BRIAN D. LOWDER, INC.

QUARTERLY NEWSLETTER

Volume 23, Issue 2 July 2020

Inside This Issue

- Financial Market Overview
- Financial Market Outlook
- Investment Outlook and Recommendations

Financial Market Overview

In our previous newsletter, I began with "*The entire 30% stock market gain in 2019 evaporated in one month, between the last week of February, 2020 through the third week of March due to COVID-19. The Dow Jones Industrial Average plummeted more than 10,000 points or 35% during the last week in February through the third week of March*".

Three months later, the U.S. stock market recovered with the best quarter in percentage terms in more than *twenty years (1998).* The overall U.S. stock market was up over 20% during the second quarter, 2020 - the best quarterly performance in twenty years since the rise that occurred immediately following the worst quarterly drop in 1987. The NASDAQ composite stock index (dominated by information technology) was up nearly 32% during the second quarter.

Large, midsize and small company *growth stocks* performed best – up 27%-31% during the second quarter. *Value stocks* of all sizes increased at a slower pace - up 14% to 19%. Technology and energy stocks performed best, rising 32% and 29% respectively.

Small-company stocks performed best, followed by mid-size companies and then large companies. The superior performance during the second quarter by smaller and midsize companies is not surprising as both categories fell further than large-company stocks during the first quarter decline.

International stocks rose about half as much as U.S. stocks – rising about 15.5% during the second quarter. Emerging markets (smaller-country international stock indexes) also bounced back rising almost 18% during the second quarter. Real estate also performed modestly – up 13.5% during the second quarter. Water utility stocks were down about 4% during the second quarter. This normally "steady" category declined about 4% during the second quarter as restaurants, gyms, sports stadiums, hotels, schools were closed and using significantly less water. Less water usage translates into less revenues and profits.

Gold prices rose 13% during the second quarter. Fixed income or bond prices were relatively flat as interest rates have declined to less than 1% for guaranteed income with maturities of 2 years or less. Short-term Treasuries earned 0.22% during the second quarter and intermediate-term Treasuries rose 0.64%. Current interest paid on new 10-year maturity U.S. Treasury Note is 0.6%.

The following chart displays sample returns of various asset categories during the second quarter of 2020 and year-to-date:

Year-To-Date 2020	2nd Qtr. 2020	Index Return (*includes dividends reinvested*)
- 9.55%	+ 17.77%	**Dow Jones Industrial Average (^DJI)**
- 3.21%	+ 20.16%	**Standard & Poor's 500 Index (^GSPC)**
- 3.42%	+ 21.97%	**DJ U.S. Total Stock Market (VTI)**
+ 9.65%	+ 27.67%	**Large-company stock-Growth (IWF)**
- 16.27%	+ 14.24%	**Large-company stock-Value (IWD)**
+ 3.96%	+ 30.21%	**Mid-Size Stocks – Growth (IWP)**
- 18.07%	+ 19.97%	**Mid-Size Stocks – Value (IWS)**
- 3.07%	+ 31.01%	**Small-company stock- Growth (IWO)**
- 23.42%	+ 19.35%	**Small-company stock- Value (IWN)**
- 11.10%	+ 15.48%	**International (EFA)**
- 10.36%	+ 17.86%	**Emerging Markets (EEM)**
- 13.86%	+ 13.53%	**Real Estate Investment Trusts (VNQ)**
Fixed Income (includes appreciation)		
+ 2.95%	+ 0.22%	**Short-term U.S. Treasury (SHY)**
+ 11.21%	+ 0.64%	**Intermediate U.S. Treasury (IEF)**
Alternative Investment Category		
+ 17.12%	+ 13.05%	**Gold (GLD)**

**All returns calculated using adjusted historical quotes from finance.yahoo.com*

Continued on page 2

Continued from page 1

FINANCIAL MARKET OUTLOOK

We just completed TWO consecutive quarters that had the most volatile stock market performance in over a decade – the first quarter with the largest percentage *decline* in 12 years followed by the *best quarterly performance* during the second quarter in 22 years. It's confusing and uncomfortable.

