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Optimism Drives Stocks to New All-Time Highs in the 3rd Quarter

We hope that this letter finds you safe and healthy during these still-unprecedented times. As a reminder, this edition of The Weiss Report is mostly to highlight what has happened in the past quarter. For this reason, there is very little discussion on what is likely the biggest issue on all of our minds: The Election. While we briefly discuss the election below, should you want deeper discussion on the election and potential market fallout, please reach out to Lenny or Lowell at the office – we will happily schedule a chat.
2020 continued to be one of the most unpredictable years in memory, as markets rose to new all-time highs in the third quarter despite a resurgence in coronavirus cases. Stocks rallied thanks to a combination of even more accommodative Fed policy, hopes for a COVID-19 vaccine and a stronger-than-expected economic rebound, before markets declined moderately from those highs in mid-September.

The third quarter began with a resurgence of coronavirus cases in the United States, as new daily cases of COVID-19 smashed through levels seen in March and April, eventually topping out at a record 78,871 new cases on July 24th. But unlike March and April, stocks did not decline following the spike in new cases, as state governments enacted more surgical economic shutdowns instead of the wholesale lockdowns that occurred in the first half of the year. That change in strategy, combined with the fact that hospitalization rates and mortality rates of COVID-19 remained far below March and April levels, helped the stock market look past the increase in cases, and the S&P 500 rose 5.51% in July.

The rally continued in August, aided by the peak and subsequent decline of coronavirus cases in some of the largest U.S. states (California, Florida, and Texas). Additionally, despite the expiration of the CARES Act stimulus, U.S. economic data continued to improve throughout August, powering stocks higher. Finally, in late August the Federal Reserve formally announced the adoption of an "average inflation target," which effectively signaled the Fed would tolerate higher inflation in the economy more so than in recent history. That policy shift is a potentially longer-term bullish event for stocks as they are positively correlated to higher inflation. Led by gains in the tech sector, the S&P 500 hit a new all-time high in mid-August and the rally continued through month-end. The S&P 500 rose 7.01% in August and finished the month in solidly positive territory on a year-to-date basis.

The final month of the third quarter, however, provided a reminder that the macro-economic outlook remains uncertain and markets can still quickly become volatile. The tech rally in August was so relentless that it elicited comparisons by the financial media to the tech bubble of the 2000s. While that was somewhat hyperbolic, the pace of the gains in the tech sector simply wasn't sustainable. And in the first few days of September, the tech rally became exhausted, the Nasdaq peaked, and stocks began a correction process that would last for most of the month. From a catalyst standpoint, the initial declines were a function of buyer exhaustion, but there were also some incrementally negative events in September that weighed on stocks. First, it became evident that there would be no new economic stimulus bill in September, as both Democrats and Republicans remained far apart in negotiations. Second, economic data began to imply a "plateau" in the economic recovery. Finally, late in the month, coronavirus cases surged in Europe and began to move higher again in certain U.S. states, prompting some concern about a return to various levels of economic lockdown in Europe and the U.S. The S&P 500 declined modestly in September but remained solidly positive for the third quarter.

Looking forward, as we begin the final quarter of this historic year, the market correction of September helped to reset expectations about the numerous unknowns still facing investors in both the short and long-term. But while the September pullback was a reminder of potential market volatility, we start the final quarter of 2020 at more reasonable market valuations, historically speaking.

Q3 Market Performance Review: New All-Time Highs

The major U.S. stock indices all extended the rebound that began in the second quarter of 2020, and just like the previous two quarters, the tech-heavy Nasdaq outperformed the other major indices. Those gains were once-again driven by the performance of some of the largest, most-well-known tech companies in the world, as they are viewed as the longer-term beneficiaries of changing personal and professional behavior in response to the pandemic. Stocks such as Apple (AAPL), Amazon (AMZN), Google (GOOGL), and Netflix (NFLX) helped send the Nasdaq to new all-time highs in July, August, and early September.

By market capitalization, large-cap stocks outperformed small-cap stocks, a reversal from the second quarter. Large caps outperformed primarily because doubts remain about how quickly the U.S. economy will return to pre-COVID 19 levels, especially with the expiration of economic stimulus in late July. Since small caps are historically more sensitive to changes in broad economic growth, that uncertainty weighed on small-cap indices, although they still finished with a positive return for the quarter. From an investment style standpoint, growth outperformed value, yet again, because of strength in large-cap tech.

