PARKSIDE INVESTMENTS

Market Commentary

June 30, 2020

Dear Clients/Friends,

After rebounding sharply in April and May, equity markets leveled off in June as health trends and economic data conveyed mixed messages to the financial markets. Despite the challenges confronting economies over the short and intermediate term, unprecedented actions taken by Congress and the Federal Reserve provided equity markets a level of confidence that seems inconsistent with the real world consequences from the COVID-19 pandemic. Despite the broad rally in the second quarter, the S&P 500 is down 4% in the first half of the year. The other broad market benchmarks have not recovered as swiftly, with the Russell 2000 small cap index still down 13% while MSCI international stock indices are down approximately 11% over the first six months of 2020.

Although equity indices remain down year-to-date, the dispersion within the benchmarks has reached extreme levels not seen since the technology bubble of 1999-2000. In addition to large cap stocks outperforming small cap stocks by nearly 10% YTD, U.S. corporations that have historically grown revenues rapidly (including technology, communications and healthcare companies), have vastly outperformed slower-growing cyclical companies that are trading at more reasonable valuations levels. The pandemic has accelerated the Growth over Value and Large Cap over Small Cap trends that were in place pre-COVID, and propelled valuations to extreme levels (both on the high and low end). Our view is that these trends are likely to reverse – and perhaps sharply so – when economic activity improves in a more durable manner.

The timing and speed for an economic recovery remains elusive. In the short-term, two risks are potentially highly problematic to the recovery scenario implied in the current stock market valuations. First, spiking COVID rates have caused some regions to stall or reverse recently reopened segments of the economy. Second, existing fiscal stimulus programs, including those guaranteeing paycheck protections to furloughed workers, will soon expire and Congress is still weighing whether additional stimulus measures will be passed.

Over the intermediate term, we continue to see unemployment levels remaining elevated for at least a few years. Recent social unrest is likely to grow as economic disenfranchisement potentially expands amongst those who might be facing prolonged out-of-work status. Additionally, the rapidly expanding government debt load presents long-term implications for tax policy and

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inflation risks. Equity markets may look beyond these issues short-term – especially if additional stimulus packages are passed by Congress – but these issues will be amongst the most important ones which need to be dealt with in a post-COVID world.

Despite these challenges, the markets may well continue with a "glass half-full" perspective toward an economy that should rebound in the third quarter – albeit at a level still well below the pre-COVID baseline. Additionally, given the unprecedented government stimulus in the system, if an effective vaccine can be widely distributed sooner than anticipated, equities could very well move higher than even the current positive outlook implies.

From a portfolio positioning perspective, at the end of the first quarter/beginning of the second quarter, we utilized accumulated cash to invest in companies/industries with durable profit margins and limited debt constraints. After the substantial bounce back in the equity markets, we have begun to take a slightly more cautious approach, particularly as it relates to segments that are more susceptible to valuation contraction.

We are placing additional emphasis on cash flow generation and stable business models that can operate in a range of economic environments. Over the next few years, many of these companies should perform exceptionally well relative to their modest valuation levels. For example, new second quarter investments included initiating a position in Sysco Corporation, the largest food distributor in the U.S, and positions in various preferred stock securities that provide an attractive 6-7% dividend yield. Finally, we are utilizing hedged ETF securities as complements to equity positions in order to soften potential volatility and capitalize on various market outcomes.

All of these investments are consistent with our view that although the worst of the COVID pandemic may be in the rearview mirror, the future remains highly uncertain, and a disciplined, diversified, and valuation based approach provides the best framework for navigating these periods.

Should you have any questions or comments about our outlook (or any other issues), feel free to reach out to any of us on the Parkside team.

Sincerely,

Alan Cole *Chris Engelman*

President Managing Director

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