ICR® 3rd Quarter Newsletter – October 2020

During the third quarter, markets mostly continued their recovery from the devastation felt earlier in the year. The S&P 500 rose about 8.5%, with growth stocks once again providing much of the fuel for that rally. At one point, the gains were even greater before the market fell almost 10% from its lofty peak. Energy was the only sector that lost in the quarter, falling 20% and bringing its year-to-date loss to an astounding 48%.

Foreign markets rose modestly with the MSCI EAFE index, which tracks foreign developed markets, gaining 4.2% - though it is still down almost 9% for the year. Emerging markets fared better, gaining 8.7%, but are also still negative in 2020. Gold continued its ascent, going from $1,800/ounce to almost $2,100 before selling off in the last few months to end the quarter around $1,900. In light of negative real interest rates and massive government spending, gold has gained over 25% this year. The ten-year treasury seems to have settled into a range and despite some gyrations, ended the quarter almost exactly where it began at 0.65%.

The Election and What It Means for Investors

Every four years, we get a lot of questions about what the election will mean for investors and how it will impact their portfolios. So, this seems like an opportunity to use this space to address some of those questions. First, as we learned in 2016, the initial market reaction may not be the lasting one. As news networks began to project Donald Trump as the next president, futures markets plummeted, falling as much as 5%. Slowly, over the next twelve hours, markets reversed course and eventually ended the next trading day up over 1%. The consensus view that a surprise Trump victory would throw the markets into chaos was true – but only for a few hours.

With that reminder that markets don't always react how we think they will, let's look at a few key areas in which the election outcome *might* have an effect. First, Joe Biden has proposed increasing corporate tax rates, personal tax rates on incomes over $400,000, and capital gains tax rates on those making more than $1 million. Increasing corporations' taxes reduces their profits which makes their stock less attractive to investors. And raising taxes on wealthy individuals could lead to less money flowing into stocks since the rich tend to be the biggest owners of equity. However, since high-income earners usually have high savings rates, this tax increase would be unlikely to affect aggregate consumer demand much, so the impact on the real economy may be negligible. The degree to which Biden's tax proposals would actually discourage stock buying is certainly debatable, but continuing the status quo on taxes from the past few years would likely be more favorable in the eyes of investors.

Prior to the pandemic, news about trade wars and tariffs often moved markets in one direction or the other. That has largely been put on the back burner this year, but when (if?) we get a handle on the virus, the president will need to address the issue. While Biden hasn't made trade a focus of his platform, the consensus view seems to be that he would be less reliant on tariffs than Trump has been, though there would likely still be tension with some countries – China in particular. Generally, the markets have celebrated news of decreased tariffs and lamented the opposite. So, perhaps, there would be a bit of relief on the trade front should Biden win.

One of the biggest issues from our perspective – and what investors have been following closely – is fiscal stimulus. Monetary stimulus has largely been the focus of markets since the Great Financial Crisis, but federal government spending in response to the pandemic was greeted with open arms by investors. The $2.2 trillion CARES Act resulted in $1,200 checks sent to over 80% of Americans, $650 billion in loans to businesses (much of which will not need to be repaid), and increased unemployment benefits for the millions of Americans who lost their jobs. And it worked. It wasn't perfect, but all of that federal spending seems to have been successful in helping the economy (and the stock market).

Thankfully, additional fiscal stimulus is one area that Democrats and Republicans seem to agree on. The questions are: how much, when, and where? A "blue wave," in which Democrats win control of both the White House and the Senate, would likely result in the largest package of federal aid, though we believe that no matter what happens on November 3rd, we're likely to see substantial fiscal spending. Where that spending is allocated might differ depending on the election outcome. For example, we might see more "green" energy investments from a blue wave and more traditional infrastructure spending with Republican control. But, either way, we are likely to see increased infrastructure spending as well as additional unemployment benefits, along with other forms of fiscal stimulus, all of which the markets appreciate.

Perhaps the worst case scenario for this election is a contested outcome. The markets despise uncertainty, and not having a clear picture of what to expect would likely create volatility. In the aftermath of the chaotic 2000 presidential election, the markets fell around 8.5% at one point amid the uncertainty of who our next president would be. That was, of course, in the heart of the tech bubble popping and should be taken in context, but that brings us to our final point.

We can analyze what this election might mean, but at the end of the day, politics really only affect the markets at the margin. Understandably, there are a lot of emotions involved in politics and it is easy for people to let their political leanings affect their views on everything – including their portfolios. We can recall people panicking when Barack Obama was elected and then others panicking when Trump was elected, and in both cases, things ended up being just fine from a market perspective. Moreover, all of the potential policy outcomes that we've discussed in this letter are just theoretical. Things never end up looking exactly like we think they will and politicians – get this! – don't always live up to their promises.

Far more important for the markets are factors like valuations, where we are in the economic cycle, new innovations, corporate debt levels, and demographics – just to name a few of the many topics that have very little to do with politics. Unless you have a crystal ball (and please let us borrow it if you do), the best investment plan is the one you can stick with through thick and thin. There will be challenges and opportunities no matter what happens in this election, but a prudent approach that looks past the political noise is the most likely path to long-term financial success.

As always, we wish you the best and hope that you are staying safe, healthy, and happy. Please let us know if you have questions, concerns, or if there is anything we can help you with – financial or otherwise.

Sincerely,

James A. Heine

James L. Cobb

Market Report (as of 9/30/20)

Index	**2020 (%)**	**3-Year Annualized (%)**	**5-Year Annualized (%)**
S&P 500	4.1	10.1	11.9
Dow Jones Industrial Average	-2.7	7.4	11.3
U.S. Aggregate Bond Index	6.8	5.2	4.2
MSCI EAFE (Foreign Index)	-8.9	-2.0	2.4

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