FORZA
Strengthening Our Clients' Financial Lives

Forza Investment Advisory, LLC

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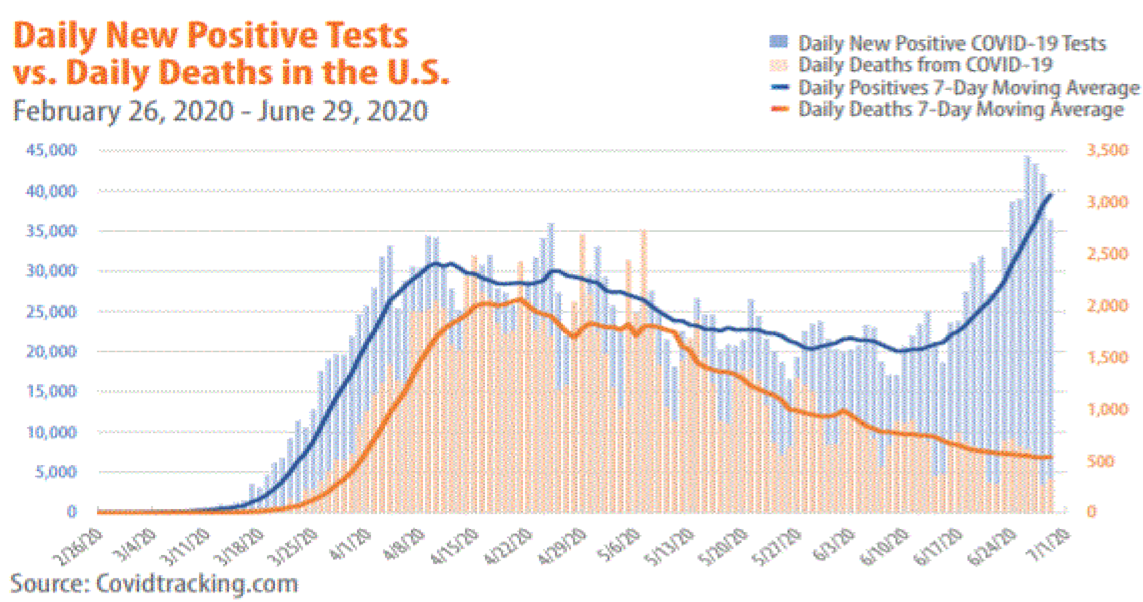
SECOND QUARTER REVIEW & 2020 OUTLOOK

When I last penned my quarterly letter in early April, we were chartering in unknown waters and markets were extremely fragile to say the least. The second quarter then began just as badly after a failed rally at the end of March until the Federal Reserve came to the rescue and the US Treasury and government outlined steps to get money into people's and companies' hands. Fast forward 3 months through a global pandemic, easing of lockdowns, bear markets, bull markets, countless records good and bad in economic data, and add in widespread protests and you have the makings of an eventful first half of 2020! Now if we can only get some sporting events going to add a little normalcy to our lives. Thank God for golf – it has been a lifesaver around here and on TV.

Question: When is a 20% rally in stocks not a cause to celebrate too hard? **Answer**: When it is only a partial rebound from the worst first quarter ever. Don't get me wrong, there is a lot to celebrate (in financial market terms) about the best quarter since Q4-1998. And we should also celebrate that the S&P 500 is only down 3% in the first 6 months considering where we were and what we went through. Remember when stocks were down 35% from their peak in March? I know, I'm trying to forget it too, but it happened and we live through it and learn from it. There are still a lot of unknowns both good and bad to come as each day we try to fight through this and learn something new.

ECONOMY

The economy as expected has taken a major hit. So much has come to a halt from restaurants, to malls, to outdoor/indoor sporting events, to schools, to travel, etc., etc. The unemployment rate bottomed at almost 15% in April! It was just earlier this year when we were at 3.5% unemployment and off to another strong year. But jobs have staged a little comeback with states reopening. Non-manufacturing activity (services) jumped in the latest month as many businesses did modified openings. The jobless rate fell to 11.1% in June with 4.8mm jobs added but 20mm still are out of work due to the virus. But now with the virus advancing again and states pausing their reopening's, we may see another spike in unemployment. The chart below shows the recent uptick in new cases as states and businesses reopen.



The spike we are seeing in new positives threatens to stall the rebound. What to do? Continue to open and protect the vulnerable, or go backwards? That will be a key question. We must get the economy reopened and people to work ASAP but in a responsible and safe way. Figure that out and we are in business. The safest way is likely a vaccine, and with some luck and much skill, we could see something by year-end. But in the meantime, businesses need to reopen before they can't. And the younger crowd especially must be more vigilant and careful.

STOCKS, BONDS and OTHER ASSETS

In Q1 there were no places to hide, in Q2 you didn't want to hide and had to look hard to find a bad return. In the US, the NASDAQ was a big winner in the quarter rising 30.6% and is actually up 12.1% YTD thanks to the FAANG-M stocks (Facebook (+36% in qtr), Amazon (+42%), Apple (+43%), Netflix (+21%), Google (+29%) and Microsoft(+50%). They also helped the S&P 500 gain 20% in the quarter. Growth stocks beat value again and small- and mid-stocks beat large but still lag YTD. Looking by sector -- technology, energy, and consumer discretionary returned over 30% as investors bought cyclicals and technology stocks. Outside the US, there were some big winners with Germany, Brazil, Australia and Russia recording mid 20's% gains but still lagging the US considerably YTD. Ironically in China, where the virus originated, its market is actually up 0.24% for the year. Silver was up 30% and Gold rose 13% as investors hedged their bets. Bonds were stable while crude oil staged a big rally after bottoming in May and rose 92%, but is still down 35% YTD!

