BOK FINANCIAL

Second Quarter 2020

ECONOMIC & MARKET REVIEW

J. Brian Henderson, CFA
Chief Investment Officer
BOK Financial

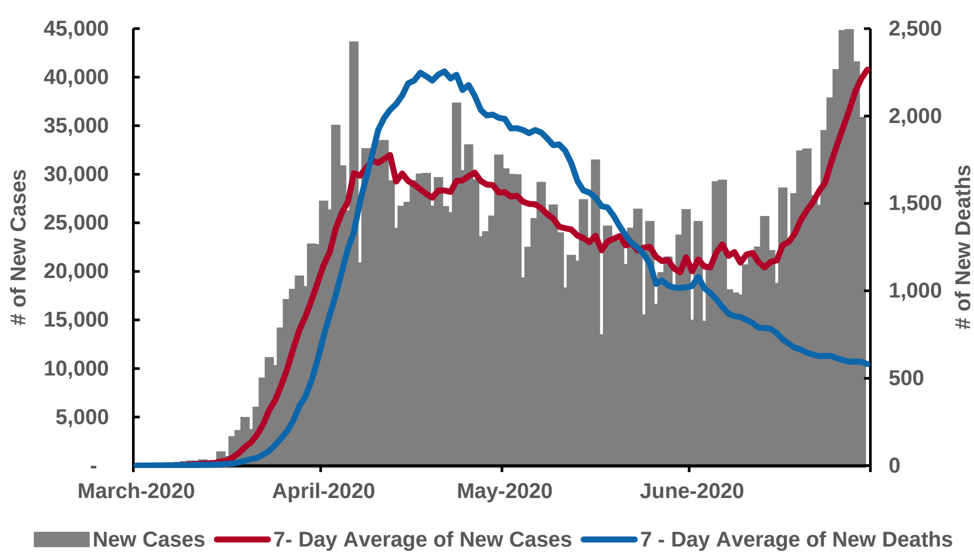
J. Brian Henderson was named Chief Investment Officer on May 1, 2020. Mr. Henderson started his career with BOK Financial in 1991, and has held multiple leadership roles across the investment management team during his tenure.

Q2 – Summer Waves

Riding on a wave of U.S. government income and financial market support, the S&P 500 Index turned in one of its best quarterly returns ever, up 20.5% for the second quarter, albeit up from a sharply lower bottom at the end of the first quarter. Given the complete wipeout in economic growth that occurred worldwide in March and April, it's hard to believe the S&P is now only down slightly year-to-date, and that the growth and tech-heavy NASDAQ Composite actually reached new all-time highs, up over 12% year-to-date! The strong get stronger, and the growth companies that were winning prior to the virus continue to thrive with 0% interest rates and slower economic growth as far as the eye can see.

The virus trumps all. With phased-in re-openings, the economic music started playing again in May alongside lower percentage volumes in case counts, net hospitalizations, and ICU capacity trends that appeared to have peaked in April. Overall, global case counts continue to rise, alarmingly led by the U.S. The markets are looking through the headlines about growing case counts to the severity of the cases, the daily and weekly case rate of changes, average virus spread indicators, age demographics of new cases and deaths at the global, national, state and local levels, and monitoring consumer behaviors with high frequency mobility, travel, and other daily economic activity data. On average, most, but not all, of the trends have been encouraging, which is setting the tone for positive financial market outlooks.

COVID-19 Case Waves in U.S.



Key Points

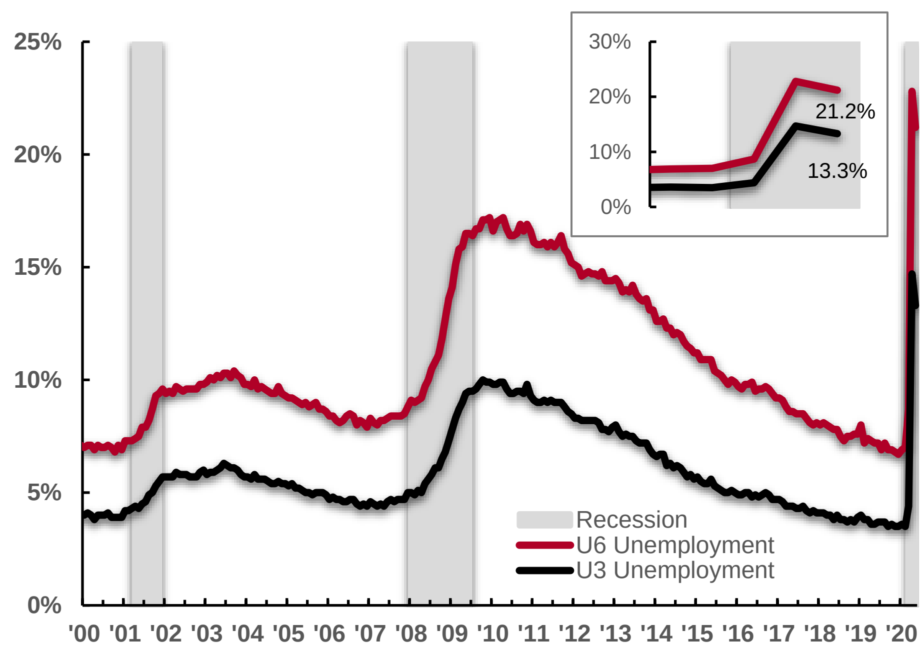
- COVID-19 had a significant impact on the market and economy, but both are now improving.
- Massive monetary and fiscal stimulus have been enacted, with more to come.
- A return to "normal" remains dependent on a successful re-opening and development of a treatment/vaccine.
- Oil prices dropped precipitously, but have had a significant turnaround.
- Fortunately, it appears the worst of the economic decline is behind us.

