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Stolper Asset Management
An Independent Registered Investment Adviser

Portfolio Comments
For the Quarter Ending September 30, 2020

The past three months of 2020 marked the third consecutive quarter of business not-as-usual. As we end September, new reported cases of the coronavirus in the U.S. are currently trending down, while deaths attributed to it globally have surpassed the one million mark. Edging back toward some kind of 'normalcy' in the workplace, in education, and in everyday life has been a rocky, inconsistent path with scant ground of consensus opinion. With the U.S. Presidential election less than two months away, intertwined in national and local government policies have been deep political divisions, heightened by social and economic disparities that have been magnified of late.

To quote Wayne Gretzky, the Canadian ice-hockey player, "A good hockey player plays where the puck is. A great hockey player plays where the puck is going to be." The air of unrest in the financial markets, and the broader economy, is no doubt somewhat due to the fact that we don't know where we are going to be, at least in the short term. In the COVID recession, economic conditions are too closely linked to the trajectory of the pandemic, and the development of solutions to address it, to be able to forecast with confidence the course of recovery.

And then there is the U.S. stock market aggregate performance. If a person had somehow managed to avoid news of it for the first nine months of the year only to check in at the end of this month, they would be forgiven for thinking it had been a subdued, but uneventful investing period. The S&P 500 closed on September 30th at 3,363 representing a strong return of 8.93% for the third quarter, and 5.58% for the first nine months of 2020. The index set a new record closing high of 3,581 on September 2nd. The less momentum stock-heavy Dow Jones Industrial Average (DJIA) ended September at 27,782 for a return of 8.22% in the past three months but -0.90% for the year to date. During the quarter, both indices notched astounding gains of over 50% from their March lows earlier in the year. There was a pullback during September as Congress failed to agree on additional domestic fiscal aid and COVID cases rose again in Europe. Additionally, the Volatility Index (VIX), a measure of the market's expectation of the level of near-term price fluctuations, remains elevated.

These performance numbers overlaid on the backdrop of the economic reality for the majority of corporate America has caused some head scratching and there are a number of forces at play. The S&P 500 index is 'cap-weighted', meaning the larger the market capitalization of a member company (price multiplied by shares outstanding), the greater its weight in

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the index. This exaggerates the effect of the largest stocks on the list. The largest sector in the S&P 500, Information Technology, represents over a quarter of the index and has been the best performing year-to-date, rising around 25%. Consumer Discretionary is a close second-best performing sector and garners another 11% of the index's weighting. At the other end of the spectrum, Energy has fallen a whopping 50% in price terms, and its weighting has dropped to close to only 2%. Financials, 10% of the index is the other major laggard, falling close to 25% since the start of the year.

To emphasize the skew effect the disparate performance of these cap-weighted sector buckets has had on the headline market performance numbers, year-to-date data from Raymond James through October 1st, cites the S&P 500 price return at 4.1%, but the S&P 500 Equal Weight (where each stock is given an equal weighting in calculations) price return was -6.3%. A handful of large, popular momentum stocks (notably big tech names) have played a large role in boosting the index over the past few years. It has been estimated that since the end of 2017, 15 companies in the S&P 500 account for approximately 95% of its gain, leaving the rest of field close to flat.

We emphasize this phenomenon, which we see no sign of abating soon, to encourage interested parties and investors to not wholly rely on stock market levels as a proxy measure for our nation's economic health. We consider it necessary in our capacity to keep a close watch on a range of underlying indicators in an effort to gauge the direction and velocity of the 'recovery puck'. Frankly, it's a mixed bag for now, but there are some encouraging signs.

September's U.S. Manufacturing PMI moved higher as a positive indicator for the manufacturing sector, which bodes well for output and employment recovery on the back of a rebound from the second quarter's slump. The latest initial jobless claims held steady for the week to September 25th at 870,000, but the unemployment rate fell fast to 8.4% in August, down from the pandemic peak of 14.7% in April. Both new and existing home sales have surged to above pre-pandemic levels, spurred by the relocation forces and opportunities created by the pandemic and the rise of work- and study-from-home, as well as record low interest rates.

