PLANNING POINTS...

Second Quarter 2020

Index	2019	YTD 6/30/20	Avg. Annual Return Since 12/31/01
S&P 500	31.5%	-3.1%	7.7%
Dow Jones Industrial Average	25.3%	-8.4%	7.9%
NASDAQ	35.2%	12.1%	9.3%
Russell 2000	25.5%	-13.0%	7.5%
MSCI EAFE	22.0%	-11.3%	5.1%
BBG Barclays US Aggregate Bond	8.7%	6.1%	4.7%
FTSE 3 Month US T-Bill	2.3%	.5%	1.3%

STOCK MARKET REVIEW

It seems every quarter for a while now we write about records, whether they be about volatility levels, all-time highs (stocks) or all-time lows (yields). Markets have kept investors on their toes for well over 2 years.

The second quarter for stocks began near the lows recorded on March 23rd and have since sprinted remarkably higher unabated by much of anything. In fact, during the quarter, the S&P 500 chalked up its strongest 50-day move (+39.3%) since 1952.

For Q2, the NASDAQ and small cap stocks (Russell 2000) led the way, returning 30.6% and 25.4% respectively. The S&P 500 was up almost 21% and international stocks (EAFE) lagged, despite a strong finish, with a gain of 14.9%. In spite of solid returns for the quarter, performance was not broad-based.

As we wrote in the last *Planning Points* newsletter, "the economic toll (virus, oil, etc.) is significant, but the magnitude and duration of the impact is unknown". After 3 months, we still feel the same. Interestingly, the stock market as a leading economic indicator appears to be discounting something else or perhaps markets are not functioning efficiently, which is a common and expected occurrence in the short run.

Corporate earnings forecasts for the next several quarters have plummeted and unemployment has skyrocketed. Many industries are facing devastation and may become obsolete. Throughout the country states, municipalities and citizens are stretched and will continue to face significant financial hardship. In spite of the crisis, the stock market has paid no heed and instead advanced to near all-time highs, providing another example of why we should avoid making decisions (or timing the market) based on headlines.

The market is also a forward-looking machine that discounts all information, so even on a day when the worst jobless claims number in history was reported, the stock market gained 6%.

Some widely followed measures of stock valuations, whether they be based on a function (or a multiple) of earnings, sales, cash or book value, are higher than they were at the market peak in February. In an environment of elevated uncertainty, how can this be?

We do not have all of the answers, but liquidity and stimulus from the government is coming out of a firehose with what appears to be an endless tank of water. With interest rates near all-time lows and almost zero on the short end, we believe investors, including institutional investors like pension plans, insurance companies, and foundations, have no choice but to invest in stocks because alternatives like bonds, CD's and cash are lousy.

As we expected, volatility moderated during the quarter to about a third of its excessive peak in March. We continue to expect volatility to remain high through the election and have raised our antennae for the possibility of much higher capital gains tax rates.

In the last newsletter, we suggested that if your stock allocation has dropped below your target, consider adding to stocks in a prudent fashion. However, as a result of the impressive performance recently and elevated valuations, we now caution investors to review their stock allocation and tap the brakes if their allocation is now above their target. Amazing times!

BOND MARKET REVIEW

Volatility has moderated significantly in the bond market compared to the first quarter and interest rates have flatlined to historically low levels. Most bond market participants, practitioners, theorists, etc. would have never envisioned rates at these levels, let alone consider the impact of negative interest rates.

10-year U.S. bond yields started the year at 1.92%, finished the first quarter at .70% and stagnated to finish at .65% for 2Q. Allow me to repeat…10-year U.S. bonds are yielding .65%! Even a 30-year bond, yielding 1.40% pales in comparison to inflation rates. The flight to safety has been historical and the rush to buy bonds and hold cash has cratered yields.

Repeating our thoughts from the last *Planning Points*, "our expected returns for bonds for the future has fallen significantly." We suggest opportunities exist for investors willing to assume a reasonable amount of credit risk, but recommend limiting interest rate risk.

10 THINGS YOU SHOULD KNOW ABOUT NEGATIVE INTEREST RATES - Hartford

A central bank is responsible for setting a nation's monetary policy. To encourage lending and spending, the US Federal Reserve (Fed) has set interest rates at nearly zero to make borrowing inexpensive. But to support the economy even more through the COVID-19 pandemic, there's debate about whether the Fed should introduce a controversial policy—negative interest rates—to incentivize spending that much more.

It's all about reaching goals: A central bank's ultimate goals are to keep the country's currency and economy stable and to maintain a healthy employment rate. By raising or lowering interest rates, central banks such as the Fed can impact those goals by influencing a country's money supply.

A tool that works two ways: If the Fed is concerned that rapid economic growth will lead to high inflation, it can raise interest rates—make it more expensive to borrow money—in an effort to slow spending. If the economy needs support, lowering rates can help encourage spending and business investment. For example, the Fed reduced rates to near zero after the Global Financial Crisis, started raising them in 2015 as the economy's recovery took hold, then lowered them again during the COVID-19 pandemic when the economy shut down.

Desperate measures: In extreme circumstances, central banks can even push interest rates below zero. While they've never been used in the US, the European Central Bank and the Bank of Japan have had negative interest rates for several years as part of their recovery from the Global Financial Crisis.

Isn't it automatically bad when something is negative? In theory, negative rates are meant to keep money flowing in the economy by making it more beneficial to spend money than to save it. Another way of looking at it is a little pain now in exchange for a potential long-term gain in the form of an economy that keeps growing.

So wait, negative rates can actually be a good thing? Negative rates could be beneficial for businesses and some consumers since it drives the interest rates on mortgages and loans to rock bottom—or even pays them to borrow money. Essentially, negative rates make for a good time to invest in big purchases that need to be financed.

