SILVERCREST
ASSET MANAGEMENT GROUP

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Corporate Speakers

- Richard Hough; Silvercrest Asset Management Group; Chairman and CEO
- Allen Gray; Silvercrest Asset Management Group; Managing Director
- Roger Vogel; Silvercrest Asset Management Group; Managing Director
- Jody Hansen; Silvercrest Asset Management Group; SVP and Research Analyst

Operator: Ladies and gentlemen, thank you for standing by and welcome to the Silvercrest U.S. Value Equity Team Call.

I would now like to hand the conference over to your speakers for today, Rick Hough, Chairman and CEO, Allen Gray; and Roger Vogel. You may begin.

Richard Hough: Thank you and thank you very much for joining us. This is Rick Hough, Chairman and CEO of Silvercrest, and it's my privilege to be joined this morning by Roger Vogel, our lead portfolio manager for the firm's U.S. value equities capability.

Prior to Silvercrest, Mr. Vogel, who was a founder of the firm along with other partners, in 2002 ran value equity portfolios at Donaldson, Lufkin, & Jenrette and prior to that was at Manufacturers Hanover Trust leading value equity portfolios.

Also joining us this morning is Allen Gray. Allen has been a partner of the firm since 2008 and leads all of our business development and consultant and other client relationships for the institutional business and is also a member of the executive team.

Allen has spent his career working with investors, both institutional and high-net-worth, collaborating on the business development plans and business operations of value and other equity teams. Thanks for joining us this morning, Roger and Allen. I look forward to a conversation about the portfolios in this very difficult time that the U.S. and the globe faces with the coronavirus.

I thought we'd just kick it off, Roger, by talking about your experience over the decades in managing equity portfolios on behalf of clients. You've been in the business for, I would think, about 40 years. What crisis have you managed through and how do you see this particular crisis in the markets and in the environment different from others you've faced as well as from the Great Financial Crisis of 2008?

Roger Vogel: Thank you, Rick, and thank you to everyone on the call. And first, I just want to offer my hopes that everyone is healthy and safe and best wishes to everyone and your families that you continue to be healthy and safe. It's certainly the most important thing at this time.

But as Rick mentioned, I have been doing this for a while. I have lived through the 1987 crash, the Great Financial Crisis of 2008–2009 and various intermediate crises that we've seen from time to time. Perhaps not terribly reassuring, I can't say that I've seen anything like this with the rapidity of the decline both in the equity markets and the impact on the overall economy.

I would say that, and not to sound cavalier, I do feel a little bit better about the current situation than I did in the Great Financial Crisis where, with banks failing, there was a great worry about the future of capitalism as a whole.

And not to have misplaced confidence, but I do feel that science will eventually prevail and that we will figure out a way to get through this with increased testing and eventually hopefully a vaccine. So I am hopeful that this crisis will be a crisis measured in quarters and certainly not in years and that's been our basic operating tendency, if you will, that we will get through this and that it's going to be a case of months and quarters rather than quarters and years.

And under that premise, that's how we're managing the portfolios at this point and unfortunately, our forecasting ability is not appreciably better than anyone else at this point. We're all waiting to see when the economies around the world gradually begin to reopen, but the current situation does appear to be fairly untenable for any foreseeable length of time.

But we have—personally, I have seen these types of debacles historically and our basic premise of running above average, quality portfolios has generally kept us in good stead through previous crises and I believe we'll see a similar outcome as we navigate our way through this one.

Richard Hough: Roger, you often talk about the high quality of the portfolios and what you're doing with regards to analyzing the various companies that go into building your value strategy. What do you mean by high quality? How do you define it and how has that changed or become different in navigating this environment?

Roger Vogel: Well, Rick, it's been pretty constant. We are value-oriented investors, but we've always believed that we construct a relatively high-quality value portfolio. The spread of our return on invested capital for our companies versus our benchmarks tends to run in the 300 to 500 basis point area, 3 to 5 percentage points and we're within those ranges currently.

Our level of embeddedness tends to be below that of our benchmarks as well. Whether you look at debt to total capitalization or, the way that we prefer to look at it, net debt to EBITDA and the way most banks will tend to look at it, we are fairly significantly better capitalized in our benchmarks as well. Our free cash flow generation is typically around 90% of net income. So, our companies are cash generative, have above-average returns and generally very solid balance sheets.

So what we've tried to do through this crisis is even in the early stages of this, while everything seems to want to go down and in some cases the higher-quality names are even punished more severely as they're an easy source of liquidity for people who just want to get out of the market, we do think we have opportunities to further improve the quality of the portfolio. So that's been job one, to address those issues where the balance sheets had some risk to them.

