On balance, we remain on the optimistic side of the ledger regarding both the economy and stock market. There are certainly some big unknowns that will eventually come to light, such as how bad will the earnings and economic numbers be? When will a robust medical solution for the Coronavirus arrive? Or perhaps, most importantly, when will things get back to normal?

## The Economy may not falter as badly as the consensus indicates

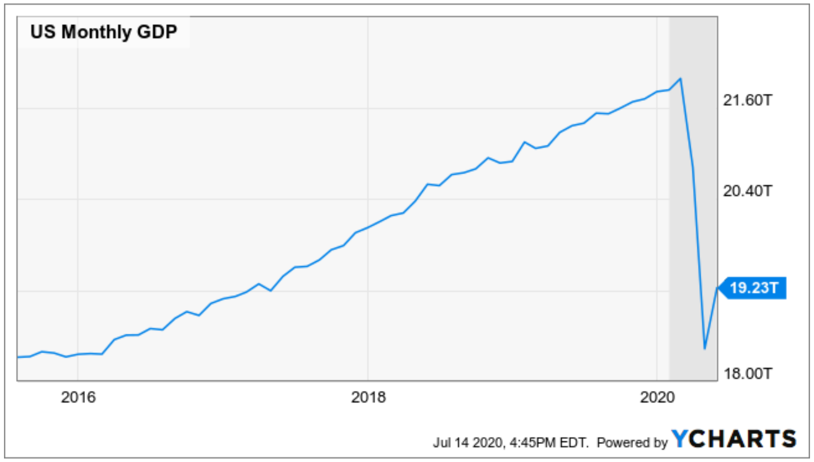
As of July 14, the median estimate of Wall Street economists, according to CNBC/Moody's Analytics, for the 2nd quarter 2020 Gross Domestic Product (GDP) is a decline of 35.4% versus the 1st quarter. That would represent the largest (by far) GDP decline in at least 100 years. We may indeed look back in a few years from now and try to fully appreciate this possible outcome before us. On the other hand, the decline may be even greater – or milder.

We fall in the milder camp.

Certainly for a few weeks and possibly months, the economy 'seemed' like one-third was shut down – at least visibly. Stores and restaurants were shuttered, travel plans scuttled, and the roads were quiet. We believe it is fair to say the worst of those cave-dwelling days are behind us.

Additionally, much of the behind-the-scenes activity remained intact through those dark days. If you have had a chance to look at any of the government lists of "essential services," it was quite large – at least the one that declared our business as essential. In our estimate, most of the largest economic segments remained relatively unimpacted – essentially every aspect of financial services, healthcare, utilities, real-estate (rent & mortgage payments), communication services, food (agriculture and groceries), technology, and all-levels of government continued at relatively normal levels. Collectively, these segments represent a large majority of the economy.

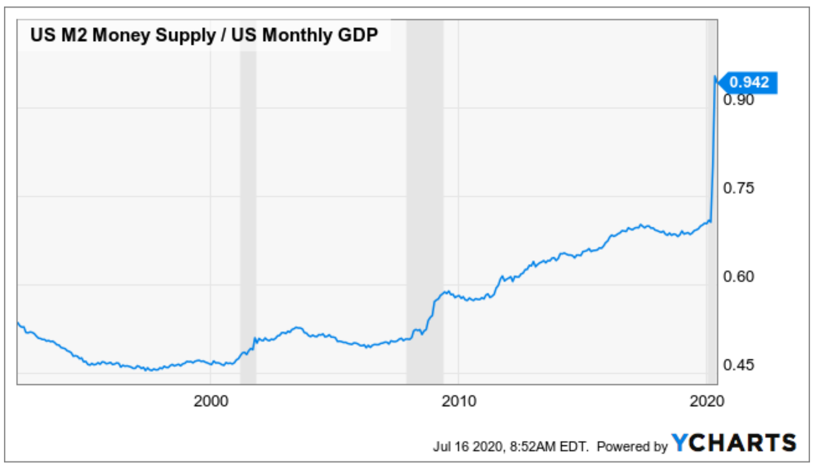
Further, when we observe other economic indicators, such as the monthly GDP estimates provided by Macroeconomic Advisers® by IHS Markit (IHS), the decline looks milder. While official GDP data from the Bureau of Economic Advisors (BEA) is reported quarterly, IHS claims to employ the same calculation methods as the BEA, and from our perspective seem more reasonable. At its lowest point (April 2020), GDP was off by just over 16%. In May, activity picked-up and sits approximately 12.5% off the high.




Source: IHS Markit.

## There is a tremendous amount of cash on the sidelines

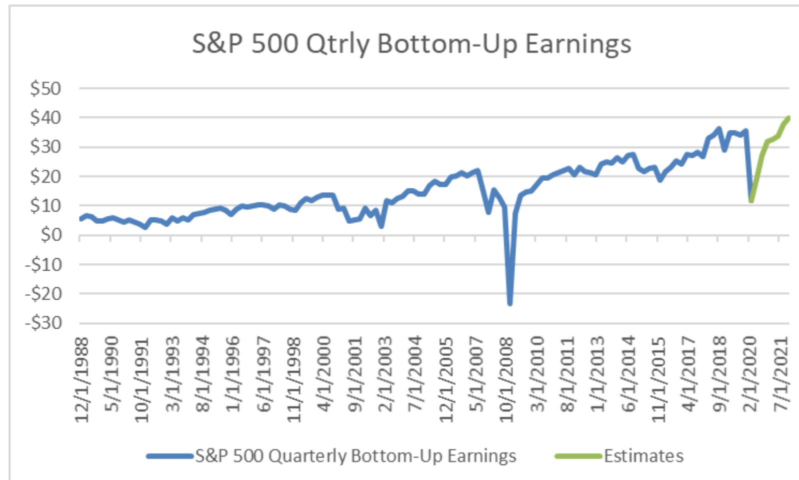
M2 is a measure of money supply that includes currency, travelers' checks, checking & savings accounts, and money market funds in the U.S. economy. Even though it is referred to as money 'supply,' it also represents the amount of money consumers, businesses, and institutions demand to be readily available. In our view, this represents kindling that potentially ignites economic activity. Right now, there is historically high levels of money on the sidelines – not just in absolute terms but relative to the economy. This effectively implies that as confidence returns, there will be a lot of money ready for spending.




