BRIAN D. LOWDER, INC.

QUARTERLY NEWSLETTER

Volume 23, Issue 3 October 2020

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FINANCIAL MARKET OVERVIEW

This year is easily the most volatile – in terms of financial market performance – since I started in this business in 1986. The entire 2019 appreciation, which was well-above average, was eliminated in just 4 weeks from mid-February thru March 22nd, 2020. Stocks plummeted 35% due to COVID-19. Three months later (June 30, 2020), the U.S. stock market was up 20% and after another three months (Sept, 30, 2020), the overall stock market was up 51% since the March 22nd low and is now up over 5% year-to-date. Yet, no one is excited, enthusiastic, or confident that the rebound will hold.

The overall U.S. stock market was up about 9% during the third quarter, 2020, but the gain was not broad-based. A dozen or so very large growth stocks became favorites to chase. The technology stock index was up 11.5% and the NASDAQ composite stock index (dominated by information technology) was up nearly 10% during the third quarter.

Once again, large, midsize and small company *growth stocks* performed best – up 10%-13% during the third quarter. Look at the chart below for year-to-date performance: Growth stocks, especially large companies, are up 24%, and nearly 14% for mid-size companies.

Value stocks of all sizes increased at a much slower pace – about half as much as growth stocks. Value stocks still have *negative performance* so far this year.

Energy stocks were clobbered – down over 20% during the third quarter. Exxon and Chevron are now paying 10% and 7% dividends; the same dollar dividend divided by a new lower stock price means new purchasers can earn over a 7%-10% dividend yield compared to 0.6% interest on a 10-year maturity U.S. Treasury. Obviously, stock dividends paid by energy companies are not guaranteed like the interest and return of capital for U.S. Treasuries, but the difference between interest received on a safe and very low guaranteed return on fixed income (bonds and certificates of deposit) and dividends paid by several large U.S stocks dividends is astonishing.

Small-company stock performance was the lowest compared to large and mid-size companies. International stocks rose about half as much as U.S. stocks – rising about 4.6% during the third quarter. Emerging markets (smaller-country international stock indexes) were up slightly more than U.S stocks – up over 10% during third quarter following an 18% return during the second quarter, however, the total return year-to-date is still down 1%.

Investment real estate performed modestly – up 1.3% during the third quarter. A growing number of commercial tenants whose businesses have

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suffered during the pandemic are not current on their rent payments, yet home prices are soaring (more on this topic later in this newsletter). Water utility stocks were down about 5%-7% during the third quarter. This normally "steady" category declined about 10% this year as restaurants, gyms, sports stadiums, hotels, schools were closed and using significantly less water. Less water usage translates into less revenues, yet most of water utility costs are fixed. Net result is profits are down.

Gold prices rose nearly 6% during the third quarter and the metal is up nearly 24% so far this year. 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 a measly 0.07% during the third quarter and intermediate-term Treasuries rose 0.21%. Current interest paid on new 10-year maturity U.S. Treasury Note is still near 0.6%.

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

Year-To-Date 2020	3rd Qtr. 2020	Index Return (*includes dividends reinvested*)
- 2.65%	+ 7.63%	**Dow Jones Industrial Average (^DJI)**
+ 5.58%	+ 9.04%	**Standard & Poor's 500 Index (^GSPC)**
+ 5.08%	+ 8.80%	**DJ U.S. Total Stock Market (VTI)**
+ 24.15%	+ 13.22%	**Large-company stock-Growth (IWF)**
- 11.63%	+ 5.54%	**Large-company stock-Value (IWD)**
+ 13.80%	+ 9.46%	**Mid-Size Stocks – Growth (IWP)**
- 13.00%	+ 6.19%	**Mid-Size Stocks – Value (IWS)**
+ 3.95%	+ 7.24%	**Small-company stock- Growth (IWO)**
- 21.49%	+ 2.52%	**Small-company stock- Value (IWN)**
- 7.04%	+ 4.57%	**International (EFA)**
- 1.17%	+ 10.25%	**Emerging Markets (EEM)**
- 12.72%	+ 1.32%	**Real Estate Investment Trusts (VNQ)**
		Fixed Income (includes appreciation)
+ 3.01%	+ 0.07%	**Short-term U.S. Treasury (SHY)**
+ 11.43%	+ 0.21%	**Intermediate U.S. Treasury (IEF)**
		Alternative Investment Category
+ 23.95%	+ 5.83%	**Gold (GLD)**

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

FINANCIAL MARKET OUTLOOK

Most investors who did not make significant changes to their investment portfolios earlier this year are still down slightly for the year. Some accounts with higher allocation to large-company growth stocks are up 5%-10%%.