On a sector level, 10 of the 11 S&P 500 sectors finished with a positive return for the third quarter. As previously mentioned, tech outperformed, but so did consumer discretionary and materials sectors, as investors rotated into some of the hardest hit sectors in the market on the hope that coronavirus cases would continue to recede and people would venture back out into the economy, visiting malls and restaurants, and traveling sooner than previously expected.

Defensive sectors, those that are historically less sensitive to expected changes in the economy such as utilities, consumer staples, and healthcare, lagged the S&P 500 in the third quarter, although they all posted solidly positive quarterly returns. The only S&P 500 sector to finish with a negative return in the quarter was energy as investors continued to worry about future global demand in the context of still-elevated oil supplies.

US Equity Indexes	Q3 Return	YTD
S&P 500	8.93%	5.57%
DJ Industrial Average	8.22%	-0.91%
NASDAQ 100	12.62%	31.65%
S&P MidCap 400	4.65%	-8.97%
Russell 2000	4.93%	-8.69%

Source: YCharts

International markets rallied in the third quarter as European and Asian economies continued to re-open. But many foreign developed markets closed well off the highs of the quarter as coronavirus cases spiked in parts of Europe, particularly in Great Britain. Emerging markets outperformed foreign developed markets thanks to a continued decline in the U.S. dollar paired with strength in Asian markets, as the coronavirus outbreak remains broadly contained in that region of the world.

Commodities also moved higher in the third quarter thanks to a declining U.S. dollar, combined with cautious optimism for an eventual global economic rebound. Oil prices were volatile in the third quarter but still finished with a positive return as OPEC maintained discipline on supply cuts which helped offset concerns about global oil demand expectations. Gold, meanwhile, added to the gains of the second quarter thanks to the aforementioned weakness in the U.S. dollar, still-recovering inflation expectations and steady bond yields amid the historic global central bank stimulus.

Switching to fixed income markets, the total return for most bond classes was again positive in the third quarter, as bonds now have realized a positive return for each quarter so far this year. The leading benchmark for bonds, the Bloomberg Barclays US Aggregate Bond Index, saw slightly positive returns in third quarter marking the eighth consecutive quarterly gain.

Longer-duration bonds again outperformed those with shorter durations in the third quarter as global central banks (including the Federal Reserve) reiterated that rates would stay low for years to come. That anchored shorter-duration bonds, and in turn increased the appeal of higher-yielding, longer-maturity bonds.

Corporate bonds again saw solidly positive returns in the third quarter thanks to the better-than-expected economic recovery. High-yield bonds outperformed investment-grade bonds during the quarter, reflecting surprisingly strong corporate commentary during the most-recent earnings season combined with optimism that a continued decline in coronavirus cases would help business continue to recover.

Fourth Quarter Market Outlook

Markets and the economy have staged a historic rebound since the late March lows, and while we all welcome this impressive comeback, we enter the final quarter of the year keenly aware that some of the biggest unknowns for the markets and the economy will be resolved positively or negatively in the next three months.

Starting with the obvious, November 3rd is Election Day, and apropos for 2020 this election will be one of the most uncertain in our lifetimes. Beyond the most important question, "Who will win the Presidency?" markets are also focused on whether the Democrats will be able to take control of the Senate. If so, and Biden wins the Presidency, Democrats would control both the legislative and executive branches of government, a scenario dubbed the "Blue Wave" by the financial media. Such a scenario would result in the increased potential for policy changes which would likely create short-term market volatility.

However, any near-term volatility associated with a Blue Wave would likely be small compared to the worst-case scenario for the election, namely that there is no clear winner by the end of Election Day and the election becomes contested which would result in the entire country being dragged through a similar episode of Bush vs. Gore in the early 2000s. In that outcome, we should expect significant short-term market volatility until a winner is declared, potentially as late as mid-December.

Unfortunately, the election is not the only source of potential uncertainty and volatility coming in the next three months. Hopes for a COVID-19 vaccine have helped stocks rally to current levels, and there are now three separate vaccines undergoing final Phase III trials. Those trials will likely reach their conclusion in the coming weeks, perhaps before the election. If those trials fail to produce a viable vaccine candidate, that will also create volatility as markets are expecting widespread COVID-19 vaccine distribution by early to mid-2021.

Finally, by the end of the fourth quarter, investors will learn the fate of the stimulus bill currently stuck in Congress. There's near-universal agreement the economy could use more stimulus, but the politics of the election, combined with Republican and Democrat differences about how much money should be spent and where that money should go, have prevented stimulus from being passed and delivered to the U.S. economy. Markets expect a stimulus bill to pass by year-end, and if that fails to materialize, it will create more volatility.

