Level Four Capital Management

WEEKLY INSIGHT

HIGHLIGHTS

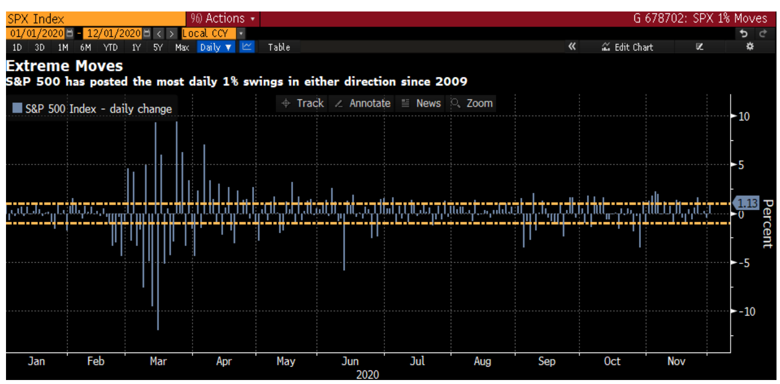
- Equities finished higher to close out the week, led by the Tech-heavy NASDAQ which gained 2.17% on the week, followed by the Russell, S&P 500, and Dow Jones.
- Energy was the best performing sector on the week, overcoming OPEC + decision to begin tapering production cuts in January. The sector posted positive gains for a fifth straight week and rallied a record 28% in November.
- Consumer Discretionary lagged broader index strength with weakness in homebuilders after pending home sales came in lower than expected.
- Non-farm payrolls came in lighter than anticipated, posting an increase of 245K jobs for November. The headline number was the slowest pace seen during the economic recovery.
- The S&P 500 has posted 109 (47%) daily 1% swings in either direction this year, the most since 2009.
- Hiring slowed the most within sectors who are most susceptible to rising COVID-19 cases, including leisure, retail and the hospitality sectors.
- A group of bipartisan senators released a proposed $908B aid package which was generally well received by members of both the Democrat and Republican parties. The deal did not include another round of $1,200 direct payments to Americans.
- Valuations may be over-extended in the near term with multiple firms highlighting why including Deutsche Bank, Bank of America, and Bloomberg.
- Shoppers flocked to Cyber Monday deals, racking up a record $10.8 billion in U.S. sales, or a 15% increase over last year, according to Adobe Analytics.
- Chinese Foreign Minister Wang Yi said that China remains committed to a Phase 1 trade deal with the United States despite a record monthly trade surplus of $37.5 billion with the United State in November. The Shanghai Composite Index was up 1.06% last week.

MARKET COMMENTARY

LAST WEEK

Equities finished higher to close out the week, led by the Tech-heavy NASDAQ which gained 2.17% on the week, followed by the Russell, S&P 500, and Dow Jones. Value outperformed growth slightly, however both posted healthy gains of over 1.50%. It continued to be a volatile week, and one of the most volatile on record amid the ongoing pandemic, economic uncertainty, and U.S. Presidential Election. The S&P 500 posted its 109th session on Tuesday in which it experienced a 1% move in either direction, the highest absolute figure since 2009 when there were 118 sessions which crossed the 1% threshold.

Source: Bloomberg as of 12.08.2020



Themes remained largely unchanged from previous weeks with a number of push/pull factors still in place which included:

- Vaccine optimism that remains elevated
- Unexpected positive developments regarding a fifth stimulus package
- COVID-19 trends which continued to worsen
- Overextended valuations in the near term

SECTOR PERFORMANCE

Energy was the best performing sector again and posted gains of 4.5% on the week with crude ending higher for a fifth straight week. The continued move higher came after a record ~28% gain in November, and overcame the decision by OPEC+ to begin tapering production cuts in January.

Healthcare was the second best performing sector and outperformed with strength in vaccine candidate-related names. Hospitals, Biotech, and select insurers were also pockets of strength throughout the week.

Technology provided leadership after Semiconductor and Hardware-related names were among the standout performers, including Western Digital Corp +12.9%, Qualcom +9.6%, Apple +4.9%, and NetApp +12.6%.

