As of 9/30/2020

Q4 2020

Spectrum Investor® Quarterly Newsletter

SPECTRUM INVESTMENT ADVISORS

Jonathan Marshall
Chief Investment Officer

James Marshall
Chairman/Founder

Newsletter Summary:

U.S. COVID-19 cases continue to rise
Growth stocks boosted by tech
Value stocks lifted by reopening
S&P 500 earnings recovery estimated by year-end 2021 (Factset)
Interest rates lower for longer
US Election on the horizon

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See important disclosures on Page 6

Our ADV Part 2A-2B & privacy notice can be found on our website.

US stocks turned in a second consecutive quarter of dramatic gains, continuing a historic stock market recovery that few predicted in the depths of the March 2020 downturn. Despite a stretch of volatility that dampened momentum in September, the S&P 500 and Dow Jones Industrial Average gained 8.9% and 8.2% respectively over the past three months, which capped the best two quarter performance since 2009. Both indexes are up more than 28% since the end of March 2020 (*WSJ*, 10/1/20, return includes dividends).

Markets. The chart below shows the S&P 500 is slightly above where it started this year, up 5.57% for 2020 as of 9/30. In comparison, the tech-heavy Nasdaq Composite has gained 25% to 9/30, carried primarily by five large cap tech stocks.

Investor optimism. In spite of ongoing challenges with COVID-19 and uncertainty over the upcoming U.S. election, investors grew more optimistic about the stock market over the summer. Why?

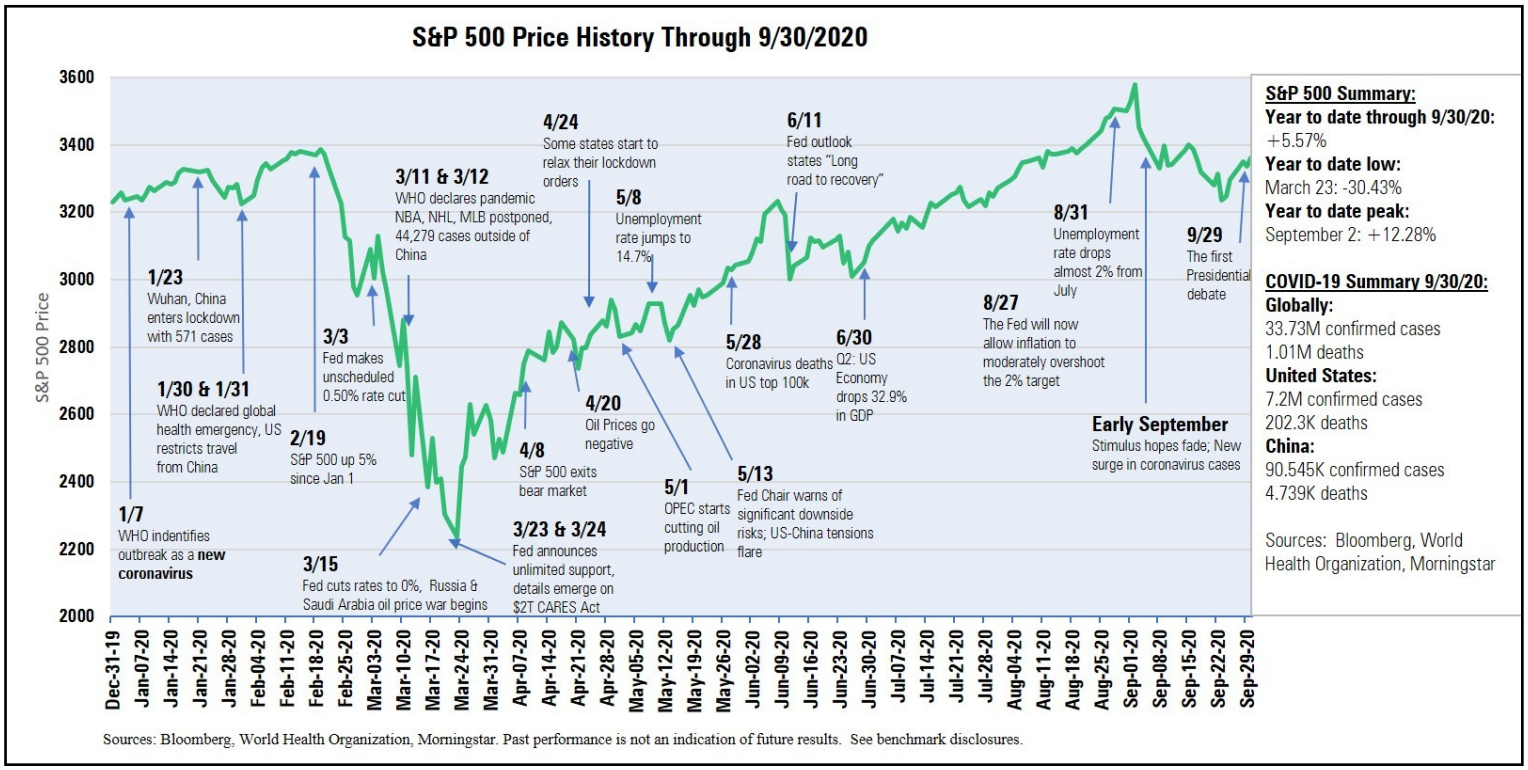
1. The Federal Reserve. The Fed was able to stabilize markets in March, providing confidence they could do the same in the event of a potential second shock. They have also been clear that interest rates will remain lower for longer. The Fed is now willing to tolerate periods of inflation above its 2% target to compensate for periods like the current one, when inflation is running below its goal of 2%.

