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Quarterly Review and Outlook

What's next? This question is undoubtedly being asked daily with both hope and trepidation by investors. There can be little doubt that the remarkable series and confluence of events during the first six months of this year have been disturbing and confusing to all. We have witnessed a seismic shift in global economic development from widespread activity and trade to a sudden shutdown of most economies as a result of the virulent and accelerating impact of a virus unforeseen by investors, government bodies, and the vast majority of scientific and medical experts. In the U.S., the securities markets have whipsawed from optimistic new levels in February to bear market lows in late March, followed by rather astonishing recoveries in April, May, and June.

The speed and magnitude of the market moves have been the presumptive results of the rapid deterioration in employment data and corporate cutbacks in output and inability to provide confident guidance for future sales and earnings. This was followed by unprecedented monetary and fiscal measures which had the effect of steadying the bond and credit markets, offering support for corporate activity and stimulating the prospects for recovery in employment.

So, which chapter of the most recent past will be the prologue for the future of our securities markets? We may be foolhardy to step into the deep and still murky waters; and our congenital optimism may also be challenged, but we will strive for honest objectivity.

Starting with the fixed income sector, we believe that our Federal Reserve has essentially guaranteed substantial support for this very important segment and for a reasonably long period, interest rates will likely be stable and market returns will be rather uninteresting as to capital appreciation potential. For those accounts with an established position in government issues, we would stay with these because of their security and probable relative stability over the next two years. If increased current income is a requirement, we continue to suggest higher dividend paying stocks which have strong balance sheets distinguished by sound current cash flow and sensible and demonstrated policies for dividend increases. In many cases, there are examples of top quality corporations offering dividend returns of two to three times that of current coupons on government securities or tax exempt issues of high tax issuers which have already been bid up to unattractive levels.

Most of us know the old stock market adage that equities are always forward-looking and, while occasionally can get caught up in the fervor or the moment, in aggregate will almost always reflect the future salient, lasting, and correct fundamental outcomes. Well, who are we to argue with history? Nevertheless, it is necessary to attempt to list, investigate, and challenge the often-conflicting premises in the effort of gaining some important support and traction for our investment positioning.

To many investors and other interested observers, the current levels of many stocks and sectors are so out of touch with current and possible future trends and outcomes as to border on the ridiculous or possibly dangerous. It is a given that no one can likely compile a list of worries that contains every worry, and we will not attempt the task. In the arena that we live and compete in, we promise to turn up the focus on the items that we judge to be most critical, while not ignoring those that can sneak up or suddenly gain criticality.

To our minds, the most critical issues which could impact investor sentiment relate directly to the corona virus, U.S./China relations, the sustainability of the domestic economic rebound, and the possible lingering effects of the rising and seeming expansion of the social unrest on the economy and its potential political fallout.

At this moment, the status of the virus is mixed. While data gathering sources are open to interpretation, it seems that while the overall flattening of the patient curves has been noted, the rise of identified cases has occurred in several stateside locations. It is not clear as to whether the increases are primarily due to improved testing protocols and availability or are the tip of a second wave domestically caused by a relaxed attitude toward preventative measures. Equally unsettling has been the rebound in cases in international areas which earlier had been thought to be safe and cleared for reopening. Our stance is to continue to watch the data carefully until we have higher probabilities of increased comprehensive testing, confirmed evidence of effective interim treatments, and clear horizons for any vaccines, which are showing positive turns.

The arenas of geopolitics are well established as caverns of despair and broken promises! The complicated relationship with Chinese leadership has floundered several times in the past three years as the result of national and personal objectives and egos, not to mention other international considerations and disruptors. As we have stated in earlier letters, there is a growing recognition of China's policies and actions to utilize regulatory requirements to gain access to technologies of many Western companies. These actions have resulted in contentious counter- measures by all parties, but not in severing of national relations. Trade is both a hammer and fig leaf in negotiations between the American and Chinese governments and is deeply imbedded in the supply chains of many goods and services important to both. Permanent changes in this complex area will be difficult, if not impossible without serious financial implications. At this moment, we view the China efforts as mixed with a negative tone.

The domestic economic picture is considered to be a likely and sustainable positive force for investors. The initial economic data as states and businesses reopen have been encouraging. Positive results on most recent reports concerning manufacturing, employment, retail sales, and housing seem to be broad enough to qualify as "green shoots" with sufficient breadth and depth to support further recovery on an expanding basis. If so, we would expect to see a recovery in capital spending and industrial trade which are critical elements in longer term economic health. Certainly, any localized lockdowns could cause temporary concerns, but we judge broad scale dislocations to be unlikely.

As a further support for renewed and sustained economic progress, we expect the Fed, the administration, and Congress to continue to provide broad scale support for businesses, employment, and potentially important infrastructure projects. The negative effects of the pandemic and shutdowns were rapid, and the recovery from same will be slower, but longer lasting and more meaningful for investors.

The most difficult issue facing our country now is the distressing divisiveness of our citizenry and its manifestation in the seeming lack of interest in finding common grounds for avoiding heightened and more intense social unrest. This document is not a venue for arguing the pros and cons of any constituency, nor would it be correct or realistic to avoid the dilemma which honorable individuals and groups are facing. Suffice it to note that this highly charged situation, with its many underlying currents, has the potential to be another cause for economic, social, and political uncertainty.

At this juncture, the equity markets are consolidating the recent sharp gains from the March lows. During the past three to four months, we have dedicated our combined efforts to gauging the financial health of our holdings in client portfolios. It would be accurate to state that our commitment to strongly capitalized companies with established business franchises and a record of well-planned successful new endeavors has stood us in good stead for our clients. We are not short-term traders and are always sensitive to specific client objectives, while keeping a keen eye for new opportunities with definable growth potential. We pledge to remain alert to significant risks as well as potential long-term opportunities in such broad areas as industrial and applied technologies and scientific and medical breakthroughs. We welcome frequent conversations and updated reviews with our clients, and we encourage you to stay in "touch" during these volatile times.