Financials outperformed slightly with strength in banks as rates climbed near their higher levels since March. The 10-year on Friday closed at 0.965%.

VACCINE OPTIMISM

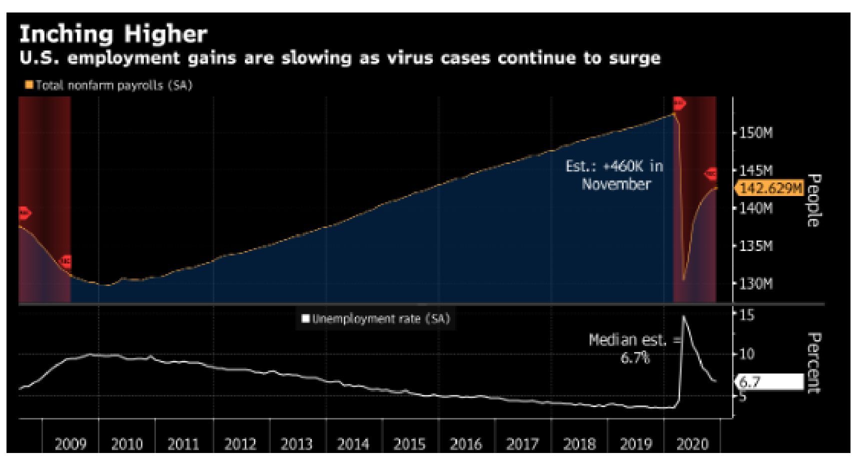
One of the primary tailwinds behind market price action continued to be COVID-19 vaccine optimism, although there was nothing incremental to note. Despite Pfizer slashing 2020 production targets for their vaccine candidate by 50% last Thursday due to previously announced supply chain disruptions, the company said that they remain on target for 2021 deliveries. Most recently, a new poll from the Pew Research Center showed that 60% of Americans respondents now say they would definitely or probably get a vaccine, compared to the 51% from September's results.

HIGH FREQUENCY DATA

Economists, analysts, and companies continue to note a slowdown in high-frequency data as states continue their rollback and re-opening plans. Visa was the most recent credit card company to note a slowdown in November payment volumes, while Delta also highlighted that they have seen the slowing of bookings as cases throughout the U.S. spike.

Additionally, with the holidays right around the corner and the virus surging, spending could slow into the mid-to-later part of December as some holiday shopping may have been pulled forward due to lesser overall travel and scaled back holiday plans. This year consumers spent a record $10.8B on Cyber Monday, an increase of 15.1% a year ago, however falling short of Adobe Analytics' forecasted $12.7B.

In addition, although the labor market has been a relative bright spot throughout the economic recovery, nonfarm payrolls missed expectations on Friday, posting an increase of 245K jobs. The headline number was the slowest pace seen during the economic recovery as hiring slowed significantly in industries who are most susceptible to rising Coronavirus cases, including leisure, retail, and the hospitality sectors.



Source: Bloomberg as of 12.08.2020

STIMULUS HOPES

Renewed hopes for a fifth Coronavirus relief bill also helped buoy the risk-on tone seen throughout the week. In an unexpected turn of events, a group of bipartisan senators released a proposal for a $908B aid package which included:

- $300B in PPP funding
- $180B for unemployed Americans ($300/week for four months)
- $160B for state and local governments
- $80B for schools, $10B for USPS

In the surprise move, Democratic leadership supported the package despite originally holding out for a $2T+ stimulus deal prior to the November election. Helping add to the optimism was Senate Majority Leader Mitch McConnell who said things are starting to move in the right direction and that a compromise was within reach, although stopped short of endorsing the plan.

EQUITY RALLY OVER-EXTENDED?

In recent weeks, discussions surrounding the equity rally and how it may be overheated have come back into focus. This is partially due to the incredible run seen in November as the Dow posted its largest gain since 1987, while the S&P had its best November since 1928, and the Russell 2K gained the most on record, posting an 18.29% return for the month.