But not everyone benefits: Banks may choose to eat the cost of negative rates rather than pass it on to consumers as a fee for depositing money with them. But even so, interest rates would be so low that savers could actually lose money by keeping it in the bank, especially after factoring in inflation. Bondholders may also lose out—a bond with a negative yield wouldn't pay back enough interest to cover the original purchase price.

However, bonds would still be an important investment: Even if rates in the US were negative, US government debt is still considered a high-quality, "safe haven" investment. Low or negative rates don't negate creditworthiness.

Negative rates abroad could actually pay for US investors: There's currently more than $12 trillion of negative-yielding debt in global market. But professional money managers may have the skill and experience to turn that negative into a positive by applying currency hedging to potentially generate positive returns for US bond investors.

You won't find negative rates in your macroeconomic textbook: There's debate as to the effectiveness of negative rates. It's a very modern strategy—in 2014 the European Central Bank was the first to cut short-term rates below zero. With such a limited history, it's difficult to determine whether or not it's been effective, making it a somewhat controversial tactic.

Unlikely to happen here, but worth understanding what the fuss is about: The Fed has consistently opposed pushing rates below zero. In light of Europe and Japan's experience, the concern is that the risks outweigh the reward in the US: Both banks and consumers could be too negatively impacted to reap the potential long-term benefits.

SPECUALTION SNAPSHOT

Toyota is over twice the size of Ford, GM and Chrysler combined. With a market capitalization of about $280 billion, Tesla Motors is 40% larger than Toyota, yet ranks 10th globally in sales with near 1% market share.

We are pleased to announce the addition of Natalie Methner, Client Concierge, to our dedicated and experienced team. Natalie brings 5 years of prior financial industry expertise to our team, with nearly two years with Raymond James. She holds several insurance licenses and is pursuing additional licenses in the financial industry.

Natalie and her husband, Ryan, along with their boys Jack and Tyler, enjoy traveling, boating, and sports. She is an active member and Concessions Coordinator for the Mount Pleasant Oilers Athletics Sports Boosters. Natalie earned her Bachelor of Science Degree in Marketing at the University of Wisconsin - La Crosse.

Natalie joins Gavin & Associates already trained in many of the systems and processes we currently utilize. In addition, her marketing/social media proficiency and experience with compliance and regulations are complementary skills. Her responsibilities will be similar to those of Nora and Stacey, providing administrative support to the office, handling client requests, and supporting Michael and Dan. She is committed to placing the best interests of our clients first and maintaining strict confidentiality in all of her functions.

As a valued client, we know that you expect a high degree of professionalism, integrity and experience from our team. To maintain our reputation as a premier financial services firm in the region, we recognize the importance of carefully selecting and retaining the best suited associates for our team. Natalie's enthusiasm, industry knowledge, and professionalism has been warmly received by our team and clients.

Please welcome Natalie to *your* team!

WEDDING ANNOUNCEMENT

We are delighted to announce that Stacey's oldest daughter, Lyndsay Hill, will soon be celebrating marriage with Nate Schweers. The new bride and groom will reside in Des Moines, Iowa. Lyndsay currently works as a pharmaceutical tech and Nate is currently a MLB scout and acquiring a second job as a property manager.

We have seen Lyndsay grow into a wonderful woman and are super excited about her future. Please congratulate Stacey for this fantastic news.

AND A BIG THANK YOU!

Earlier this spring, Gavin & Associates announced an incentive match program exclusively for our clients partnering with United Way of Midland County to raise funds for the ALICE population in our community. In spite of so much uncertainty and upheaval in our local community, and with the tremendous support of you, together we raised over **$16,500** in desperately needed funds. Thank you very much!

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The S&P 500 Index Total Return is a broad-based measurement of changes in stock market conditions based on the average performance of 500 widely held common stocks. It consists of 400 industrial, 40 utility, 20 transportation, and 40 financial companies listed on U.S. market exchanges. This is a capitalization-weighted calculated on a total return basis with dividends reinvested. It represents about 75% of the NYSE market capitalization.
The Dow Jones Industrial Average Total Return covers 30 major NYSE industrial companies. The Dow represents about 25% of the NYSE market capitalization and less than 2% of NYSE issues. It is a price-weighted arithmetic average, with the divisor adjusted for stock splits. This Index includes the effects of reinvested dividends.
The Russell 2000 (TR) Index - The Russell 2000 Index covers 2000 of the smallest companies in the Russell 3000 index, which ranks the 3000 largest U.S. companies by market capitalization. The Russell 2000 represents approximately 10% of the Russell 3000 total market capitalization. This Index includes the effects of reinvested dividends.
The NASDAQ covers 4500 stocks traded over the counter. Represents many small Composite index company stocks but is heavily influenced by about 100 of the largest NASDAQ stocks. It is a value weighted index calculated on price change only and does not include income.
The MSCI EAFE Net Dividend is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the United States & Canada. Approximates the minimum possible dividend reinvestment. The dividend is reinvested after deduction of withholding tax, applying the rate to non-resident individuals who do not benefit from double taxation treaties. MSCI Barra uses withholding tax rates applicable to Luxembourg holding companies, as Luxembourg applies the highest rates.
The Barclays Capital Aggregate Bond Composite index is a measure of the investment grade, fixed-rate, taxable bond market of roughly 6,000 SEC-registered securities with intermediate maturities averaging approximately 10 years. The index bonds from the Treasury, Government-Related, Corporate, MBS, ABS, and CMBS sectors
The FTSE 3 Month U.S. T-Bill Index is a measurement of the movement of 3-month T-Bills. The income used to calculate the monthly return is derived by subtracting the original amount invested from the maturity value.
Inclusion of these indexes is for illustrative purposes only. Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance. Individual investor's results will vary.

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