Obviously, this is really—it comes down to a liquidity issue. Earnings are going to evaporate. The first quarter, we just started getting earnings reports. We can talk a little bit about the early reports so far. Mostly banks, but at least one industrial company that we can comment about has reported, but as earnings unfold, companies have generally been very loath to offer guidance for the balance of this year. Many companies, most companies have withdrawn guidance they originally had pre-crisis.

So, earnings I don't want to say are irrelevant, but certainly Q1 earnings are inconsequential at this point and Q2 and Q3 earnings are obviously going to be tremendously impacted by this. So, it really gets down to liquidity. Who has the liquidity to get to the other side?

And once again, this is a function of timeframe. We're operating that this will be a one, two or three quarter type phenomenon and that as we move towards the end of calendar 2020 into 2021, I'm certainly not suggesting that it will be all things back to normal again, but there should be at least a return to some type of normal.

So you will have to see how consumers have reacted to this and how consumer behavior gets changed and we'll certainly keep our eyes open to that, but first and foremost is getting through this rough patch from a balance sheet perspective and a cash flow perspective. So what we've seen so far is as many companies have suspended their share repurchase programs, we've seen a couple of dividend suspensions, but generally dividends have hung in there so far and we'll just have to see how that plays out.

Many companies have tapped their revolvers with their lender—from their lenders just to have cash available on hand and some companies have even turned to the debt market. A company that we did eliminate from several of our strategies, Cinemark Holdings, the cinema chain, obviously one of the most tremendously impacted by this crisis. I saw some data this morning actually that the U.S. box office was all of $5,000 last week. So that's effectively a 100% decline from a year ago.

Cinemark, while reasonably capitalized, did go to the debt markets a couple of days ago and raised $250 million of debt at I think it was 8.75%. So, a substantial premium, but this does give them the wherewithal to operate in a zero-revenue environment for the foreseeable future.

So I suspect that we'll see some companies try to tap the debt markets where they can and they may have to pay somewhat egregious interest costs to do that, but this initial stage is all about how do we get to the other side.

Richard Hough: So Roger, just as a quick follow-up to that, you mentioned the low interest rate environment and companies going out to market whether to fund operations or to assure that they have the liquidity needed. Given the cheap debt refinancing that the Fed playbook or government to bail out stressed companies, what is the hope for or the role of value investing in that kind of environment?

For example, why did we not, at least on a short time horizon, see a shift to value outperforming other strategies in the last two major corrections in the fourth quarter of 2018 and the—and I guess there was a correction in late 2016 and certainly the first quarter of this year?

Roger Vogel: Well, a lot of it, Rick, gets to index construction. When you look at value versus growth, for example, from a 30,000 foot perspective, if you will, certainly the growth indexes are dominated by technology and healthcare and then whether you talk about the crisis in the fourth quarter of 2018 or the current crisis, those areas are perceived as more resilient in this type of an environment, whereas the value indexes are dominated by financials, energy and in industrials, three areas that are seen as more suspect.

Certainly the energy side is even an entirely different equation as they suffer with a double whammy now both from tremendous demand destruction as well as the recent squabble between the Saudis and the Russians which has caused a meltdown in the price of oil, making drilling just about uneconomic for many producers at this point.

So, I think it's really a case of index makeup. As value investors, we're disappointed at the performance of value relative to growth. Certainly through the initial stages of this decline, growth has done significantly better than value and large cap has done significantly better than small cap. Maybe some of that is to be expected and I guess the argument that growth investors would offer is that, well, with interest rates near zero, growth stocks are a long duration asset, so you should be willing to pay a higher multiple for that. It's a source of innovation, certainly on the healthcare side and on the technology side.

So there is a—there certainly is a degree of truth that you would expect the growth stocks to hang in better, but where there is a bit of a dislocation is getting down to relative valuation metrics and the gap between value and growth is now approaching the levels last seen in the tech bubble of the late 1990s into the spring of 2000. So, I'm not meaning to suggest that we're going to see an imminent collapse in growth stocks, but the relative valuations of the two schools are getting—are reaching extreme levels that we don't see very frequently.

So, we're disappointed in the performance of value, but certainly the industries that have been mostly impacted—energy, financials—would tend to be more populated on the value side than on the growth side.

Richard Hough: Thanks, Roger.

Allen Gray: Roger, this is Allen—this is Allen Gray, Roger. In addition to focusing on quality, risk management [and] preservation of client capital have also been sort of hallmarks of the long-run approach and so in this environment when you think about diversification, portfolio construction, not only position sizes, but the traditional way you've looked at sector diversification, has any of that changed or are your thoughts changing at all as you look at that?

