SECOND QUARTER 2020

Matt's Market Update

IN THIS REPORT

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Market Review

Global equity markets continued to climb higher in June to finish off a Q2 for the record books. The Dow Jones Industrial Average gained +1.82% in June (and +18.51% in Q2) for its best quarterly gain since 1987. The S&P 500 climbed +1.99% and 20.54% respectively, for its best quarter since 1998. The NASDAQ Composite finished the quarter with a gain of +30.63%. Best quarter since 1999. For the month, the index gained +5.99%. The technology heavy index finished with a gain in 11 of the final 13 trading days to end the quarter. The Russell 2000 index had its best quarter since 1991 with a gain of +25.42% after a June gain of +3.53%. While no records were set for overseas indices, strong performance was also present with a +4.52% June gain for the MSCI ACWI ex US index and a +7.0% gain for the average manager in the Morningstar Diversified Emerging Markets peer group. Not to be outdone by equities, various commodities also witnessed powerful rallies in Q2. WTI oil saw its best gain since 1990, gold had its best quarter since 2016 (and is up now 7 quarters in a row) and silver logged its best quarter since 2010.

The market has rallied over the past three months in the face of truly horrific economic news. What can explain the massive gains we've witnessed in the face of major concerns over the economy and the ongoing COVID-19 pandemic? We can thank the Federal Reserve. During Q2, the Fed expanded its balance sheet (aka printed money to buy financial assets) by nearly $2 Trillion. As this stimulus is injected into the economy, risk assets (equities) have appreciated. With the Fed throwing so much money at the crisis, nearly all asset classes have seen gains. The investment community is clearly under the impression that Fed Chairman Jerome Powell will simply not allow the stock market to decline. As you'll note from the chart on this page that compares the price movement of the S&P 500 plotted against the size of the Fed's balance sheet, there's a strong correlation. It's no coincidence that the broad equity market started to recover in late March as the Fed rolled out one stimulus plan after another. One final note on the chart, you can see the red line representing the Fed's balance sheet leveling off and slightly declining as the quarter ended. At the same time, the recent peak for the S&P 500 index was in early June. Can the rally in equities sustain if the Fed pulls back? Will the Fed pull back or is more stimulus likely in the near future? These are key questions heading into Q3.

FED BALANCE SHEET VS S&P500

Source: ZeroHedge

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Aside from additional announcements of Fed stimulus, the following are also key factors for investors to focus on as we head into Q3:

- Trends in COVID-19 case count, hospital capacity and deaths. Unfortunately, these trends seem to be heading in the wrong direction across much of the country as we begin Q3.

- News on potential vaccine developments or treatments for COVID-19. The optimistic case is a breakthrough by year-end in line with the traditional start of flu season.

- Potential new rounds of fiscal programs. The Paycheck Protection Program (PPP) and similar programs are scheduled to sunset at various points this summer. The expectation is that they'll be modified or extended in an effort to keep supporting the economy.

- Company earnings and outlook. Many firms have suspended their earnings guidance due to the shutdown in Q2. As the economy gradually reopens, investors will be on the alert for signs that conditions truly bottomed last quarter.

- While justifiably taking in a back seat so far, the November elections (and potential economic implications of the result) will likely move to the forefront.

Momentum to Continue?

Last quarter we presented a chart showing the period ending February 19, 2020 was the fastest ever drop of 30% for the S&P 500. It only took 22 days!. In Q2 we've witnessed the reverse. As of June 3, 2020, the S&P 500 gained +37.7% over the prior 50 days. As indicated in the chart below, this was only the seventh time in 45 years that the index rallied by more than 20% during a 50-day period. If history is any guide, the index would be expected to continue rising over the coming 12 month period. The historic average gain following a 20+% return over the prior 50-day period was 17.3%.

Date	50-Day Return	Next 12-Mo. Return
3/6/1975	26.9%	18.2%
10/22/1982	35.6%	20.3%
3/26/1991	20.8%	8.7%
6/24/1997	20.5%	26.4%
12/18/1998	23.8%	19.4%
5/19/2009	34.2%	22.8%
9/16/2009	21.3%	5.2%
6/3/2020	37.7%	?
Average		**17.3%**

Source: LPL Financial

Know Your Policy

It can be daunting for investors that manage their own portfolios. Some investors do not know where to start. Recent volatility only increases that confusion and potential anxiety. In our opinion, every investment strategy starts with something called an Investment Policy Statement (IPS).