There is a perceived disconnect between what the financial markets have done, how our lives may be permanently changed with COVID-19, and the true status of our economic recovery. Add the upcoming November presidential election to the mix and everything becomes completely blurred.

The obvious factor that has been impacting the financial markets this year is COVID-19. After only six months into this crisis, there is a growing consensus about how people become infected and how we can better deal with it while waiting for a vaccine or effective treatment.

Contracting COVID-19 from occasional encounters with people outdoors or contaminated surfaces is not common. Rather, the major culprit is close-up person-to-person interactions for extended periods of time in crowded spaces such as retirement homes, indoor events, poorly ventilated areas where people are talking loudly, bars, etc. Health agencies have identified respiratory-droplet contact as the major mode of COVID-19 transmission. Simple benign activities like speaking and breathing produce respiratory droplets that can disperse in the air and potentially infect people nearby.

Preventative measures such as, wearing masks, wiping down surfaces and using hand sanitizers are good, but the bigger risks are close-range face-to-face interactions and having many people in an enclosed space for long periods of time.

More information on how to deal with this pandemic is sure to come over many months or perhaps years ahead and adjustments should be expected. In the meantime, what we are learning from these recent findings is very valuable in helping businesses and governments devise reopening strategies to protect public health WHILE getting our economy going again. Simply stated, it's imperative that we (all countries) adapt and move forward.

There will be instances of permanent displacement for some companies and their employees. A few big retailers (i.e. J C Penny and Nieman Marcus) who were already financially challenged with high debt levels and struggling business models will go under and disappear. Other small businesses that didn't maintain at least three months business expenses in reserves will also disappear. According to Opportunity Insights (Harvard University), there is a 16% decline in the number of small businesses that are open since January first. It's also likely that healthy existing businesses and new ones will step into that space. We are already seeing employment numbers (June) rise faster than anticipated.

Investors' attitudes are already transitioning from preparing for and reacting to the worst-case scenario to accepting the unknown and dealing with it. Interest rates are at a historic low and the Federal Reserve will continue providing "easy money" until we transition out of this conundrum. The economy was severely and temporarily damaged in March through May, but it is adapting and recovering rather quickly.

Spend less time focusing on which businesses will not succeed and more time embracing the companies that have adapted quickly. For example, video conferencing has exploded. With gyms closed, Peloton and workout courses via computer and live streaming are experiencing phenomenal growth. Improvement in other industries will take time - such as airlines, gym/exercise companies, restaurants, retail stores, cruise operators and energy companies.

Expect continuing uncertainty and expect more volatile days on Wall Street. Depending on the day, news related to COIVID-19, state reopening policies, getting employees back to work and students back in class, the health of our economy, etc. - news on any of these fronts could send the market higher or lower.

The stock market is recovering quite well and is down just over 3% year-to-date, but it takes a larger *percentage gain* to recover a 35% loss from February 19th to March 20th. Mathematically, it takes a 53% gain to recover a 35% loss and breakeven in **dollar terms**. If you have $100 and lose 35%, you have $65 remaining. It takes a 53% gain on $65 to reach your $100 original capital.

Everything considered, the stock market is about where it should be. It's not the end of the world yet

Continued on page 3

Continued from page 2

we have big challenges ahead to overcome. At current stock valuations, Wall Street views the COVID-19 crisis as manageable.

It's not a question about whether we will have a recovery because we are already well into this phase. The question is how fast and how long will it take to get back to resembling a pre-COVID-19 economy. California, Texas, New York and Georgia have recently experienced a resurgence of cases – lengthening the time to recovery. Further, some people believe the magnitude of cases will increase this Fall – just like the Flu season.

Bottom line, the unusual degree of uncertainty confronting consumers and investors may constrain economic activity for the rest of the year. Expect continued daily or weekly volatility in the financial markets. Likewise, after all of the gyrations, expect the stock market to be relatively flat…until the November election grabs everyone's attention.

INVESTMENT OUTLOOK AND RECOMMENDATIONS

Expect second quarter GDP (Gross Domestic Product) to be horrible. Estimates range from negative 15% to 40%. We already know this and the stock market has already adjusted too. Don't react when these statistics are released in the month ahead – it's history. By the time the actual GDP numbers figures are calculated and released in the press, it's old news and we may see only a day or two of panic reaction by day-traders and short-term investors.

