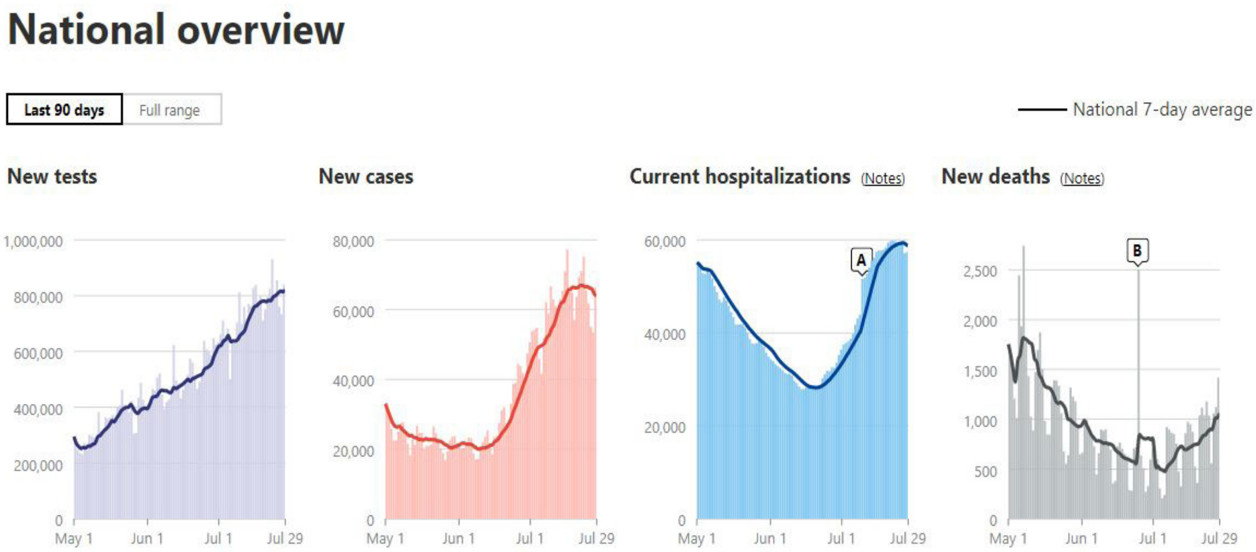
Week in Review

Friday, July 31st 2020

- WITH OVER 26% OF COMPANIES HAVING REPORTED EARNINGS, 81% of S&P 500 companies have reported a positive earnings-per-share (EPS) surprise, with 71% reporting a positive revenue surprise. Earnings have been 11.4% above estimates (above the five-year average), and sales are 3% above estimates (also above the 5-year average). The number of companies who were previously not providing guidance but now are, vs companies who were providing guidance but now are not, has improved to 5-to-1. Investors may view this reversal as potential green shoots of confidence that corporate America is getting back on its feet.

- A RECENT MIT STUDY cited in the Boston Globe claims that the actual number of COVID-19 cases may be 12 times higher than reported, with 50% more deaths. If that is true, it would imply that the infection fatality rate is 0.68% (1.59% for the US). Combined with positive incremental data on deaths, the trajectory of COVID growth may not be unsustainable for a robust US healthcare system. The study concludes that mask-wearing and social distancing remain the most viable short-term options, and that we are nowhere close to herd immunity.

