Investor Insights & Outlook

October 2020 3rd Quarter Concorde Investment Management

Domestic and International Economic Overview

A Message from Concorde Investment Management

We have an app for your smartphone or tablet that allows you to view your entire portfolio and includes a vault where you can access your quarterly reports, billing summaries, and share documents with Concorde from a secure portal. If you are not yet set up with the app and would like to utilize this feature, please contact Barbie Spicer for assistance.

We are again combining the domestic and international sections in order to highlight the overall issues of economic activity across the globe all being impacted by the Coronavirus.

The 3rd quarter GDP for the U.S. grew at a record pace. The U.S. had an annualized number of 33.1%. That's on the heels of an annualized 5% decline in Q1 and an annualized 31.4% drop in Q2. Sounds great except that is not a V recovery, more like a reverse check mark. Think of it this way, if you lose 50% of 100, to get back to even you need to have a growth of 100%. To put it in perspective, the current recession is an approximate 10.1% annual decline in real GDP. That compares to a 4% decline during the financial crisis and a 26.7% decline in real GDP during the Great Depression.

The current economy is not recovered and won't be until we have a vaccine. This is highlighted from Chase Bank and their 'high-frequency economic activity' index that measures restaurant activity, hotel activity, etc. At the bottom of the pandemic in April, there were zero people eating out, air travel declined 96%, hotel occupancy declined 70%, credit card transactions declined 37%, and mortgage applications were down 35% on a year over year basis. Currently, seated dinners are down 43%, air travel is down 70%, hotel occupancy is down 32%, credit card transactions are down 4%, and mortgage applications are up 22% (see the fixed income section below…..low rates are driving activity). All of that high frequency data has improved however not back to a baseline number. We expect to hover at our current level of activity until a vaccine or vaccines arrive.

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Domestic and International Economic Overview (continued)

Unfortunately, this highlights the need for an additional fiscal package for those Americans not as fortunate as others and, as you might have noticed, Washington isn't functioning like a well-oiled machine ahead of the election.

We are unfortunately having rising cases again in the U.S. and Europe. Pandemic fatigue is real and when populations see changing case numbers (the metric the press seems to report on the most rather than hospitalizations) behaviors change. Declining case numbers result in lax behaviors which then beget rising cases. This yo-yo effect will continue until we have a vaccine or herd immunity.

A note on the upcoming elections. We will send out an update once there is some clarity around the results, which could be delayed past next week, however it is important to recall that we manage investments over the long term. While the election seems to have a dramatic short term effect, there are other global structural issues that we focus on rather than a number of what if's that could take place depending on the political party make-up of the Presidency and Congress.

Fixed Income

As a baseline, market yields on essentially all maturities of U.S. Treasury notes and bonds were essentially unchanged for the quarter. Despite continued uncertainty for the economic outlook, a return to market stability kept flight to quality buyers from driving yields lower and the floor provided by Federal Reserve purchases kept yields from rising from the selling by investors with optimistic growth or rising inflation scenarios. Other domestic credits including corporates, asset and mortgage backed securities, and municipals saw yields drop slightly as buyers supported prices in search of returns despite above average risk for the near future. On a global basis, convertible bonds have been one of the best performing asset classes year to date now that equities have rebounded from first quarter lows and yields, even for lower quality bonds, have stabilized. Lower volatility characteristics along with modest income and potential equity upside have generated a growing appeal for convertibles in the current return starved climate.

With regards to investing in fixed income going forward we still believe large exposure to longer-term high-quality bonds is risky at current yields as the potential damage to total returns from even a modest rise in yields is significant. High quality short term corporates (despite quite low yields), short to intermediate term revenue based municipals and the aforementioned convertibles asset class represent decent value in the current environment created by strong demand for income and the desire of central banks to keep yields suppressed. In the domestic market, the sectors with the worst year to date performance, high yield (junk) and lower rated commercial mortgage backed securities, both have a high degree of risk even at current prices and should be avoided until the outlook clears or pricing more fully reflects risk to investors.

