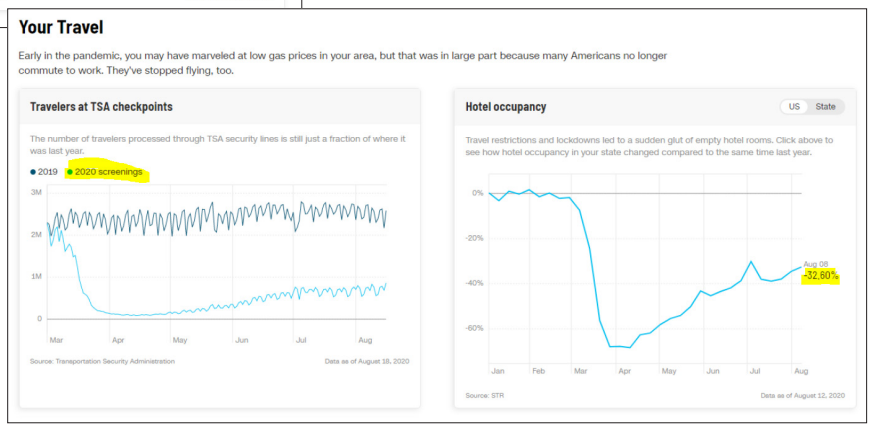
MADISON PARK
CAPITAL ADVISORS

WEEKLY MARKET UPDATE

August 18, 2020

Disruptors and Innovation

As we are all aware, the economy has changed substantially over the past six months. Many businesses and industries have stumbled and many have closed all together, many of which are in an area of the economy that had previously proven more resilient – services. One of the best movements of our economy over the past 40 years has been the transition to more of a service driven economy from a manufacturing economy (something China is trying to emulate now). That has tended to lead to a more stable economy with less severe recessions. However, the service economy has been the weakest part of our economy during this current COVID-driven downturn, with many industries still in a deep recession. You can see from the charts below that many of those industries have a long way to go in order to get back to previous levels. The big question is whether people want to go to restaurants, hotels, movies etc., like they did before. We will only know this in the fullness of time.



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This next chart is difficult to see, but 'Leisure and Hospitality' unemployment is still down 25%, and that's just the official number. It is likely much higher than that when we factor in COVID-19 "temporary" layoffs. As we've been saying, does it really matter what the cause of unemployment is? The bottom line is you are not receiving a paycheck.

Economic News Release

Table A-14. Unemployed persons by industry and class of worker, not seasonally adjusted

HOUSEHOLD DATA
Table A-14. Unemployed persons by industry and class of worker, not seasonally adjusted

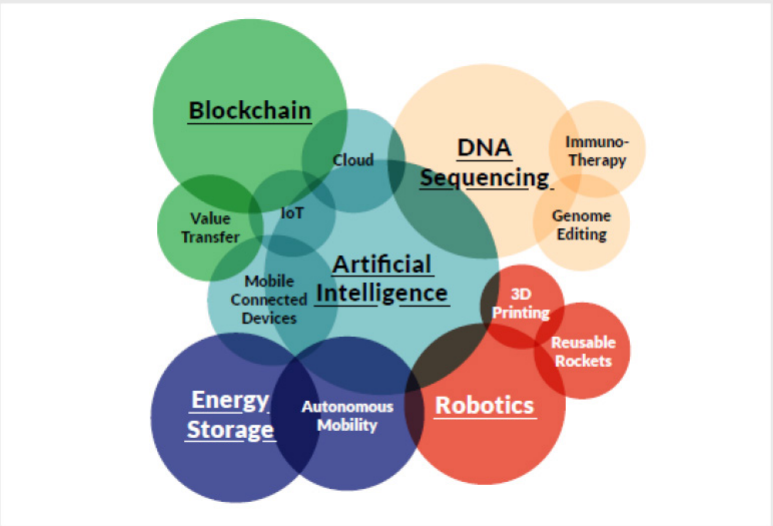
Industry and class of worker	Number of unemployed persons (in thousands)		Unemployment rates	
	July 2019	July 2020	July 2019	July 2020
Total, 16 years and over(1)	6,556	16,882	4.0	10.5
Nonagricultural private wage and salary workers	4,633	13,460	3.5	10.0
Mining, quarrying, and oil and gas extraction	18	110	2.3	15.4
Construction	386	870	3.8	8.9
Manufacturing	472	1,306	3.0	8.6
Durable goods	295	798	3.0	8.4
Nondurable goods	178	510	3.1	9.0
Wholesale and retail trade	779	1,924	3.9	9.7
Transportation and utilities	277	1,067	3.7	13.8
Information	103	311	3.9	12.3
Financial activities	169	463	1.7	4.7
Professional and business services	835	1,340	3.4	7.6
Education and health services	757	1,920	3.1	8.0
Leisure and hospitality	805	3,456	5.3	25.0
Other services	233	691	3.4	10.8
Agriculture and related private wage and salary workers	77	88	4.4	5.7
Government workers	816	1,794	3.9	8.4
Self-employed workers, unincorporated, and unpaid family workers	216	799	2.1	7.8

Footnotes
(1) Persons with no previous work experience and persons whose last job was in the U.S. Armed Forces are included in the unemployed total.

NOTE: Updated population controls are introduced annually with the release of January data. Effective with January 2020 data, industries reflect the introduction of the 2017 Census industry classification system into the Current Population Survey. This industry classification system is derived from the 2017 North American Industry Classification System (NAICS). No historical data have been revised.

