BLUE GRANITE CAPITAL, LLC

INVESTMENT COMMENTARY, OCTOBER 2020

To our clients, friends and their families, we hope this finds you healthy and safe and that you enjoyed a relaxing summer season.

After a swift rise to new highs, equities fell 3.80% in September, registering one of the market's weakest monthly performances in the past decade. We had anticipated a pullback of some magnitude given the market's rise was primarily driven by a handful of technology and social media companies that had rallied more than 50% from the Covid-related shutdown's March low. This tech-inspired rally persisted through most of the third quarter and represented the lion's share of the S&P 500 Index return, during which time the S&P's 'other' 450 stocks were largely ignored by investors. A rally of this extent, by such a narrow group of index members, is generally not viewed as a reliable long-term indicator of a robust market, especially in the midst of a struggling economy. The rather extraordinary focus on technology added risk to the market in the context of broader suppressed economic growth.

In our view, the post-pandemic stock market rally produced an overabundance of investor confidence, as the investing public largely ignored economic realities resulting from the mandated shutdown. We have maintained that, despite increased confidence, the rally would be difficult to sustain in the current economic environment. The path to economic recovery remains challenged until 12 million unemployed Americans can get back to work. Since consumer spending comprises 70% of economic (GDP) growth, and with millions still out of work, we cannot expect a return to normalcy for some time. Many of the unemployed have few options as their respective employers may have either closed their businesses or are operating at a fraction of previous capacity. The new "work and shop from anywhere" paradigm has created compelling opportunities for some businesses and new technologies (and their stocks) while, conversely, other sectors may be permanently impaired. Adjusting to these changes will take time both from an economic and investment standpoint.

To this end, current stimulus proposals are clearly politically contentious and indeed Congress may lack the conviction necessary to pass any measure, at the expense of delaying an economic recovery. At best, the stimulus is an imperative stopgap measure to help many Americans survive, though it will ultimately do little to resolve the paramount goal of meaningfully reducing unemployment. Despite trillions of dollars in government assistance, and the possibility of another round, only a portion of the recovery may come to fruition given the multitude of businesses that remain closed or are running at a fraction of capacity. Also worrisome is the massive level of government debt which will remain a huge burden that must someday be repaid. Without a stimulus package, consumer demand may slow considerably and cause the economy to stall in the fourth quarter. Should this occur, the Fed must then consider more aggressive policy to catalyze economic growth and boost business. While it's likely that Fed and government policy tools will be further deployed to support the economy, our expectations for stimulus are low until the election.

With technology stocks leading the S&P 500 to a 10% mid-month correction, a key consideration is which other sectors will lead to a broad-based rally and provide a more robust framework for further stock market appreciation. Apple, Amazon, Facebook, Google and Microsoft are great technology companies that by many measures now appear overvalued and point to the likelihood for a rotation in stock market leadership into other sectors. As such, we are currently more positive on stocks in leading companies within sectors whose performance has more recently lagged and are attractively priced for upside performance.

As always, and surely in uncertain times, Blue Granite remains focused on its essential tenets: capital preservation while conservatively growing your portfolio and generating dividend income. With cash on hand, we are navigating buying opportunities in those stocks with more compelling valuations. We are also intensely focused on risk mitigation, and we anticipate continued volatility as investors digest economic and Covid-related matters that are likely to remain the main drivers of stock market direction for the foreseeable future.

While the news and events surrounding the presidential election are captivating, there also may be near term and protracted risks for both the markets and the economy. Which candidate is better qualified to lead and fix the economy, improve healthcare, bring a Covid vaccine to the market, appoint a Supreme Court Justice, negotiate trade deals with China and bring our divided country together will be decided by the voters. However, the totality of these issues will impact investor sentiment through the election and implies a likelihood of significant market swings. That is, of course, until there is an eventual shift in market focus to the next 'big thing'.

While we believe that our conservative approach is of utmost importance during disruptive periods such as these, we also know that over time we can expect renewed stability and confidence in our economy, and growth in the companies that comprise your portfolio. In the meantime, we are always here for you, so please don't hesitate to let us know if you have any questions or issues that you would like to discuss.

Best regards,

Scott, John, Dave & Richard