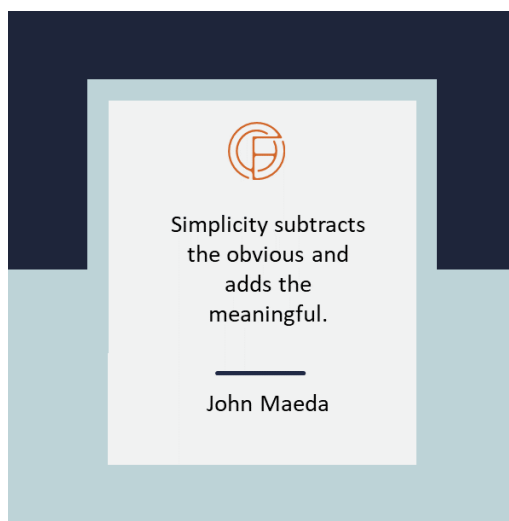

O.F.O. Partners



Part One: Simplicity

July 2020

In such turbulent times as these, families like yours seek a simple goal: to manage their wealth responsibly so that they don't get knocked off course.

In this summer's letter, we will discuss how the virtues of simplicity can keep you on track. Now is a time when the danger of overthinking is high. The halfway point of 2020 is a great time to look at why this is true. We will prove how a return to basics improves results for sophisticated investors.

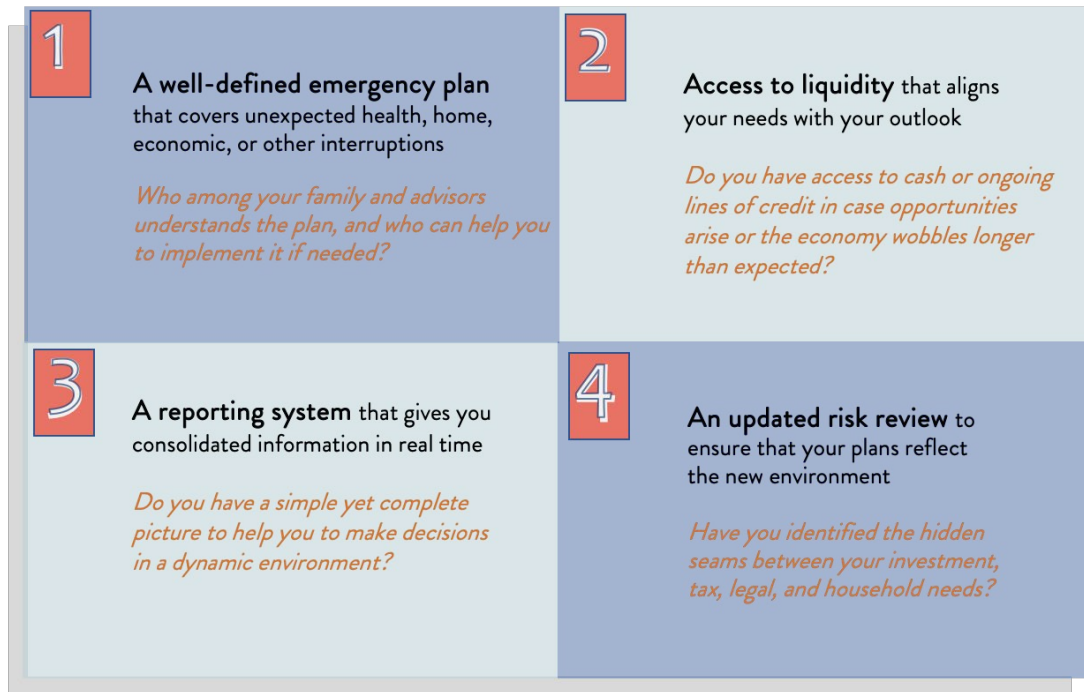
Essential Errands

Since the COVID crisis began, each of us has had to adjust. We have sacrificed our chosen routines. We're only running essential errands.

Most of you will be happy to see 2020 go. You didn't ask for these limitations. But the experience has also held surprising benefits for those of you who have discovered new clarity about your priorities. Focusing on the essential helps you to see what is truly important.



The fragile economy has added financial uncertainty to the levels of stress that may be building in our daily lives. Restoring confidence around wealth can be as simple as completing life's other essential errands. We recommend four areas to start.



This framework covers the basics. You would be amazed by the number of families with unlimited resources that overlook these areas. Yet these plans are easy to enact if you have the right partner to keep you focused. There is a role for advanced planning over time, but essential errands are for today.

**“Success is simple. Do what’s right,
the right way, at the right time.”**

- Arnold Glasow

The Power of Constraints

Haiku poetry captures nature in only 17 syllables. George Lucas made Star Wars with a \$11 million budget. The crew of the Apollo 13 invented an air filter mid-flight by using plastic bags and a soggy sock. Constraints like these force us all to be thinkers, innovators, and to find elegant solutions.