Bottom line, the resiliency of the U.S. economy and markets is both admirable and encouraging, as the economic and market recovery from the worst pandemic in 100 years has been nothing short of extraordinary. That rebound verifies the value of sticking to a well-constructed, diversified financial plan aimed at achieving long-term investment goals.

However, our experience has taught us not to be complacent simply because the market has been resilient. So, while we have all welcomed the strong market rebound in Q2 and Q3, the fact remains that a lot of important unknowns will be resolved in Q4, and because of that, there is the possibility for more market volatility during the final three months of 2020.

While short-term volatility might reappear between now and year-end, the markets in 2020 have once again demonstrated that a long-term approach combined with a well-designed and well-executed investment strategy can overcome periods of elevated volatility, market corrections, bear markets and even global pandemics.

We understand the risks facing both the markets and the economy, and we are committed to helping you effectively navigate this challenging investment environment. Successful investing is a marathon, not a sprint, and even intense volatility like we experienced in the first half of this year is unlikely to alter a diversified approach set up to meet your long-term investment goals.

Therefore, it's critical for you to stay invested, remain patient, and stick to the plan, as we've worked with you to establish a unique, personal allocation target based on your financial position, risk tolerance, and investment timeline.

Finally, we thank you for your ongoing confidence and trust and please rest assured that our entire team will remain dedicated to helping you successfully navigate this market environment.

Enclosure #1 – Our first enclosure is the Investment Strategy Quarterly piece from Raymond James. This provides a quick understanding of relevant themes in the investment world. Additionally it provides an economic snapshot as well as a tactical outlook. We like to include this in the Weiss Report as a handy two-page reference – even in moments like this.

Enclosure #2 – Our second enclosure is a discussion on inflation and what recent Federal Reserve moves could mean in the future. Brian Wesbury, from First Trust Advisors, provides a look at some statistical points and weighs in with his thoughts on what inflation may look like after this.

Enclosure #3 – Our last enclosure is a new writing from our team member Lenny Weiss. He provides a discussion on fear and panic – specifically how those emotions can impact investing.

continue or forecasts will occur. The information has been obtained from sources considered to be reliable, but Raymond James does not guarantee that the foregoing material is accurate or complete. Any information is not a complete summary or statement of all available data necessary for making an investment decision and does not constitute a recommendation. Investing involves risk and you may incur a profit or loss regardless of strategy selected. Investing in certain sectors may involve additional risks and may not be appropriate for all investors. The Bloomberg Barclays US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market.

Enclosure #2: Information was developed by First Trust, an independent third party. The opinions of Brian Wesbury are independent from and not necessarily those of RJFS or Raymond James.

*Prices of DJIA and NASDAQ as of 07/07/2018.

First Trust
Monday Morning OUTLOOK

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The Fed Gambles on Inflation

Over the past couple of decades, the Federal Reserve has coalesced around an idea about inflation that is little more than theoretical, with no real data to back it up. That "idea" is that 2% inflation is the "correct" amount of inflation.

The target is not just a one-year target, it is seemingly a permanent, long-term target. We find this idea very problematic. For example, the Fed's favorite measure of inflation, the PCE deflator, has averaged 1.5% over the past decade. But the Fed now says it could let inflation in the future run high so that the long-run average rises to 2%. No one knows exactly what this means, but one interpretation is that the Fed is willing to have inflation run at 2.5% for the next ten years so that the 20-year average is 2%.

Really? Why? If we look back over the past ten years, low inflation didn't hurt the economy, it helped it. Unemployment had fallen to 3.5% in February, the lowest since the 1960s. Yes, we know we're just emerging from the problems related to COVID-19, but that's an outside shock to the economic system, not something monetary policy can plan for ahead of time. It had nothing to do with the Fed or the level of inflation.

We have always believed that the underlying reason for the existence of the Fed was to maintain a stable value of the dollar. The most stable environment is one with no inflation. As Steve Forbes has always said, if a carpenter shows up at a job site and his yardstick is a different length than it was the day before, it is awfully hard to build a house, maybe impossible.

The same is true for the value of the dollar. It's far more complicated to make an investment, build a plant, or sell goods to a foreign country if the value of your currency changes over time making the value of revenues and investment change with it.

