ADVISER INVESTMENTS

Adviser Outlook

OCTOBER 2020

QUICK TAKES

- ✔ U.S. stocks climbed back into positive territory for the year by the end of the third quarter despite the global economic crisis prompted by the coronavirus pandemic
- ✔ Economic activity has seen a strong bounce off the lockdown lows, but further recovery could be slow and uneven
- ✔ Heading into flu season, rising COVID-19 cases here and abroad are a concern. Progress toward a safe and effective coronavirus vaccine will be key to "getting back to normal"

Both the U.S. economy and stocks have bounced back rapidly after plumbing recessionary depths earlier this year during the pandemic-induced global lockdown. However, the hotly debated V-shaped recovery now looks more K-shaped, with some portions of our economy prospering while others fall behind. The same could be said for the extremely bifurcated stock market, where the differences between winners and losers have widened as some stocks soar to record highs and others lose ground.

Through the end of September, the economic and market rebound could be pinned in large measure on what Federal Reserve Chairman Jerome Powell characterized as "by far the largest and most innovative fiscal response to an economic crisis since the Great Depression." We would also give credit to the Fed's monetary response, which has contributed to the investment markets' stability and recovery.

As we write, some portions of the U.S. stock market have regained pre-pandemic highs, yet our economy has only clawed back about half of the record 22 million jobs that were lost. Neither economic nor market gains have been easy or consistent.

Another "V" we are watching, stock market volatility, has fallen since earlier this year, but increased in September to above its long-term average level. We expect such volatility to persist. Of course, the votes Americans will cast in the upcoming election and the development of a safe and reliable vaccine are a couple more Vs that are pings on our radar.

Before we discuss our outlook for the final stretch of 2020 and beyond, let's consider market activity over the past three months.

Third Quarter Review

After a rapid rebound in the late spring, U.S. stock market gains slowed in the third quarter, and reversed course in September. But the summer surge was enough to put the broad market back into positive territory for the year, as you can see in the table on the next page. Stocks in emerging markets outpaced those in the U.S. and developed foreign markets in the third quarter, gaining 9.6%, though they are still down for the year.

In the U.S., the gulf between leading and lagging market sectors remains wide. The top three performing sectors in the third quarter consisted of stocks in the consumer discretionary, technology and industrial

QUARTER REVIEW	
	✔ The S&P 500 returned 8.9% during the third quarter and is up 5.6% year-to-date, gaining 51.7% from the market bottom in March
	✔ Driven by falling interest rates, the U.S. bond market has outperformed stocks, both U.S. and foreign, with a 6.8% return this year
	✔ Consumer discretionary and technology stocks, up 18.9% and 12.1%, respectively, were the top sectors in Q3, while energy stocks were hit hardest, down 19.0%

areas. The energy sector was the only slice of the U.S. market with a negative return in the third quarter.

Bond yields are low and likely to stay that way for some time to come, but the broad U.S. bond market has been a steady performer, up 6.8% for the year. The yield on the benchmark 10-year Treasury has been in a holding pattern over the last five months or so, keeping to a tight range; it sat at just 0.69% at quarter-end, down from 1.92% at 2019's close. With yields so low, higher-risk alternative income investments are being promoted by pundits and certain advisers, but their potential for losses is multiples of what we expect in the bond market. For our money, the continuing value of bonds' shock-absorbing qualities in a portfolio cannot be overstated.

Our Outlook

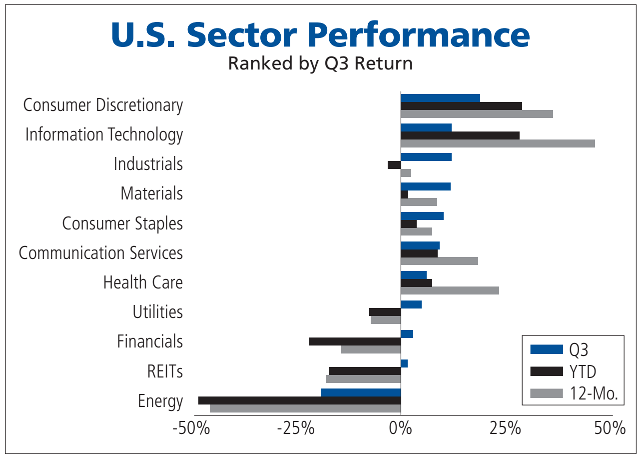
Much of the volatility in the stock market this year can be traced to heightened uncertainties over the coronavirus, the election and both the pace and quality of government, corporate and individual responses to the pandemic. While some of these factors will remain open-ended questions heading into 2021, others will be answered in the coming weeks and months.