2. Innovation versus COVID-19. Significant gains were made in testing, treatment, and progress toward vaccination over the last six months. According to Scott Gottlieb, former FDA commissioner, we could see vaccinations available on a limited basis as early as December, with more widespread availability throughout 2021.

3. More stimulus. It is widely believed that we need, and will get, more government stimulus in the neighborhood of $2 trillion. The question is when and can it be effectively targeted to areas of need.

4. Upside surprises. Many aspects of the recovery have bounced back faster than expected. In markets for example, although S&P 500 corporate earnings were negative in the second quarter, 84% of companies beat expectations. In the last five months, the U.S. unemployment rate dropped from 14.2% in April to 7.9% in September. It took 35 months to go from 10% to 7.9% unemployment following the financial crisis.

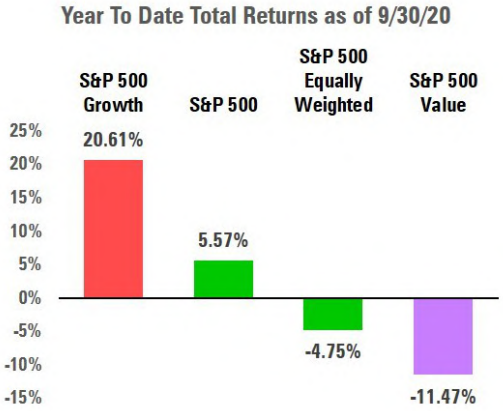
According to Morningstar's Chief U.S. Market Strategist Dave Sekera, markets will need the following to continue upward momentum: an uncontested election, stimulus approval, and a successful vaccination rollout in the first half of 2021. At current valuations, doubts or disappointments in these key areas would be headwinds and a set up for potential corrections.



Quarterly Economic Update Continued

Uneven recovery: All areas of the markets have improved since March, but at much different speeds. Social distancing continues to be the primary factor. More time at home has created a boom for tech firms that help keep us connected and entertained. On the other side, the limited reopening of the economy has meant a limited recovery for sectors like travel and energy. Most tech firms can be found in growth (red) while most travel and energy stocks fall in the value category (purple).

The chart on the right shows the impact this has had on stock performance with growth leading the way and value not quite back into positive territory.



In August, Apple became the first publicly traded company to reach a market cap of $2 trillion. It is the largest publicly traded company in the world, and worth more than all 2000 companies combined from the Russell 2000 small cap index. Together, Apple, Microsoft, Amazon, Facebook, and Google make up more than 22% of the market cap weighted S&P 500 index. This has helped boost the return of the S&P 500 (green) in spite of the equally weighted average return of the 500 companies actually being down -4.75%.

In another sign of the times, Exxon has been removed from the 30-stock Dow Jones Industrial Average and replaced by Salesforce, a cloud-based software company. Exxon had been a member of the Dow since 1928.

Stay diversified. If we struggle with COVID-19 for a prolonged period, we may see growth continue to lead. However, at current valuations, a solid reopening with the help of vaccinations would likely see value stocks (energy, travel, financials and materials) begin to outperform. Tech valuations are high at the moment with a forward price to earnings ratio of 34, but they are still below the bubble levels of the 1990s (FWD P/E ratio: 53) with much better balance sheets and cash flow generation. Technology has represented the most consistent area of relative strength for the S&P 500, not just year-to-date, but for the past decade (Jeff Buchbinder, Equity Strategist & Portfolio Manager at LPL Financial, 9/28/20).

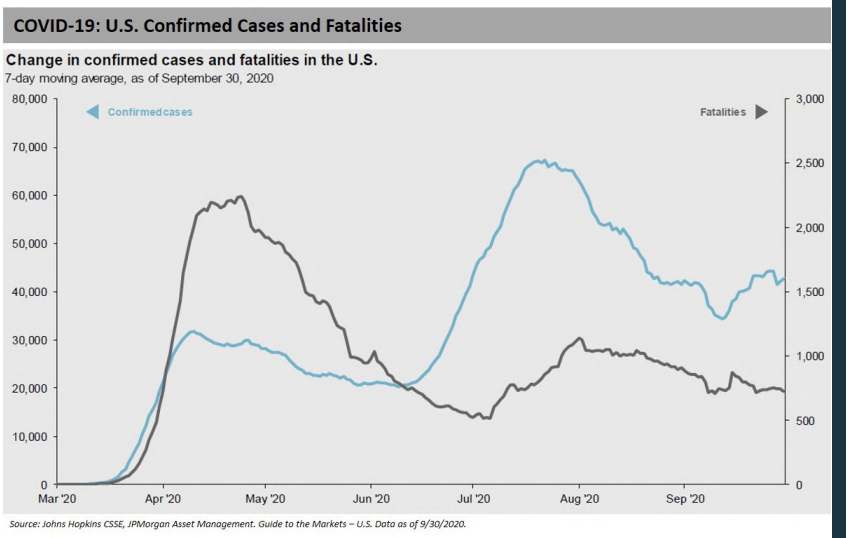
National debt. The elephant in the room. The Congressional Budget Office (CBO) thinks the federal debt will soar from 79% of Gross Domestic Product (GDP) last year to 189% of GDP in 2049, compared with its forecast of 144% a year ago, due to pandemic-related borrowing and Congress's increase in descretionary spending. Interest rates are projected to stay low, allowing government debt to continue to grow, which will likely result in weaker productivity and weaker US investment. The European Central Bank cut its short-term interest rate to below zero in 2014, with the Bank of Japan doing the same thing in 2016, and they are still struggling to get inflation back to 2%. Inflation that is chronically too low remains a perplexing challenge to central banks, which have an easier time fighting inflation when it's too high.