While it appears the largest fundamental risk to U.S. equities is related to a vaccine and the subsequent ability to distribute it, there have also been focus on the valuations in the near term. With the S&P 500 trading at 23x forward earnings, slightly below the June peak of 25x, and 71 companies across the U.S. whose valuations now exceed $100B (the most number of companies ever with the next closest being 65), multiple notable firms have come out highlighting the potentially overextended levels seen including:

Deutsche Bank who said the S&P 500 CAPE ratio is now at its second highest level ever, only behind the 2000 dotcom bubble.

Bank of America highlighted that their Bull/Bear indication has accelerated toward extremely bullish levels.

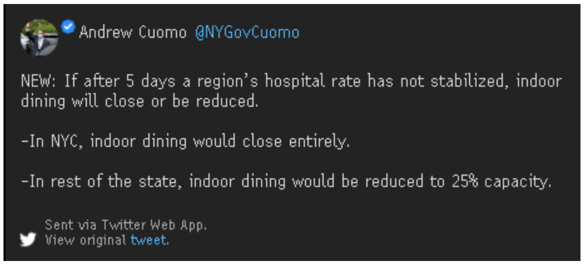
Bloomberg pointing out numerous potential warning signs, including a 20-year low in the put/call ratios five-day moving average, a seven-year high for companies trading above their 200-day moving averages (93%) and the recent inflows seen into equities which stands at $115B in just the last four weeks alone.

Source: Bloomberg as of 12.08.2020

THIS WEEK

U.S. domestic stocks fell to start the week as Coronavirus infections surged across the U.S., triggering investor fears of additional restrictions. The S&P 500 fell 0.19%, from an all-time high, led by Energy, Real Estate, Materials, and Financials. After more than a month of outperformance, Energy-related names finally succumbed to pressure, declining 2.44% while Crude declined 1.3%. The reversal was a noticeable one after the Energy sector gained over 30% since the start of November, while broader index gains stood at 11%.

Eight of the 11 sectors finished lower on the session, however Communication Services, Utilities, and Technology were the standout performers, catching a safety bid and closed higher. Growth outperformed value, with stay-at-home names buoying the broader momentum/ growth trade.


Andrew Cuomo @NYGovCuomo

NEW: If after 5 days a region's hospital rate has not stabilized, indoor dining will close or be reduced.

-In NYC, indoor dining would close entirely.

-In rest of the state, indoor dining would be reduced to 25% capacity.

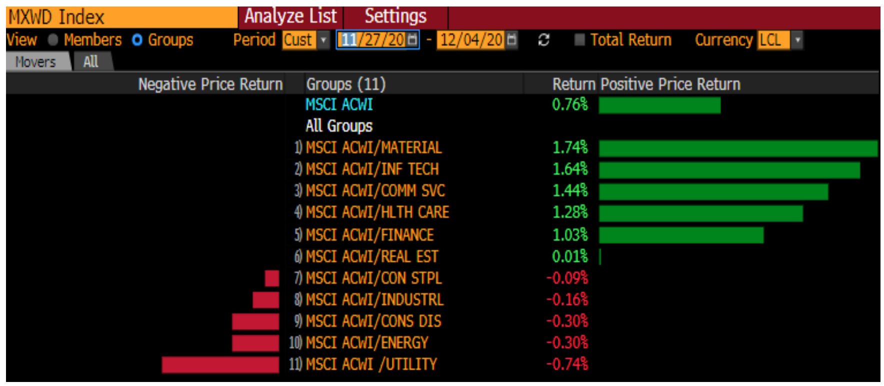
Sent via Twitter Web App.
View original tweet.

Source: Twitter as of 12.08.2020

It was a quiet Monday session with U.S. benchmarks trading in negative territory for most of the session. Indexes took a leg lower in the morning after New York Governor Andrew Cuomo announced that indoor dining would be closed if the regional hospitalization rate has not stabilized after five days. Additionally, adding to downside pressure was Dr. Anthony Fauci commenting and warning that the middle of January could "really get bad".