Roger Vogel: Not really, Allen. We've been constructing portfolios in a similar matter throughout my career. We are big believers in the merits of diversification with the exception of our Focused Value strategy, which is limited to a 20-stock portfolio. We have relatively broad sector diversification, touching all nine sectors that the Russell indexes are constructed with. We do have guardrails in place to give us minimum exposures relative to those indexes and maximum exposures.

And through time, this has proven to be one of the factors why our volatility tends to be somewhat less than many of our competitors and typically at or below our benchmark levels as well. So, we haven't changed portfolio construction. We're still trying to stay within those bandwidths on a sector basis.

We also have not raised cash in the portfolio. Oftentimes we get the question, well, should you be raising cash here? That is a very difficult equation, I think, to navigate successfully and I think the lesson that I took away personally from the financial crisis in 2008–2009 is that nobody rang a bell in February 2009 saying we're safe to get back in.

So I think that's challenging and perhaps I'm shifting the onus more to our portfolio managers who are in dialogue with their direct clients that can decide on their various risk appetites and how much they want to be exposed to the market.

But in our case, the team and I are focused on keeping our portfolios as fully invested as possible. Generally, all of our portfolios now are certainly less than 5% in cash and I wouldn't anticipate us either changing our sector allocation overall or altering our standing on cash as a percentage of asset.

Allen Gray: Okay. So as a follow-up to that, as we started this downturn in the market, what were you thinking and doing in terms of repositioning and how do you feel about where you're looking to go from here with individual positions, the kinds of companies you're looking for?

Roger Vogel: Well, as I mentioned a little bit earlier, I think in the initial stages of the decline, even though we went into this with a higher quality portfolio, and I'm relatively pleased that all of our strategies are ahead of their benchmark at this point with the exception of our Equity Income portfolio, which unfortunately had greater direct exposure to the consumer segments most impacted by this debacle.

Cinemark that I mentioned previously, Delta Airlines, obviously that's been severely dislocated, Pebblebrook Hotel on the hotel side, Dine Brands on the restaurant side, all companies that have been severely impacted by this.

So that portfolio is about 100 basis points at this point behind its benchmark, but we're hopeful that we'll be able to close that ground. So initially it's been a case of jettisoning some of the companies that we feel are most directly impacted by this where we did have questions about their ability to navigate to the other side, also concerns about what the consumer's going to look like when we eventually come out of this.

Will folks who—at least in my household now, I don't think we've ever streamed more media content than we are right now. Perhaps that will have a permanent impact on cinema chains. Maybe people will get used to the fact of ‘ it's not so bad here’ to stream things at home. Maybe people will eat out less, maybe people will travel less, maybe people will trade down in hotels.

So these things I think are all probably too early to really handicap at this point, but we have tried to reduce exposures of those companies that are most directly impacted to try to just improve the overall cash flow dynamics of the portfolio. At some point, however, and this is once again taking a lesson from the playbook of 2008–2009, you do have to stick your neck out a little bit and at least consider some of the industries and companies that have been more severely impacted, but only if you feel that you have the balance sheet strength to navigate the downturn.

So, we've been reluctant to do that as of yet. We've turned over quite a few rocks, but really have not been exploring that area with new investments at this point because I think it's still a little bit early. So as we get better news about the economy opening, as the curve starts to flatten around the world, that will certainly be a strategy that we'll entertain, and certainly I don't mean to suggest compromising the overall quality of our portfolio, but really trying to follow the playbook from 2008–2009 where in 2009, we did buy some companies that were perceived as a little bit more cyclical.

I think of the aerospace industry as an example when, back in 2008–2009, no one was going to fly again and eventually those stocks rebounded. So, I don't think that really the place to really go right now is in the perceived winners. The packaged food companies are seeing tremendous benefits right now from pantry loading. That's great right now. Valuations seem to reflect that and then a year from now, once again, under the premise that this gradually abates, people are going to start to worry about comparisons.

So, I'm not sure that there's a whole lot of value really left in the perceived winners at this point. So, we will probably do some rotation away from some of our companies that have been fairly resilient into more areas that have been more greatly impacted.

Richard Hough: You know, Roger, you just mentioned the playbook from 2008, some of the lessons we learned, but you also commented on the guardrails in the portfolio and we had a question from an investor about exactly what those guardrails are, how you view them within the portfolio.

Roger Vogel: Sure, from a couple of risk control measures that we use. One, and this is once again with the exception of our Focused Value portfolio due to its limited number of stocks, [it] operates under somewhat different constraints, but in the rest of our managed strategies, a couple of points. One, we don't let position sizes get over 5% of any portfolio. So right now, we have a very small handful of 4% positions, but we won't let them get over 5% of the portfolio.