Updates on the Election - Washington to Wall Street. It is unlikely stimulus will be passed before the election. PPP funding has $130 billion left over, which may be utilized in the stimulus package. Voter turnout in 2016 was only 57%, which means an increase in voter turnout could be pivotal. Eighty percent of voters say the economy is the number one factor in determining how they will vote.

Candidate Joe Biden's tax plan would roll back some of President Trump's corporate tax cuts from 21% to 28%, which in theory might trim the value of stocks 5% or so. The tax increases are coming at a time when many firms have carry-forward losses that could run for years, which could limit the impact of increased taxes (*Fidelity Funds Monitor*, 9/20). For those earning more than $400,000, candidate Biden plans to restore the top personal tax bracket from 37% to 39.6%. There is also a possible increase in capital gains tax from 20% to 39.6%, which could create some pressure on the markets at year-end (*Forecasts & Strategies,* Mark Skousen, 9/20). For more on the election see page 5.

Dr. David Kelly, Chief Global Market Strategist at JPMorgan, said not to take too much of a bet during the presidential election. The most important impact for the election is to get a decisive victory that can be settled within 48 hours vs. a drawn out outcome causing uncertainty. Should we get a sweep either way, it will likely result in a major stimulus package which, long-term, could be inflationary. Regarding a tax increase, Dr. Kelly believes any tax increase would not happen in 2021, but rather in 2022. Our national debt has increased by $4.2 trillion, so eventually taxes will need to increase to pay for it, but only when our economy recovers. Increasing taxes too soon or too much can be detrimental to our economy.

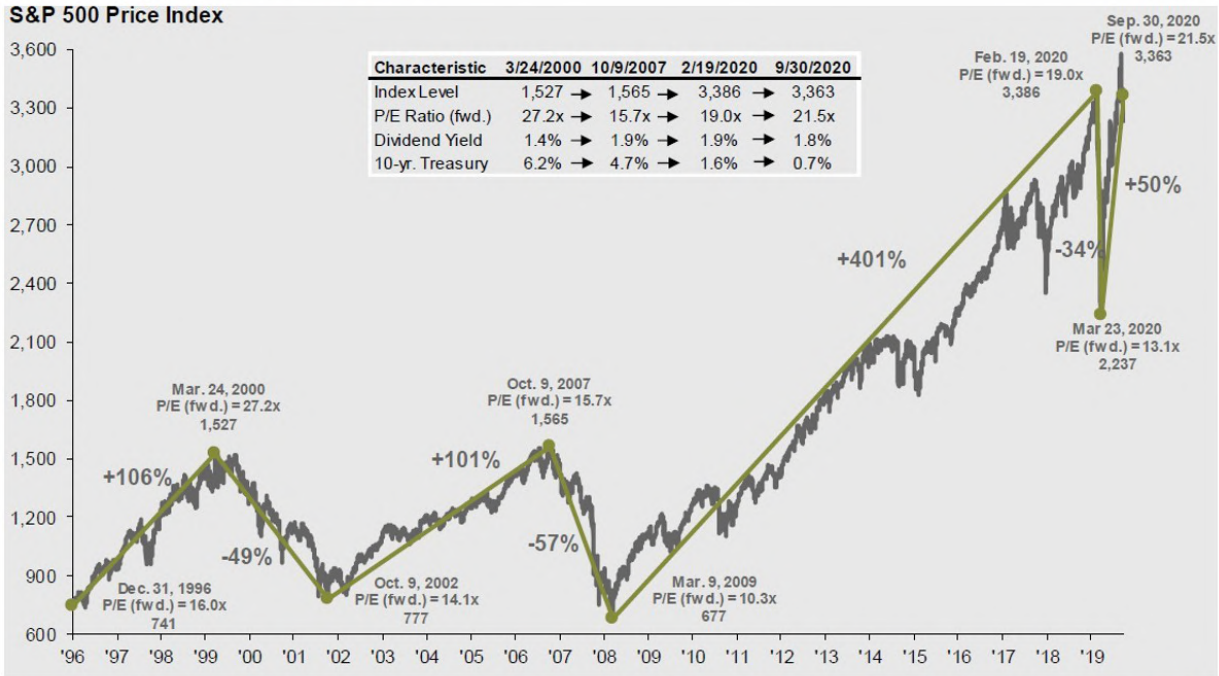
Dr. Kelly summarizes the COVID-19 economy as a slump, a bounce, a crawl and a surge, once we have a vaccine. He stated that citizens who become infected with coronavirus from ages 70-79 have a 5% mortality rate if they are male and 2% if they are female; the primary reason President Trump was taken to the Walter Reed Medical Center after contracting COVID-19. Daily new cases of COVID-19 are rising once again in the U.S., partially due to rising case counts in the Midwest. However, the chart below shows we remain below the peak levels in late July.



