PALLAS
CAPITAL ADVISORS

Week in Review

Friday, May 15th 2020

- PUBLIC PENSION PLANS returned a median of -13% in the first quarter of the year, according to Wilshire survey results released earlier in the week. This represents the worst quarterly returns for respondents over the past four decades, since the inception of the survey. Chicago Teachers' Pension Fund Investment Chief, Angela Miller-May, indicated that these results don't show the full extent of the losses since reports of private equity, real estate, infrastructure and other private assets will be reported at a later date. Separately, the Executive Director of the Maine Public Employees Retirement System, Sandy Matheson, expects that the state's annual pension contribution will rise to $927 million from a previously estimated $808 million, if stocks fall back to prior lows before the fiscal year end in June. When investment returns decline, the shortfall is typically shouldered by government revenues.

- FOLLOWING THE JOBS REPORT, another 3 million workers applied for unemployment benefits in the prior week, bringing the total number of applications to 36.5 million since the pandemic began. Florida, Georgia and Connecticut reported the highest number of new claims, each showing more than 200,000 applications. They were also among the few states that saw a weekly rise in claims last week. The number of workers drawing on unemployment insurance continues to remain elevated. The increase in payments rose from 22.4 million to 22.8 million participants.

- THE DOW DROPPED MORE THAN 500 POINTS MID-WEEK after Federal Reserve Chairman, Jerome Powell, said additional stimulus could be needed to support the economy's recovery. The declines were broad, with 29 of the 30 stocks in the index moving down. All 11 sectors of the S&P 500 also declined following the speech, with shares of energy, airline and bank stocks falling the most. Halliburton posted -9.1%, United Airlines Holdings UAL posted -11.17%, and Wells Fargo lost -6.3% during the day's downturn. All three of these companies have lost more than half their value for the year to date. Within his speech, he voiced his concern about the fragility of the recovery and saw the future as "highly uncertain and subject to significant downside risks."

- THE TOPIC OF TARGETING NEGATIVE RATES came into greater prominence after futures markets began betting on negative rates. However, Federal Reserve officials voiced that it is unlikely to use negative interest rates as a method of stimulus given the harmful impact to the banking system. The policy makers have said that they prefer to stimulate growth with tools similar to those employed during the global financial crisis, which was dominated by government purchases of long-term securities.

- CONSTRUCTION FIRMS CAN BEGIN OPERATIONS in limited capacity across New Jersey and in the northernmost counties of New York as both states allowed a limited economic restart. The New York Governor said that northern sections of the state had met the required hurdles for a limited reopening. State officials also said earlier in the week that regions in the Finger Lakes had met the requirements as well. New York's reopening will allow construction, manufacturing, agriculture, forestry, fishing, as well as retail for curbside pickup, drop-off, or in-store pickup. The state reviewed federal guidelines that considered statistics relating to hospitalizations, deaths, and the capacity for testing and tracing new infections.

- THE COMPETITIVE RISKS INCREASED FOR TESLA, which remain shuttered while automakers in Detroit reopen. The situation has caused tension between Elon Musk and California officials. Rivals could more quickly restock dealerships with new vehicles ahead of the California based car company. General Motors, Ford, and Fiat have brought back a subset of employees this week in preparation of resuming vehicle production starting May 18. When local authorities said Tesla's factory should remain closed, Elon Musk called the disparity "insane."

- FOOD DELIVERY COMPANIES remain unable to grow profits. Grubhub and Uber Eats are merely breaking even, despite one of the best delivery service opportunities in decades. While sales are growing, increased promotional costs, funding for worker safety equipment, and reduced commissions from strapped restaurants have cut into margins. Restaurant owners may receive as little as 50% of the proceeds of the food sales after fees, commissions, and price adjustments are made due to customer complaints. This has spurred restaurants to connect directly with clients and pay their own staff to make deliveries.

- SANOFI CHIEF EXECUTIVE OFFICER, PAUL HUDSON, engendered outrage when he signaled that the US would be ahead of the rest of the world in receiving whatever vaccine was developed to counter the current pandemic. The rationale for the prioritization stems from the United States early contribution in funding the firm's research efforts. Health advocates have warned that this would subject vulnerable countries to mass fatalities and economic collapse. "Nobody should be pushed to the back of the vaccine queue because of where they live or what they earn," said South African President Cyril Ramaphosa. The leader of France's Socialist Party, Olivier Faure, suggested that Paris-based Sanofi risked being nationalized and Prime Minister, Edouard Philippe, tweeted that "equal access to a vaccine is not negotiable."

- FOR THE SECOND QUARTER, THE IEA INCREASED ESTIMATES FOR GLOBAL OIL DEMAND by 3.2 million barrels a day, to 79.3 million. This was a shift from the prior month, when the agency's chief described the period as "Black April" when the agency warned that cutbacks by producers weren't enough to prevent the world's storage tanks being overwhelmed by the middle of the year. Global oil supplies may drop by 12 million barrels a day, roughly 12% from the prior month as OPEC+ implement production cuts. Such efforts are compounded America's shale producers, where output may be down 2.8 million barrels a day.

Thinking Ahead

The market's sharp rebound in the midst of declining economic indicators is perhaps the strongest signal of our nature to persevere through the greatest of challenges. While countless amounts of data have been aggregated to support either the upside or downside scenario, few would argue that we are not already looking towards better day's, where we continue to work, educate, care, and connect. Our latest monthly commentary considers a few of the emotional and sociological shifts that we have seen, and their associated influences upon the markets. In short, the pandemic has forced us to reconsider our priorities, perhaps fostering a unity of purpose which helps improve our relationships, both locally and as global citizens.

From a more practical standpoint, the core function of capital markets centers on the allocation of resources, directing funds at the aggregate level, towards opportunities and projects that improve our wellbeing. This path is sometimes meandering as we examine how shocks to the system and competing forces change the landscape. Eventually, we begin to understand how current value propositions deteriorate, and how new ones evolve to take their place.

Despite the unsettled ground beneath us, the Pallas team remains firm in our belief that fundamental insights supported by a data-driven discipline still provides the most meaningful foundation for investing. This requires that we consistently review new ideas to improve internally managed strategies or seek external expertise that offers differentiated and diversifying opportunities. It also means that we must be disciplined in finding inconsistencies in how markets value the assets that shape a better future. In simpler terms, our team continues to craft investments that directly connects better outcomes for shareholders and society.

We will continue to provide weekly market updates. In the meantime, you can access our thought leadership pieces on our Insights page and by following us on LinkedIn.

You can access a recording of all prior webinars here.