Memo to: Oaktree Clients Only

From: Howard Marks

Re: A Different World

Our powers and choices are limited in the coronavirus environment, but one thing I can do is communicate. Thus I will continue to write, in the hope that it'll be helpful . . . even though there's often nothing profound to say about the future.

It's odd to say, but as little as three weeks ago, it seemed we were in an environment of "business as usual." The stock market started to fall on February 20-21, but only by a percent or less per day.

On February 24, I flew to Los Angeles to prepare for our biennial client conferences, scheduled for March 11-12 (U.S.) and March 18 (Europe). We didn't conduct ourselves any differently from usual. The combination of geographic distance from China, little proliferation of information about the disease, and the lack of testing in the U.S. made most people outside Asia unconscious of the threat from the virus.

On February 26, while about to fly to San Francisco for client meetings (and then onward to Washington and Oregon), I was informed that the State of Washington had imposed a no-visitor, no-travel period for a minimum of two weeks. Given that most people hadn't yet made changes in their behavior, this seemed abrupt and severe. But the authorities in Washington were ahead of the trend, because shortly afterwards the first U.S. case – and then the first fatality – occurred at the Kirkland, Washington nursing home that quickly became a key U.S. hotspot for the virus.

The stock market decline began in earnest in the last week in February, with declines on all five days adding up to an 11.5% drop in the S&P 500. Observers began to cut their estimates of economic growth, but I felt the idea of any growth – i.e., that output would be more in 2020 than in 2019 – seemed too rosy.

One of the questions I get most frequently concerning my memos is, "How long does it take to write one?" When I have a fun topic and it's not time-sensitive (like "You Bet!"), the answer can be months. But I decided on Sunday March 1 that the virus called for a memo, and it was issued on March 3. **Of course, its theme was "nobody knows." Not very helpful, perhaps, but when you don't know, it can be a big mistake to act as if you do.**

In the first week of March, U.S. media started to talk about actions people should take, and the investment pundits cut further into their growth estimates. But only isolated cases of the virus were reported, and daily behavior remained largely unchanged. Conferences began to be canceled, and we reached the decision to cancel ours on March 4. But we concluded that we could serve our clients by livestreaming the key sessions, and on March 7 I flew to Los Angeles to participate.

By the time of the livestreaming sessions on March 11, we were avoiding large groups but still seeing colleagues and friends in limited numbers. That day we told employees they **didn't have to**

come in, and on the 13th we told them they **shouldn't come in**. Oaktree has experienced two cases thus far, but neither seems to have become grave or produced spread. We're optimistic that our young colleagues will recover fully. This weekend gave us a chance to thoroughly clean our offices, and we've fully-implemented our business continuity plans, which are working well. All of our personnel are now working remotely, except for a few people performing essential functions in our offices. We believe we can operate effectively in this fashion for as long as necessary.

While almost all Oaktree people are staying away from the office, I feel we're operating at a high level. The good thing about our business is that it doesn't require in-person meetings or physical contact with raw materials or finished goods. My colleagues and I have been spending long days working from home and feel we've been quite productive.

While on that subject, I want to stress the importance of social distancing or self-isolation. As long as there's no preventive vaccine and no cure (other than treating symptoms and nursing sufferers back to health), our only tool is minimizing spread through contact. Most people accept the wisdom of canceling conferences (and public events) and closing offices (and schools). **But the benefit of these actions can be undone through socializing.** I hope those of you in affected countries will avoid group activities, avoid physical proximity, avoid touching surfaces others have touched, and avoid coughing on others and vice versa. It sounds extreme, but it's important. My colleague, Emmett McCann, provided a link to a write-up by Asaf Bitton, head of Ariadne Labs, a public health joint venture between Brigham and Women's Hospital and Harvard School of Public Health. Here's one piece of advice that particularly appealed to me: **"No kid playdates, parties, sleepovers, or families/friends visiting each other's houses and apartments."** Separation can be essential for your health, your family's health, and the health of others.

Let's assume we're not going to set our level of precaution exactly right. **In my view the question is simple: would you rather be too safe or not safe enough?**

In recent days, clients have begun to ask about opportunities in our markets. Yield spreads have widened substantially, and people who were thinking about investing when opportunities improved (or who contracted to do so) understand that there's been great progress in that direction. High yield bonds, loans and CLO tranches, for example, offer markedly better investment opportunities than they did in the very recent past. In particular, in recent years the opportunities in U.S. distressed debt have been few, far between and highly concentrated in energy and retail. The catalyst for broader supply was unimaginable. Now it's clear that companies of all kinds are likely to find that revenues decline faster than costs, run into cash flow problems, and be denied access to the capital markets. **For this reason, we're going to make preparations for organizing our next distressed debt fund. We feel it's important to start that process now.**

As you know, the people of Oaktree were pioneers in the management of non-investment grade debt, and they invested successfully through debt crises in 1990-91, 2001-02 and 2008-09. Each included a good dose of fear – fear is required for prices to reach crisis levels – but never before fear for one's health. We think bad news and rising fear lie ahead. As usual, our experience, and the fact that up until now our portfolios have been positioned cautiously, should enable us to respond. We wish you all the best personally, and we fully intend to take advantage of the improved investment opportunities.

March 16, 2020

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