In wealth management, successful families can benefit from a similar focus. The goal is not to remove choice, but to identify the trade-offs that appear as your menu of options increases.

Here are a few simplifying constraints to consider. First, **excess diversification** can be seductive during a crisis. Small positions are a distraction, like extra words in a Haiku. They add complication and detract from your results. **Trim your holdings** to the level that satisfies your risk and allocation targets. The same is true for accounts – consolidate those that receive low attention.

Liquidity is another constraint that deserves your focus. Private investments that lock up your capital for long periods have changed investing, much as CGI effects changed movie-making. After the success of the original Star Wars trilogy, George Lucas learned that limitless special effects can work against a good story. Fans panned his bloated Star Wars prequels - even with their dazzling visuals. Likewise, private strategies can open up new avenues. But **illiquidity makes it harder** to track your progress along the way - or to change course when your story calls for it.

Trusts and family partnerships can add powerful benefits to your investment and tax plans. **Design your tools flexibly.** Think of how

the Apollo 13 astronauts were able to repurpose simple items into life-saving equipment. Long term planning with trusts and partnerships complicate your mission, even as they help you to go further with your wealth. A good rule of thumb is to solve at least two problems for each new structure you create - for example, limiting taxes while adding creditor protection to your assets. The best tools serve multiple purposes, even when you're not in a pinch.



Apollo XIII astronauts Jim Lovell, Fred Haise, Jack Swiggett



Simplicity is Ultimately a matter of focus

When you look back on 2020, what will you see? Will you see little things that add up to bigger outcomes? If you focus your efforts, then you can plan big while working small. Let your advisors be your partner in keeping things as simple as possible, and no simpler.

We hope to see you soon,
Ezra Levine, Doug Moon & Karen Sugar

Part Two: Six Months in an unfamiliar world

In the first half of 2020, the coronavirus drove people to shelter at home and businesses to halt. Initially, public markets around the world mirrored that experience in both speed and depth. The longest bull market for U.S. stocks came to an abrupt end. Lending markets, as measured in credit spreads and liquidity, signaled distress. Companies, governments, and banks drove a surge in global demand for U.S. dollars.

Policymakers launched, and then expanded, a range of emergency programs to meet these threats. The U.S. government provided \$3 trillion of fiscal rescue spending, plus another \$3 trillion in new Central Bank lending. So far, the economic response to COVID-19 has been vastly more successful than the public health response in fighting the pandemic.

But the health crisis remains unresolved. Financial intervention, regardless of the scope, cannot sustain people's needs or replace the value of organic economic activity. For this reason, market participants have begun to evaluate asset prices and corporate liabilities in a new light as U.S. businesses begin to reopen. First, they seek to forecast the timing and character of a return to normal. Second, there must be some reckoning of the structural changes swept in by these massive rescue policies.



U.S. fiscal support in 2020. Source: IMF.

The U.S. Stock Market Puzzle

The S&P 500, which had been down by as much as 31 percent for the year, is now just three percent below its starting level. This resilience has surprised many investors. The rapid return is out of synch with the business environment. For example, earnings estimates about future profits have evaporated, with 40 percent of S&P500 companies withdrawing guidance about the future. Meantime, the stock market had its strongest 3-month return since 1998, adding 20 percent. Technology shares showed even more enthusiasm, rising 30 percent in the quarter and boasting a 12 percent gain year to date.

We recognize that the behavior of the stock market and the state of the economy are loosely affiliated over short periods of time. Still, the bounce back in stock prices during the second quarter has only two explanations. First, that monetary and fiscal policy will continue to bail out weakened business and consumer sectors. Second, that the worst of the COVID impact on corporate earnings has already passed. A resurgence in cyclical stocks in May and June reflected this hopefulness.

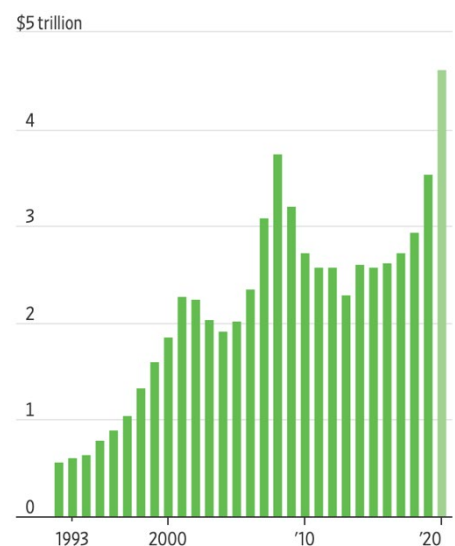
Where does this leave stock market investors? Broad stock market indices in the U.S. are expensive unless the virus is on the wane and profits are poised to return swiftly. Pockets of the economy, and certain industries, remain depressed and may represent value. Larger-than-normal price swings that emerged in February may continue for some time.

