Morgan down 13.55%. (Side note in weirdness: ExxonMobil was down less at -12.22%).

Environmentally, the fall in oil prices is worrisome. Many decarbonized ideas, which we love, just became relatively more expensive v oil. We saw this in stocks like Tesla, as batteries/solar are still slightly harder to use than carbon-based sources. Additionally, in the past, when we see pump prices fall, we often see consumers buy less fuel-efficient vehicles. We worry that chronically low oil prices will prompt many industries to stall their move away from carbon.

While Mr. Trump accurately tweeted "life & the economy go on," his many other unhelpful, inaccurate, ceaseless statements have deadened the ears of many.

In times of great calamity, which we hate to admit, may be nowish, folks like us who pay taxes and trust society, and trust the amazing institutions of our democracy, dream that policymakers will step in, globally, and work to provide thoughtful, constructive and actionable responses to the now two (and hopefully just two) global crises. It's never that we implicitly rely on government to solve problems, it's that we do expect it to help and to provide guidance and stimulus when needed. The US needs both now. From our desk, sort of overlooking The Grand Princess as it docks in Oakland, Dr. Anthony Fauci, the current director of the [US National Institute of Allergy and Infectious Diseases](#), seems to be the best guiding light on COVID-19. It would nice to see the policymakers work together to provide support for the many holes that will continue to grow in our economies as more and more people stay at home and the day-to-day fabric of life changes.

Where do we go from here? Last week, for clients who have large cash balances, we began to sell puts on broad sector ETFs. Effectively, we sought to provide "insurance" to the market when the cost to buy that "insurance" rose dramatically. We did this at roughly 15% out of the money. In hindsight, we started this trade too early. That said, we executed

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this strategy to great effect in the 2008-2009 time frame where we took assignment (painful as it felt) and continue to happily hold those positions to this day. We will be content to do the same again if the market provides us with the opportunity to do so.

There is no doubt the markets are going to move far more than we want over the next few days and weeks. It is here when investors gauge the real downside of their asset allocations. Remember, the allocation that works is the one that you do not sell on days like this.

In thinking about Risk, we refer readers to one of the most powerful discussions we recall from Howard Marks ([September 3, 2014](#)) "[Risk Revised](#)."

"However, while volatility is quantifiable and machinable - and can also be an indicator or symptom of riskiness and even a specific form of risk - I think it falls far short "the" definition of investment risk. In thinking about risk, we want to identify the thing that investors worry about and thus demand compensation for bearing. I don't think most investors fear volatility. In fact, I've never heard anyone say, "The prospective return isn't high enough to warrant bearing all that volatility." **What they fear is the possibility of permanent loss.**

Permanent loss is very different from volatility or fluctuation. A downward fluctuation - which by definition is temporary - doesn't present a big problem if the investor is able to hold on and come out the other side. A permanent loss - from which there won't be a rebound - can occur for either of two reasons: (a) an otherwise-temporary dip is locked in when the investor sells during a downswing - whether because of a loss conviction; requirements stemming from his timeframe; financial exigency; or emotional pressures, or (b) the investment itself is unable to recover for fundamental reasons. **We can ride out volatility, but we never get a chance to undo a permanent loss.**

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