This is what worries us about the commitment to 2% long-run inflation. No one knows exactly what it means, or for that matter, why it is appropriate. Again, inflation averaged 1.5% over the past ten years with no serious consequences to the economy. By allowing inflation to average 2.5% over the next ten years, how does that change the past? The answer: it can't!

What it does do is change the future. In essence, the Fed is saying they really don't have a 2% inflation target, they have a target above 2% for the foreseeable future. And this is worrisome. The money supply has exploded in recent months as the Fed has monetized federal debt. Inflation is on the way higher. For example, this year the Fed said the PCE Deflator would be 0.8%, but it is already 1.4%, and looks more likely to rise than fall.

And if it rises to 2.5%, the Fed will say that is OK, because the average over some period of time (which it can make up by using any number of years of history) is still 2%. Back in the 1970s, the Fed kept saying inflation was rising, but it was all because of temporary factors (like oil) and it would fall later. But, once inflation is out of the bottle, it doesn't come down until the Fed tightens, like Paul Volcker did in the late 1970s and early 1980s.

So, letting inflation rise above 2% is potentially very dangerous. The Fed has created an artificial target and given itself an excuse for causing more inflation. If 2% is really the target, the Fed should claim victory when it is less than that and fight to keep it from rising above.

Unfortunately, the Fed is making arguments about inflation that are designed to give it freedom to do whatever it wants and that may actually lead to a devaluation of the US dollar. This is a violation of the real reason for the Fed and it worries us about the future of inflation in the United States.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
10-5 / 9:00 am	ISM Non Mfg Index – Sep	56.2	**56.3**	57.8	56.9
10-6 / 7:30 am	Int'l Trade Balance – Aug	-$66.2 Bil	**-$67.2 Bil**		-$63.6 Bil
10-7 / 2:00 pm	Consumer Credit– Aug	$14.0 Bil	**$14.8 Bil**		$12.2 Bil
10-8 / 7:30 am	Initial Claims – Oct 3	820K	**815K**		837K

INVESTMENT STRATEGY QUARTERLY QUICKVIEW

OCTOBER 2020

THEMES

Race for the White House: The Home Stretch

In reviewing the historical analysis, we have seen periods where election outcomes have caused short-term volatility, but more importantly, we see that this volatility generally quickly corrects itself. In addition to the presidential election, the House and Senate elections will also be important to watch, as the ability to enact a legislative agenda is correlated to who holds a majority in the House and Senate. We expect volatility around the election to continue leading up to November. However, we urge investors not to overreact to near-term swings in the market created by Washington activity because, historically, this volatility typically corrects itself quickly as the result settles.

Has the Euro Zone Finally Forged Fiscal Unity?

While the heavy toll of the COVID-19 pandemic will not be forgotten, the latest economic crisis has led to some surprising reactions, primarily in the area of fiscal policy. The severity of the crisis spurred a n unprecedented stimulus initiative funded by the central European Council, signaling continuing growth in Europe.

COVID-19 360°: An Update

COVID-19 has wreaked havoc on both physical and economic health in the US, and our nation's divided response has hindered our ability to most effectively combat the crisis. Though we have seen improvements in the fatality rate and testing levels, we will likely continue to see surges in cases in different states and regions until we reach herd immunity through infection or vaccine. The pandemic is likely to continue to impact nearly every area of our lives, from educating children to what travel we partake in to how we chose to vote and even the outcome of the upcoming election.

For more information, refer to the full Investment Strategy Quarterly.