The election is an obvious source of concern until the votes are counted and one side concedes, but based on past election cycles, the party winner is less

U.S. Stocks Again Positive in 2020

	Q3	YTD	12-MO.
MSCI Emerging Markets	9.6%	-1.2%	10.5%
MSCI U.S. Broad Market	9.2%	5.4%	15.0%
S&P 500	8.9%	5.6%	15.1%
Dow Jones Industrial Average	8.2%	-0.9%	5.7%
MSCI EAFE	4.8%	-7.1%	0.5%
Bloomberg Barclays U.S. Agg. Bond Index	0.6%	6.8%	7.0%

Note: Ranked by Q3 returns. Performance numbers are total returns, reflecting reinvested dividends through 9/30/2020. Source: Morningstar.



Source: Morningstar.

important than fundamental factors (earnings, interest rates, economic activity) in determining future stock market performance.

For more on why we do not use election polls or results as an investment indicator, read our *Focus on Market Cycles, Not Election Cycles* special report, which you can request from your team or find on our website (**adviserinvestments.com/markets-elections**).

As we look ahead to what could be one of the most consequential earnings seasons in years, the gaps between winners and losers should quickly become self-evident. High-flying tech and pandemic-ready companies set the pace for much of the 2020 recovery and will likely continue to deliver strong results. That said, the mega-techs took a breather in September with the NYSE's FANG+ index falling 4.9% and the tech-heavy NASDAQ 100 dropping 5.7%—providing yet another example of why we believe in the benefits of a diversified portfolio.

Beyond technology, home improvement stocks, online retailers and grocery stores have all benefitted this year, as have home entertainment stocks. On the flip side, the energy sector and travel and leisure providers, along with brick and mortar retailers and commercial real estate companies have all suffered

OUR OUTLOOK

- ✔ The pace of the recovery depends not only on having a proven vaccine widely available but also on Congress committing to infrastructure spending and fiscal stimulus
- ✔ Trends supporting pandemic-ready companies and hampering vulnerable businesses are likely to persist and drive the direction of investment and economic momentum
- ✔ Foreign small- and mid-cap stocks are an overlooked asset class that can generate long-term gains. Health care continues to be a steadfast component of our disciplined diversification

due to coronavirus-related shutdowns. We think these trends will persist, at least over the next three to six months.

As eviction protections expire and layoffs keep coming, we hope that Congress and the White House respond to Fed Chairman Powell's call to pass the next stopgap support measure sooner rather than later.

On top of direct fiscal stimulus, a large infrastructure spending bill should be high on Washington's agenda for 2021 no matter who wins the election. As noted, the economy has recovered 10.6 million of the 22.2 million jobs lost this year, but employment growth may begin to turn back down. An investment in the country's physical and digital infrastructure would create jobs for a generation, establish more equitable access to opportunity and, combined with the Fed's business-friendly interest-rate policy, boost economic growth.

The pace of the economic rebound has slowed in some areas and flattened out in others. We won't get an indication of how much the U.S. economy bounced back in the third quarter until Oct. 29—mere days before the election—and when we do, it will be backward-looking. Estimates for economic growth range from the high teens up to 35% or so on an annualized basis. Even if the most optimistic projections are on target, our economy will still be 3% smaller than it was last year.

