Portfolio Manager Commentary

October 23, 2020

Trustmark Investment Advisors, Inc.

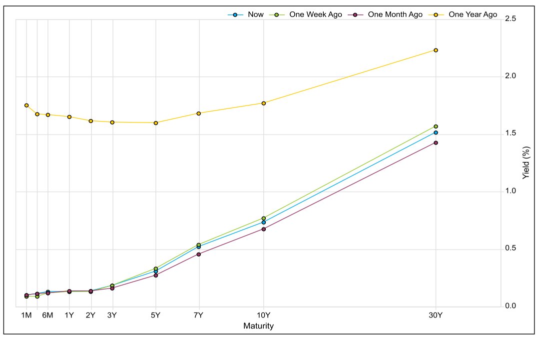
Economic Outlook

The U.S. Index of Leading Economic Indicators came in at +0.7% for September, versus +1.4% for August. Also, the NAHB Homebuilder Index came in at a strong level of 85 for October versus 83 for September.

Fixed Income

Some bond traders on Wall Street are starting to question the big short position that has built up in long-maturity Treasuries on the expectation of a Democratic sweep in next week's U.S. elections. In the market for options on Treasury futures, trades have emerged in the past week that are betting against a jump in volatility or a major move higher in yields before the end of the year. Specifically, these bets would benefit from ten-year yields staying below one percent, which is less than 15 basis points away from Friday's close. Many of these trades came to market last Friday, one day after the last Presidential debate. These positions go solidly against the prevailing narrative, fueled by polling suggesting the Democrats may take both the White House and the Senate, which could lead to massive fiscal stimulus next year. If these options traders are correct and Congress doe not come under one party rule, longer yields could face a sharp reversal. Leveraged investors have never had a bigger bet on losses in bond futures. In the cash market, ten-year yields have continued to grind higher going into the election. "It's now such a common narrative that there will be a Blue Wave and that there will be an enormous amount of stimulus and it will be inflationary," said Peter Chatwell, London-based head of multi-asset strategy at Mizuho International Plc. But with a different electoral outcome, or even if polling begins to shift before November, "that could see some investors piling back into Treasuries." Ten-year yields rose about ten basis points last week, the most since August, to end the week at 0.84%. Thirty-year yields increased even more last week, about eleven basis points to 1.64%, driving the spread between five-year and thirty-year yields to the steepest since 2016. In economic news this week, GDP for the third-quarter is expected to rise by over 30% on an annualized basis as the economy begins to gather some momentum after lockdowns caused major economic pain in the first half of the year. A larger than expected print for this number could cause yields to move higher later this week. Granted, many market participants expect that the Federal Reserve would act to avert any significant jump in yields that would roil the market, no matter who wins the coming election. Also, with a contested election a real possibility after November 3, it may take time to see which side of this futures trade is correct.

Change in Treasury Yield



Current Generic Bonds Yields

Treasuries		Agencies		Corporates		Municipals	
3 mo.	0.09%	3 mo	0.09%	3 mo	0.19%	3 mo	0.31%
6 mo	0.11%	6 mo	0.10%	6 mo	0.23%	6 mo	0.31%
1 yr	0.12%	1 yr	0.13%	1 yr	0.24%	1 yr	0.33%
2 yr	0.16%	2 yr	0.15%	2 yr	0.32%	2 yr	0.35%
5 yr	0.38%	5 yr	0.52%	5 yr	0.73%	5 yr	0.55%
10 yr	0.84%	10 yr	0.92%	10 yr	1.60%	10 yr	1.21%
30 yr	1.64%	30 yr		30 yr	2.73%	30 yr	2.00%

Equity

U.S. Equity finished with modest gains as the S&P 500 Index notched a 0.13% gain for the week. There were no real standouts for sectors as Industrials (+1.10%), Utilities (+0.82%), and Technology (+0.78%) were the three leaders. Energy (-1.95%) trailed the most. Headlines continue to be fairly quiet as the main talking points include politics heading into the election, fiscal stimulus, September retails sales beating expectations, and a focus on a slight uptick in Coronavirus cases.