Concurrent to this emergence of the services sector over the past 40 years has been an explosion in technology driven disruption, a trend that has meaningfully picked up steam in recent months. Disrupted economies tend to embrace disruptive technologies. As companies rethink how they do business and consumers rethink daily life, technologies that were waiting in the wings suddenly experience mass adoption (think Zoom) and new technologies emerge to meet previous unrealized needs. Not unsurprisingly, we are seeing new industries sprout up that bring with them new opportunities and jobs, as well as wealth creation. Think about all the jobs that have been both lost and created by the personal computer. Same thing with the internet. Many of today's largest companies weren't around when we had the tech bubble and subsequent crash. Some of these companies are new even in the last few years. Below is a picture of the many disruptive innovations that are currently changing our lives, courtesy of our friends at ARK Invest. Some we are aware of, many we are not. If you would like to read the entire research report, click here.

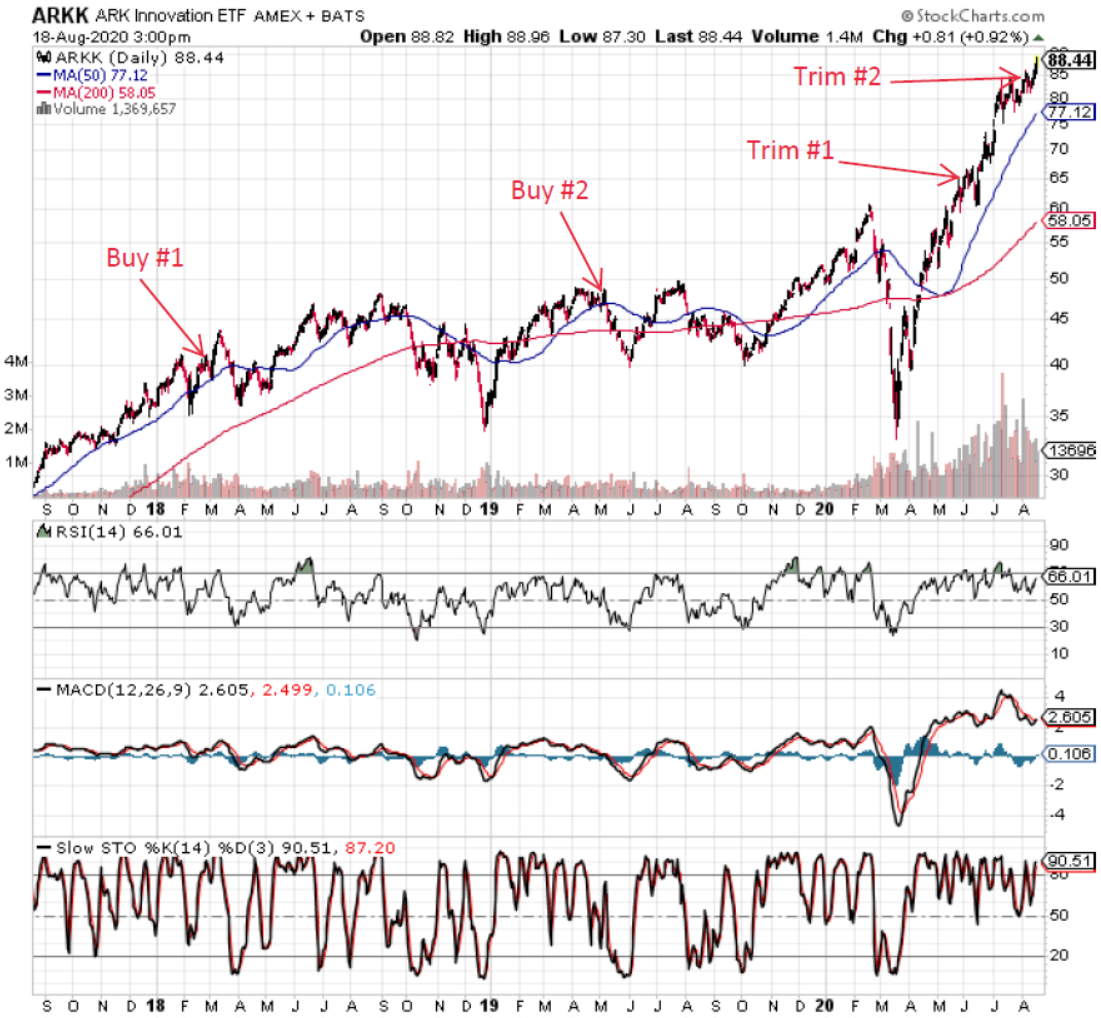
FIGURE 3
ARK's Cluster of Major Innovation Platforms



Source: ARK Investment Management LLC, 2019

As for us, we have made a sizable allocation to innovation and that has certainly been a big winner in this COVID recovery (see chart below). The question is how much is the right amount? 5%, 10%, more? I will point out that because it is a new area of investing, many of these investments are quite volatile. If you look at the chart below, you will see many periods that you

could lose 20%, 30%, or more. As we know, everybody likes volatility when it's to the upside, but when things go down, we all want to shy away from those assets. So we are left with a precarious balancing act to find that "right" amount. I have noted the two buys we made over the last couple years and you will notice there were drawdowns from those points and into the COVID pullback, only to see it rocket higher over the last six months.



We expect that those innovation platforms will continue to evolve over the course of the next 10-20 years, with many of the companies that are here today not necessarily being around when some of these technologies are fully developed. Think about all the first-generation internet retailers like Homegrocer.com that were a bit ahead of their time. Not bad ideas...just bad timing.

As always, we welcome your comments and questions. In the meantime, we'll continue to test our assumptions, dig into our research, and lean into our model as we seek to be ever mindful of risk while pursuing long-term returns for your portfolio. Our model has partially flipped to more stocks, so if we see this continue over the course of the rest of the month, we will likely be making some adjustments.

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