In summary, expect volatility ahead, with the election around the corner. We suggest the average investor stay the course, primarily due to the Fed outlook of lower for longer interest rates. As they say in the investment business, "Don't fight the Fed." For more on the markets, visit our website at **www.spectruminvestor.com** and click on Resources to access weekly and monthly economic updates from market strategists.

S&P 500 Index at Inflection Points: The chart below illustrates the performance history of the S&P 500 from 1996 to 9/30/20. As of 3/23/20, the S&P had dropped 30%, but recovered, down 8% as of 6/30/20. The S&P finished up 5.6% as of 9/30/20. As of 2/19/20, the 10-year Treasury was 1.6% and is now down to 0.7% as of 9/30/20, which compares to the dividend yield of the S&P 500 of 1.8%. The current yield on stocks is higher than the yield on bonds, which favors stocks (see chart inset).

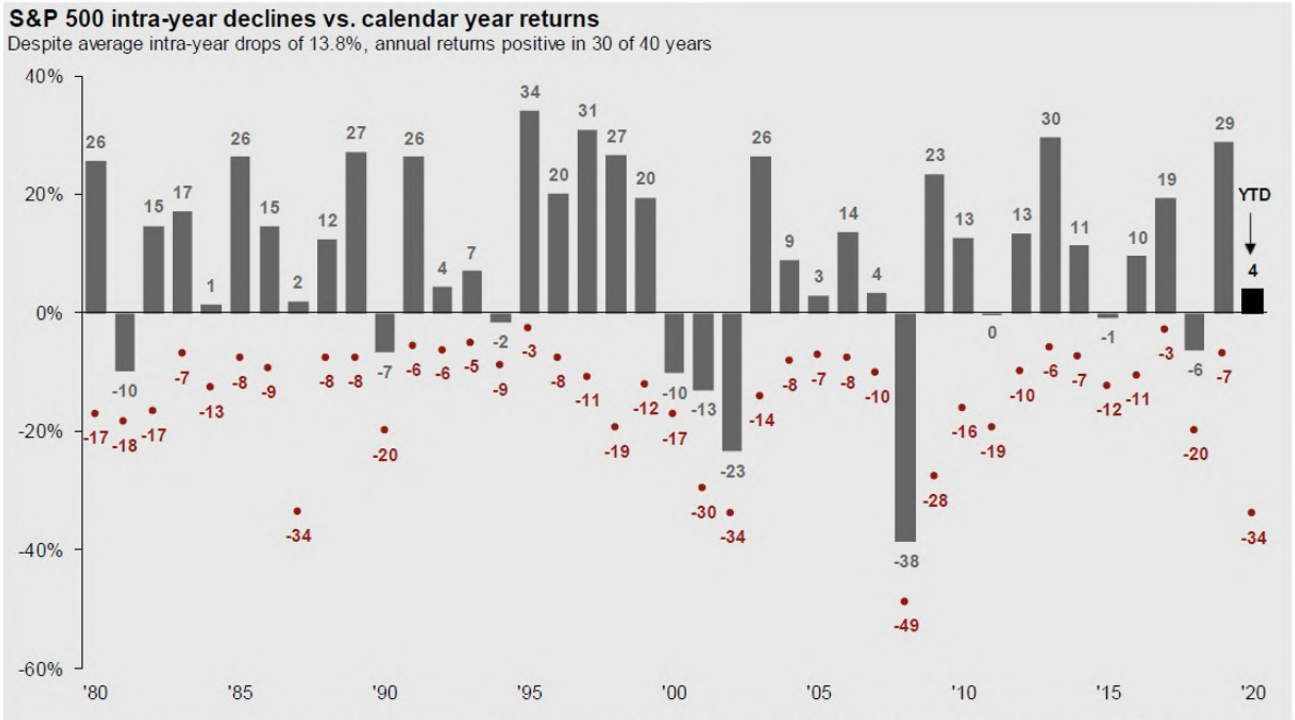
S&P 500 Index at Inflection Points



Source: Compustat, FactSet, Federal Reserve, Standard & Poor's, J.P. Morgan Asset Management. Dividend yield is calculated as consensus estimates of dividends for the next 12 months, divided by most recent price, as provided by Compustat. Forward price to earnings ratio is a bottom-up calculation based on the most recent S&P 500 Index price, divided by consensus estimates for earnings in the next 12 months (NTM), and is provided by FactSet Market Aggregates. Returns are cumulative and based on S&P 500 Index price movement only, and do not include the reinvestment of dividends. Past performance is not indicative of future returns. See benchmark disclosures Guide to the Markets – U.S. Data as of 9/30/2020.

Annual Returns and Intra-Year Declines: The chart below illustrates the year-end return of the S&P 500 Index vs. the intra-year declines for the past 40 years. As of September 30, 2020, the S&P was up 4% as investors battle between the opposing impacts of the coronavirus pandemic and unprecedented stimulus. According to JPM, the stock market historically finished up during 75% of calendar years. This chart can help a long-term investor understand the volatility of the market, and why, in most cases, we believe the best thing to do is stay the course.