Cash and Bonds: Rainy Day puddles increase while income trickles

As the second quarter began, U.S. companies were sitting on \$1.7 trillion in cash. Throughout the quarter, companies issued more debt and suspended dividends to protect cash. Assets parked in money market funds have increased to a record \$4.6 trillion. Since February, more than \$3 trillion of new consumer and corporate assets have moved into cash.

The rise in cash holdings, decreased investment, and slowing of money through the economy raise the risk of a deflationary environment. The money-printing and debt issuance of policymakers swings in the other direction, towards inflation - where too much money chases too few goods. Most investors are caught in the middle, unable to earn a reasonable savings income without risking liquidity, changes in credit conditions, or loss of principle.

Assets in money-market funds



Note: Figures for 2020 are through June 10.
Source: Refinitiv Lipper

“The process by which banks create money is so simple that the mind is repelled”

- John Kenneth Galbraith, Economist

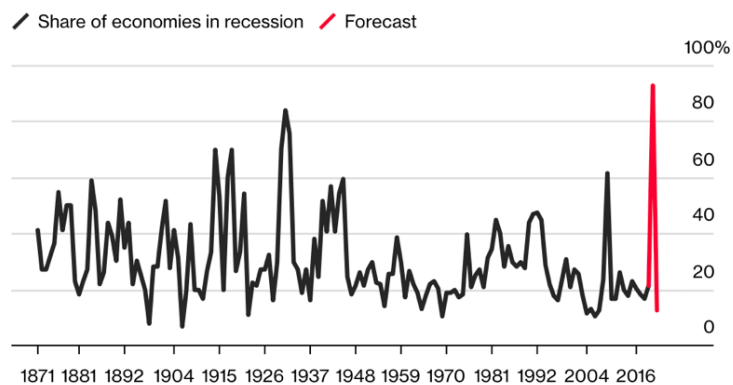
Where does this leave depositors and yield-seekers? Clients would do well to pay attention to cash and liquidity. This includes a firm understanding of your sources and uses of cash over the next 18 months. Also, keep tabs on your bond investments. Your safest assets are providing meager yield these days.

Europe and Asia

Developed markets outside of the U.S. face challenges restarting their economies as well. In a world of globalized trade and finance relationships, the virus has caused a high degree of synchronization. Despite many countries' success in slowing the spread of infections, the IMF estimates that by the end of this year 170 countries -- or nearly 90 percent of the world -- will have a recession in 2020. Global growth is forecast at -4.9 percent for the year, disproportionately affecting low income households.

Synchronized Downturn

More than 90% of economies are set to experience a recession this year



Source: World Bank

European policies emphasized wage subsidies for workers, betting on a swift turnaround in business activity. This has forestalled the massive increases in unemployment experienced in the U.S. Cases of infection have dropped off for now and businesses are preparing to resume normal activity.

Private Markets

Wealthy families increased their participation in private investment partnerships, real estate, and direct investments during the recent 10-year economic expansion. The performance of these assets, before and after the pandemic, will be critical in deciding if these assets will be valuable to your portfolio during a full economic cycle.

In private equity, coronavirus brought an end to one of the longest merger and acquisition waves in history. During the second quarter of 2020, companies struck \$485 billion worth of deals globally,



down more than 50 per cent from the same period last year. The fall in activity was particularly sharp in the U.S., where overall acquisitions collapsed almost 90 per cent from a year ago, to \$75 billion. Private equity sponsors represented the highest portion of buyers this year, since the industry has raised \$2.5 trillion of capital from investors to commit to deals.

The number of hedge fund liquidations soared at the beginning of the year. More than 300 firms shut their doors, the highest since the fourth quarter of 2015. Newly created hedge funds also sank to a near-record low. Total industry assets fell below \$3 trillion after decades of growth in assets and newly launched funds.

Part Three: Now Hear This

Here are a few articles and sounds tied to the questions we've pondered this spring.

[Charles Ellis Interview](#)

Bloomberg Radio interview with Charles Ellis, founder of Greenwich Associates. Charlie describes the constraints that investors faced in the 1960's and 1970's, revealing why complicated investing and tech innovation have not yielded better customer results.

[Essentialism: The Disciplined Pursuit of Less](#)

Greg McKeown's book on essentialism isn't about getting more done in less time. It's about getting only the right things done.

[The Illiquidity Discount](#)

Cliff Asness of AQR Capital writes that "conventional wisdom suggests that you get a return premium for bearing illiquidity. But what if this is backwards?"

[A Crisis Like No Other, An Uncertain Recovery](#)

Here is the International Monetary Fund's June summary of economic conditions around the world.

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