There are many variations of an IPS. We go back to basics when we design portfolio strategies for clients. Each is individualized to a client's goals and objectives. The IPS doesn't have to be a long document; it can be as short as a page.

Regardless of the length of the document, each IPS should have the following topics addressed:

Risk Tolerance – This is probably the most difficult area to address as it provides the backbone to some of the other sections of the IPS. It allows the investor (or hired investment advisor) to be able to develop an appropriate portfolio. We refer to it simply as the pillow test and what level of risk will continue to allow the investor to sleep at night?

Time Horizon – What period will the investor's portfolio be invested over? Short term, i.e., one to five-years; intermediate, five to ten-years; long-term, over 10 years; a lifetime or in perpetuity (in the case of an institution). This is very individualistic to the investor and helps determine the overall composition of the portfolio.

Liquidity Needs – Does the client need periodic distributions from the portfolio or is the portfolio designed for growth? This can help determine how much cash or short-term liquid investments should be held in the portfolio to satisfy necessary obligations. Our general rule of thumb is to keep six to twelve months of cash on hand to meet these short-term obligations.

Tax Implications – This is usually dependent on whether the investment account is tax-deferred, tax free or taxable. For example, suppose an investor is in a high tax bracket and investments are held in a taxable account. They may want to avoid taxes (of course, unless they need income from the account) by investing in tax-free bonds, low dividend or capital gain paying equity-strategies (such as passive index funds).

Trading Restrictions – When it comes to taxable accounts or legacy assets, i.e., gifted securities with emotional attachments, the investor may want to avoid taxes associated with the sale of such assets. They may also want to hold onto certain investments for sentimental value (usually not a great idea as the advisor has to work around those positions in their management of the portfolio).

Special Circumstances – This may be associated with estate planning directives, i.e., special needs trusts, or charitable aspirations.

Asset Allocation, Asset Classes and Allowable Ranges – So much thought goes into this topic, as we will probably cover this segment of the IPS in its own future article. After taking into account all the above, the investor can now design an asset allocation. This is usually accompanied by a relative market benchmark for performance comparisons over time.

In summary, this section can be very extensive to give the investor flexibility in how to invest the portfolio. This section should also detail which types of investments or strategies are, if any, prohibited in the portfolio. Lastly, this part could include allowable allocation ranges for individual asset classes to more or less help manage volatility. Think of it as risk guardrails to maintain in the ongoing management of the portfolio.

Monitoring and Rebalancing – Once the IPS is established with the above, the portfolio needs to be monitored on whether it is meeting its objectives from a return and volatility perspective. Also, address how often the portfolio should be rebalanced back to its target allocation. Most rebalancing for long-term portfolios is performed semi-annually or annually, yet each client may differ based on objectives and trading restrictions.

Periodic Review of IPS – Lastly, the IPS should be reviewed periodically in case objectives, investor circumstances, and/or risk tolerance change. The IPS is not a static document. It needs to be reviewed and amended as circumstances warrant.

As you can tell, the IPS is an important document. It becomes an integral part of a well-crafted financial plan. If you need assistance with making sure you are on the right path to reaching your financial goals, please talk with your financial advisor or reach out to one of our financial planners.

Our Portfolio Strategy & Allocation Outlook

As volatility subsided and equities began to recover in April, we made several small tactical shifts to our individual client model allocations. Our goal was to add to positions and themes that are currently working in the markets, while trimming back on those areas currently out of favor. As always, maintaining broad diversification was a priority. The following changes were implemented:

