Our Viewpoint this month takes the form of a letter from Mark Mirsberger, our CEO. Mark has been leading Dana for almost twenty years, and shares a perspective that only experience can bring. Dana has had professionals working remotely around the country for decades, but the current situation has led to even more dispersion in terms of physical location. Despite this, every one of us feels closer to each other as we work through this pandemic. Our business has gotten far busier and more hectic, not less, as large parts of the economy have ground to a standstill. During this crisis, we have had to try and focus on both the short term and the long term as events evolve, something that is difficult to do under stress. Mark has always been able to do both, and it is an essential skill for a leader. I hope you enjoy his letter and that it provides some perspective in the current situation.

Joe Veranth, Chief Investment Officer
March 27, 2020

Dear Friends,

First and foremost, I hope you and your entire family are safe and doing well. I wanted to update all of you on our latest insights as information and markets are changing quickly. These are truly unprecedented times, and they are very unsettling and stressful for all of us – it’s why I started drafting this at 5am when I couldn’t sleep. Please don’t take my inability to sleep comment as worrisome as those that know me know I like to play golf and tennis early in the morning. The problem is there’s no place to do those now, so I can’t help but think about work and financial markets and how they are impacting clients and friends.

Rest assured, my entire family (including my daughter who got home from Australia before they entirely closed their borders) is doing well, and our entire Dana team is healthy and fully engaged. Our employees have been equipped for years with the tools and technology to work remote, so we remain 100% operational despite us being more spread out and distanced than ever. Thank goodness we live in a digital world where research and technology are portable and accessible almost everywhere.

March has been a strong reminder that investors and financial markets hate uncertainty. As the COVID-19 pandemic has spread and unexpectedly shutdown a global economy for an indeterminate amount of time, the stock and bond markets have experienced extreme stress and volatility. Exactly how bad has this uncertainty impacted the markets? By late March, many market indexes were down 25%-40% year-to-date.

Realize most of these indices made all-time highs as recently as mid-February, so their decline has been dramatic and abrupt. For those that have been following the markets for years, this drop has paralleled some of the following declines we’ve seen in the past:

- October 19, 1987   Dow Index fell -22.6% in 1 day
- 2000-2002 Dot.com bubble   Nasdaq fell -66.9% during the 3 years
- 2008 Financial Crisis   S&P 500 Index fell -52.5% from 2007 to March 9, 2009

While history never exactly repeats itself, it usually rhymes with the past, and yet what started this decline is unique. Unlike past declines, the most recent volatility was not due to the severe over-valuation of stock prices (2000 Dot.com bubble), or due to the Fed raising interest rates too quickly (1987 & Q4 2018), or due to a collapse of the banking and financial system (2007-Q1 2009). This uncertainty is due to a dangerous viral pandemic that is being treated by shutting down the global economy for an uncertain amount of time. The unknown length and depth of this slowdown is really the challenge. While certain industries and personal hygiene habits may forever be impacted (let’s at least hope good hand washing continues forever), this
slowdown won’t last forever and the world will come through it and economies will restart – we’re already seeing this in China where the outbreak originated.

During the past month, we’ve been attempting to de-risk and adjust our investment strategies for the quickly changing environment. In our equity strategies, we sold several holdings in February and March that are the most exposed to travel related industries, including some of our best long-term performers: Royal Caribbean Cruises (RCL) and Delta Air Lines (DAL). While our equity strategies remain committed to applying our disciplined relative value investment process, we are keenly focused on company balance sheets and finding those best equipped to navigate near-term supply and demand shocks and tighter credit markets.

While the volatility and stress within the equity market has been well and widely reported, the volatility within the bond market has been equally as dramatic and yet significantly under-reported. For those that follow financial markets and interest rates, they know the Federal Reserve has taken dramatic actions this month by cutting the Fed Funds rate several times, ultimately to zero. All Treasury rates followed lower, as short rates have fallen 150 basis points since mid-February, and long rates have fallen about 100 basis points. Additionally, the Fed purchased up to $300 billion of Treasury and mortgage-backed securities last week (almost twice as much as any week during the Financial Crisis of 2008). So while U.S. Treasuries remain safe, they have fallen a lot and offer very low income going forward.

What’s been remarkable the past few weeks is that nearly all other sectors of the bond market have sold-off tremendously in the short-term, and this has resulted in most bond indices experiencing the following negative total returns so far in 2020:

<table>
<thead>
<tr>
<th>Bond Index</th>
<th>Total Return</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-3 Year ICE Bofa Corporate Bond Index</td>
<td>-2.4%</td>
</tr>
<tr>
<td>1-10 Year ICE Bofa Corporate Bond Index</td>
<td>-4.5%</td>
</tr>
<tr>
<td>3-7 Year ICE Bofa Municipal Bond Index</td>
<td>-0.6%</td>
</tr>
<tr>
<td>Aggregate Municipal Bond Index (iShare MUB)</td>
<td>-0.4%</td>
</tr>
<tr>
<td>High-Yield Corporate Bond Index (iShare JNK)</td>
<td>-13.1%</td>
</tr>
<tr>
<td>Aggregate Preferred Stock Index (iShare PFF)</td>
<td>-15.6%</td>
</tr>
</tbody>
</table>

While this is hurting portfolio valuations, it is creating better income opportunities for the future, as yields in these sectors are at some of the highest levels we’ve seen since 2008.

So, what do we know and what are our thoughts going forward? We know we are in uncharted territory and no one knows the depth and duration of the current COVID-19 economic impact. We also know market stress causes security and asset class dislocations and that investors that are able to handle risk and volatility are able to capitalize on the opportunity created by others that can’t. History also shows us that the stock market has withstood many shocks and challenges over the past 100 years, and yet has historically been positive about 70%
of calendar years and has compounded at over 9.5% annually even after the most recent downturn as measured by the S&P 500 Index since 1926. We do not see the current COVID-19 crisis as permanently changing this fact pattern. We also know that historically a portfolio of 30% stocks and 70% bonds has shown to have lower volatility risk and better returns than 100% bond portfolios.

Going forward, we expect the stock and bond markets to remain volatile for a few months, but many long-term opportunities are being created right now. As weak bond holders and funds being hit with liquidations were forced to sell securities at any price, we saw and took advantage of some of the following opportunities:

- Short, high quality municipal bonds with yields between 2-3% tax-free
- Short, investment grade corporate bonds with yields between 3-5%
- Preferred stocks with yields of 6% and higher
- Numerous ETF and Closed-end bond funds selling at significant discounts to their underlying net asset values generating yields 6-10%

As I often remind clients, there is no wrong asset allocation, as each client’s allocation should be customized and fit for their own risk tolerance and time horizon, but future income and investment growth are dictated by the levels of risk taken and the asset allocation maintained. Maintaining a long-term perspective is very difficult when markets are falling, but as our Founder Mike Dana reminded our equity team in the depths of the 2008 Financial Crisis, “Investors wait a lifetime to buy quality companies at such tremendous value.”

These are truly unsettling times and it’s most important for all of us to remain safe and healthy through this crisis. Know that all the resources of Dana are focused on helping our clients navigate the markets and that we’re always available to answer questions or make portfolio adjustments. Please don’t hesitate to call or email your questions or concerns. We will continue to communicate our insights through our Dana Viewpoint, and I will share other useful information as it becomes available. Thank you for your continued confidence in Dana Investment Advisors.

Stay safe, we’re all in this together,

Mark R. Mirsberger, CPA
Chief Executive Officer