

# PALOUSE CAPITAL MANAGEMENT, INC.

## Quarterly Commentary for 3Q20

### October 2020

#### Top 1,000 - Market Cap Changes\*

10/20/2020 5:09	Five Day	Three Months	YTD	One Year
<b>Top 1,000</b>	0.3%	8.6%	10.9%	19.5%
<b>Largest 100 Equities</b>	0.4%	8.4%	16.0%	25.3%
<b>Largest 500 Equities</b>	0.3%	8.5%	12.5%	21.4%
<b>Smallest 500 Equities</b>	-0.2%	9.7%	-3.6%	3.3%
<b>Consumer Discretionary</b>	0.2%	15.9%	37.9%	42.6%
<b>Consumer Staples</b>	0.7%	7.9%	4.7%	9.0%
<b>Energy</b>	-1.7%	-19.1%	-49.0%	-45.2%
<b>Financials</b>	-0.7%	3.8%	-18.3%	-10.1%
<b>Health Care</b>	-0.4%	3.8%	11.8%	26.6%
<b>Industrials</b>	0.6%	13.8%	4.5%	10.7%
<b>Information Technology</b>	0.9%	13.8%	33.0%	47.6%
<b>Materials</b>	-0.2%	8.1%	5.3%	12.5%
<b>Communications Services</b>	1.0%	3.7%	13.1%	20.0%
<b>Utilities</b>	0.8%	7.8%	-0.3%	2.0%
<b>Real Estate</b>	-2.4%	3.8%	-5.9%	-6.5%

\*All calculations based on internal analysis of 1,000 domestic companies. Changes are based on the change in float adjusted market cap for companies that were in the model at the beginning and end of each period. The model does not use published index data and does not include the effect of dividends.

#### Market Recap

Equities were strong for the first two months of 3Q20, surging about 16%, continuing on a strong trend that began in late March. While stocks had a nightmare correction when Covid-19 surged, the recovery has been extremely impressive. September was a relatively weak month, but broad markets were still up about 9% in the quarter. While almost all sectors were up in 3Q20, the consumer discretionary sector was the big winner. Energy had an awful quarter, continuing a trend, even though crude prices were up slightly. Small caps trailed large caps in 3Q20, but they have shown interesting strength recently. Value stocks made a nice comeback against growth stocks in September, going against a long term trend.

Earnings growth was generally tepid, but improving, before the Covid-19 crisis. Earnings expectations dropped off a cliff when the crisis started, but time told that the sell side was too negative. Second quarter earnings season was better than expected, although much of that had to do with weak visibility and a lack of guidance. Third quarter earnings season is off to a decent start. While the economy is still in a recession, public company earnings expectations generally held ground; some industries, like hospitality and airlines, remain very weak and they will likely remain that way for a long time.

#### Other Data

10/20/2020 5:09	Last Data Point	One Week Change	Three Month Change	One Year Change
<b>Crude Oil (WTI)</b>	\$40.88	0.7%	6.2%	-24.2%
<b>Gold Spot</b>	\$1,899.29	-1.6%	4.9%	27.3%
<b>Fed Funds Upper Bound</b>	0.25%	0 bp	0 bp	-175 bp
<b>Fed Funds Lower Bound</b>	0.00%	0 bp	0 bp	-175 bp
<b>Two Year Treasury Rate</b>	0.14%	-1 bp	0 bp	-146 bp
<b>Ten Year Treasury Rate</b>	0.75%	-3 bp	12 bp	-101 bp
<b>Thirty Year Treasury Rate</b>	1.53%	-4 bp	20 bp	-71 bp
<b>Two to Ten Spread</b>	0.60%	-2 bp	12 bp	45 bp
<b>Dollar Index</b>	\$93.68	0.7%	-2.4%	-4.0%
<b>Jobless Claims - New</b>	898	6.3%	-36.8%	311.9%
<b>Jobless Claims - Continuing</b>	10,018	-10.4%	-40.9%	492.4%
<b>Vix</b>	27.41	9.6%	-1.9%	98.8%

Bryn Harman, CFA ♦ Palouse Capital Management, Inc. ♦ 509-220-4253 ♦ [bharman@palousecap.com](mailto:bharman@palousecap.com)

2026 N. Washington Street, Spokane, WA 99205

Source: Bloomberg. Past performance is not indicative of future results.

## PCM All Cap Market Model

10/20/2020 5:09	Price to Earnings Ratio*	Price to Book Value**	Upside to Target	# Stocks
<b>Top 1,000</b>	22.4x	3.6x	9.5%	1,000
<b>100 Largest Equities</b>	23.1x	4.8x	9.4%	100
<b>500 Largest Equities</b>	22.5x	3.9x	9.1%	500
<b>500 Smallest Equities</b>	21.1x	2.0x	11.9%	500
<b>Consumer Discretionary</b>	35.2x	9.0x	7.4%	124
<b>Consumer Staples</b>	18.6x	4.6x	6.3%	53
<b>Energy</b>	65.5x	0.8x	42.0%	25
<b>Financials</b>	11.0x	1.1x	14.6%	128
<b>Health Care</b>	18.8x	5.0x	12.5%	156
<b>Industrials</b>	28.4x	4.7x	5.6%	135
<b>Information Technology</b>	27.9x	9.1x	6.7%	186
<b>Materials</b>	19.8x	2.5x	7.5%	45
<b>Communications Services</b>	20.1x	2.9x	12.6%	42
<b>Utilities</b>	18.9x	2.0x	4.9%	39
<b>Real Estate</b>	49.7x	2.8x	11.0%	65

All calculations based on internal analysis of 1,000 domestic companies. The model does not use published index data.

\* Calculated by comparing market capitalization to estimated earnings one year out.