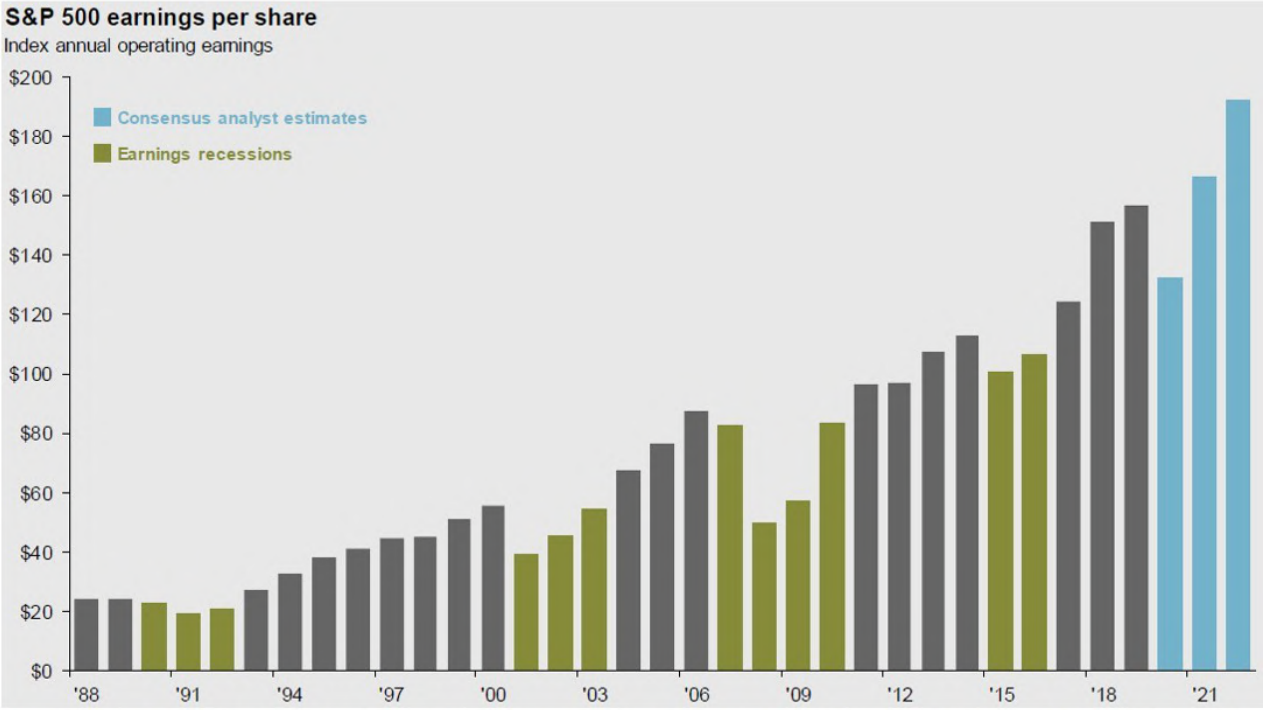
Annual Returns and Intra-Year Declines



Source: FactSet, Standard & Poor's, JPMorgan Asset Management. Returns are based on price index only and do not include dividends. Intra-year drops refers to the largest market drops from a peak to a trough during the year. For illustrative purposes only. Returns shown are calendar year returns from 1980 to 2019, over which time period the average annual return was 8.9%. Past performance is not indicative of future results. See benchmark disclosures. Guide to the Markets – U.S. Data as of September 30, 2020.

Corporate Profits: In addition to interest rates and the Federal Reserve, a key indicator of the market is earnings. According to FactSet (10/2/20), the earnings on the S&P 500 as of 2020 are projected to decline 18%. However, as the light blue bars illustrate, the earnings projection for the S&P 500 for 2021 is up 25.7%, which favors stocks.