Even though the overall stock market has made a recovery since the March 22nd low point and reached new highs over the Summer, our economy is still in crisis mode. Businesses and schools are opening up and then shutting down or implementing new restrictions. One month, the coronavirus crisis seems to be inching toward a path of recovery and then positive cases spike – even the President and First Lady tested positive. This back and forth uncertainty are making life difficult to assess, much less providing any level of comfort and confidence with the financial markets. Now, with the Presidential election less than 30 days away, another howling wind of uncertainty is upon us.

For the first time in my voting lifetime, policies, vision, course of action, etc. of the presidential candidates doesn't matter to most voters. The only central question I hear is: Do you LIKE __________.

The big unknown is: How long will it take for the U.S. and world economic growth to recover and return to the ideal 2-3% annual growth rate that we had just prior to the pandemic? Will the current President or a new Party make any difference in spurring economic growth? Without a vaccine, economic growth could stay lower for longer than people expect regardless of who is

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President. Some people believe the current environment is the "new normal".

Here's the current state of our economy: The U.S. unemployment rate last month dropped from 8.4% to 7.9% - still over twice the rate before the pandemic. Over 700,000 workers left the labor force making the real unemployment rate closer to 8.3%. Politics and the election are a near-term issue providing an abundance of uncertainty over the next 3 months but the economy will determine the stock market's future course over the next year.

Corporate Profits and Gross Domestic Product: As a whole, GDP was down 5% in the first quarter as the impact of COVID-19 began in late February. In the second quarter, GDP was down over 31%. We won't know the actual third quarter figure until later, but with businesses, sports, schools, vacation destinations etc. still closed or partially open, the GDP figure is going to be very negative and far below the positive 2%-3% growth in the previous 5 years.

From a **current** economic view, business production and activity are still struggling – not good.

Presidential Election uncertainty – huge and not a good sign.

Positive outlook: Interest rates are at their lowest point in my lifetime. Certainly not a positive for conservative investors who will earn less than a 1% return on their safe and secure short-term CDs and bonds. However, for borrowers, the ultra-low rates are a positive, especially for homeowners. Home mortgages are now below 3%! Home prices are spiking and buyers are willing to pay a premium price for a home.

In San Diego, a moderate monthly rent amount is about $3,000 per month. For the same $3,000 monthly rent payment, a borrower can secure a loan for about $725,000 and still pay only a $3,000 monthly mortgage payment. This provides a nice incentive to buy a home verses renting. Subsequently, home prices are jumping up in value.

The pandemic is taking a psychological toll on our normal positive outlook. Very few people entertain what the economic or investment scenario would look like if or when a vaccine or effective treatment for COVID-19 is developed. I'll give you a picture: a cork releasing from a champagne bottle. And the INITIAL surge in the stock market will occur no matter who wins the election.

Another support that is drawing investors to the stock market is the low interest (rates) offered on the safe fixed income category. A new ten-year maturity U.S. Treasury Note pays only 0.6% interest. Savings accounts and money market funds pay less than 0.2%. New one-year Certificates of Deposit offer less than 0.2% interest.

Alternatively, large and established companies are paying 2%-5% dividends. Buying stocks of well-known and solid companies is an attractive alternative. Interest rates are at a historic low and the Federal Reserve will continue providing

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"easy money" until we transition out of this conundrum. The Federal Reserve's estimate calls for very low rates for another 2 years. Dividend-paying stocks are an attractive alternative to low-paying fixed income securities.

Again, 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.