THIS WEEK INTERNATIONAL

Last week, global equities gained 0.76%, led by materials and information technology. Energy was down 0.30% as holiday tourism is threatened by a surge in COVID-19 infections. Consumer discretionary traded lower, as government income assistance programs continue to face political challenges to get renewed in certain countries. The JP Morgan Global Composite PMI dropped from 53.3 in October to 53.1 in November due to restrictions imposed in Europe. United Kingdom Prime Minister Boris Johnson is heading to Brussels to attempt to close the Brexit trade deal this week. The world economy weighted year-on-year inflation ticked up to 2.4% from 2.3% a month ago.



Source: Bloomberg as of 12.08.2020

EUROPE

Several members of European Central Bank (ECB) Governing Council hinted that they will support a 12-month extension of the emergency bond program. The size of the program will be a topic of discussion during the next meeting, given that several members want to limit the program to 500 billion Euros, whereas other members target a higher number. ECB policy maker Martins Kazaks said, "we need to bear in mind that the pandemic program is an emergency instrument, and it shouldn't go on longer than needed." The Euro STOXX Index gained 0.18% last week, led by Travel and Leisure, up 5.87%.

In the United Kingdom, soccer fans received the green light to return to stadiums for the first time since March. Under the new protocol, up to 2,000 fans are allowed to attend games while respecting social distancing guidelines and the new health and safety rules. According to ESPN, "hugging, high-fives and back-slaps will not be allowed as the league hopes a smooth and safe return of spectators will allow them to successfully lobby the government to allow pilot events with larger crowds." The FTSE 100 index was up 2.87% last week.

Christmas ski season in the Alps will likely be cancelled after Germany, Italy, and France pressured Austria to join a continent-wide shutdown. The Alpine nation of Austria plans to keep its hotels and restaurants closed until January 7th and ask travelers from countries with high infection rates to quarantine. Switzerland plans to keep its resort open for Christmas with some restrictions. Bloomberg points out that "for many ski resorts, the Christmas and New year period accounts for about 30% of winter tourism revenue." The CAC 40 index ticked up 0.20% last week, while the DAX declined 0.28%.

APAC

Chinese Foreign Minister Wang Yi said that China remains committed to a Phase 1 trade deal with the United States. As of October, China's imports of U.S. goods stood at $75.5 billion, which is half the level required by the trade deal. The latest data from China General Administration of Customs shows that exports surged 21% year-on-year in November, while imports modestly grew 4.5%. During the same period, China's trade surplus with the United States reached a monthly record high of $37.5 billion. The Shanghai Composite Index was up 1.06% last week.

In Japan, the government announced a new round of stimulus that includes subsidies to the travel industry and the extension of unemployment payments through February 2021. The measure is part of the government's plan to restore the national economy to pre-COVID-19 levels by March 2022. The new stimulus package will be funded by the third extra budget expected to be voted by the parliament this week. The International Monetary Fund estimates that Japan's debt will rise to 266% of GDP by the end of 2020. The NIKKEI 225 was up 0.40% last week.

EMERGING MARKETS

Brazilian President Jair Bolsonaro said that his administration cannot extend the COVID-19 cash handouts to informal workers indefinitely. The benefit is set to expire at the end of the year. The comment came in the context of stalled negotiations regarding the new social program proposed by Bolsonaro which lacks a reliable funding source. The Brazilian real rallied on the news, as investors welcomed the prospect of fiscal austerity. The Brazil Ibovespa Index was up 2.87% last week.

In South Korea, more than a dozen of lawmakers are lobbying for a bill that will broaden the Bank of Korea's mandate to include employment stability. In the context of growing Central Banks' influence on the broad economy beyond inflation management, the proponents of the bill think that it is time for Korea's Central Bank to rise to the same level of responsibility. Bank of Korea Governor Lee Ju-Yeol said he would participate in the parliamentary discussions regarding the mandate of the Central Bank. He also expressed his concerns regarding policy decisions leading to conflicting outcomes. The KOSPI Index advanced 3.72% last week, led by materials, up 8.7%.

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