Source: IHS Markit, Federal Reserve, YCharts.

## Corporate earnings may rebound quickly

While it sometimes seems as though we have dug a large hole that will take years to get out of, companies may be earning historically high profits by the end of 2021. In fact, the "bottom-up" consensus is for the S&P 500 earnings to reach previous highs by the 3rd quarter 2021. While we tend to agree with consensus here, it would not surprise us to see a relatively high percentage of companies use this current period to take higher-than-average losses (i.e. write down assets, reduce goodwill, etc.) similar to what was observed in 2008-2009.




Source: Standard & Poor's.

## We may have a Coronavirus vaccine by early 2021

While we do not have a tremendous amount of data to support this idea, we do have some very good indications from the pharmaceutical industry and companies that a vaccine is on track for an early 2021 arrival. For example, Moderna Inc. has a vaccine in Stage 3 testing. Its recent article in the New England Journal of Medicine ([www.nejm.org/doi/full/10.1056/NEJMoa2022483](http://www.nejm.org/doi/full/10.1056/NEJMoa2022483)) claimed “no severe adverse events” and “anti–SARS-CoV-2 immune responses in all participants” which optimistically can be interpreted (our interpretation) as reasonably safe and effective for the 47 participants in that trial. Other major pharmaceutical companies are also claiming similar reasons for optimism.

Despite these reasons for optimism, there are many unknowns such as: how long will a vaccine’s antibodies last? Will the antibodies actually be effective in preventing a COVID-19 infection? Will it work on all ages? Etc. On balance, however, we consider the unusual times we are in and the apparent willingness by the government to get something to the masses quickly. Both factors act as accelerants for approving something that is highly likely both safe and effective – despite a departure from the typical timeline.

## Stocks are relatively attractive

Despite arguably higher price-to-earnings ratios (32x based on S&P earnings through 06/30/2020 which includes a partial estimate vs. a median value of 22x since 12/31/1988, stocks are attractive on other measures. For example, dividend yields are higher than 10-year treasury bonds. While not a slam dunk in terms of compelling value, higher yields mean that for many investors stocks are a good source of income. Currently dividend yields provide an approximate 1.3% advantage over 10-year treasury bonds.


## Conclusion

While this report has a largely optimistic tone, we remain cautious on the current amount of corporate debt which is historically high. At some point, this debt level could lead to a sell-off in equities assuming the potential for a higher default rate. We believe the strong run-up in stock prices by a limited number of very large stocks deserves our attention as well. It could be an early sign of a bubble, but at this point, the underlying businesses seem to justify the prices – in our view. Overall, we believe earnings and the economy will largely return to their former glory mostly in 2021 and 2022 assuming a vaccine is widely available in the 1st half of 2021.

Given the moderately optimistic outlook and despite some cautions, we believe investors should maintain their long-term asset allocation. If a market correction greater than 10% were to occur for any number of reasons such as the upcoming election or a pick-up in Coronavirus cases, cash on the sideline should be invested accordingly.

### Jack Brown, CFA, *Chief Investment Officer.*

Mr. Brown is a partner and the firm's Chief Investment Officer. He was the founder of Laureola Asset Management, a private investment firm that merged with Aviance Capital Partners. Mr. Brown was a Director for Prudential's Strategic Investment Research Group, managed a due diligence team at Smith Barney, and was a sell-side analyst for UBS. He has been managing investment portfolios since 2005, and his research has been published in multiple peer-reviewed professional journals. Mr. Brown earned a Master of Business Administration (MBA) from Drexel University and a Bachelor of Arts in Economics from Indiana University of Pennsylvania. He holds the Chartered Financial Analyst (CFA) designation and is a past president of the CFA Society of Naples.

### James Neel, CFA, *Founding Member / Sr. Portfolio Mgr.*

Mr. Neel is a founder, partner, and Senior Portfolio Manager for the firm. He was the Senior Resident Officer at Bessemer Trust, Resident Manager at Brown Brothers Harriman, Chief Executive Officer and President at Dreman Value Advisors, and Portfolio Strategist and Equity Mutual Fund Manager at Kemper Financial Services. Mr. Neel has managed portfolios for pension plans, foundations, mutual funds, and high net worth individuals throughout his more than thirty-five years in the investment industry. Mr. Neel earned both a Master of Business Administration (MBA) and Bachelor of Arts in Economics and Political Science from Michigan State University prior to serving four years as an United States Naval Officer. He holds the Chartered Financial Analyst (CFA) designation.

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Mr. Chapman is a Portfolio Manager for the firm. Prior to his current role, he served as Portfolio Manager and Senior Analyst at Private Capital Management, Portfolio Manager at Invesco, and Senior Analyst at JPMorgan Chase. Mr. Chapman earned a Bachelor of Science degree in Petroleum Engineering from the University of Texas. He holds the Chartered Financial Analyst (CFA) designation.