Given the focus on vaccine research, it's not surprising that some investors are coming around to our belief that the health care sector represents a strong, long-term investment opportunity. We continue to view health care as a key strategic holding, and not just because drug companies are racing to find a coronavirus vaccine and develop better treatments. In fact, the

PERSONAL FINANCE FOCUS

Last Minute Money Moves

MANY OF US WILL BE THRILLED to say sayonara to a year defined by COVID-19. But it's not too late to make the most of your finances in 2020 before the year turns. Here are a few thoughts to explore at home or with your Adviser Investments team.

- **Review Your Medicare Coverage:** The Annual Election Period (AEP)—from Oct. 15 through Dec. 7—is the only time recipients can update their supplemental or prescription coverage for 2021. For more on Medicare, check out our reference guide or "Medicare Made Simple" podcast.
- **Look Into Tax-Loss "Harvesting":** You can deduct up to $3,000 in losses against your ordinary income for 2020 and use excess losses in future years. We actively seek to identify clients' tax-loss harvesting opportunities, even for investments held away from our care, and we are happy to help you think through strategic sales.
- **Consider Charitable Giving:** Charitable donations are a great way to make a difference in the world and leave a legacy while saving on taxes. For more, check out our podcast on the topic, and our special report, *Making the Most of Your Charitable Giving*.
- **Max-Out Retirement Contributions:** If you're below 2020's 401(k), IRA or health savings account contribution limits and have cash to invest, it's a great opportunity to reduce your taxes while investing for your retirement. Our *Key Financial Data* guide has the annual limits.
- **Leave Your RMDs to Grow Another Year:** In 2020, Congress let retirees forego taking required minimum distributions (RMDs) from their retirement savings accounts. That means a full year of letting your assets compound without forced withdrawals.

Please set up a time with your wealth management team to discuss advantageous moves you can make before the calendar flips to 2021. They are ready to help.

To access the podcasts, reports and articles referenced above, please visit adviserinvestments.com/client-outlook/resources.

Year-End Finances Checklist

Review Your Medicare Coverage	❏
Look Into Tax-Loss "Harvesting"	❏
Consider Charitable Giving	❏
Max Out on Retirement Contributions	❏
Required Minimum Distributions	N/A

vaccine itself may not be a profitable product, but the potential for strong earnings rests in the medical supply chain companies that produce it, those that design and build the delivery systems and the specialized shippers who distribute it globally.

Besides health care, we also believe there are overlooked opportunities in smaller foreign stocks. Our research team has shown that a better return history with a similar risk profile to large foreign company stocks makes this potentially fertile ground for skilled active managers. Just this year, foreign small-cap stocks gained 55.3% from the March bottom through quarter's end compared to large-cap foreign stocks' 39.1% gain. You can read our analysis in our special report: *Going Small Overseas—Why It Makes Sense*. (Find it here: **adviserinvestments.com/small-overseas**.)

Seeing U.S. stocks gaining ground for the year, hitting new highs even as the coronavirus continued to spread, seemed like the longest of longshots during the depths of the COVID-19 crash. But as we approach year-end, that's exactly what's happened, reinforcing our commitment to sticking with our long-term investment strategy through periods of short-term upheaval while seeking opportunities to better protect and grow your wealth throughout.

ADVISER INVESTMENTS' QUARTERLY UPDATE

WEDNESDAY, OCTOBER 28, 4:30 PM EDT

Register at: AdviserInvestments.com/webinar

A replay will be posted to our website following the live event

COMPANY NEWS

Three Cheers for Our Crew!

From left to right, Nicolette Shaw, Michelle Indeck, Steve Johnson, Dick Veidenheimer, Adriana Sorrentino, Chris Keith, Karrie Gorman. Not pictured: Kevin Turner, Jake Lynch.

THANKS to our remarkable IT team, we had the technology in place to allow us to seamlessly adapt to working from home without sacrificing our fundamental objective of providing personalized service and peace of mind to each and every client. But that wouldn't be possible without a dedicated handful of Adviser Investments employees staffing the office throughout the pandemic. They've stepped up to make sure all the essential tasks necessary to serve our clients are completed, from maintaining our remote work infrastructure to handling the mail. (And even making sure our plants get watered.) We can't thank them enough. Hats off to them and our whole AI crew!

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