We don't own—we won't own more than 10% of any individual company's outstanding shares. So that's really more of a small cap issue of course. We do have probably five to ten companies where we're somewhere around 5% plus ownership, but we won't let that get over 10% to get us into a potential illiquid situation should things turn out different from our forecast.

But probably the most important thing is our sector construction and the way that we do this is from each—for each sector, we take a 50% weighting from the value sector, so if I would look at the large cap market, for example, that would be from the Russell 1000 Value and 50% from the core benchmark exposure, which would be the Russell 1000 and actually the S&P 500 is very close to the Russell 1000 as far as index construction goes—sector construction goes.

So, by taking 50% weighting from the core benchmark and 50% weighting from the value benchmark, what we do is flatten out some of the extremes of the value benchmarks. For example, we tend to be much more over-weighted in technology than the value benchmarks and much more under-weighted in financial services and that certainly has helped us through this current crisis.

Technology stocks, as I mentioned earlier, have done relatively quite well, so our increased exposure to technology has certainly helped us from a sector allocation perspective and our relatively lower exposure to financial services has helped us as well.

So, we do that for all nine sectors that Russell dices their indexes into and within that—so I'm sorry. Within that neutral exposure, 50% from the core benchmark, 50% from the value benchmark, we in turn want to have at least 50% exposure to that blended average and not more than 200% exposure.

So historically, we have not added or subtracted a whole lot of value from our sector allocations even though we may not look very much like our value benchmarks, but by doing it this way, it does two important things.

One, we're never naked any sectors because we really don't think that sector rotating is a very successful strategy over time and it keeps us from making a bet—the portfolio sector bet where we're not one of those firms who's going to go all-in in one particular sector because we think it's very attractive at the expense of running naked in various sectors.

So I think over time, that held us in good stead and once again, primarily shows up in relatively modest levels of volatility.

Richard Hough: Thanks very much. With regards to the current environment, we were talking about the quality of the companies that seem to be, at least right now, outperforming. As you look down the road and think about how investors may look at future returns or think about what they value, do you see dividend paying stocks as being significantly more important or not during the post-corona period? Is that—given the quality of companies that can continue paying in increasing dividends, is that going to be something that you look at more closely in the portfolio or that you think the market at large will value?

Roger Vogel: That's a really interesting question and I think there are some interesting cross currents right now. Investors may be generally aware—let's look at the airline industry for example. The airlines are taking money from the government to make payroll and the quid pro quo, if you will, is that the airlines are not allowed to pay dividends or share repurchases until September of 2021, limiting their options of returning capital to their shareholders.

For those industries that are perhaps more dependent on government aid, there is, I think, an increasing specter of, well, if you didn't buy back all your stock over the last several years, maybe you wouldn't be as bad off as you are right now and looking for a bailout, if you will, from the government. So, I'm going to be curious to see how buybacks are perceived.

Now, certainly buybacks have been a strong support for the overall market and a good percentage of S&P earnings growth actually. If that becomes a bit of a fading option for capital allocation, the question becomes, well, what's going to take its place? Are companies going to just let cash build on their balance sheets? Are they going to be willing to pay more regular dividends and/or special dividends? Are they going to ramp up M&A spending? Are they going to ramp up CapEx or what's going to happen?

So, I think it's a little early, but I would say that we've sensed over the last couple of years there's maybe been less of a favoritism on share repurchase. I mean, most every company has had some type of share repurchase program in place, but our sense is that over the last couple of years, that's maybe slowed just a tad and I don't know whether this accelerates that change.

So certainly, we think dividends are important in longer time periods. Academic studies suggest that dividends are a very substantial part of your return. So, when we meet with our corporate management teams and we get into discussions about capital allocation, we always raise our hands for dividends because it's cash money in our investors' pockets. Share buyback, yes, we understand the math, but there can be lots of inopportune times that companies wind up reacquiring their share. So, we've always liked the specter of dividend.

So that's a great question and I'm just not sure how that's going to play out at this point. I think traditional dividend-paying companies are likely to continue to pay dividends. An example, a data point of one, J.B. Hunt, a wonderful trucking company, high-quality trucking company reported their earnings today and they suggested that they would continue to opportunistically buy back their share. So that's one data point that says they don't feel any pressure not to do that.

So, we'll have to see how that evolves, but I think dividends will remain a popular way to return cash to shareholders and that the margin might even be a more preferred metric, perhaps along the lines of special dividends. So, we'll have to stay tuned, but if anything, I think this environment will maybe increase the popularity of dividends.

