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THE TEMPO VANTAGE

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Of Presidents and Pandemics

The third quarter of 2020 was a great time to be an investor, with returns for most equity categories between 5% (small caps) and 11% (NASDAQ).

Let the good times roll. Right?

Not so fast. Recall that the market had fallen precipitously in the first quarter in reaction to the pandemic. At the time I thought the decline was overdone (see 1Q Tempo Vantage). Essentially, the gains in the second and third quarters were an unwinding of the market's initial knee jerk reaction.

By the end of the third quarter, both the S&P 500 and the NASDAQ had fully recovered from the initial decline, with year-to-date gains of 5.5% and 25%, respectively.

But the strength in large cap and technology stocks masked weaknesses in other areas of the stock market.

Through September, small-caps, mid-caps, and international stocks were down 9%, 9% and 7%, respectively.

Returns for bonds were more muted, with the BarCap Agg making just 0.6%. But there was strength in select areas of the bond market. Inflation bonds (+3%), high yield bonds (+4%), emerging market bonds (+2.5%), and global bonds (+3%) all had terrific quarters as compared to the Agg.

This is all well and good, but what really matters is where the markets will go from here.

In answering this question, I usually look to a variety of metrics (P/E ratio, market sentiment, yield curve, etc.).

At the moment, however, there are only two things that matter to the stock market: the pandemic and the election. They are not unrelated.

The key for any meaningful gains at this point is to get beyond the pandemic.

It is no secret that this administration's response to the pandemic has been, well, less than ideal.

If Trump wins the election and continues on the current trajectory, it seems clear that the pandemic will not only last quite a while longer, but we may be in for a second wave of cases (has the first wave ended?) as he continues to recklessly push business as usual without regard to safety.

If Biden wins, there is hope that measures that should have been taken months ago to stem the pandemic will finally be taken. The market is a forward-looking vehicle. With a Biden victory, investors may finally be able to envision a post-pandemic world.

Essentially, we are in a holding pattern until the election, and I wouldn't expect a lot of net movement either way in the stock market.

Tempo Financial Advisors' 3rd Quarter Investment Performance

Coming in to September, **Tempo Lifestyle** accounts had overcome the first quarter bear market and were making new highs for the year. Unfortunately, the market decline in September brought accounts back into the red through the first three quarters.

For the third quarter Tempo accounts gained between 4% and 6%. This is about half a percent below benchmarks. Year-to-date returns are down between 1% and 4%, which also trail benchmarks by a few percentage points.

Why have we trailed this year? Three reasons.

- Early in the year our bond holdings trailed the BarCap Agg. Most bond categories trailed in Q1, as is often the case when there is a flight to safety amid severe market declines.
- We hold small-cap and mid-cap stocks, both of which have trailed large caps. The benchmark does not contain small and mid-cap stocks. I recognize that I have chosen a relatively basic benchmark (large cap stocks, international large cap stocks and bonds). Had I chosen a different benchmark, we might not be trailing at all!

- More recently, our overweight in infrastructure stocks has held us back as returns have trailed the averages.

Once we are beyond the election, I believe the government will undertake massive infrastructure programs and these stocks will benefit. It will be more pronounced should things tilt toward the Democrats.

Tempo Dynamic Growth accounts gained 4.6% in the third quarter. This is exactly in line with benchmarks, down to the tenth of a percent. I am happy with these results given that our allocation to equities is at the minimum allowed in the strategy (40%).

I'm not happy about our year-to-date returns. As you may recall, Tempo accounts had a very rough first quarter, losing more than 15%. Although we have gained more than 11% in the last six months, we still have a way to go before breaking even for the year.

Accounts have been rebalanced for the fourth quarter. We remain with a 40% allocation to equities.

The biggest change is that technology stocks are gone in favor of covered call funds. (Call me if you want to understand what these are.) Suffice it to say that the recent volatility in the market has caused the model to become even more conservative as we near the election.

Tempo's Income strategies, **Dynamic Income** (+1.8%) and **Diversified Income** (+2.8%), both had terrific quarters, outperforming the benchmark by 1% and 2%, respectively.

The same cannot be said for year-to-date results. Diversified Income held up quite well in the initial pandemic decline, and positive returns in Q2 and Q3 have brought year-to-date returns into the black.

Dynamic Income has not been as successful in 2020. The terrible first quarter has overshadowed the remainder of the year and made it all but certain that we will suffer a loss in 2020 larger than any previous loss, by far.

Dynamic Income clients should not despair. We have more than 12 years of good results in Dynamic Income, and one lousy quarter does not change that fact. I expect that moving forward we will resume a steady diet of positive quarters.

Reminder

Please contact us if there has been a change in your financial circumstances that would warrant a fresh perspective on your portfolio.

Daniel J. Traub