Back in June, the Organization for Economic Co-operation and Development (OECD), a developed country think-tank, predicted the American economy would shrink by 7.3% this year. Two weeks ago, they revised this forecast to a contraction of only 3.8%. We are still facing a recession, but hopefully one not as dire as initially feared, and also not as severe as most of our European counterparts.

The U.S.'s economic stimulus was the world's biggest, both in nominal terms and as a percentage of Gross Domestic Product (GDP). A large proportion of households saw their disposable income rise with the distribution of stimulus checks and enhanced unemployment-insurance payments. Even though this initial emergency funding has expired, it continues to fuel consumption. Going into the end of September, House Democrats unveiled their latest new Coronavirus stimulus bill in the form of a $2.2 trillion relief package that includes another round of checks for those that qualify, reinstatement of the $600 weekly jobless benefits, and an extension the Paycheck Protection Program that expired in August with over $130 billion in unused funds. Both Republicans and Democrats have expressed support for additional stimulus, but have been unable to bridge the divide on the amount and details. This latest bill will likely meet resistance in the GOP-led Senate, with the Republicans less willing to endorse more deficit spending at this level, and more vocal in pointing to evidence of an already-recovering economy.

A separate, but related, component of the unprecedented economic support system that was rapidly put in place in response to the pandemic, has been the Federal Reserve's seemingly boundless willingness to come forth with all guns blazing. They continue to provide liquidity to the finance sector to ensure smooth functioning markets, hold interest rates at rock bottom to keep borrowing costs low, and mop up government, mortgage-backed, and even corporate debt to stave off any danger of an asset price collapse. Beginning in March, the Fed's balance sheet rapidly ballooned from around $4 trillion to the $7 trillion mark, but has since held pretty steady around this level over the summer.

In a departure from a long-held policy, Fed Chairman Jerome Powell announced at the end of August that the 2% inflation goal will now represent a multi-year average of inflation, not a set target. They will therefore be unconcerned if it temporarily 'runs hot' and goes to, say 3%, for a period. In our current zero nominal rate environment this could mean a Fed real rate of return (inflation adjusted) of -3%, a bullish environment for stock prices on the face of it. Of course, if inflation did indeed begin to creep up, the Fed would likely revisit its zero-rate policy, although Fed Vice-Chair, Richard Clarida, recently stated in an interview that The Federal Open Market Committee (FOMC) would not even think about hiking the federal funds rate until the inflation figure reaches 2%, or maybe even beyond. The current consensus expectation is that the rate will stay at zero through 2023.

A zero-interest rate environment is certainly beneficial for government borrowing and debt servicing with the federal debt, when measured as a percentage of GDP, already is as high as it was at the peak of World War II. A recent report by the Congressional Budget Office (CBO) forecasts that federal debt held by the public is projected to equal 98% of GDP by the end of this year, and rise to 104% of GDP in 2021. The government's fiscal year ends September 30th, and the CBO predicts around a $3.7 trillion deficit for this budget year, with spending totaling about 32% of GDP (the highest level since 1945) and revenues falling to about 16% of GDP.

The rush for cash, the low cost of borrowing and the Fed's direct support of the corporate bond market for the first time has also set company debt issuance soaring to record levels this year. According to data from Refinitiv, U.S. corporate bond issuance reached over $1.9 trillion in the first 8 months of 2020, surpassing the previous annual record set in 2017. Investment-grade bond yields also plumbed record lows.