Equity Markets

The domestic equity market continued to recover in the third quarter although at a more moderate pace than the dramatic rebound in April through June. This pattern seems to be mirroring the general economic recovery since widespread shutdowns in March and April as the initial reopenings created a surge of employment gains, but subsequent progress has been more difficult. The equity market outlook going forward for the next year is likely to reflect the rate of economic progress with an emphasis on cyclical and consumer-oriented sectors and less on the large technology and work from home beneficiary businesses. All sectors of the S&P 500 except for energy rose in the quarter, with outperformance by the materials, industrials, and consumer discretionary segments. Growth indices continued to outpace value although the gap narrowed in the quarter. If the cyclical sectors discussed above continue to do well then value investing will continue to gain ground.

On the international front, markets generally rose although at a slower pace than U.S. markets. The variance in quarterly returns was wide as the Chinese, Indian, and EM indices all rose strongly and other country indices such as Brazil and Russia dropped. The U.K. markets continued to generate poor performance this year with concern over post Brexit trade deals in addition to the Covid impact and is down over 20% year to date.

Looking forward, in the U.S. there does appear to be greater upside in the cyclical and value sectors and those areas could outperform even under a moderate recovery scenario over the next two years. The leading technology and tech enabled consumer equities which have vastly outperformed as a result of true fundamental strength may be due for a period of consolidation. International equity investing should be implemented on a selective basis. Valuations for international compared to domestic markets are historically cheap, but this is likely justified as risks are higher from the recent health, trade, and globalization trends. We are currently capturing our international allocation from several larger U.S. based companies with global revenue exposure and dominant market positions.

Representative Indices Performance Year to Date (9/30/20)	
S&P 500	5.6%
Russell 1000 Growth	24.3%
Russell 1000 Value	-11.6%
EAFE (Developed International)	-6.7%
FTSE 100 (U.K.)	-22.2%
Emerging Markets	9.7%
China Shenzhen	29.2%
Brazil	-40.8%

Charitable Giving

Everyone has their own reason for gifting their assets or a portion of their income to charitable organizations. Some find comfort in helping others who are less fortunate, while others simply want to share their good fortune. Many of the institutions of art, sciences and education are supported in large part by those who want to give something back in appreciation for their contributions to the community or the individuals themselves.

Presently, the tax code offers incentives for gifting of one's assets or incomes. Tax deductions are given for current contributions and, for estate owners, charitable gifts can reduce the size of the estate to help minimize estate taxes.

Often times, an individual will designate a charitable beneficiary in their will to benefit the organization after the individual dies. By using charitable gifting techniques, a donor may be able to benefit the charity while living without having to sacrifice the income that an asset can generate. Understanding how properly structured charitable gifts can provide current benefits for both the donor and the charity could be important for the charitably inclined.

Charitable Remainder Trust

A remainder trust enables the donor to transfer an asset while retaining the right to the income it generates. The asset becomes the "remainder" which is owned by the charity. Remainder trusts, if properly structured, can qualify for a current tax deduction. There are three types of remainder trusts:

Unitrust: A unitrust the income the donor receives is based on a percentage of the current fair market valuation of a trust asset. Each year, as the asset is valued, the income is adjusted based on the new valuation.

Annuity Trust: Instead of a percentage of the asset value, the donor is paid a fixed amount annually.

Pooled Income Fund: Donors can pool their donated assets in a fund that is operated by the charitable organization. The donors then receive a proportionate share of income from the fund that is paid throughout their lifetime. Payments can vary each year based on the valuation of the underlying assets in the fund.

Charitable Lead Trust

Also known as an Income Trust this vehicle transfers the income rights to the charitable organization. Generally, the income rights are assigned for a specified period of time after which the remainder passes to the donor.

Charitable planning involves tax issues that should be discussed with a qualified tax or financial professional.