October 2020

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MARKET SUMMARY

Equities

MSCI AC World	565.2
Price / Earnings	23.0x
Dividend Yield	2.1%
S&P 500	3,363
Price / Earnings	25.6x
Dividend Yield	1.8%

US Interest Rates

2 Year Treasury	0.1%
10 Year Treasury	0.7%
30 Year Treasury	1.5%
Bloomberg US Agg.	1.2%

US Corporate Spreads

Investment Grade	1.5%
High Yield	6.0%

Equity Volatility

CBOE SPX Volatility	26.4

US Economic Figures

GDP Growth 2Q20	-31.4%
Unemployment	7.9%
Inflation (core)	1.7%
Fed Funds Rate (mid)	0.1%
3 Month LIBOR	0.2%

Commodities

Oil (Brent)	$40.95
Natural Gas	$2.53
Copper ($/lb.)	$3.03
Gold ($/oz.)	$1,886

Foreign Exchange

Euro	$/€	1.17
Japanese Yen	¥/$	105
Chinese Yuan	元/$	6.78

Market summary data as of:
September 30, 2020

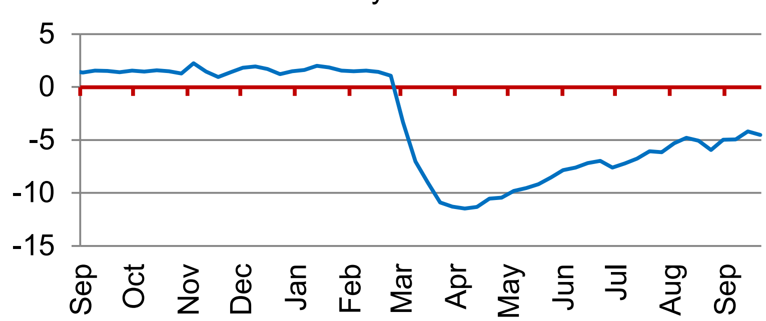
Warp(ed) Speed

The recovery from the depths of the COVID crisis continues. Trends in society and the economy, which reflected severe lockdowns months ago, are improving. We would surely prefer the pace and consistency of improvement to be higher but take solace in the facts that point in the right direction.

With the unique nature of this year's economic and market conditions rendering many traditional measures of the cycle less helpful due to lag and frequency issues, we highlight a number of real-time indicators that give a sense for how much the current situation has and is improving.

The New York branch of the Federal Reserve in recent years began publishing an index comprised of daily and weekly data points that provide a snapshot of current activity. This measure shows the economy operating at a 4.5% lower level than a year ago while steadily improving.

Exhibit 1: NY Fed Weekly Economic Growth Index %



Google's device mobility data (yes, they know where you are and what you're doing) paints a similar picture of global activity that is still down from a pre-COVID baseline but materially improved from earlier lows. As we discussed in our April letter *Scylla & Charybdis*, most of the hit to the economy and corporate earnings was due to government mandates. Many lockdown requirements remain, but data and scoring by Oxford University regarding the stringency of government-imposed restrictions show an easing from the worst levels.