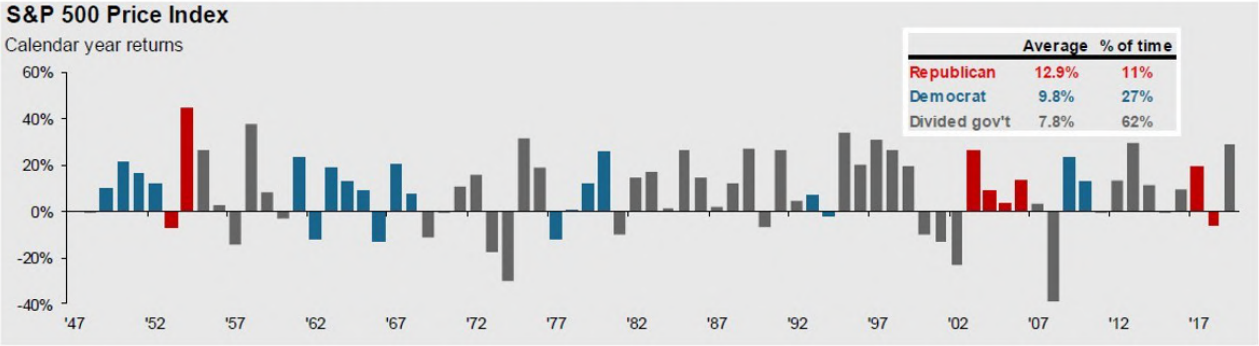
Corporate Profits

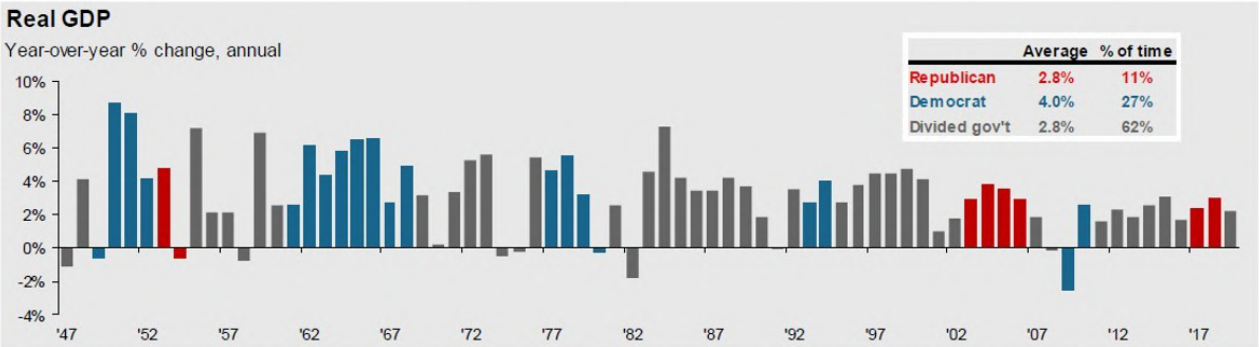


Source: Compustat, FactSet, Standard & Poor's, JPMorgan Asset Management. Historical EPS levels are based on annual operating earnings per share. Earnings estimates are based on estimates from FactSet Market Aggregates. Past performance is not indicative of future returns. See benchmark disclosures. Guide to the Markets – US Data as of 9/30/2020

Government Control, the Economy and the Stock Market: The average return of the S&P 500 since 1947 is 12.9%, with a Republican president and a Republic-controlled Congress (11% of the time). With a Democratic president and a Democratic-controlled Congress, (27% of the time) the average return of the S&P 500 since 1947 is 9.8%. A divided government averaged a return of 7.8% (62% of the time). **GDP growth** since 1947 averaged 2.8% (11% of the time), with a Republican president and a Republican-controlled Congress. GDP growth averaged 4.0% (27% of the time) with a Democratic president and Democratic-controlled Congress. In a divided government, the GDP growth averaged 2.8% (62% of the time).

Government Control, the Economy and the Stock Market





Source: FactSet, Office of the President, JPMorgan Asset Management; (Top) Standard & Poor's; (Bottom) Bureau of Economic Analysis. Top chart shows S&P 500 price returns. See benchmark disclosures. Guide to the Markets – U.S. Data as of 9/30/2020.

In Other Words

Presidential Elections and the Markets

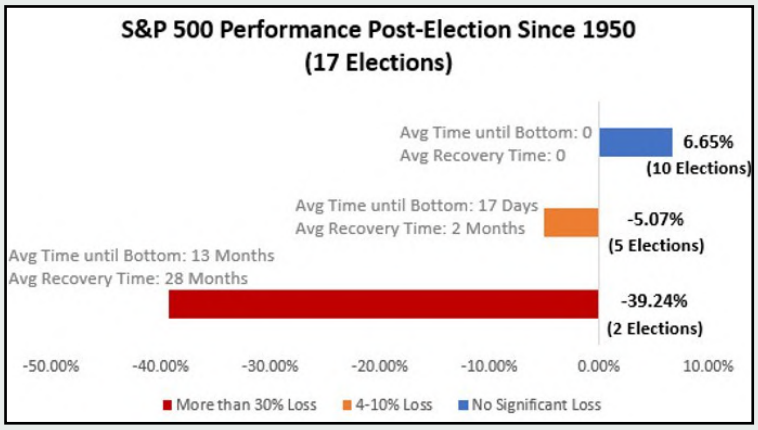
Angie Franzone | Newsletter Editor

As I sit down to write this article I am joined by my two 9-year-old daughters, currently attending virtual school and continually interrupting me to request a snack, give me a play by play of every background conversation happening on the Zoom call and to let me know that someone keeps putting their mouth over the camera and it's distracting. Gee, what's it like to be distracted... Is there an in-person mute button I can press?

The year 2020 has been challenging to say the least and emotions are running high, throw a presidential election in the mix and it can feel almost too overwhelming to handle. The key is not to let a pandemic or a looming election affect your investment decisions. You are investing for the long-term, so stay focused on your financial goals, investment time-frame and risk tolerance.

Famed investor Benjamin Graham has been credited with saying, "In the short-run, the market is a voting machine. In the long-run, it's a weighing machine." What this means is that in the short-term, markets react to news, such as the election of a new president, but in the long-term they follow the fundamentals of investing. Markets don't like uncertainty and it doesn't get much more uncertain than who the next president will be, but the volatility caused by this uncertainty is often short-lived.

According to Hartford Funds' 2020 Election Survey, 45% of investors said they plan to make changes to their investments because of the election. If we look back in history, however, making changes solely based on an election may not be in your best interest. Since 1950 there have been 17 presidential elections. As the chart below illustrates, 10 of them did not see an immediate negative stock market response following the election. In five cases, the S&P 500 declined by an average of 5% within 17 days following the election, with four of them recovering the loss within a month and the other recovering within six months. The remaining two elections (2000 and 2008) saw major declines unrelated to the presidential election; the reason for those declines being the tech bubble burst of the early 2000s and the financial crisis of 2008-2009.