This is what we anticipate:

The stock market will continue exhibiting more daily and weekly volatility as news related to the economy, politics, and updates to COVID-19 cases are announced. The stock market is reasonably valued at this time assuming we continue learning how to reopen businesses, schools, etc. while pursuing effective treatment. If I were to choose only one scenario over the next six months it would be volatile days for stocks but relatively flat performance from now until the presidential elections.

We will maintain our current asset allocation (proportional exposure to stocks, fixed income, etc.) for most client portfolios. New accounts or others with high cash balances will be invested proportionally over the next 4 months.

Our biggest concern is the historically low current return (interest) on the safe/guaranteed fixed income category. New six-month and one-year Certificates of Deposit are both down to near-zero – both pay 0.15%! Corporate bonds only pay slightly higher interest. The 10-year U.S Treasury Notes are paying 0.8% and 30-year maturity government bonds are paying only 1.45% interest. So, the safe section of client accounts is going to earn very little over the next year or so.

Not only is the interest income at historically low levels, but the prices (or value) of existing bonds issued in the past at higher interest rates are selling for more than the payoff at maturity. We mentioned the growing risk in the safe fixed income category in our previous newsletter and its worth reading again.

Sometime in the future, our country will return to work, schools, etc. The Federal Reserve has pushed interest rates down to levels not seen since the Great Depression – the current interest rate on a 30-year *home loan* is now below 3%. The interest earned on a 30-year U.S. Treasury is only 1.3%.

Someday, interest rates will increase back to the normal range – say 5%-7% on mortgages and 5%-7% on 30-year Treasury Bonds. When (not if) interest rates do begin to rise, the most conservative part of a client' investment account – fixed income or bonds, is going to lose value. And conservative investors will be confused – how can I lose money on guaranteed fixed income (bonds)?

How much will the loss be? For 15 to 30-year maturity bonds, you can expect the price or value of your bond or bond mutual fund to fall 10% for every 1% increase in interest rates. For shorter-term bonds or bond mutual funds, about 3%-5%. In either case, the drop in value will exceed the interest income. The primary way to avoid a loss is to keep your bond maturities SHORT. Six-month to 2-year maturities would be the suggested range – keep in mind, the interest income will be 1% or less.

We will continue reminding clients that the fixed income portion of their accounts are earning less than 1% annually and it isn't a compelling choice to purchase 6-12-month certificates of Deposits or Treasuries that are paying the same interest/dividends as a simple money market fund. We will defer making CD and

Continued on Page 4

Continued from page 3

1-year Treasury purchases until interest rates rise.

Another option is to allocate a small portion of a client's fixed income allocation from bonds to dividend-paying stocks (paying 2%-4.5%) of large, and stable companies with 10-year plus history of consistent dividend payments and/or increases.

We will continue experiencing unusual, uncomfortable and downright scary events due to the COVID-19 virus. The only path is forward and continue to expect uncertainty along the way. Stay safe and continue protecting yourself as recommended. We will get through this challenging series of events.

Contact Us

Brian D. Lowder, Inc.

Brian D. Lowder, CFP®, CFA
Michael Kinnear, MBA, MSFS, CFP®
Rebecca Ludford
Jennifer Finley
Pamela Priest

Address
12780 High Bluff Drive Suite 100
San Diego, CA 92130

Telephone
(858) 794-6800

Fax
(858) 794-6906

Website
www.bdlowder.com

Email
brian@bdlowder.com
mike@bdlowder.com
rebecca@bdlowder.com
jenn@bdlowder.com
pam@bdlowder.com

Brian D. Lowder, Inc., a California Corporation, is a fee-only wealth advisory firm specializing in comprehensive financial planning and investment management. Brian D. Lowder, Inc. is registered with the Securities and Exchange Commission and licensed by the State of California Department of Corporations as an Investment Advisor.

Best Regards,

Brian Lowder

Michael Kinnear

Rebecca Ludford

Jennifer Finley

Pam Priest