LEAVELL
INVESTMENT MANAGEMENT

First Quarter 2020 Commentary

Dear Clients,

Please find enclosed your March 31, 2020 Investment Reports.

We are all now living through a period in history none of us will ever forget. The impact on our families, communities, and country has been profound. There remains great uncertainty, worry, and fear about the coronavirus and its impact: how widely it will spread, how fatal it may be, how long it will last. The United States and world are now facing a health crisis and an economic crisis. Both need to be fought with massive government policy responses and individual behavioral changes.

It is often said that recessions and bear markets are inevitable phases within recurring economic and financial market cycles and that investors need to be prepared for them to happen. Their precise timing is consistently unpredictable but there is *always* the risk of an unexpected "external shock" to the markets and economy (e.g., a geopolitical conflict or natural disaster). It is one thing to say it and another to actually live it. And still another when the precipitating event or catalyst for the recessionary bear market is something none of us have experienced before: a global pandemic, which has instigated an extreme societal response—including the indefinite closure of schools and non-essential businesses, shelter-at-home orders, quarantines, lockdowns, and social distancing—and has potentially overwhelmed medical facilities, personnel, and supplies.

We will get through this crisis period. Things will improve and recover. In the meantime, events are moving very rapidly, policy responses are in flux, and markets are extremely volatile.

The first quarter of 2020 has been an unprecedented period in U.S. financial market history across numerous dimensions. The U.S. stock market fell into a 20% bear market in the shortest time ever—just 22 days—and continued further, dropping 30% in a record 30 days.

Benchmark Returns

	Last Quarter	Last Twelve Months	Last Five Years
US Large Cap Stocks	-18.2%	-5.0%	7.5%
US Mid Cap Stocks	-25.7%	-16.7%	2.1%
US Small Cap Stocks	-30.1%	-23.4%	0.4%
International Developed Stocks	-23.1%	-14.4%	-0.1%
Emerging Market Stocks	-24.2%	-17.2%	-0.1%
US Bonds	3.1%	8.9%	3.4%
Global Bonds	-2.7%	0.7%	2.0%
US REITs	-27.2%	-22.0%	-1.7%

Data source: Morningstar Direct. Past performance does not guarantee future results. It is not possible to invest directly in an index. Last five years data is annualized. Market indexes include:

US Large Cap Stocks: CRSP US Mega Cap TR USD
US Mid Cap Stocks: CRSP US Mid Cap TR USD
US Small Cap Stocks: CRSP US Small Cap TR USD
Emerging Market Stocks: FTSE Emerging TR USD
International Developed Stocks: FTSE Developed Ex US TR USD
US Bonds: Barclays US Aggregate Bond TR USD
Global Bonds: Barclays Global Aggregate Ex USD TR USD
US REITs: MSCI US REIT NR USD

The typical historical bear market peak-to-trough decline has taken around 12 to 18 months. The 10-year and 30-year Treasury bond yields fell to all-time lows of 0.54% and 0.99%, respectively, on March 9. Oil prices had their biggest one-day drop since the 1991 Gulf War, plunging 25% on March 9, triggered by a price war between Saudi Arabia and Russia.

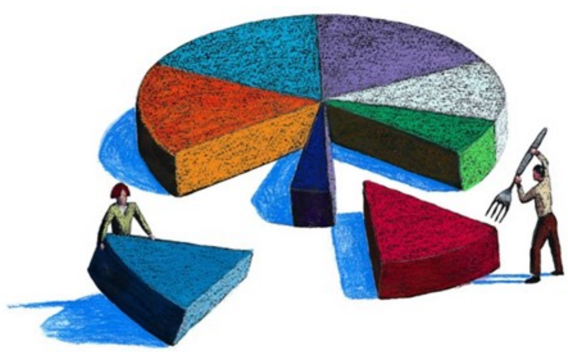
Larger-cap U.S. stocks fell 18.2% in the first quarter and small-cap stocks did even worse, falling 30.1%. Growth stocks continued to outperform value stocks. Developed international stocks fell 23.1% and emerging-market stocks dropped 24.2%. In the fixed-income markets, core bonds gained just over 3.1%, once again playing their key role as portfolio ballast against sharp, shorter-term stock market declines. As noted above, Treasury bond yields have fallen sharply. The 10-year yield ended the quarter at 0.70%, down from 1.92% at year-end.

