

THE FINAL STRETCH

We believe the market is in an uptrend but the near-term forecast is decidedly unclear. It's been a wild ride so far and President Trump testing positive for the coronavirus may only be the first of many October surprises. The market's rapid decline to the bottom on March 23rd resulted in an historic rally to record highs in September. The rally seemed to ignore the unraveling of the U.S.-China relations, antitrust actions against big tech, the potential for a Fall coronavirus wave, and a potential Democratic sweep portending tax hikes for both corporations and some individuals. A future potential negative may be a contested presidential election.

Yet the market has parsed through these concerns and the outlook for the economy and investors is not all grim. From depressed levels, economic growth continues to build. The Atlanta Fed US real GDP tracking estimate for the 3rd quarter is at +35.2%. Notably, the following economic indicators are above pre-lockdown levels: small business optimism, homebuilders housing index, non-defense capital goods spending and household durable goods consumption. ISM services remains firmly in expansion territory, with the employment component growing for the first time since February. The unemployment rate was nearly halved from April's level of 14.8% to 7.9% in October and 500,000 people per week are coming off the unemployment rolls.

Positively, as a result of the lockdown, some companies have grown stronger at the expense of their smaller competitors. Accelerated investment in technology, a surge in e-commerce, and forced expense streamlining have allowed dominant companies to grow even more dominant. They are enjoying improved margins, operating leverage, and earnings growth as demand returns. S&P 500 earnings expectations have steadily increased since bottoming on May 15th, and positive earnings revisions now stand near all-time highs.

Several factors are supporting the market. Inflation is not broadly visible, the Fed is signaling a rate increase is not in the cards for the next two years, market breadth is expanding, and credit remains well-behaved. The fiscal and monetary stimulus enacted thus far has backstopped consumption, though more is likely necessary and post-election, it is a near certainty. With prospects of continued growth off depressed levels and no attractive alternative in the bond market, equities should continue to enjoy tailwinds regardless of how the election is finally resolved. We continue to stress buying quality equities with good balance sheets and long term growth potential.

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