While past performance is not an indication of future results, **historically speaking, regardless of whether a Republican or Democrat won the election, US stocks have trended up.** As Dr. David Kelly, Chief Global Strategist at JPMorgan stated, "Please don't let how you feel about politics dictate how you feel about investing." Knowing that there will be volatility no matter who is elected and being prepared for it, is half the battle. Whether it is an election year or not, you should always have a long-term investment strategy when it comes to planning for your retirement. Stick to the things you can control, such as how diversified you are. What drives your investment decisions should be personal considerations like how long you have to invest before you retire, your investment goals and your risk tolerance, regardless of who the next president will be.

If you take anything away from this article, let it be this:

- Expect volatility and prepare for it with a plan
- Don't let election predictions drive your investment decisions
- Stick to your long-term investment strategy and stay invested

If you are concerned about your investments, be proactive and talk to an advisor at Spectrum who can help. Making a plan and diversifying your portfolio can help keep you from reacting to every new headline that pops up on your screen. Just think, the less time spent on worrying about your retirement plan, the more time you have to learn how to do "new math" instead of staring blankly at your children when they ask for help. Seriously though, Math starts in 10 minutes and I've got to get back to class.

Stay safe and be well.

Spectrum Investor® Update

Morningstar Category Averages	3rd Qtr	1 Year	3 Year
Intermediate-Core Bond	0.94%	6.65%	4.88%
Allocation 50%-70% Equity	4.85%	6.26%	5.70%
Large Cap Value	4.88%	-4.41%	2.61%
Large Cap Blend	8.06%	10.70%	9.54%
Large Cap Growth	11.54%	32.21%	18.22%
Mid Cap Value	4.34%	-10.31%	-1.16%
Mid Cap Blend	6.32%	-0.51%	3.40%
Mid Cap Growth	10.10%	24.22%	14.60%
Small Cap Value	2.99%	-14.21%	-5.49%
Small Cap Blend	4.17%	-6.57%	-0.86%
Small Cap Growth	8.21%	18.72%	11.11%
Foreign Large Cap Blend	5.77%	2.09%	0.41%
Real Estate	2.20%	14.22%	1.13%
Natural Resources	8.85%	1.42%	-1.73%

Source: Morningstar, 3 yr return is annualized. Morningstar classifies categories by underlying holdings and then calculates the average performance of the category. Past performance is not an indication of future results. Returns in Blue = Best, Returns in Red = Worst. Please see Benchmark Disclosures on pg. 6.

DOW: 27,781
NASDAQ: 11,092
S&P 500: 3,363
10 Yr T-Note: 0.68%
Inflation Rate: 1.4% (9/20)
Unemployment Rate: 7.9%

Data as of 09/30/20 unless otherwise noted. The Dow Jones Industrial Average is comprised of 30 stocks that are major factors in their industries and widely held by individuals and institutional investors. The S&P 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. The NASDAQ Composite Index measures all NASDAQ domestic and non-U.S. based common stocks listed on The NASDAQ Stock Market. Barrel of Oil: West Texas Intermediate. Inflation Rate: CPI. The market value, the last sale price multiplied by total shares outstanding, is calculated throughout the trading day, and is related to the total value of the Index. Indices cannot be invested into directly.

To determine which investment(s) may be appropriate for you, consult your financial advisor prior to investing. All performance referenced is historical and is no guarantee of future results. All indices are unmanaged and cannot be invested into directly.

Spectrum Wealth Management

Year End Checklist

Brian White, CFP® | Wealth Manager

Remember Mad Libs? You know, that game where you give a random verb, noun, adverb or adjective, then insert it into a sentence? Let's try it: The year 2020 is going to go down in history as one of the most [insert adjective] years in history.

Individuals across the globe are ready to move on to 2021, and with good reason. Before we start thinking about those New Year's resolutions and travel plans, consider a few areas of your personal finances that need to be reviewed before year-end.

Required Minimum Distributions

To begin, we're going to give you something you DON'T need to do. The CARES act, which was signed into law on March 27, suspended Required Minimum Distributions (RMDs) for IRAs and retirement plans for 2020. Prior to the CARES act, individuals had to annually take out a certain percentage of their IRA accounts after turning 72. For the 2020 year, this requirement has been suspended. Also, any inherited or beneficiary retirement accounts fall under the same laws. As of the publication date of this newsletter, there's no indication that this temporary suspension will continue into 2021.

This is good news for those individuals who do not need the additional taxable income for this year. For anyone who did their tax planning based on the distribution from their IRA, they should consider a Roth IRA conversion for that amount. Converting investments to a Roth IRA still generates taxable income, but it allows those investments to grow tax-free. Those individuals who are hoping to pass on their IRA accounts to future generations should look to a Roth IRA as their account of choice.

Tax Planning/Charitable Giving

The next area we should be thinking about is taxes. The stock market roller coaster we've been on has given many mutual fund managers opportunities to harvest losses. There may also be gains, depending on the area of the market the investment was in. Interest rates are at all-time lows, so fixed income investments may not be paying as much in interest. We still have three months to go, with an election in the middle. Capital gains, dividends and interest income could certainly be less than 2019, so it may be a good year to consider taking more capital gains. All decisions regarding the tax implications of your investments should be made in consultation with your independent tax advisor or estate planning attorney. Spectrum is not a tax advisor or estate planner.