Asset	***Q2 Return%***	***YTD***	***Asset***	***Q2 Return %***	***YTD***
S&P 500	20.16	3.18	Brazil	30.18	-38.66
Dow 30	18.26	-8.48	German DAX	23.90	-6.83
Nasdaq Comp	30.63	**12.1**	Australia	25.84	-13.62
S&P Midcap 400	24.06	-12.79	Russia	24.40	-16.9
Russell 2000	25.50	-12.96	Canada	19.64	-12.54
S&P 500 Growth	26.00	7.74	China	14.75	0.24
S&P 500 Value	13.07	-15.6	Italy	17.15	-17.52
Vang High Dividend	12.53	-14.43	Japan Nikkei	12.09	-6.55
Euro	1.62	-0.29	Euro Stoxx	16.36	-12.7
Yen	-0.54	0.32	Nymex Crude	91.75	-35.6
S&P Sectors:			Gold	13.05	**17.12**
Consumer Disc	30.51	2.55	Silver	30.34	1.98
Consumer Staples	8.50	-5.61	Nat Gas	6.77	-20.01
Energy	31.91	-34.62	1-3 Yr Treas	0.22	2.95
Financials	11.85	-23.66	Total Bond	3.50	6.43
Health Care	13.45	-0.83	IBOXX High Yield	5.90	-5.44
Industrials	16.94	-14.61	20+ US Treas	-0.23	**21.87**
Materials	25.80	-7.10	Coffee	-16.31	
Technology	30.36	14.90	Lean Hogs	-13.46	
Utilities	2.68	-11.02	Nymex Gasoline	109.37	

Many of the talking heads are chirping on about the disconnect between the economic fundamentals and the move up in stocks. Really, if you take away the FAANG-M stocks I mentioned earlier, the market is doing much worse. These 6 stocks comprise almost 25% of the S&P 500. For instance, the S&P 500 Value index is down 15.6% YTD and the Vanguard High Dividend stock Index is down 14.43%. Neither of these contain those stocks. Outside the US, the Euro

Stoxx Index is down 12.7%. So, outside of these huge companies, stocks are not doing as great overall as it seems. But you can find winners depending on where you look. This makes stock-picking a good strategy this year rather than owning the whole market. One of the issues is that these hot stocks are becoming a crowded trade, meaning that everyone owns them because they are deemed safer. At some point if/when business can get back to reopening in a meaningful way, we may see a rotation out of these stocks into the downtrodden sectors and companies. We briefly saw this mad rush in early June as investors bid up airlines, hotels, retailers and cruise ship stocks. But then reality hit and they quickly sold off. The demand did not match investor enthusiasm. So, my take is that the whole market is not running away from fundamentals and overvalued as much as the FAANG-M stocks are carrying the index.

Soon, companies will be reporting Q2 earnings. In April, a big part of the rally was that companies reported better than expected numbers. We could see this again in Q2 as many analysts have slashed estimates for what should be an even worse quarter than Q1. But the market is already looking past this first half year and into the latter half plus 2021 and 2022. So, what companies say about the outlook and current environment will be scrutinized.

On the bond front, US Treasuries have remained a place of sanctuary although with yields solidly below 1% it is hard to get much return unless we continue towards 0% yields. The Fed has been a big proponent of lower yields and has been buying corporate bonds, putting its financial support in that market as well. The Fed has stated it will not be raising rates anytime soon so owning mid-term bond fund ETFs is likely the best way to get some yield and have some price protection. Convertible bonds also offer a higher yield and equity participation.

CONCLUSION

I've tried to stay upbeat but realistic through this year's tumultuous ride. I recommended remaining invested in stronger companies through this but also staying more diversified than just owning where the returns are coming from (ie, FAANG-M). I do believe that diversification will help in the 2nd half as companies hopefully return to production and service. But you can't ignore the big safer companies. I like a barbell approach of owning great companies on one end and some cyclicality on the other. But you must be selective with cyclicals. Last quarter I talked about looking out 1,3,5-year periods and investing for the long term. Before we get there, we do have a Presidential election coming and that has already started to inject some volatility into the market. A President Biden economy and fiscal policy will be vastly different than what we've had the last 4 years if that happens. Higher taxes, ,more regulation, more government will have differing consequences than the Trump administration policies. So, we now must start factoring that possibility into the equation based on recent polls. But let's remember what polls said 4 years ago too --so best not to overreact. For equities, I still prefer the good ole US of A over international markets but acknowledge that international stocks have some attraction. I underweight financials, materials, energy, consumer discretionary. Bonds will continue to provide capital preservation and a small amount of yield in balanced portfolios. Some convertible bonds and high yield will add some risk but also yield. Gold is a good hedge and store of value in a crisis.

Everything depends on slowing down this virus, reopening our economy fully, and determining what the new normal is. We are making progress towards a vaccine but in the meantime we all need to be smart and get back to the lessons that helped slow this down just a month ago. Stay safe and healthy and feel free to drop me an email or call at any time.

Bob