Economic Snapshot

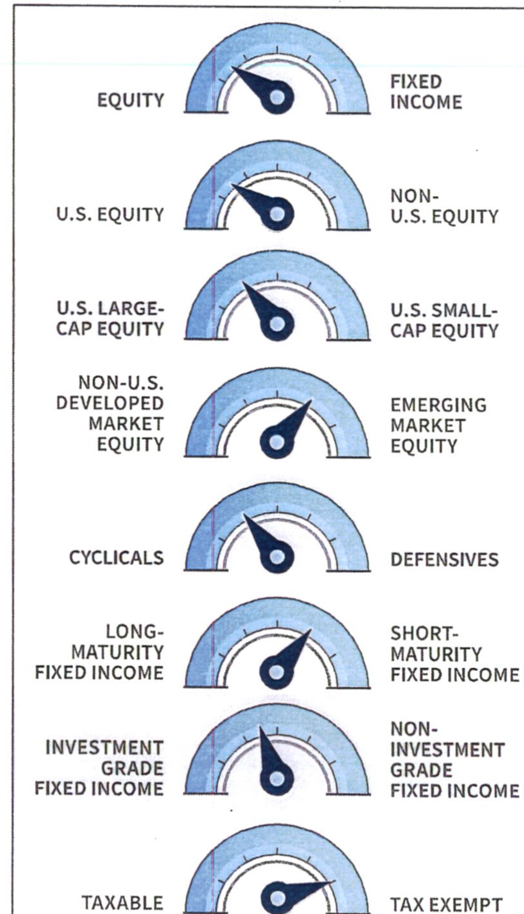
Economic Indicator

FAVORABLE	HOUSING AND CONSTRUCTION
	MONETARY POLICY
NEUTRAL	GROWTH
	EMPLOYMENT
	CONSUMER SPENDING
	BUSINESS INVESTMENT
	MANUFACTURING
	INFLATION
	LONG-TERM INTEREST RATES
	FISCAL POLICY
	THE DOLLAR
	REST OF THE WORLD

From Scott Brown, Ph.D.,
Chief Economist, Raymond James

Tactical Outlook

(3-9 months)



The tactical asset allocation outlook above reflects the Raymond James Investment Strategy Committee's recommendations for current positioning. Your financial advisor can help you interpret each recommendation within this material relative to your individual asset allocation policy, risk tolerance and investment objectives.

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INVESTMENT STRATEGY QUARTERLY QUICKVIEW

OCTOBER 2020

Capital Markets Snapshot

EQUITY	AS OF 9/30/2020*	3Q 2020 RETURN**	12-MONTH RETURN**
DOW JONES INDUSTRIAL AVERAGE	27,781.70	7.6%	3.2%
S&P 500 INDEX	3,363.00	8.5%	13.0%
NASDAQ COMPOSITE INDEX	11,167.51	11.0%	39.6%
MSCI EAFE INDEX	1,855.32	4.9%	0.9%
RATES	**AS OF 9/30/2020***	**AS OF 12/31/2019****	**AS OF 9/30/2019****
FED FUNDS TARGET RANGE	0-0.25	1.50-1.75	1.75-2.00
3-MONTH LIBOR	0.23	1.91	2.08
2-YEAR TREASURY	0.11	1.57	1.63
10-YEAR TREASURY	0.66	1.92	1.68
30-YEAR MORTGAGE	3.65	3.86	3.85
PRIME RATE	3.25	4.75	5.03
COMMODITIES	**AS OF 9/30/2020***	**3Q 2020 RETURN****	**12-MONTH RETURN****
GOLD	$1,895.50	5.3%	28.7%
CRUDE OIL	$40.22	2.4%	-25.6%

*Price Level
**Total Return

Sector Snapshot

	SECTOR	S&P WEIGHT
OVERWEIGHT	INFORMATION TECHNOLOGY	27.8%
	HEALTH CARE	14.3%
	CONSUMER DISCRETIONARY	11.3%
	COMMUNICATION SERVICES	10.8%
EQUAL WEIGHT	FINANCIALS	9.9%
	INDUSTRIALS	8.4%
	CONSUMER STAPLES	7.1%
	MATERIALS	2.7%
UNDERWEIGHT	UTILITIES	3.0%
	ENERGY	2.2%
	REAL ESTATE	2.6%

DISCLOSURE:

Data is provided by the Investment Strategy Group. This material is for informational purposes only and should not be used or construed as a recommendation regarding any security. All expressions of opinion reflect the judgment of Raymond James & Associates, Inc. and are subject to change.

International investing involves special risks, including currency fluctuations, different financial accounting standards, and possible political and economic volatility. These risks are greater in emerging markets. Commodities trading is generally considered speculative because of the significant potential for investment loss. Sector investments are companies engaged in business related to a specific sector and are are subject to fierce competition and their products and services may be subject to rapid obsolescence. There are additional risks associated with investing in an individual sector, including limited diversification. There is no assurance that any of the forecasts mentioned will occur. Asset allocation and diversification do not guarantee a profit nor protect against loss. Dividends are not guaranteed and will fluctuate. The value of REITs and their ability to distribute income may be adversely affected by several factors beyond the control of the issuers of the REITs. There is no assurance that any investment strategy will be successful or that any securities transaction, holdings, sectors or allocations discussed will be profitable. It should not be assumed that any investment recommendation or decisions made in the future will be profitable or will equal any investment performance discussed herein.