In the September 2019 newsletter, we talked about different ways to give to charitable organizations. Be sure to visit our website at www.spectruminvestor.com, under resources, to review the information in that newsletter. As we talked about earlier, the RMD has been suspended for 2020. While you're not required to withdraw funds from your IRA or retirement account, you're still able to. The Qualified Charitable Distribution (QCD) allows individuals to gift assets to a charitable organization directly from their IRA. The QCD is still available in 2020, but there may be better options for this year. Consider a gift of appreciated stock (if available) at year-end.

IRS Indexed Limits for 2020:
401(k), 403(b), 457 Plan Deferral Limit is $19,500.
Catch-up Contribution limit is $6,500. Source: www.irs.gov

Budget

Did you create a budget for 2020? If so, how much has that changed? People are spending less on travel and entertainment, but may also have reduced income. In some cases, they've substituted line items on their budget, such as replacing a vacation with a home renovation. Working from home wipes out any commuting costs, but Internet access needs to be upgraded. Where do we go from here? To begin, don't throw out the idea of maintaining a budget. A budget is a basic tenet of financial planning, especially for those in retirement. By having a flexible budget in place, you're much more likely to be able to reach your financial goals.

One of the most important parts of a budget belongs to health care costs. This time of year can be important to individuals who need to update their employee benefits options. Retired individuals are renewing their Medicare Supplement or Advantage plans. Many of us will be making choices about health insurance coverage as well as the different options for putting aside money for health care costs.

According to a PriceWaterhouseCoopers Health Research Institute (HRI) survey, 5% of American consumers used a virtual health visit for the first time this year. Of those users, 88% said they would use it for future visits. This 'Telehealth' is a lower-cost alternative for health care and is saving individuals money while providing a safer alternative to traditional office visits. A reduction in health care costs for 2020 could mean that there are additional funds in a Flexible Spending Account (FSA) that need to be spent or they will be lost. If you have a Health Savings Account (HSA), you're not required to spend the balance of the account in a calendar year. Be sure to check your spending levels to make sure you're not in danger of losing funds OR have been able to maximize your savings.

Benchmark Disclosures: Morningstar Category Averages: *Morningstar classifies mutual funds into peer groups based on their holdings. The Category Average calculates the average return of mutual funds that fall within the category during the given time period. The following indexes and their definitions provide an approximate description of the type of investments held by mutual funds in each respective Morningstar Category. One cannot invest directly in an index or category average.* ***Intermediate-Term Bonds: Barclays US Agg Bond Index****–Measures the performance of investment grade, US dollar-denominated, fixed-rate taxable bond market, including Treasuries, government-related and corporate securities, MBS, ABS and CMBS.* ***Allocation 50%-70% Equity****–These funds invest in both stocks and bonds and maintain a relatively higher position in stocks. These funds typically have 50%-70% of assets in equities and the remainder in fixed income and cash.* ***Large Cap Value: S&P 500 Value Index****–Measures the performance of value stocks of the S&P 500 index by dividing into growth and value segments by using three factors: sales growth, the ratio of earnings change to price and momentum.* ***Large Cap Blend: S&P 500 Index****–A market capitalization-weighted index composed of the 500 most widely held stocks whose assets and/or revenue are based in the US.* ***Large Cap Growth: S&P 500 Growth Index****–Measures the performance of growth stocks drawn from the S&P 500 index by dividing it into growth and value segments by using three factors: sales growth, the ratio of earnings change to price and momentum.* ***Mid Cap Value/Mid Cap Growth: S&P MidCap 400 Index****–A market cap weighted index that covers the complete market cap for the S&P 400 Index. All S&P 400 index stocks are represented in both and/or each Growth and Value index.* ***Mid Cap Blend: S&P MidCap 400 Index****–Measures the performance of mid-sized US companies, reflecting the distinctive risk and return characteristics of this market segment.* ***Small Cap Value: Russell 2000 Value Index****–Measures the performance of small-cap value segment of Russell 2000 companies with lower price-to-book ratios and lower forecasted growth values.* ***Small Cap Blend: Russell 2000 Index****–Measures the performance of the small-cap segment of the US equity universe. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership.* ***Foreign Large Cap Blend: MSCI EAFE NR Index****–This Europe, Australasia, and Far East index is a market-capitalization-weighted index of 21 non-US, developed country indexes.* ***Small Cap Growth: Russell 2000 Growth Index****–Measures the performance of small-cap growth segment of Russell 2000 companies with higher price-to-value ratios and higher forecasted growth values.* ***Real Estate: DJ US Select REIT Index****–Measures the performance of publicly traded real estate trusts (REITs) and REIT-like securities to serve as proxy for direct real estate investment.* ***Natural Resources: S&P North American Natural Resources Index****– Measures the performance of US traded securities classified by the Global Industry Classification Standard (GICS) as energy and materials excluding the chemicals industry and steel but including energy companies, forestry services, producers of pulp and paper and plantations. Past performance is no guarantee of future results. This report is for informational purposes only and should not be construed as a recommendation or solicitation to buy or sell any security, policy or investment.* ***PE Ratio*** *is the measure of the share price relative to the annual net income earned by the firm per share.*