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COLUMBUS CIRCLE
INVESTORS

General Outlook	
Markets	Stay Active
Economy	Stimulants Wearing Off
Corporate Earnings	Surprise!
Outlook	Crossroads Puzzle

Investment Environment

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Markets: Stay Active

Equities continued their strong advance from the March lows, fueled by advancements in COVID-19 vaccine development and rapid testing, robust fiscal and monetary stimulus, recovering earnings, and consumer spending strength as the economy continued to gradually re-open. Despite some late quarter profit-taking, growth stock leadership continued to thrive and increases were strong across the market cap spectrum, with mid and large cap stocks registering their best third quarter gains in a decade. Investors remained most attracted to secular leaders offering superior fundamental visibility in an increasingly uncertain political and economic environment, while elevated consumer and business optimism prompted a market leadership migration from Technology companies to more cyclical Consumer Discretionary and Industrial names. While CCI tactically shifted some sector exposures to capitalize on these pandemic and broader economic recovery benefits, the portfolios remain focused on secular leaders that exhibit strong fundamental growth and positive surprise characteristics, hallmarks of CCI's investment discipline.

The pandemic's volatile and uncertain macroeconomic backdrop supported actively managed portfolios, with the strongest results experienced further down the market cap spectrum where macroeconomic effects and computer algorithm-based trading influences and other exogenous forces are less pronounced, and fundamentally-based stock picking has been more specifically rewarded. Smaller cap benchmarks also have a greater proportion of companies generating financial operating losses and possessing excessive debt leverage, attributes that were unattractive to investors in this uncertain market landscape, enabling active managers to benefit from less exposure to them. Active management's greatest success has

Equity Markets (% Total Return)							
Third Quarter 2020				**Year to Date 2020**			
	Growth	**Index**	**Value**		**Growth**	**Index**	**Value**
Russell 1000	13.22	9.47	5.59	Russell 1000	24.33	6.40	(11.58)
Russell Mid Cap	9.37	7.46	6.40	Russell Mid Cap	13.92	(2.35)	(12.84)
Russell 2500	9.37	5.88	3.54	Russell 2500	11.58	(5.82)	(18.39)
Russell 2000	7.16	4.93	2.56	Russell 2000	3.88	(8.69)	(21.54)
Russell Microcap	6.05	3.69	1.96	Russell Microcap	8.09	(7.94)	(19.90)
S&P 500		8.93		S&P 500		5.57	
International*		4.88		International*		(6.73)	
Emerging Markets**		9.70		Emerging Markets**		(0.91)	
Gold Price Change %		5.89		Gold Price Change %		24.29	

* MSCI EAFE in U.S. $ ** MSCI EMF in U.S. $ Source: FactSet (Indices)/Bloomberg (Gold Price Change%)

been centered on growth stock portfolios focused on earnings consistency, as more than fifty percent of mid and small cap growth managers have exceeded their benchmark returns for the third quarter and year-to-date reporting periods, significantly outpacing the success rates of their value-oriented peers. The performance gap between growth and value indices remains at its widest range in several decades, driven by the scarcity of companies generating strong revenue and earnings growth, near zero interest rates (which are favorable for longer duration assets) extending over the next few years based on recent Federal Reserve comments, and the increased business model disruption from transformative technologies and healthcare practices.

Historically, aggressive monetary policy and fiscal actions facilitate dominant performance by cyclically-oriented value stocks as the economy emerges from the depths of recession and accelerates into recovery. This pattern has not yet materialized during the pandemic, as secular growth companies' superior profitability, growth consistency and financial leverage have instead been prioritized by investors because of COVID-19's unprecedented circumstances. While Consumer Discretionary and Industrial sector names have responded to the early stage v-shaped recovery like the traditional playbook would suggest, value indices are broadly plagued by higher exposures to Financials, Real Estate and Energy companies. Entities within these sectors are facing sustained pressures more now than in the past from low interest rates, overcapacity, onerous regulations, and supply alternatives. Small and mid cap equities have also lagged relative to larger cap stocks compared to historical economic recoveries, and, according to Jefferies, the rolling three year performance shortfall of small caps relative to large caps is the widest since June of 1999.[1] This provides ample opportunity for outperformance should bankruptcies remain largely confined to the select industries most impacted by the pandemic (e.g., brick and mortar retail, travel/tourism), credit spreads remain contained, and confidence in the recovery improve.

