StoneRidge
INVESTMENT PARTNERS LLC
A BELTRAITH COMPANY

Commentary Second Quarter 2020

This commentary highlights the 2nd quarter 2020 Performance Summary, Market Outlook, and Economic Commentary for the ***High Quality Large Cap strategy***. The strategy performed in line with its S&P 500 benchmark with a return of 20.50% versus the benchmark return of 20.54%.

The economy was impacted by negative headwinds in the form of the Covid-19 pandemic and its deleterious effect on all aspects of the global economy. While we continue to be in the grips of the pandemic with some line of sight on mitigation or vaccine readiness, we expect to see a continued gradual tentative reopening of the US economy on a state by state basis from its shutdown with the occasional regression in hot spots. But we do not expect a nationwide shutdown as had been experienced in the early days of the pandemic.

While the market so far has rebounded from its lows, we continue to be cautious as we expect volatility and frothiness to persist until there is abundantly clear evidence of a turnaround from a health perspective.

As such while we are confident in our balanced investment process where we emphasize quality in our stock picking, as characterized by firms with pristine balance sheets, strong free cash flows, peer leading liquidity and strong margin profiles to be able to absorb any further market shocks while weathering the current economic conditions.

2nd Quarter Equity Attribution

At the **Sector** level, the Consumer Discretionary, Energy, Communication Services, Financials, Information Technology, Utilities, and Industrials sectors positively contributed to relative returns while stock selection in the remaining sectors had a negative impact on the portfolio during the period.

At the **Stock** level**, ViacomCBS,** a Communication Services company contributed positively to results during the quarter driven by an earnings report offering several bullish data points.

Best Buy, a Consumer Discretionary Company, also contributed positively to performance during the period driven by positive earnings growth and guidance and a positive outlook on revenue generation from products selling better than expectations both online and in stores.

Apache, an Energy company contributed to outperformance due to positive earnings outlook, and a large oil discovery in offshore Suriname. The company continues to enjoy resource rich acreage around the world and is set to shift towards positive free cash flow as oil commodity prices continue to rebound.

On the negative side**, Biogen**, a Healthcare company, detracted the most from performance driven primarily by a weaker than expected earnings report and lost patent ruling.

Walgreen Boots Alliance, another Healthcare company, hurt portfolio performance due to weaker than expected earnings report, reduced guidance, and slowing prescription sales.

Exelon, a Utilities company, detracted from performance because of reduced earnings guidance as well as concerns over a federal investigation into EXC's lobbying practices in Illinois.

Top 5 Stocks by Absolute Return Contribution to Fund Performance

Security	Portfolio Weight	Contribution to Return
ViacomCBS	0.94%	0.48%
Best Buy	0.99%	0.44%
Apache	0.12%	0.28%
Whirlpool	0.94%	0.25%
DuPont	0.81%	0.21%

Bottom 5 Stocks by Absolute Return Contribution to Fund Performance

Security	Portfolio Weight	Contribution to Return
Biogen	1.33%	-0.49%
Walgreens Boots Alliance	1.05%	-0.46%
Exelon	2.21%	-0.42%
Digital Realty Trust	2.30%	-0.41%
Amazon	2.22%	-0.38%

Numbers in the News

Indicator	6/30 Value	Versus 3/31
3-month T-bill	0.13%	+7bps
2-yr. T-note yield	0.15%	-10bps
10-yr. T-note yield	0.67%	-1bps
Yield Curve (2-10yr)	+51bps	+9bps
ICE BofAML High Yield (YTW)	8.45%	+304bps
S&P 500	3100.3	+20.0%
Dow Jones Index	25,812.9	+17.8%
Retail Sales (May vs Feb)	$485.5	-28.1%AR
ISM Manufacturing	52.6	+3.5
Payroll Employment (000)	137,802	-13,288
CPI last 12 months (May vs Feb)	+0.1%	-2.2pp
Core CPI last 12 months (May vs Feb)	+1.2%	-1.2pp
Personal Consumption Deflator (PCD) last 12 mo. (May vs Feb)	+0.5%	-1.3pp
Core PCD Last 12 mo. (May vs Feb)	+1.0%	-0.8pp

Bloomberg Barclays Bond Index Returns

	Second Quarter	12 Months
Aggregate	+2.90%	+8.74%
Government/Credit	+3.71%	+10.02%
Intermediate G/C	+2.81%	+7.12%
Intermediate A+ G/C	+1.58%	+7.20%
1-3 Year Govt	+0.26%	+4.12%
Municipal Bond	+2.72%	+4.45%

bps = basis points (0.01%)
pp = percentage points
AR = annual rate
NC = no change

Data obtained from various market and government sources by Stoneridge PMG Advisors, LLC. For additional information, please contact our office.

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Market Outlook & Trends

The longest running expansion cycle in history that began in 2009, abruptly came to an end in February 2020 as the COVID19 shock forced the U.S. economy to shrink at a 5.0% annualized rate in the first quarter of 2020. In the second quarter, a strong jolt from the full impact of the shock caused the steepest quarterly decline in economic activity since the Great Depression. Incoming data during the quarter, revealed the virulent dynamics of the COVID-19 crisis – its horrific death toll and its disruptive impact.