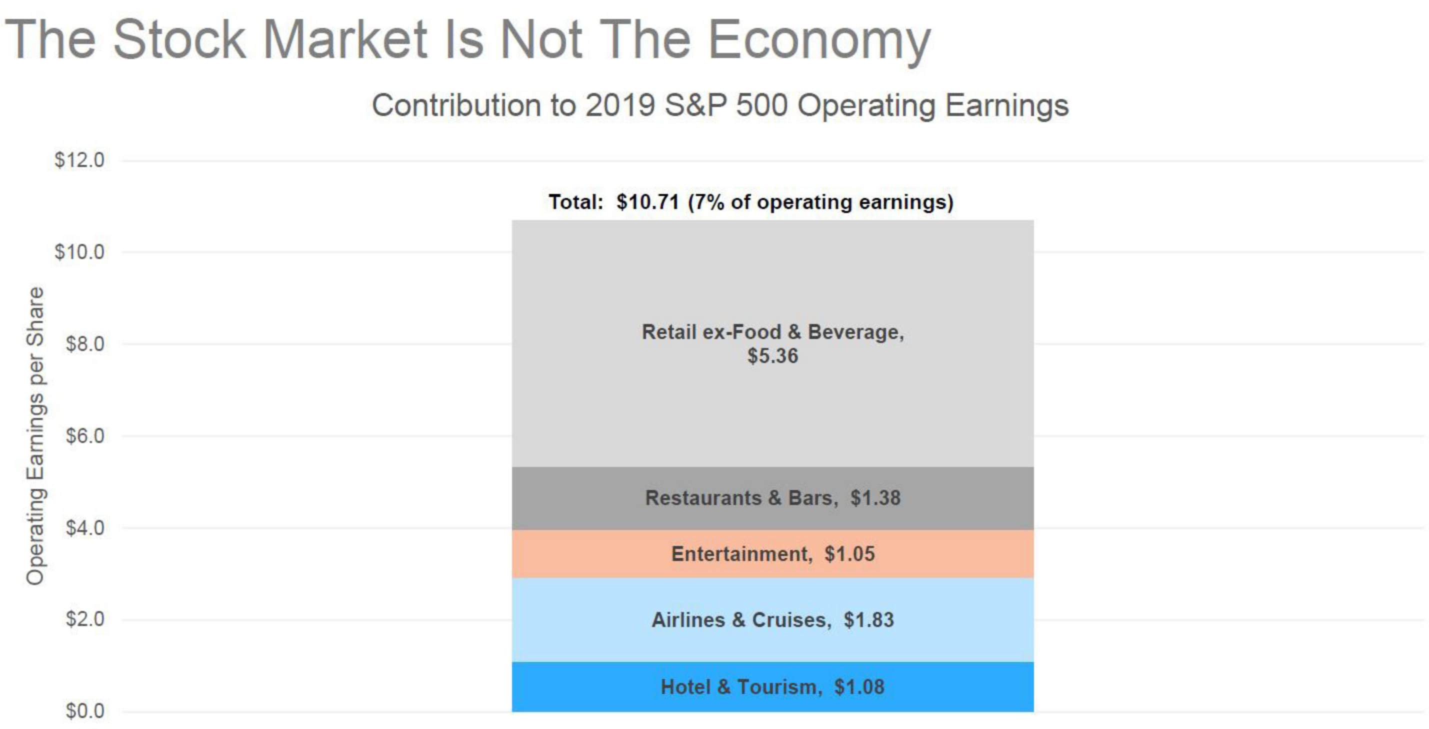
- HOSPITALIZATIONS AND NEW CASES may be peaking in the US, according to the most recent data on covidtracking.com. However, it is essential to keep in mind that long-term mentality about the virus can cause wild swings in either direction. For instance, if folks feel the virus is receding and use this as a cue to change their social distancing behavior, we could easily imagine another spike in new cases and deaths:



Source: covidtracking.com

- LEADERS OF THE BIGGEST US TECH COMPANIES stood before Congress on Wednesday, July 29th to defend their companies' practices which have been viewed as anti-competitive. While there seemed to be bipartisan agreement that action was required to reign in big-tech, the actual interactions between senators and tech leaders provided early clues to the direction the investigation(s) were going. For instance, Tim Cook of Apple faced relatively fewer questions, even though Apple has arguably the most interaction with China. Facebook was grilled for Mark Zuckerberg's acquisition strategy, while Amazon was torpedoed for its questionable use of client data to launch competitive products. While Google has done relatively little work in China, they faced the most questions on China. The Democratic leader of the hearing likened the companies to a "King" that the American people of the revolutionary era should not "bow before."