Richard Hough: It does seem that way potentially given the political environment, but as you did point out, a significant amount of the money flow into the market over the past decade has been from the companies themselves buying back their own stock, not just from outside money coming back into them—into the market, but all about a point and—

Roger Vogel: Yes. The other—I'm sorry, Rick. The other thing maybe to point out is in this period of ultra-low interest rates, retirees and savers have been penalized. The yields that they can get on fixed income securities and cash fall into next to nothing and certainly we've seen the fairly generous valuation of utility companies, for example, reside in part because, well, at least that's an area where I can get some dividend income. So perhaps if interest rates stay lower for longer, that may also increase the appeal of dividends as a—as an income substitute.

Richard Hough: Right. Yes. You could see how investors would prioritize those among an environment with persistently low rates. Allen, maybe you want to kind of discuss some history and the performance of the portfolio over time in these—through these environments?

Allen Gray: Sure. Roger, we got a question directly related to how the performance has been generally with your strategies versus the benchmark since the downturn started. I think you covered that a little bit, but you've also—over a long period of time, we've developed sort of a performance pattern and potential expectation for what generally happens with your philosophy and process and construction methodologies versus the market in both up and down environments, particularly when you start to look at duration, particularly on a downturn the longer it goes.

So, what would you say would be the expectations? What have you experienced and what would be the expectations?

Roger Vogel: Well, I think historically, at the first part of a crisis, everything goes down and as I mentioned earlier, in some cases even the best companies go down more because they're better sources of liquidity. So, it wouldn't be unusual for us to fully participate in the early stages of a decline.

As the decline persists, then investors tend to start to stratify the winners versus the perceived losers and that's where we typically start to add some relative performance where people differentiate between the good companies and the maybe not-so-good companies.

You know the old Buffett parable about nobody knows who's not wearing a bathing suit until the tide goes out. So once we get to that level and investors start to stratify their risk exposures, typically we start to pick up some relative performance at that point and that usually continues and then the recovery stage is sometimes daunting for us because the rising tide oftentimes will lift all boats whether it's a higher-quality company or not.

And that's what I was trying to suggest earlier where we have to be careful that it's fine to run a very high-quality portfolio through the downturn, but at some point you have to realize that some of the most downtrodden names are going to see the greatest percentage increases and we've already seen that. Some of the most dislocated restaurants, for example, or leisure companies, companies most impacted by the crisis have—in many cases their stocks, after plummeting, have already doubled or tripled.

Our inclination, as I mentioned earlier, is many of these companies are so dislocated, we'd rather let a greater passage of time go by before we'd entertain considering them, but that's the typical playbook for us. Go down with the market initially and then if things go on, start to pick up some relative performance and certainly in most downturns, if you look at it on an annual basis, we've been able to add value, sometimes significant amount of value.

As I mentioned, so far year-to-date through yesterday, all of the strategies are ahead of their benchmark except for Equity Income and we're disappointed in the performance of Equity Income of course, but we understand that we did have some exposure to the most severely impacted companies, but I would suspect that over time, over the next weeks and months that relative performance will hopefully improve there as well. So that's sort of the typical experience that I've seen in our portfolios over various crises.

Allen Gray: Okay. Well, that's helpful. Normally when you get a downturn like this, at some point we hit a level where clearing prices are there, there's a lot of liquidity on the sidelines, whether it's private equity or just cash that's been pulled out of the market and in money market funds. How do you view M&A activity in this kind of environment and what's been your experience with your portfolios from an M&A perspective over time?

Roger Vogel: Well, historically M&A has been an important part of our return, particularly in our small cap—smaller cap portfolios. We've had a fairly lengthy relative dry spell in M&A. We're not quite sure why. We're buying the same types of companies we always have that certainly would look financially attractive to private equity buyers or LBO buyers or larger corporate entities. This may precipitate an increased wave of M&A. Certainly private equity is sitting on a tremendous amount of cash and maybe some of these dislocations that we're seeing now will let that cash loose and maybe some of our companies will be subject of acquisition.

So, this is an environment where the strong will get stronger. So those well capitalized companies that are able to utilize their balance sheet strength to make acquisitions will probably come out of this in better stead. So I'm hopeful that this might be one of the salvations for value, if you will, that, with growth stock selling at very lofty valuations and value stocks selling at very low valuations, that perhaps the arbitrage here is private equity or the companies themselves may decide to take themselves private at these reduced prices.

So, I'm hopeful that will be one of the sort of end games, if you will, of this crisis, that we'll see a return to more M&A in the portfolio. So maybe a little bit early to think about that right now as everybody is just trying to preserve capital for the most part, but as things start to clear a little bit and the clouds lift, perhaps we will see more M&A.