Exhibit 2: Google Mobility Trends

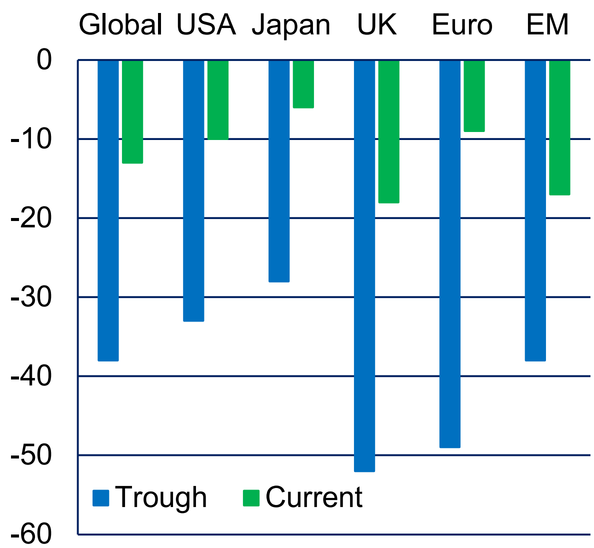
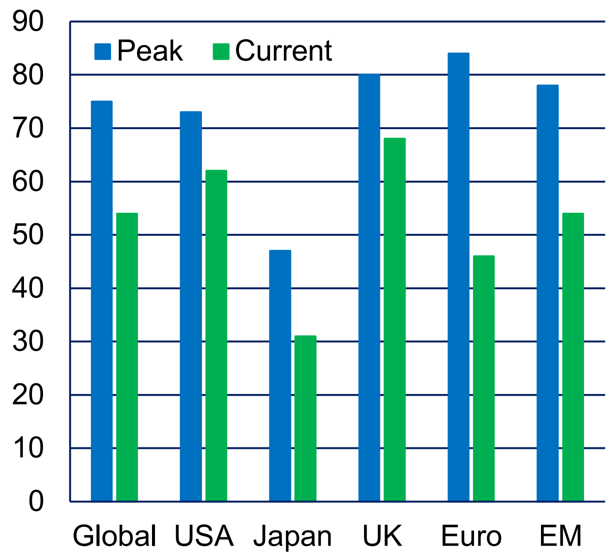
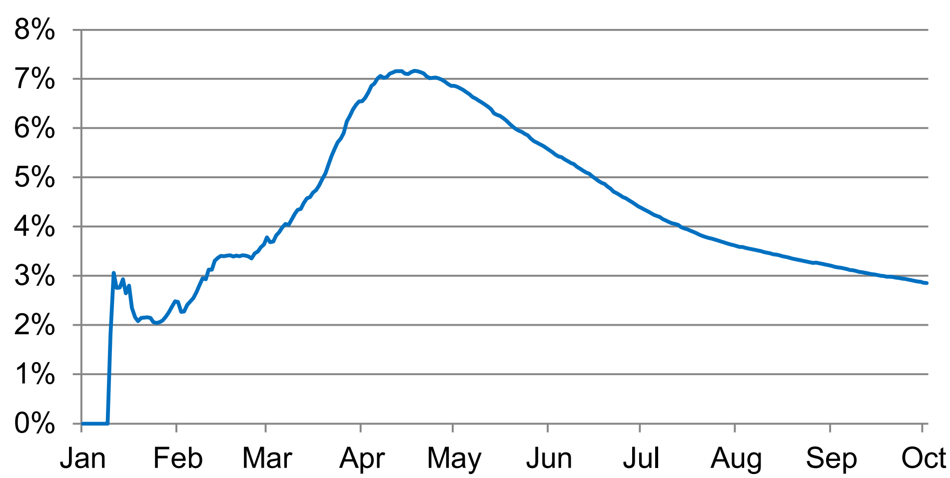


Exhibit 3: Oxford Lockdown Stringency Index



The path of the pandemic remains the primary factor governing the speed of the economic recovery. A breakthrough with an effective vaccine would mark the endgame in our battle with the virus. Operation Warp Speed, the US federal program providing public funding for private vaccine development, aims to produce and deliver 300 million doses of safe and effective vaccines, with the initial doses available by January 2021. Meanwhile, advances in treatment methods and products like Gilead's Remdesivir and Regeneron's synthetic antibodies can limit the deadliness of the pandemic until a vaccine solution is found. Indeed, the effect of improved treatment protocols and drugs is already resulting in a lower mortality rate.

Exhibit 4: Global COVID-19 Mortality Rate on Confirmed Cases



We discussed in recent letters the massive monetary and fiscal stimulus provided to cushion the economic blow resulting from government restrictions and a shift in consumption patterns. In recent months, authorities have expanded their commitment to super-loose monetary policy and super-high deficit spending. The Federal Reserve at their September meeting extended the timeframe for zero interest rates through the end of 2023 with Chairman Powell proposing a substantial increase in central-bank-funded government stimulus beyond the unprecedented amounts already spent. Congress and the Treasury Department are negotiating another spending package that will likely be in the trillions of dollars.

These steps have led to further extreme moves in financial markets -- notably, a persistence of record-low long-term interest rates and a continued widening of the valuation of growth stocks relative to the rest of the market. Market prices have been warped by policy and have become detached from historical norm and the fundamental trend toward recovery in the economy and corporate earnings.