- TO REITERATE A CENTRAL ARGUMENT FOR THE STOCK MARKET'S METEORIC RISE: the stock market is not synonymous with the economy. A recent CNBC article estimated that 7.5 million small businesses may be at risk. In stark contrast, only 7% of operating earnings in the S&P 500 ($10.7 billion) comes from the business segments most highly affected by COVID-19:

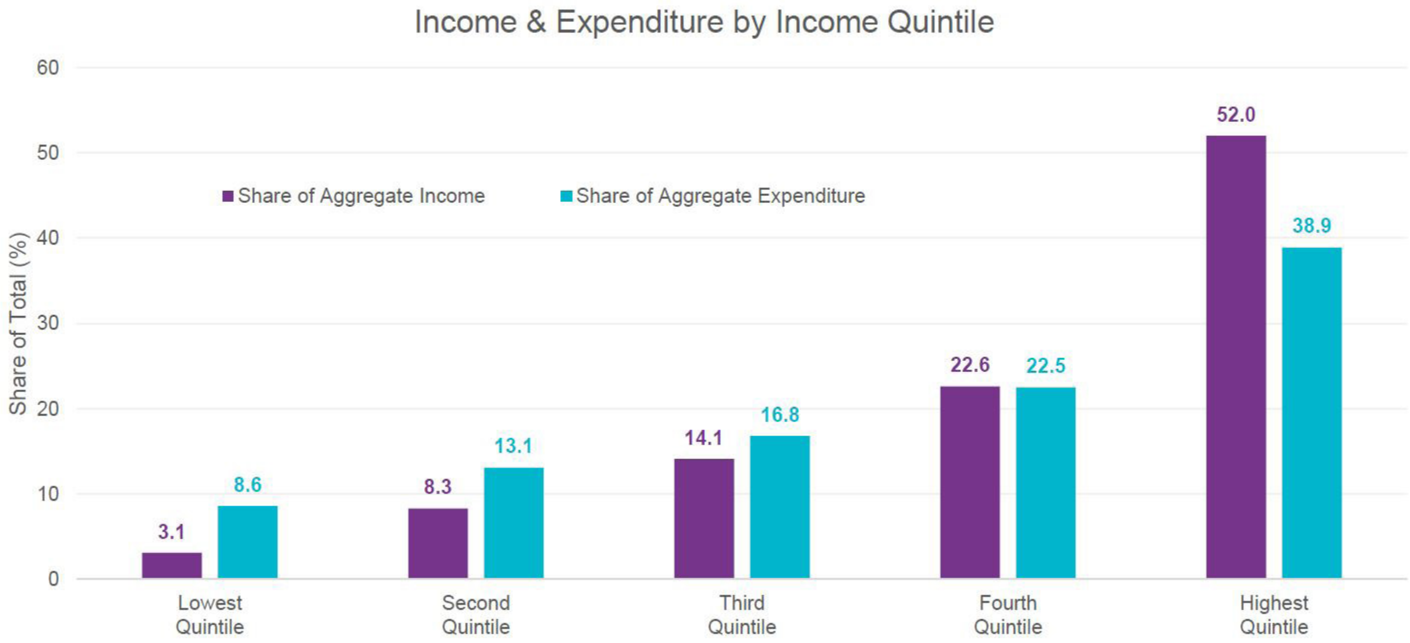


Source: Natixis PRCG, JPMorgan Asset Management - Guide to the Markets. March 31, 2020

- TO FURTHER DRIVE THIS POINT HOME, we notice that, unfortunately, the pandemic is hitting lower income brackets much harder. While the total share of job losses falls 65% into the category of those earning 75k or lower, these brackets only account for a small portion of aggregate expenditure:

PALLAS CAPITAL ADVISORS

Are We Overestimating Lost Consumption?



Source: Natixis PRCG, The International Monetary Fund Fiscal Monitor. April 2020

- THE MAJOR RISK REMAINS that there may not be another stimulus (or that it is not big enough.) As of Thursday, 7/30, Congress remains at odds over a package. Without one, consumer spending, which accounts for 70% of the US economy, could be at risk.

Thinking Ahead

Pallas Capital Advisors recognizes the value of having a conservative mindset. During these important times, when uncertainty is historically high, we believe that the evidence favors having a balanced approach to asset allocation. While valuations in equities and bonds remain high, unprecedented global monetary policy has driven interest rates to all time lows, such that over 22% of all global debt trades at negative yields ($14 Trillion). With that in mind, we believe it is paramount to keep long-term client goals in mind when designing asset allocations. On the other side of volatility lies opportunity.