Allen Gray: Okay. Are there any particular areas of the market that, if you had a wish list, you'd have you and your team grinding through trying to find opportunities? Are there areas in your portfolios from a sector allocation where you feel you want to change your focus or your weighting?

Roger Vogel: Well, we've—for some time now, we've been trying to increase our overall healthcare exposure in our portfolios. Obviously a very large, important part of the economy, a dynamic part of the economy. It's very hard to find palatable stock selling at reasonable valuations in our mind. So, it's been a slower slog than we would have hoped. I'm hopeful even though healthcare and tech have been two of the areas that have generally proven to be more resilient thus far that we will see some opportunities there, but it's really across the spectrum.

We're running screens every night on the entire universe of investable equities for us and seeing where the opportunities might lie. We're torturing EBITDA and earnings estimates by 10%, 25% and 33% to see how those [result and] valuations compare to 5-, 10- and 15-year median valuations. So, we're trying to hunt for the dislocation.

So, we've really been of two mindsets. One, for companies that have gone down as much as the market or less than the market where we feel that's just unjustified given the quality of the company, those are potential opportunities for us and as I mentioned, we're not quite there yet, but in the next weeks and months, we'll also consider those companies that have gone down much more than the market where we think the weakness is just grossly overdone, but they're only when we feel very confident and the cash flow is under distressed scenario.

So, we've been trying to stress test our estimates as much as we can. Right now, I would say that we tend to be about 15% below consensus estimates in our basic valuation models. So, I think we're modeling fairly conservatively. In many cases, both consensus estimates have also—have already begun to contract pretty quickly and we'll just have to see where the opportunities come up at that point.

Richard Hough: Roger, it's always been important to your strategy to engage with management. I believe you won't make an investment unless you've met with management and that's part of your investment screen. It's also an important view for getting a bottom-up on-the-ground perspective on the economy. How are you maintaining the dialogue with management teams in this environment and what kind of insights are you receiving for the portfolio?

Roger Vogel: Well, we've had virtual road shows, if you will, or private meetings with our companies telephonically through the crisis. I have not been in the New York office now for over three weeks and none of—no one on the team has met with any individual company face to face, so we've been doing it remotely.

I'd certainly would prefer to be in the office. Typically, we would meet with one or two companies a week directly at Silvercrest and then attend various investor conferences or visit companies at their headquarters. So, I miss that part of the equation. It's an unfortunate reality right now that that just is not available to us.

So, we are still trying to stay in contact with existing holdings as well as potential in investments as well and the dialogues are primarily along what you would expect. Companies are not offering any—by and large not offering any guidance into 2020. As I mentioned earlier, they're really trying to preserve as much liquidity as possible. Most of them have tapped their revolvers.

We are relatively sanguine and what our—what we're hearing from our regional bank management teams in that they seem to be quite willing to work with their borrowers. They're not really looking to put their companies into bankruptcy, their customers into bankruptcy. They don't—not interested in collateral, they're not interested in operating companies. So, we get the feeling that the banks will do everything they can to support their borrowers.

JPMorgan reported their earnings yesterday, I guess it was and let's see, I think I have this here. Bear with me for a second and I can quote directly what Chairman Dimon said on the conference call, "For our customers who are struggling financially during this time, we are providing relief such as a 90-day grace period for mortgage, auto and car payments as well as waving or refunding certain fees. We continue to support our customers and clients by providing liquidity and advice during this challenging market environment."

And that would generally be what we're hearing from our other bank management teams, that they're very willing to work with their clients. What seems to be maybe a little bit more confrontational is the relationship between tenant and landlord. Many companies have been—are not paying their April rent and obviously their landlords are frustrated by that. They still have mortgages to pay, they still have maintenance to do and it'll be interesting to see how that plays out.

So, there are puts and takes there, but I'd say in general our companies are trying to navigate this as best they can. We don't have a whole lot to go on right now because companies really are reluctant to offer any type of guidance. They seem to have addressed liquidity needs as best they can, but nobody really knows. It's all contingent on when the economy is allowed to reopen, and I don't think anyone is really clear on where we are from that standpoint.

I will tell you another anecdote that came off the J.B. Hunt call today was they are reducing their capital spending by about 25% this year. From where they had originally thought that their 2020 CapEx would be, it's now going to be about 25% lower. So obviously that reverberates through the economy. So, it's not just the consumer-facing industries that have been on lockdown with zero revenues—

Richard Hough: Right. Right.

Roger Vogel: —like the movie theaters or the restaurants. If capital spending goes down, and that touches a lot of different parts of the economy as well.

