

It has been a few months since our last market letter. Obviously, many schedules have been upended this year and the pace of change is breathtaking. The MCM team sincerely hopes you and your family are physically and mentally healthy this summer. The stress level is elevated on everyone while this plague meanders through the world. Please call if you want to discuss your portfolio or life in general! We all need to vent for sure.....

MARKET OVERVIEW

To say that 2020 will go down in history is the understatement of the year. The extreme up moves in January and February hid the increasing fragility of the markets and global economy as the virus spread and economic growth was slowing organically. The increase in downside volatility in March only heightened investor anxiety as gains were locked in and fear increased. The travel lockdown marked the low in equity markets but not the low in fear; fear of a depression and of a spreading global pandemic whose danger was unknown.

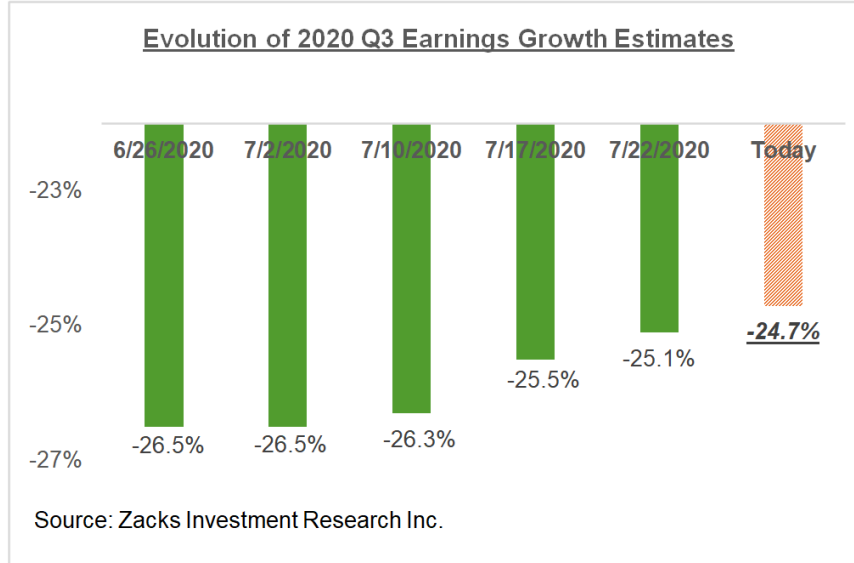
Market Sector Returns	YTD 2020	2019	2018
S&P 500 (total return)	0.00	31.5	-4.4
DJIA (total return)	-7.34	25.3	-3.5
NASDAQ Composite	16.2	36.7	-2.8
Russell 2000 (small cap)	-11.37	25.5	-11.0
MSCI Emerging Mkts	-2.68	18.4	-14.6
US Aggregate	0.2	8.7	0.0
US Treasury	26.7	6.9	0.9
Municipal Bonds (20 yr)	3.5	7.5	1.3
US Inv. Grade Corp	7.5	14.5	-2.5
High Yield Bonds ("Junk")	-1.3	14.3	-2.1
Gold	28.8	18.4	-0.9
WTI Crude	-32.0	35.3	-25.3
BBerg Commodity	-15.2	7.7	-11.2

Fast forward to the end of July. As seen in the table, most major averages have recouped the major losses of February and March and now either sit in a 'normal' correction (Russell small cap) or are in a bull market (NASDAQ). It is as if you went to sleep and not much has happened.

Large cap stocks have continued to outperform smaller stocks and we are witnessing the continuation of the "winner take all" economy. As government shut down "non-essential" businesses, small firms took the brunt of the damage especially in the service sector. Back in April, only 4 stocks (MSFT, AAPL, AMZN, GOOGL) have supplied almost 70 percent of the 2020 YTD market move. (Since then, market breath has improved and many more firms are participating in the rally – a healthy development.) These MEGA stocks are the dominant position in most funds and continue to keep getting more and more investment flow. Also, the new investment craze of ESG investing (environmental, social & governance) is dominated by the mega tech names. In our view much of this outperformance is warranted by the dominant economic footprint of these tech giants as they gobble up more and more of the consumer and business spending.

Total earnings for the 205 S&P 500 firms that have reported this quarter are down 40 percent, on 7.6 percent lower sales. Firms are unable to provide forward guidance on business prospects as well but optimism is increasing. Technology firms are beating estimates but the earnings are down as a group. Financial firms' earnings are lower by 56 percent. Full year 2020 S&P 500 earnings are expected to be down -23.5 percent on -5.3 percent lower sales. Q3 earnings

estimates are improving from where the June expectations were but remain 25 percent down.



Fed Policy

As most of you know, we have been advocating for several years that the Federal Reserve will have a difficult time raising short term interest rates very aggressively and that longer term rates will remain “lower for longer.” The pandemic has done nothing to change this thesis.

Furthermore, since the market crash in March, the global central banks are back to work buying everything they can to assist in “stimulus” and to avoid a bad debt meltdown. The chart below shows the amount of **NEGATIVE YIELDING** debt across the globe. The fourth quarter of 2019 seemed to mark a turning point as rates moved higher and less negative but the onset of Covid 19 changed all that. Globally, we are back to \$16 trillion in negative earning paper, not great for the banking system or for savers.



Gold and silver have made a run since April as some investors are beginning to think the massive monetary and fiscal stimulus will end in higher levels of inflation. It is hard not to think this way. Supply chain disruptions and product hoarding by consumers could also stoke the flames of inflation. We are keeping a watchful eye on a potential change in the inflationary outlook due to the global monetary tsunami from the pandemic. More to come on this.

2020 second half OUTLOOK

We believe the 2021 earnings growth rate should show improvement over the 2020 figures. The equity markets are richly priced after the 45 percent rebound from the March lows. MASSIVE policy support and skeptical investors may help to move the equity markets forward. High valuations, pandemic uncertainty and the November elections may provide a negative counterweight to these risk markets.

Do not hesitate to call with any questions and/or concerns. We always look forward to hearing from you.

Eric McDonald, CFA
Tyler Sturdivant

MCDONALD CAPITAL MANAGEMENT

PRINCIPAL/SENIOR PORTFOLIO MANAGER Eric C. McDonald, CFA emcdonald@mcdcap.com	Contact Information Islay Capital Management, LLC dba McDonald Capital Management 8001 Quaker Avenue, Suite J Lubbock, TX 79424 (806)744.8617 (800)734.8617
CLIENT SERVICES Yolanda Hiracheta yhiracheta@mcdcap.com mhayden@mcdcap.com	
ASSOCIATE PORTFOLIO MANAGER, TRADER Tyler Sturdivant tsturdivant@mcdcap.com	

All material of opinion reflects the judgement of Adviser at this time and are subject to change. This material is not intended as an offer or solicitation to buy, hold or sell any financial instrument or investment advisory services.