\*\* Calculated by comparing market capitalization to last reported shareholder's equity.

## Market Model and Outlook

Our simple market model - which is based only on average sell side target prices - now suggests that there is a 7.7% one year upside potential to the all cap market, an improvement over last quarter but on the low side of the historic range. We are calculating the market's forward P/E ratio at 22.7x, a high number but in line with the recent range. Higher multiples are supported when interest rates are very low, as they now are, at least in theory. We therefore do not think that high multiples portend a coming correction.

That said, the primary issue right now is the upcoming election. The Democrat plan calls for higher taxes on corporations, investors and wealthy people, which would probably not be good for equity markets. Increasing taxes when the economy is so fragile is also something that could prolong the recovery for a long time. The next few weeks will be very important, but a change in government is

largely baked into market valuations; we therefore maintain that a serious correction is unlikely in the near term.

## Weekly Report, Conference Call and Podcast

Our clients are invited to receive our CIO's weekly podcast and weekly report. In addition, all clients are invited to participate in our weekly conference call. We provide these services to our clients free of charge and they are not available to non-clients. In the weekly report and the audio programs, Ken Roberts and Bryn Harman discuss market developments and trends that we observe in our week to week research efforts. Please contact Bryn Harman at [bharman@palousecap.com](mailto:bharman@palousecap.com) for more information.

### Important Disclosures:

Palouse Capital Management, Inc. ("PCM") is an SEC registered investment adviser located in Spokane, WA. Registered investment adviser does not imply a certain level of skill or training. PCM may only transact business in those states in which it is registered or has completed the appropriate notice-filing requirements. Prospective clients should consult with a financial consultant to review their investment objectives and financial situation before determining whether any investment, security, or strategy is suitable. A copy of PCM's Form ADV Part 2A & 2B providing information regarding PCM's services, fees, and other important disclosure items is available on PCM's website - please contact Bryn Harman at 509-220-4253 to obtain copies of these documents. Any opinions expressed in any PCM-authored documents are subject to change without notice and, due to the

rapidly changing nature of the security markets, may quickly become outdated. No information should be interpreted to state or imply that past results are an indication of future performance. All materials presented are compiled from sources believed to be reliable and current, but accuracy cannot be guaranteed. No portion of this document should be interpreted as legal, accounting or tax advice.

All analysis in this report was provided by Bryn Harman, CFA, PCM's Chief Executive Officer and Chief Investment Officer. Mr. Harman can be reached directly at 509- 220-4253 or [bharman@palousecap.com](mailto:bharman@palousecap.com).

If readers have any questions about anything mentioned in this report please feel free to contact us any time at 800-624-3833. Readers can also refer to our website, [www.palousecap.com](http://www.palousecap.com), for more information and can email PCM's Chief Investment Officer directly at [bharman@palousecap.com](mailto:bharman@palousecap.com) with any questions. Readers should not assume that any investments in the securities mentioned in this program were or will be profitable or will continue to be held in the future. Pursuant to Rule 206(4)-1(a)(2)(A) we will provide a list of all trades made on behalf of clients in the past year upon request.

All data used to create this report was provided by Bloomberg L.P. unless otherwise indicated.

The PCM market model examines the universe of the 1,000 largest actively traded equities trading in the United States (referred to as the "Top 1,000"). The "Price to Earnings Ratio" is calculated by comparing the total capitalization for each market cap range and each sector to the total estimated net income (from sell side estimates) for the respective market capitalization range or sector. The "Price to Book Value Ratio" is calculated by comparing the total capitalization for each market cap range and each sector to the total last reported shareholder's equity for the respective market capitalization range or sector. "Upside to Target" is calculated using float adjusted market capitalization weightings and the one year upside potential to the average sell side target price for each security.

"Market cap" means market capitalization.

"LCV" refers to PCM's Large Cap Value Strategy.

"TR" means our Large Cap Total Return Strategy.

"SMID" means Small to Mid Capitalization and also refers to our Small/Mid Cap Value Strategy in certain contexts.

"ACT" means our All Cap Tilt Strategy.

"DI" means our Diversified Income Strategy.

"SPX" refers to the Standard & Poors® 500 Index ("S&P® 500"). The Standard and Poor's 500 Index is a free-float capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic equity market. The S&P 500 equal weighted index is the equal weighted version of the SPX. The S&P® High Dividend Yield Index measures the performance of 80 high dividend yield equities within the SPX. The S&P SmallCap 600® index is a capitalization weighted index that measures the performance of 600 small capitalization stocks.

The Russell 3000® Index is a float-adjusted, market capitalization weighted index comprised of equities of the 3000 largest domestic companies. The Russell 2500® index is a subset of the Russell 3000 index comprised of the 2500 smallest cap equities in the Russell 3000 and represents the SMID segment of the domestic equity market. The Russell® 2000 Index is a subset of the Russell 3000 index comprised of the 2000 smallest cap equities in the Russell 3000 index and represents the small cap segment of the domestic equity market.

#### **About Mr. Harman:**

Bryn Harman, CFA is the Chief Investment Officer and Chief Executive Officer of PCM. Mr. Harman holds a Bachelor of Commerce degree (Finance and Economics) from the University of Saskatchewan (1992) and he earned the Chartered Financial Analyst designation in 1997. Bryn began his career with a financial planning firm in 1994. Since then, Bryn has worked in several investment and corporate finance roles in Western Canada and the Pacific Northwest. Bryn is the former Director of Research for an investment management firm that had over \$2 billion in assets under management at the time. Mr. Harman has been a portfolio manager with PCM since 2011 and he has held the position of Chief Investment Officer since 2013. Mr. Harman is a 50% owner of Palouse Capital Management.