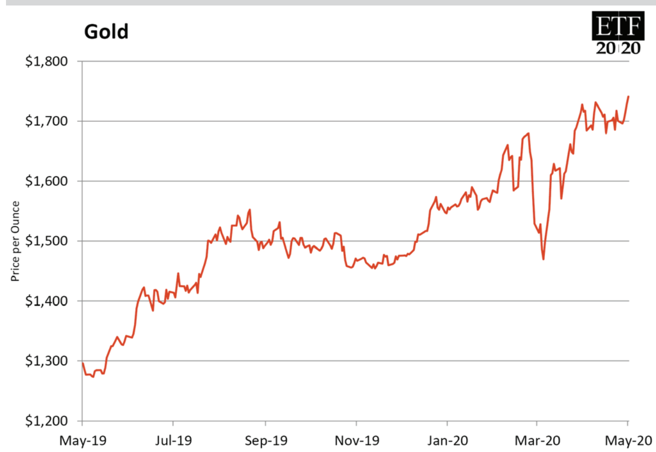
1. **Increased exposure to growth.**
   One defining characteristic of global equity markets over the past five years has been the relative outperformance of growth strategies over value. Even during the sharp market declines in March, growth performed better than value. We added to our existing position with our large-cap growth manager while trimming back exposure to value managers. We took this action in both the domestic and foreign equity segments of the portfolios. While the magnitude of outperformance for growth managers over value managers is likely to shrink in the future, we still believe this recent trend of growth outperformance can continue. During periods of economic contraction like the one we're currently witnessing, investors tend to place a premium on companies that can continue to grow their earnings despite the many challenges. Value stocks

are more sensitive to the cyclical nature of the economy and in our view are likely to continue to struggle until a true recovery takes hold.

2. **Increased exposure to active managers.** In addition to trimming value-oriented strategies, we also reduced index exposure as we allocated more to active. Industries and companies that can adapt well through the recession will be rewarded while those that don't will be penalized severely. We expect the performance gap between winners and losers to widen and therefore want more exposure to active strategies that can be more selective in constructing portfolios.

3. **Increased exposure to gold.** We added to the gold position we started in Q1. Gold is in a clear bull market as we've witnessed higher prices for the precious metal for the past seven quarters, an uptrend well underway prior to the current pandemic. See the chart on this page. As we mentioned in last quarter's report, gold has many positive portfolio attributes including: a safe haven during periods of market stress, a hedge against actions taken by central banks that devalue the currency and an asset class that is still very much off the radar of most investors despite the ongoing bull market.

GOLD
It's broken out, and it will head much higher.



Source: Thomson Reuters

Please let us know if you'd like to discuss your personal investing and financial planning needs.

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Market Scoreboard

Index Returns (%)	Q2 2020	YTD	1 Year	3 Year	5 Year	10 Year
S&P 500	20.54	-3.08	7.51	10.73	10.72	13.99
DJIA	18.51	-8.43	-0.54	9.08	10.61	12.99
NASDAQ	30.63	12.11	25.64	17.88	15.06	16.90
Russell 2000	25.42	-12.98	-6.63	2.01	4.29	10.50
MSCI ACWI Ex USA	16.12	-11.00	-4.80	1.13	2.26	4.97
Barclays Aggregate Bond	2,90	-6.14	8.74	5.32	4.30	3.82

Source: Morningstar

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S&P 500 TR: A market capitalization-weighted index of 500 widely held stocks often used as a proxy for the large-cap segment of stock market.

Russell 2000 TR: Consists of the smallest 2000 companies in the Russell 3000 Index, representing approximately 7% of the Russell 3000 total market capitalization often used as a proxy for the small-cap segment of the stock market.

Barcap Aggregate Bond TR: The Barclays Capital Aggregate Bond Index is a market capitalization-weighted index, meaning the securities in the index are weighted according to the market size of each bond type. Most U.S. traded investment grade bonds are represented. The index includes Treasury securities, Government agency bonds, Mortgage-backed bonds, Corporate bonds, and a small amount of foreign bonds traded in U.S.

MSCI EAFE NR USD: Widely accepted as a benchmark for international stock performance, the EAFE Index is an aggregate of 21 individual country indexes that collectively represent many of the major markets of the world.

DJ US Industrials TR USD: Computed by summing the prices of the stocks of 30 U.S. companies and then dividing that total by an adjusted value--one which has been adjusted over the years to account for the effects of stock splits on the prices of the 30 companies.

NASDAQ: Measures the performance of all issues listed in the Nasdaq Stock Market and is often used as a proxy for the large-cap technology segment of the U.S. stock market.

DJ/UBS Commodity: The DJ-UBSCI is composed of futures contracts on physical commodities and is often used as a proxy for broad-based exposure to the commodity markets.

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