Economy: Stimulants Wearing Off

The global monetary and fiscal response to COVD-19 has been enormous, with Bank of America estimating that $20 trillion of stimulus ($8 trillion monetary and $12 trillion fiscal) has been enacted.[2] By comparison, the Great Lockdown of 2020 domestic response has been much more pronounced than the Financial Crisis of 2009 (in terms of percentage of Gross Domestic Product (GDP)), with monetary stimulus of 35% compared to 15% and fiscal actions at 30% vs. 24% according to this same report. These decisive actions were essential with second quarter GDP declines greater than 30%, and provided impetus for a near polar opposite 25-30% increase in third quarter GDP according to recent projections. During September, as the growth trajectory of economic progress plateaued, investors became concerned with the economy's sustainable growth beyond the initial stimulus injections. Represented within the CCI Economic Monitor (which tracks 22 key data points), this curve flattening has straddled the demarcation line between modest contraction and modest growth for the last month after having risen steadily from recession back in April/May. Moderation in Consumer Spending, Industrial Production, and Employment trends created this pause for concern, along with stalled negotiations in the nation's capital for extending further fiscal support to struggling consumers and small businesses.

During the pandemic's initial stage, individuals utilized stimulus checks, supplemental unemployment benefits, and reduced expenditures on consumer experiences (e.g., entertainment, restaurants, travel) as a way to increase spending and bolster their savings due to heightened uncertainty. Spending by the lower income cohort actually grew more notably than the higher income segment, but this difference quickly evaporated after the unemployment stimulus enhancements expired, requiring consumers to increasingly use savings (which declined from 34% to 14%) to maintain overall consumer spending. Adding to concerns about the sustainability of using savings to fund expenditures and the aggregate pace of consumer spending, job growth decelerated meaningfully from nearly 5 million in June to 1.5-1.8M in July/August and 660,000 in September. Employers, particularly in service-oriented industries such as leisure/hospitality and the small to medium-sized segment, continued to struggle with the gradual economic re-opening, the financial strife it has created, and pandemic-induced permanent changes to their business models and resources. Lastly, resurgent COVID-19 cases in some regions of the country, and especially throughout Europe, provided a renewed threat that lockdowns could re-materialize and further challenge the near-term economic recovery.

Corporate Earnings: Surprise!

Typically, fundamental investors use corporate earnings as a foundational tenet of their investment process. Earnings growth has become increasingly scarce (helping support growth's outperformance versus value), with the S&P 500 not reporting aggregate EPS increases of any note since the fourth quarter of 2018 and more than 50% fewer benchmark constituents reporting mid-teens revenue gains compared to a decade ago. Second quarter results reported throughout the last several months have shown an escalation in the prevalence and magnitude of positive surprise, as 84% of S&P 500 companies exceeded consensus (greater than 72% five year average) and surpassed estimates by an astounding 23% (far superior to the 5% five year mean). Consumer Discretionary and Industrial stocks experienced the most pronounced upside to consensus expectations, validating CCI's increased exposure to these sectors based on stronger fundamental trends and improved economic tailwinds. This overall robust positive surprise helped mark a trough in estimate revisions which had declined precipitously since March, as 60% of companies now have upward forecasts compared to only 10% several months ago. Importantly, our long-term monitoring (which compares the 10 day average of earnings revisions for portfolio holdings to all domestic companies, using independent Factset data) shows a consistently greater proportion of CCI holdings experience positive earnings revisions compared to the broader universe. Investment style leadership frequently tracks EPS progression off trough levels, as confidence in an earnings path towards year-over-year increases (forecasted for first quarter of 2021) is often accompanied by value stock outperformance. Thus far, investors have not fully followed this playbook due to greater uncertainty in several elements of the recovery.

Outlook: Crossroads Puzzle

Equity markets are at the crossroads of several challenges, and investors require master puzzler skills to navigate the heightened uncertainty and synthesize a mosaic of disparate pieces. These risks include the pace of economic recovery, given the resurgence of COVID-19 cases, diminished fiscal stimulus benefits, unproductive negotiations to extend assistance, and increases in those permanently unemployed due to secular pandemic disruption. The upcoming Presidential election and ensuing policy changes of significance (e.g., tax rates, infrastructure, healthcare), along with ongoing trade tensions and uncertain timing regarding the broad availability of COVID-19 vaccines provide further investor angst. As visibility improves, market leadership should continue to oscillate between sectors and across investment styles, but stocks will likely remain volatile until investors develop increased confidence in the sustained impact of these pressures and more persistent trends emerge. Longer-term, investors will have to grapple with issues such as technology and healthcare disruption, inflationary effects of the Federal Reserve's new flexible targeting and record levels of fiscal/monetary stimulus, changes to the Supreme Court composition, and resolutions to social injustice. For CCI, our focus remains on holding companies best positioned to traverse these various obstacles and generate consistent fundamental growth above consensus expectations, consistent with our ***Positive Momentum & Positive Surprise*** investment discipline.

[1] Jefferies, "Q3 Performance Scorecard," October 1, 2020, page 2.
[2] Bank of America, "Global Investment Strategy," September 28, 2020, pages 6-7.