Exhibit 5: 10 Year US Treasury Yield & Inflation %

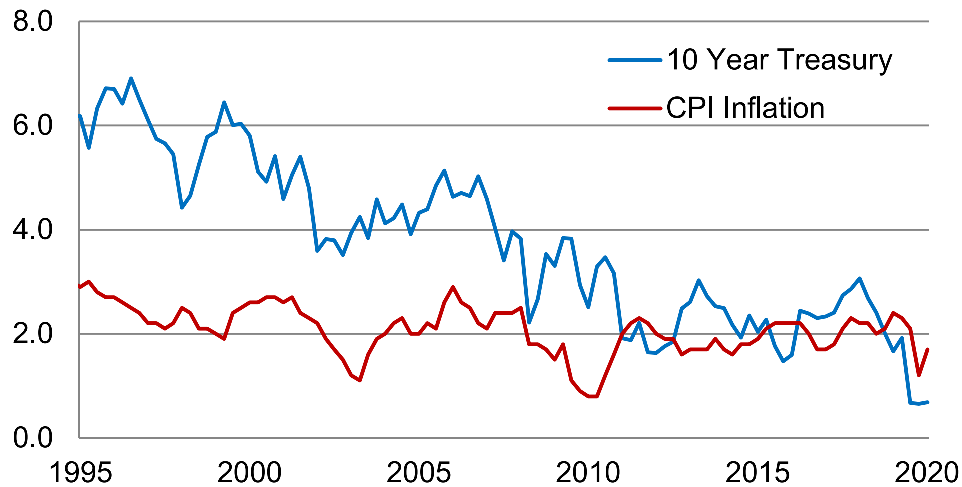
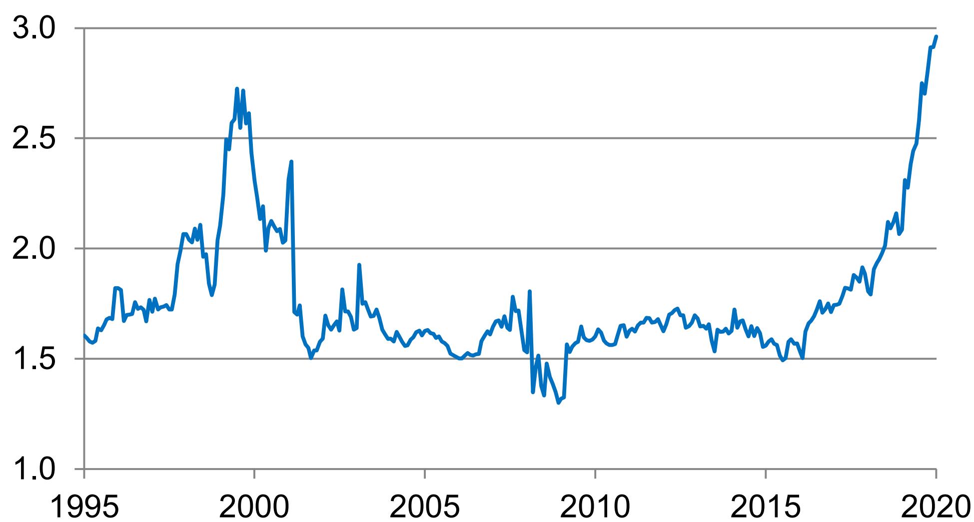


Exhibit 6: Global “Growth” vs. “Value” Stocks Relative Valuation
(Equally-Weighted Relative Price/Earnings, Price/EBITDA, & Price/Book)



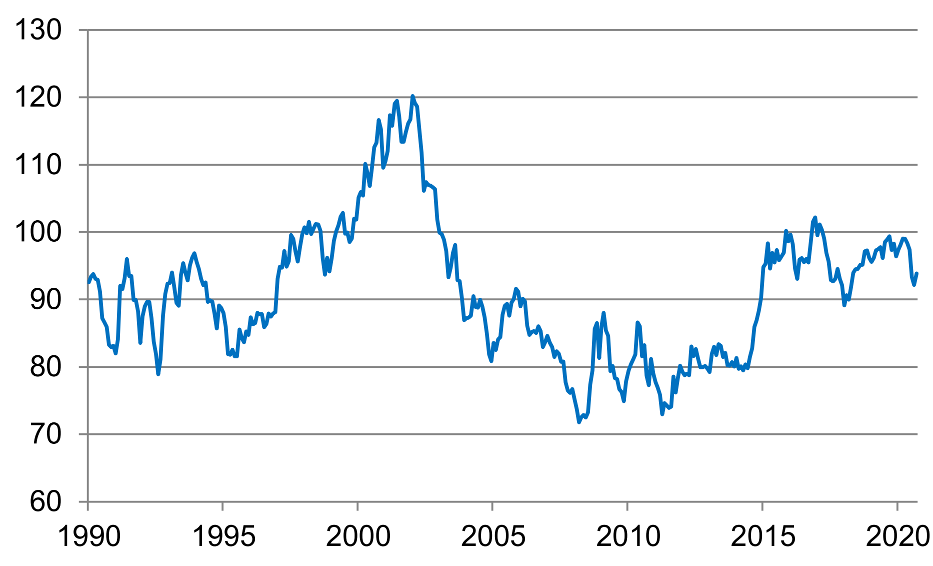
How long these imbalances will remain or if they will get more extreme is impossible to know. Such is the unpredictability of capital markets in the short term. We believe, however, that the current state of affairs – long-term treasuries that yield a rate lower than inflation and mega capitalization growth stocks in the US trading a high double-digit and triple-digit price-to-earnings multiples – will not be sustained in the medium and long term. An adjustment is in order.