Richard Hough: Yes. And of course we saw that in the Great Recession, so I'm sure it's helpful to have management's guidance with regards to their performance at that time as well and also with regards to how today's experience is a bit different.

On that note, we've got about 10 minutes left of the call, Roger, and I thought we'd just open it up to a couple of questions from those listening in before we close out here. So, if the moderator could take questions at this time.

QUESTIONS AND ANSWERS

Operator: Thank you.

Richard Hough: Thanks very much. We'll just hold and wait for that for a minute, but, Roger, these management teams, are they seeing something significantly different from the crisis in terms of what they're managing and how they performed or does it feel like it's just as opaque for them as it was then and they're just taking the fundamental moves that a business would to preserve its cash, assure their lines of business can reopen as the economy does, et cetera?

Roger Vogel: Yes. I think that's right, Rick. I think it's quite opaque at this point. This is uncharted territory. So, job one is to preserve liquidity and I think that's how the companies are operating. I mean, we've seen unbelievable dislocations here. Some of the auto dealers are saying their same-store sales are down 50%. Obviously the restaurants are near zero, the cinemas are near zero, retailers in many cases are just limping along, hotels' occupancy is down 85% or 90%, the airlines, Delta I think has said that they're down 95%.

So, this is uncharted territory. So the link to the financial system in some cases are valid and in many cases are not so valid. So, I think everyone is uncertain, but to your point, really liquidity is job one.

Richard Hough: Yes. I think we have a question pending from Caller 1 if we could open up [his] line.

Operator: Your line is open.

Richard Hough: Good morning.

Operator: Check to see if you're on mute, Caller 1.

Richard Hough: You may have to unmute your phone. Okay. Guess that one's not going to work. Do we have any other questions pending in the queue?

Operator: Our next question comes from the line of Caller 2. Your line is open.

Richard Hough: Hey, [Caller 2]. How are you? It's good to hear from you.

Caller 2: Yes. Yes. Hi. Hi. So my question is we got a pretty good rally here, a little bit of a down day today, but I wondered what your thoughts are, Mr. Vogel, on what a lot of pretty smart Wall Street people have been saying about retesting the lows, [that we possibly]—we retest the lows in these situations, although this may be somewhat [generic], as you mentioned, but I wondered what your thoughts might be.

Roger Vogel: Thanks for the question, [Caller 2]. And yes, I've read a lot of the strategists are suggesting that it's inevitable that we retest a low. So, there are a few folks who don't think we will. I think it really—not to be too wishy-washy on the response, I think it really depends on the news that we get as far as a reopening schedule. If we get news relatively quickly, and I guess the President has suggested that, in coalition with some of the governors, there's going to be some news on that score at least in the next week or two, I'm not sure that we necessarily have to retest the lows.

So, I think the problem with a lot of the strategists is that there are so many—such a limited amount of data to parse. From a data mining perspective, you don't have too many things to look at right here. Most of the ones that I've seen are leaning heavily on the Great Financial Crisis, there's the post-9/11 experience, some go back to the Cuban Missile Crisis, we've got the 1918 pandemic, but there's really not that many observations.

So, I'm a little bit skeptical of a lot of what I read, that it's inevitable that we retest these lows. So I think it really comes down to more of a function of consumer confidence and if we get any good news at all about the curve continuing to flatten or progress on more widespread testing or development of a vaccine or even just the economy starting to reopen in various stages, I'm not sure that we necessarily have to revisit those very dramatic lows. I'm not suggesting that we're looking at a V-shaped recovery either, but I think it will take quite a while.

For modeling purposes, we're kind of—and once again, this is a best guess, but we're sort of thinking, well, maybe 2021, if we use a base case of maybe two-thirds of what 2021 estimates we're looking at before the crisis, maybe that's not an irrational place to start and obviously that's going to be different from company to company and industry to industry, but that's sort of a base case for us.

And once again, we're operating under the premise that this is not going to be four more quarters from now. Then obviously that 2021 forecast is not tenable, but if we do start to reopen the economy over the next weeks and months, business will or should start to recover somewhat.

So long-winded answer to your question. I apologize, but I'm not sure that we necessarily have to retest the lows here.

Richard Hough: Thanks, Roger. We have [Caller 1] back in the queue, but first I'm going to call on [Caller 3]. Good morning, [Caller 3], if your line's open.

Operator: Your line is open.

Caller 3: Good morning.

Richard Hough: Oh, hey, [Caller 3].

Caller 3: Roger, I was curious what your thoughts are on, once we're beyond the crisis, what the levels of federal debt might mean for market performance out two, three, five years?