Next year is going to be a pivotal one. Battling COVID-19 remains uncertain, however, a huge part of the unusual degree of uncertainty confronting consumers and investors today (Presidential Election) will be gone very soon. Expect continued daily or weekly volatility in the financial markets through the remainder of this year.

INVESTMENT OUTLOOK AND RECOMMENDATIONS

The stock market will continue exhibiting more daily and weekly volatility as news related to the economy, politics/election, and updates to COVID-19 cases are announced. The stock market is reasonably valued at this time assuming we continue learn, adapt and move forward to reopen businesses, schools, etc. while pursuing effective treatment, therapeutics and/or a vaccine.

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 periodically over the next 4 months.

Worth Repeating: Our biggest concern is the historically low current return (interest) on the safe/guaranteed fixed income portion of client portfolios. New six-month and one-year Certificates of Deposit are down to 0.10% and 0.20% respectively. Corporate bonds only pay slightly higher interest. The 10-year U.S Treasury Notes are paying 0.6% and 30-year maturity government bonds are paying only 1.50% interest.

So, the safe section of client accounts is going to earn very little over the next year or so. Any fixed income alternatives that advertise a higher yield must be examined carefully, as there is additional risk for the higher return offering.

Not only is interest income at historically low levels, but the prices or value of existing bonds that were issued in the past when interest rates were higher 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.

Looking forward, don't look at the historical return for bonds in 2020 year-to-date – which is above 10% because most of that gain is NOT interest. Most of the total return came from capital appreciation or price increases – bonds that have higher interest rates (because they were issued years ago when rates were higher), have jumped in value – most well

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above what these bonds will pay at maturity. That gain will not repeat unless interest rates go to zero or negative. **Expect the fixed income portion of your portfolio to provide 1% or less in the year(s) ahead.**

Yes, there are many bonds that offer 4% or higher interest, but you must compare the *quality – i.e. Safety Rating*. Everything – corporates, high yield bonds, convertible bonds, etc. have lower credit quality rating compared to U.S. Treasuries and certificates of deposits.

We are continuing to deal with this low-income environment by moving some funds into high-quality and established stocks that pay 2% to 5% dividends. Yes, the safety isn't the same as a guaranteed Treasury or CD, but the modest additional risk is worth receiving 2%-5% dividend income compared to less than 1% for Treasuries and CD's.

IMPORTANT: Secondly, over two months ago, we reviewed all client accounts under our management and created a very large "emergency block sell trade" file. This large SELL block trade file will – if executed – reduce client stock holdings by 50% with one push of a button. Only a handful of clients have opted out of this block sell trade file.

We have not and will not guess who will win the Presidential election nor will we make pre-emptive sell trades. At the same time, it is more responsible and much better to have a downside game plan completed, in place, and ready to implement compared to reacting (emotionally) when the stock market falls precipitously.

Lastly, the relatively few stocks that are advancing up to 100% or more so far year-to-date and the much higher return on tech/information technology sector stocks is *eerily reminiscent of the late 1990's.* Tech stocks were all the rage and everyone retold their stories of making so much money on this or that technology stock trade. Then, an UNRELATED, SUDDEN and UNPREDICTABLE EVENT occurred that demolished the stock market for 3 years (World Trade Center attacks). Tech stocks were demolished.

Value stocks – meaning recognizable company names that have been around for many years with established products have not kept pace with growth stocks this year. This category is much safer than growth and tech stocks plus many of these companies pay 2% to 5% dividend income. This category is very attractive from a future price gain perspective, is fairly valued and a good source to pursue higher income that clients are losing in the low interest rate fixed income category.

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 1.6%.

The economy will find its footing sometime in the future. Interim news events and politics will continue to negatively impact the financial markets. The news is full of downbeat opinions. Consider for a moment the other side: our country has been through much worse over the past 150 years. When we find our way through this pandemic, don't be surprised

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to see the financial markets act like a cork ejecting from a champagne bottle.

The only path is forward and expecting uncertainty. Stay safe and continue protecting yourself as recommended. We will get through this challenging series of events.

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Best Regards,

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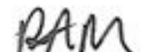

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