Q2 Performance	
S&P 500	20.5%
Russell 2000	25.4%
Barclays Aggregate Bond	2.9%
MSCI EAFE	14.9%
MSCI Emerging Markets	18.1%

Recovery Coming, But Expect Choppy Seas Ahead

With the negative economic impact from the virus starting in February and peaking in May, we just went through one of the sharpest and shortest technically self-imposed recessions in history. From here, we can expect a gradual but uneven economic recovery, largely dependent on the virus. While some economic indicators are going to snap back sharply (e.g., U.S. GDP growth is estimated to be up 20% or more in the 3rd quarter), it will still feel like a recession. Economic activity is improving off of a very low base. The U.S. economy remains in bad shape, but the rate of change is positive and the financial markets are keying off of this trend. There will be setbacks. We expect the unemployment rate to remain above 8% for the rest of the year, and we're still in a negative credit cycle that is rippling through the corporate, mortgage, and other loan markets. In the service sector, travel, restaurant and hospitality-related industries that depend on face-to-face customer contact make up approximately 10% of U.S. jobs. These industries have been hit particularly hard and will be the slowest to recover. Based on TSA passenger volumes, 90% of would be travelers aren't ready to jump back on an airplane for business or pleasure.

Unemployment Rate High, But Showing Signs of Improvement[1]



We'll likely see more case count flare-ups with the re-opening similar to what we are seeing now in Arizona, Texas, Florida, and California. Testing is definitely much more widespread now than back in March. The threshold for another complete shutdown of the U.S. economy is probably very high, but we could see localized quarantining in virus hot zones, especially where hospitalization trends are near critical levels. Our economy has survived the worst and is learning new ways to do business in spite of the virus. A breakthrough from any of the 100+ potential vaccine candidates in the pipeline would be a huge shot in the arm for the economy and markets.

Economic Life Preservers

Knowing that the U.S. fiscal and monetary policymakers are ready to do more to support the economy and financial markets is a real confidence boost for consumers, corporations, and investors. To date, the amount of support already has far exceeded that provided during the Great Financial Crisis of 2008-2009. Of course, the economic damage is much worse this time, too – the U.S. unemployment rate approached nearly 15% versus a peak of 10% in 2009. The $2 trillion CARES Act, along with the Federal Reserve's 0% interest rate policy and more than $4 trillion in quantitative easing helped buoy the stock market and economy during the quarter. These policies have provided a bridge for a start to the recovery, but more will be needed. With expanded unemployment benefits and the Paycheck Protection Program, U.S. workers' incomes have largely been replaced (in some cases, more than 100%) during the early months of the shutdown, and jobs have been saved from unnecessary business bankruptcies. Even so, self-sustaining income generation from real job growth and increased revenues without the government's support is years away. We are going to need a longer bridge.

Other Sharks in the Water

As if the uncertainties caused by the virus weren't enough, other risks for investors are lurking, chief among them is the political risk associated with the upcoming election. It is a presidential election year, and it's not too early to be thinking about how the market may respond to a potential change in the presidency, as well as Democrats taking over the Senate. The virus and current condition of the economy have not been good for President Trump's reelection prospects. Current polls and betting odds favor Biden and the Democrats this November. Given Biden's recent statements about his intention to repeal tax cuts, some economists believe a Biden presidency could result in higher corporate tax rates in 2021, potentially shaving off approximately 5% of profits for companies in the S&P 500 Index. In the near term, it's likely that the federal government will approve further personal income support programs and incentives to help the economy continue its recovery.

Another risk is the continued deterioration in our relations with China. Both sides of the political aisle lean against China, and we saw what the tough talk on tariff threats did to the markets last summer. Both sides are looking for political wins, and China – believed to be ground zero for the virus – is an easy target.

A View to the Horizon: Bet on the Future of the U.S. Economic Recovery

Long term investors should position their portfolios to benefit from the gradual economic recovery. We favor U.S. large cap stocks and, in particular, growth companies with stronger balance sheets and positive cash flow. It's going to take time, and we may take two steps forward followed by one step back. With cash yields at 0%, investment hurdle rates are low. The Federal Reserve, White House, and Congress will likely do more to support the markets and the economy from here.

[1] The official unemployment rate is represented by U3. The U6 unemployment rate includes discouraged, underemployed and unemployed workers.

Disclosures

Data Source: Bloomberg, Federal Reserve Bank of St. Louis

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