Senate Republicans seem to be the largest obstacle ahead of a new stimulus plan as House Speaker Pelosi and Treasury Secretary Mnuchin cite progress in their stimulus talks. The two sides are currently $400B apart; however, the level of enhanced unemployment benefits, corporate liability, protections and funding for state and local governments, as well as childcare remain unresolved.

As noted by Bespoke Investment Group, the Advance/Decline line, a measure of market breadth, is tracking closely to the S&P 500. This means that as the S&P 500 Index is advancing, the majority of stocks in the index are also advancing with it, which is typically a sign of strength. This is contrary to the Advance/Decline line in 1999-2000 when the line was steadily decreasing, and much farther below the S&P 500, which shows a negative divergence – a sign of weakness.

Index Returns	Last Week	YTD
Dow Jones Industrials	0.05%	1.88%
S&P 500 (LCap)	0.19%	7.83%
S&P 400 (MCap)	0.05%	-3.18%
Russell 2000 (SCap)	-0.23%	-2.08%
NASDAQ Composite	0.79%	30.08%
MSCI EAFE (Int'l)	-1.43%	-5.53%
iShares Real Estate	-2.38%	-10.54%

Source: FactSet Research Systems

Asset Allocation

Current Sentiment

Cash	Favorable
Short FI	Neutral
Intermediate FI	Neutral
Inflation-Adjusted FI	Neutral
High Yield FI	Unfavorable
International FI	Unfavorable
Equity Income	Neutral
Large Cap Equity	Favorable
Mid Cap Equity	Neutral
Small Cap Equity	Unfavorable
International Equity	Unfavorable
Emerging Markets Equity	Unfavorable
Real Estate	Neutral
Commodities	Unfavorable

Summary below - Current stance on most asset classes:

Cash - Overweighting due to market volatility and uncertainty from Covid-19.

Short Term Bonds - Relative to Intermediate Bonds, the reduced duration is preferable given the oversold long-end of the curve.

Intermediate Term Bonds - The current trading range of intermediate bonds warrants a neutral position with limited upside potential. Some opportunities still remain in certain sectors.

Inflation-Adjusted Bonds - Low inflation expected in near-term providing zero real return.

High Yield Bonds - Spreads are rising given the market turbulence and exposure to unnecessary credit risk when compared to Treasuries would not be advised.

International Bonds - Foreign bonds offer good diversification qualities and higher yield opportunities, however, risks have been elevated recently and investment should be made cautiously.

Equity Income - High quality and higher-dividend-paying companies remain attractive for long-term investors given their favorable risk-adjusted profile and current yield curves.

Large Cap Stocks - A favorable weighting is recommended. Growth continues to be a more favorable style and should continue to be overweighed versus Value.

Mid Cap Stocks - Mid cap exposure remains neutral - more attractive than small caps but not as attractive as large caps.

Small Cap Stocks - In broad market corrections, small cap stocks will suffer most with increased volatility. Underweight until a clearer picture of recovery ensues.

International Stocks - Given most foreign investment is in developed markets and European countries, until sovereign debt concerns are alleviated, an underweight is recommended.

Emerging Market Stocks - Stronger balance sheets, less debt, and better growth potential make emerging markets more fundamentally attractive than developed countries longer-term. However, trade uncertainty and dollar strength provide a headwind for EM in the near term.

Real Estate - Pricing has begun to stabilize and long-term valuations appear attractive. Real Estate should continue to be a strong alternative to other asset classes.

Commodities - Global demand should support higher prices if the global recovery remains on track. Volatility will be higher, and commodities will be susceptible to short-term price shocks, however, if used in conjunction with other asset classes, risk can be reduced substantially within a diversified portfolio. Used alone though is not recommended as the short-term outlook is not favorable.

Sources of statistical information are Bloomberg and Ned Davis Research.