Financial markets in 2019 were a positive surprise for many investors; however, the start of 2020 has been the exact opposite. Coming into the year, the potential was there for a moderate rebound in the global economy on the back of reduced U.S.-China trade tensions and extensive global central bank monetary accommodation. In January and early February, there were signs the manufacturing sector had bottomed and a nascent global recovery was indeed underway. Stock markets rallied to all-time highs. However, the onset of the coronavirus and the increasingly aggressive U.S. and global response to try to slow its spread has drastically changed everything. It seems most investors, economists, politicians, and central bankers agree that the U.S. economy is headed into recession in the second quarter with a sharp contraction in GDP and an unprecedented rise in unemployment and jobless claims. The consensus also appears to believe the recession will be short in duration, with a rebound beginning around the third quarter. But this is by no means a sure thing. To the extent equity markets are not fully discounting a more severe outcome, downside risk remains.

The effectiveness of the medical response and economic policies (and their impact on human behavior at the societal level), will help answer the fundamental economic question of how severe and how long the economic downturn and recession will be. And the answer to the economic question will help answer the investment question of how severe and how long the equity bear market will be. We expect financial markets to react positively at the first signs of a flattening in the number or rate of new daily cases reported, as we saw happen in China in February, and as also happened during the SARS epidemic in 2003.

The near-term economic damage from the United States' and other countries' response to the virus now looks almost certain to be severe (barring some unexpected major medical breakthrough in the near future). Fed chair Jerome Powell said GDP growth was likely to be negative in the second quarter, and beyond that the economic outlook was highly uncertain, as it depends on how widely the virus spreads: "I would say in fact, unknowable." In this case of a severe external shock, the government's economic policy responses are critical. There are two main levers: monetary policy (central banks) and fiscal policy (government spending, tax cuts, unemployment insurance, loans, debt forgiveness, etc.).One lesson learned from the 2008 financial crisis is: When it comes to the policy response, go big and go fast. Time is of the essence. Governments need to make a credible commitment to "do whatever it takes" to support the economy and prevent the negative spiral from taking hold.

At an emergency meeting on Sunday March 15, the Fed cut the federal funds rate to near zero and restarted quantitative easing in order to keep interest rates and borrowing costs low. The Fed also initiated a number of programs—going beyond the tools it enacted during the 2008 financial crisis—to try to ensure enough credit, loans, and liquidity are flowing to banks, businesses, households, and the overall global financial system. It is likely the Fed will do still more if necessary. While extremely accommodative monetary policy is necessary, it is not sufficient to mitigate this economic crisis. Only fiscal policy can have a large enough and direct enough impact necessary to support and sustain individuals and businesses until the storm has passed and the virus containment measures show signs of working. On March 27, Congress passed, and the president signed into law, a $2 trillion stimulus package. Similar support measures are being debated or implemented around the world. Discussions continue about additional steps to take in support of markets and the economy.



As investors, it is so important to maintain our focus on our long-term financial goals and objectives. As hard as it may be, from an investment perspective we need to try to look through the current environment of fear and concern—emotions which, given the circumstances, are totally justified and felt by all of us—to the almost certain outcome of the virus crisis receding and economic recovery occurring.

As a long-term investor, trying to time market tops and bottoms is a futile effort. The evidence is overwhelming that most investors diminish their long-term returns trying to do so. They are more likely to chase the market up and down, buying high and selling low. Research, analysis, patience, experience, and having a disciplined investment process come most into play in these environments.

We sincerely hope that you and yours remain healthy and manage well through this challenging period.

Timothy S. Healey
Chief Investment Officer

Janet R. Hayes
Chief Operating Officer

Please advise us if you would like copies of our annual Securities & Exchange Commission Disclosure Brochure (Form ADV), a Prospectus for The Government Street Funds or a record of how your proxy statements were voted.