The near-term trajectory of the federal debt path will no doubt be impacted by election results in November. At the top, the incumbent Republican Trump-Pence ticket is facing Democratic nominee former Vice President Joe Biden, who selected California Senator Kamala Harris as his running mate. The first, of three, presidential debates, just took place and proved to be chaotic and combative. By all accounts, it failed to serve either candidate, or the voting public. National polls currently give Mr. Biden a mid-single digit lead over President Trump, but the Electoral College system appears to favor Mr. Trump, with a number of key potential swing states leaning red. Besides, polls need to be read with a grain of salt, we are still over a month out, and the unscientific feeling appears to be that the Presidential outcome, and a Democratic sweep of both Houses, is still a "toss up".

This month saw the passing of Supreme Court Justice Ruth Bader Ginsburg, a liberal icon, at the age of 87. She served for more than 27 years and was only the second woman to be appointed to the position. In a decision that sparked controversy over its timing just before a Presidential election, President Trump moved quickly to fill the vacancy with the nomination of Amy Coney Barrett, a judge on the Seventh Circuit Court of appeals, whose track record shows a conservative bent. Senate

Republicans are widely expected to confirm Ms. Barrett ahead of the November 3rd election.

Abroad, every other region and country is dealing with the medical, social and financial fallout from COVID-19 as well. Latin America is the current epicenter of the pandemic, India is also experiencing a surge, and there are indications of a resurgence of cases in several EU countries. The Eurozone is struggling through its worst economic recession in 90 years. With Euro area interest rates already negative, the European Central Bank (ECB) has limited ammunition to help highly indebted countries such as Italy and Spain, the zones third and fourth largest economies, who are both highly dependent on tourism and have proved hotbeds for the pandemic. According to the International Monetary Fund (IMF) both counties will see their economies contract by 12.5% this year and their public-debt-to-GDP ratios with be 150% for Italy and 120% for Spain. With the countries not in control of their own currency, deflation risk is of particular concern given its impact on government debt servicing capabilities. In response, Christine Lagarde, the ECB President, has become increasingly vocal in calling for additional fiscal stimulus measures for the region.

Britain left the European Union eight months ago and there is only a month remaining for negotiations to conclude with Brussels over the terms of the relationship, including critical trade agreements. The pandemic thrust Britain into the deepest recession of any major developed country (according to the OECD), and another wave of cases has thwarted reopening plans. According to the same set of data, China is the only big economy set to expand in 2020.

We are well aware that investor resilience has been severely tested so far this year, and the upcoming contentious White House battle is adding to the pervading atmosphere of uncertainty. However, the current situation of unprecedented stimulus, a super-accommodative Fed, low interest rates, and low inflation can work to counteract the economic effects of election uncertainty, geopolitical tensions, potential tax changes and virus unknowns.

We continue to focus on strong fundamental analysis to aim to build robust portfolios of securities that are well-positioned to withstand market volatility. In our investment decisions we continue to emphasize quality, durability and reasonable valuations and maintain confidence in eventual full recovery. As always, we align these decisions with the long-term goals and objectives of our clients. There are many unknowns, and every institution, community and individual is doing their best to navigate, us included. We hope this finds you and your loved ones well, we thank you for your continued confidence in us, and we are always available as your financial advisor to talk, help and address your questions.

The S&P 500 is an unmanaged index of 500 widely held companies and over 80% of the U.S. equities market. The Dow Jones Industrial Average (DJIA), commonly known as "The Dow", is an index representing 30 companies maintained and reviewed by the editors of the Wall Street Journal. The information contained in this report does not purport to be a complete description of the securities, markets or developments referred to in this material. The information has been obtained from sources considered to be reliable, but we do not guarantee that the foregoing material is accurate or complete. Any opinions are those of the investment adviser representatives of Stolper Asset Management and not necessarily those of RJFS or Raymond James. Expressions of opinion are as of this date and are subject to change without notice. Investing involves risk and you can lose principal. There is no assurance any strategy will be successful. There is no guarantee that any forecasts made will come to pass. Past performance may not be indicative of future results. This information is not intended as a solicitation or an offer to buy or sell any security referred to herein.

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