FUNDAMENTAL EQUITY

LARGE CAP VALUE

GREAT LAKES ADVISORS

A WINTRUST WEALTH MANAGEMENT COMPANY

MANAGER COMMENTARY

Third Quarter 2020

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MARKET REVIEW

U.S. equities ended 3Q20 with increased volatility and a modest decline but a positive return for the period. The massive fiscal actions are winding down and relaxation of some COVID-19 restrictions are not consistent in all areas. The Russell 1000 Value Index advanced 5.59% in the third quarter of 2020. The broader market, represented by the S&P 500, also gained 8.93%.

Russell 1000 Value Sectors

All sectors had positive returns in 3Q20 except for Energy, which declined a jarring -19.5%. Sectors that were hurt by the sudden downturn continued to lead the recovery with Consumer Discretionary up +15.1%, Industrials +11.6%, and Consumer Staples +9.2%. Technology reversed some of its gains in the last month of the quarter and generated an anemic 0.2% return.

THIRD QUARTER ATTRIBUTION

The Great Lakes Advisors Large Cap Value strategy gained 4.09%, 150 bps below the benchmark. In total, sector positioning detracted from active return by 83 bps:

- Our underweight position in Information Technology helped relative performance by 21 bps, and our lack of exposure to Real Estate improved relative performance by 16 bps.
- Our overweight position in Energy and the higher than typical cash position were negative contributors by detracting 64 bps and 44 bps, respectively, from relative performance.

Stock selection within the respective sectors detracted 67 bps from active return.

SECTOR	GLA WEIGHTING	R1000V WEIGHTING	GLA RETURN	R1000V RETURN	SECTOR ALLOCATION	STOCK SELECTION	ACTIVE CONTRIB
Comm Services	7.32	9.21	14.92	7.91	-0.04	0.45	0.41
Consumer Disc.	8.46	7.52	10.42	15.08	0.08	-0.34	-0.26
Cons. Staples	6.72	8.31	9.04	9.22	-0.04	-0.01	-0.05
Energy	6.91	4.72	-19.39	-19.54	-0.64	0.02	-0.62
Financials	23.22	19.22	3.68	3.76	-0.08	-0.01	-0.09
Health Care	16.36	14.15	0.10	6.97	0.06	-1.15	-1.09
Industrials	12.79	12.44	12.02	11.60	0.01	0.13	0.14
Technology	5.83	9.93	0.85	0.17	0.21	0.01	0.22
Materials	3.57	4.67	8.53	11.96	-0.09	-0.06	-0.15
Real Estate	0.00	3.89	0.00	1.32	0.16	0.00	0.16
Utilities	4.17	5.94	12.84	5.79	-0.01	0.28	0.28
Cash	4.65	0.00	0.03	0.00	-0.44	0.00	-0.44
TOTAL	**100**	**100**	**4.09**	**5.59**	**-0.83**	**-0.67**	**-1.50**

Source: FactSet. Performance numbers are gross of fees.

MARKET OUTLOOK

The world's greatest detective, Sherlock Holmes, knew:

"The emotional qualities are antagonistic to clear reasoning."

–Sherlock, *The Sign of Four*

This does not, however, mean we don't acutely feel the tumult of the equity market, the political to and fro, the suffering caused by the COVID-induced economic shutdown, or the social unrest in our great country. And judging by the exceptional noise in the U.S. equity market – noise often below the surface and unobserved to those who follow the headline indices – investors are clearly not immune to wild swings of emotion.

On to the Economic Review:

- Profits are down, volatility is up, and doubts about the path of recovery are manifest.
- To combat this, the Fed and Treasury are maintaining easy conditions, which have resulted in positive economic surprises since May. Will positive surprises hold for the rest of the year?
- Despite the easy conditions, underlying demand weakness has resulted in well-contained prices.
- This demand weakness is reflected in soft commodity prices, with the exception of gold.
- Marginal growth in doubt regarding the future of the Dollar as the reserve currency often results in rising gold prices.
- Why the marginal increase in doubt? Money Supply is up 23% year over year, and Debt to GDP ratio has soared to 136%.
- The economy shed an unprecedented number of jobs this spring. To date, we've recovered about half of these positions.
- Despite the job losses, rate cuts from last fall plus an additional leg down this spring have led to an incredibly robust housing market.
- Stable, strong house prices combined with a solid rebound in equity markets have left asset-heavy households better off, and have abated the slide in consumer confidence.
- It's also true that those whose household wealth is driven primarily by income are suffering inordinately – thus the "k-shaped recovery" description is accurate.
- Retail sales have rebounded nicely, with a shift to online shopping having accelerated.
- The Inventory to Sales ratio is very low, and a precursor to a demand shock at some point. ISM Manufacturing and Non-manufacturing indices are indicating expansions ahead – so poor Industrial Production numbers may fade in the months ahead.

In terms of where this leaves equity markets, the sole truth is poor visibility. Stocks remain very expensive relative to fundamentals, but the duration of the poor EPS numbers is an unknown. A high P/E ratio based on a non-recurring event means little. We can say that stocks are rich at this point – but it's hard to know just how expensive. One thing we do know is stocks are certainly more attractive than bonds, sporting a 1-3% yield premium – despite their low earnings yield.

To bring it back home, we evoke one more quote from Mr. Holmes in *The Sign of Four*:

"I never guess. It is a shocking habit — destructive to the logical faculty."

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