Roger Vogel: That's a great question, [Caller 3], and I apologize for not addressing that earlier. I do think that there is a risk that multiples don't recover as fully as we might hope because there are various things in the hopper here. We're going to run up tremendous deficits here and I would have to think that's got to be a degradation of PE multiples over time as we figure out a way to eventually get that restored to more normalized circumstances.

The other thing that we haven't talked about is: has this crisis weakened the President's chance of being reelected, and I don't want to put a political hat here on one way or the other, but at least Vice President Biden has articulated a tax platform that would increase tax rates on both individuals and corporations, returning the corporate rate back up to 28%. That would have a negative impact on S&P earnings. If buybacks become less of a favored vehicle, that would have a negative impact on S&P earnings.

So I think you're exactly right that while the counter balancing argument, I guess, is that with interest rates this low, the old Fed model would suggest that stocks are widely undervalued here, but it remains to be seen, with the deficits that we're talking about, are we going to see a resurgence in inflation and how actually are we going to navigate our way out of this?

So, I think that's a great point and at this stage, I would think that that's got to be a depressant on overall market multiples. So, I certainly don't see us getting to a 20x multiple anytime in the next couple of years.

Richard Hough: Thanks, [Caller 3]. That was a great question. I think we have [Caller 1] back in the queue if we could open his line.

Operator: Your line is open.

Caller 1: Thanks, guys, for hanging in there. Sorry about the mute. I couldn't hit it quick enough. Just to parlay on what the gentleman said on global debt, I think the number was $275 trillion before this coronavirus hit the globe. After the stimulus money is completed and the funding is done there, do you believe that the banking system is propped up with enough liquidity, unlike 2008, to stabilize this market? Because I know a lot of stuff was happening in the repo market, but I understand the central banking systems not only globally, but here in the U.S. may be affected.

Just your thoughts on liquidity in the banking industry because companies at 0% sales or 95% being down, liquidity plays an issue after the stimulus bills are over. What's your thought process on the liquidity of the banking industry?

Roger Vogel: I might turn this one over to Jody, if Jody is still on the call. Jody does most of the financial services analysis for us. Jody, are you there?

Jody Hansen: Yes, I am, Roger.

Roger Vogel: Can you handle that one?

Jody Hansen: Yes.

Roger Vogel: I know that's a tough one, but give it your best shot.

Jody Hansen: Sure. Well, thanks to the—out of the 2008 and 2009 debacle with new regulations and stress liquidity ratios, the banks, in my memory, have never had more liquidity than they have now. So, you know that a bigger portion of banks' balance sheets are in securities portfolios, liquid securities portfolios, treasuries that they can (technical difficulty) and that's a good thing.

Right now, that liquidity is sitting on bank balance sheets, so bank deposits are up and short term, we're seeing some good things out of that. Banks now are more rapid to reduce their—or pass-along lower interest rates to their depositors. So, in fact despite, in the first quarter, a precipitous drop in interest rates, banks net interest margins have only dropped a couple of basis points, which is remarkable. So, we saw that from JPMorgan, Bank of America and PNC Financial among others that have reported.

So I think banks—both in liquidity and capital, there's no question now that the whole banking system has much more capital now than it did before and a piece of evidence that I [deduce] for that is before banks can buy back shares, for the past six years, banks have had to have the Federal Reserve and the OCC approve their capital plan. So compared to the past crises, I feel most optimistic about the bank's ability to weather this.

Caller 1: Okay. Terrific. Thank you so much.

Richard Hough: Thank you very much, Jody, and with that, I think we've been at this about an hour. I want to thank Roger and Allen joining us this morning and the entire equity team for their participation and thank you for all of those who dialed in to listen to our U.S. value equity team and Roger talk about the portfolio and how we're repositioning and discussion of our playbook in this very difficult environment. It's really a privilege for us to work with you and your family and we're grateful for that opportunity.

Our PMs of course who work directly with you are sophisticated investors in their own right, overseeing asset allocation and your specific family needs and your primary guide through this environment and in general, but we're really pleased and proud of our investment teams and the opportunity to give you access to their current thinking in this environment.

Going forward, we will keep questions@silvercrestgroup.com available and we will try to respond to those and get them to the right portfolio manager or investment team on your behalf as we go through this environment. I want to thank all of those who submitted questions in advance that helped inform how this call proceeded and I hope you join us for future calls with various professionals at our team, whether that's at the Investment Policy and Strategy Group, our tax and family office services group or our growth equity team or other teams at the firm such as in fixed income or high-yield fixed income. Please look for those in the future.

Once again, thanks for joining us and we wish you and your families all the best. Thanks so much.

Operator: Ladies and gentlemen, this concludes today's conference. Thank you for your participation. You may now disconnect. Everyone, have a wonderful day.