A possible, if not likely, catalyst for that adjustment would be further success in medical technologies that allows us to resume a more normal level of economic activity. A higher and broader cyclical dynamic would put upward pressure on long-term yields and downward pressure on the valuations of this year's high flyers. Given the dominance by size that these areas have in their respective markets, a discounting of a post-COVID environment could limit returns in the major headline indices.

That still leaves room for positive returns in what has been a bipolar market. Corporate bonds can benefit from tightening of credit spreads, and the stock market outside of mega cap technology and "stay at home" stocks can benefit from a broadening of demand. The average stock in the US and globally is still down over 6% this year.

Further opportunities may present if monetary policy is slow to react to a cyclical improvement. The Fed has shifted its policy yet easier toward "inflation averaging", which may help end or reverse the 12-year rally in the US dollar versus other currencies. Securities denominated in foreign currency and precious metals such as gold and silver would stand to benefit.

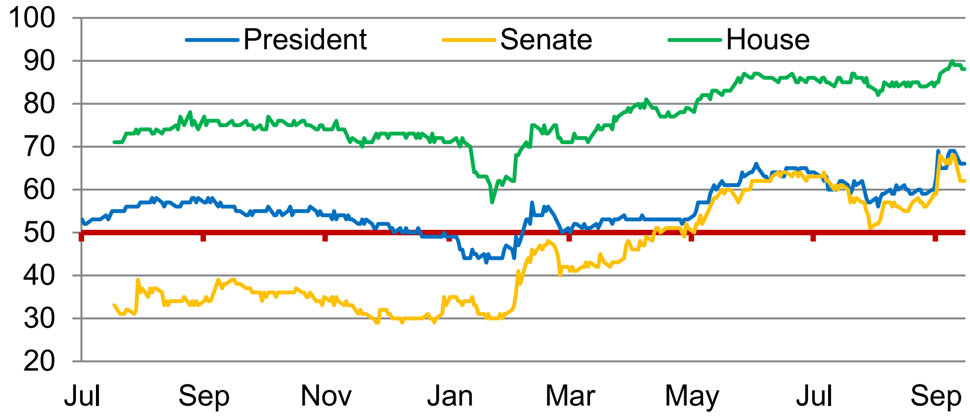
Exhibit 7: Trade-Weighted Dollar Index



The effect of the election is a common question we've fielded from clients in recent months. Simply put, there isn't a binary effect of one party over another occupying the White House being good or bad for the performance of capital markets. The situation is nuanced. Should the Democratic Party sweep the presidency and both houses of congress, investors would contend with higher corporate taxes, capital gains taxes, and regulatory burden. Those negatives might be offset in the short term by the Democratic Party's preference for higher stimulus spending and a less stringent stance on trade.

Should the Republican Party retain the presidency and/or the senate, the potential for major change is limited, and a post-COVID environment could look a lot like conditions prior to the pandemic.

Exhibit 8: PredictIt Democratic Party Control Probability %



We look forward to more normal times when we can return to seeing clients in person. Meanwhile, we hope that you and your families will stay healthy and safe. We are available to discuss with you – via phone or video call -- the capital you've entrusted with us and the evolving economic and market environment. We're grateful for the opportunity to work with you.

With best regards and wishes to your health and safety,

Jeffrey E. Bernardo CFA

Gregory M. Estes CFA

Steven M. Herbert CFA

Milena D. Spasova CFA CIPM

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