Past performance is not indicative of future results. The performance mentioned does not include fees and charges which would reduce an investor's returns. Fixed income securities are subject to interest rate risk. Generally, when interest rates rise, bond prices fall, and vice versa. Specific sector investing can be subject to different and greater risks than more diversified investments. Investing in small-cap and mid-cap stocks generally involves greater risks, and, therefore, might not be appropriate for every investor. High-yield (below investment-grade) bonds are not suitable for all Investors. When appropriate, these bonds should only comprise a modest portion of your portfolio. Specific sector investing such as real estate can be subject to different and greater risks than more diversified investments. Declines in the value of real estate, economic conditions, property taxes, tax laws and interest rates all present potential risks to real estate investments.

ALTERNATIVE INVESTMENTS involve specific risks that may be greater than those associated with traditional investments and may be offered only to clients who meet specific suitability requirements. There is no guarantee that any of the alternative strategies listed will be successful or that they will prevent loss.

INDEX DESCRIPTIONS: Please note that all indices are unmanaged and investors cannot invest directly in an index. An investor who purchases an investment product which attempts to mimic the performance of an index will incur expenses that would reduce returns. Standard & Poor's 500 (S&P 500): Measures changes in stock market conditions based on the average performance of 500 widely held common stocks. Represents approximately 68% of the investable U.S. equity market. The Dow Jones Industrial Average is an unmanaged index of 30 widely held securities. The NASDAQ Composite Index is an unmanaged index of all stocks traded on the NASDAQ over-the-counter market. The MSCI EAFE (Europe, Australia, Far East) index is an unmanaged index that is generally considered representative of the international stock market. The returns noted do not include fees and charges which will affect an investor's return.

Bond prices and yields are subject to change based upon market conditions and availability. If bonds are sold prior to maturity, you may receive more or less than your initial investment. There is an inverse relationship between interest rate movements and fixed income prices. Generally, when interest rates rise, fixed income prices fall and when interest rates fall, fixed income prices rise.

The Weiss Report
Volume 23, Number 3
Enclosure #3

On Fear and Panic

By Leonard Weiss

I am not a psychiatrist. I am not a psychologist. I am not a social worker. I am not medically qualified to be an expert on the subject I will develop in this piece.

However, I have watched people buy and sell in stock and bond markets for over 40 years including four complete market cycles. As an anecdotal observer, I think I have experience in an area called behavioral decision making. No matter what decade, I have seen how investors handle the fear/panic cycle. For the most part, no matter what the decade, investors tend to act the same way in stressful and volatile times.

Many think fear and panic are the same thing. In the context of investing, I think the two are different. I assert that fear is an internal response to the unknown. It's an innate force to signal to us that we need to act on potential danger. While panic is the external decision making process that we attempt to implement to protect ourselves from our internal fear.

A few years ago, I attended an investment conference that featured a former anthropologist who career changed to a financial advisor who spoke about the behavioral aspects of decision making in the fear/greed cycle of markets.

She explained that we are hard wired, literally, to react to inner fear of the unknown. She told a simple story: Two cavemen are sitting outside the cave cooking a rabbit for dinner. They both heard a rustling in the grass. One cave man jumped up, screamed loudly and dove back into the cave. He reacted to his/her fear, and in panic he chose to dive back into safety. This person is our chemical ancestor. Multiply this hard wiring exhibition over millions of years of generations, and today most people react to the unknown with an inner reaction of fear, and panic into a decision to help manage it.

Incidentally, the other cave man, who reacted to the sound with complacency ended up being dinner for the tiger, trolling in the bush. That person obviously is not our ancestor.

An easy way to see first fear and then panic is seen every fall, when five days before a hurricane makes landfall there is a stampede for water, food, plywood etc. This might be more normal than not because no one knows where a hurricane will hit and how long they will be without power etc.

But in the investment world, managing fear and panic promotes decisions that don't seem to be relevant to the underlying emotions.

Consider what has happened over the last six months managing our lives as Covid-19 began to spread. As the pandemic spread, many horded toilet paper, hand sanitizer, antiseptic wipes, and antiseptic soap. Without any data on what was actually needed, consumers were buying months or years of supplies. This was very much so a panic situation.

One last demonstration of panic to manage our financial fears may be is how individuals are saving almost 22% of the stimulus money received. We have money in the bank, yet we won't spend it.

In normal times, the savings rate ranges from 5% to 8% in any given year. A savings rate this large implies that we manage fear with the panic decision to horde money!

In summary, I am convinced that fear is hard wired into our existence. Panic is the decisions we make to mollify our fears. While the onset of the virus stoked our fears, the massive selling in the stock market was our behavioral panic response.