Consumption Collapse and Rebound ❖

Measures adopted to slow the spread of COVID-19 caused a collapse in consumption during March and April. The worst impact was realized during the month of April. Retail sales fell 14.7% – the biggest monthly decline since this data series began in 1992. Sales at restaurants and leisure spending declined more than 30% as people stayed home. Discretionary spending on items such as clothing fell by 75.2%, and several major retailers filed for bankruptcy. Unit sales of automobile plunged almost 50% in April. But, thanks to swift and massive fiscal stimulus, there was a stronger than expected rebound in May. Still, analysts estimate that personal consumption likely contracted at an annualized rate of at least 30% in the second quarter.

Plunge in Manufacturing ❖

The sharp contraction was not limited to retail sales and the services sector. Industrial production declined 12.5% in April following a 4.6% decline in March as U.S. manufacturers shutdown their production lines. The plunge in monthly manufacturing output in April was steeper than at any point in the last century. Manufacturing activity continued to remain depressed in May. But there were encouraging signs of a revival in June as factories gradually started reopening.

Staggering Job Losses ❖

The precursor to the collapse in consumption and manufacturing was the disruptive shutdown of nonessential businesses, which triggered widespread furloughs and job losses. A cumulative total of over 40.7 million people filed for unemployment insurance benefits in the first ten weeks following the shutdown. During the initial weeks, the sudden flood of unemployment filings overwhelmed the system for handling the claims in many states. The official nonfarm payroll fell by 20.8 million in April and unemployment rate rose to 14.7%. About 7.5 million jobs were cumulatively added back during May and June as furloughed employees were recalled upon the reopening of the economy. Nevertheless, the job losses from the shock are ongoing and the unemployment rate remains in the double digits.

Swift Policy Response ❖
As the COVID-19 crisis vividly unfolded during March and April, both monetary and fiscal policy makers sprang into action to provide relief for beleaguered businesses and workers. New fiscal spending on pandemic aid, including payroll protection and unemployment benefits, has approached $3 trillion. Notably, there was coordinated policy response to the crisis from Congress, the Administration, and the Federal Reserve. As part of the COVID-19 relief package, known as the CARES Act, Congress appropriated $454 billion to be utilized by the Treasury as a backstop for absorbing potential losses in programs to support the flow of credit to businesses. The Fed, in coordination with the Treasury, has utilized this earmark to create new facilities supporting the markets for corporate bonds and loans. The announcement of these initiatives more than helped stabilize the financial markets.

Flood of Liquidity ❖
In responding to the COVID-19 crisis, the Fed pumped massive liquidity into the financial system. The Fed's balance sheet expanded in size as well as scope, at a pace that dwarfed the quantitative easing actions undertaken during the financial crisis of 2008. The flood of liquidity swept through the markets for not only Treasuries and mortgage-backed securities but also a wide range of risk assets including commercial paper, municipal securities, and other credit securities. Apparently, this helped disconnect risk asset prices from the economic data reflecting the damage inflicted by the pandemic. In the second quarter, the S&P 500 Index climbed steadily, shrugging off the dire economic data, and retraced most of its first quarter losses. Firms with access to financial markets easily raised capital to shore up liquidity at low cost, as investors snapped up record issuance of investment-grade corporate bonds. Concurrently, there was record issuance of new debt by the U.S. Treasury, most of which was purchased by the Fed.

Near term Outlook ❖
During the second quarter, U.S. GDP likely contracted at an annualized rate of more than 30%. If so, it will have been the steepest quarterly contraction in history. A snap-back recovery may have begun as businesses reopened in May, leading to forecasts of double-digit annualized growth rate in the third quarter. However, this view is subject to headwinds from a resurgence of virus infections. By the end of 2020, the overall level of output is expected to be lower than in 2019. The prospect for sustained recovery remains uncertain under the cloud of COVID-19. But there is no uncertainty about the trajectory of the U.S. sovereign debt. The debt-to-GDP ratio is on track to rise rapidly and exceed the historic record levels seen during World War II.

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Current Portfolio Positioning

Currently, our strategy is most over-weighted in the Information Technology sector. We expect continued 5G rollout opportunities, and the accelerated shift towards cloud application software due to the Covid-19 pandemic to benefit firms in this sector. We are also overweight in the Consumer Staples, Financials, Real Estate, Materials and Utilities sectors.

Our strategy is currently underweighted in the Industrials, Healthcare, Consumer Discretionary, Communication Services, and Energy sectors. A continued lack of clarity on occupational safety due to the pandemic and its effect on the labor force as well as its effects on demand for goods and equipment keeps us underweighted in the industrials sector.

On a stock selection basis, we are positioned towards firms with strong balance sheets, ample free cash flows, peer leading liquidity and durable margin profiles. In these uncertain times we believe these quality stocks will better absorb any further market turbulence while outperforming due to their market-leading positions. Also, we are poised to take advantage of any short-term dislocation in prices due to excessive market sentiments while being fully cognizant of the underlying global economic condition.

Please do not hesitate to contact us if you have any questions or wish to discuss the portfolio or markets in greater detail. We appreciate your continued confidence.

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