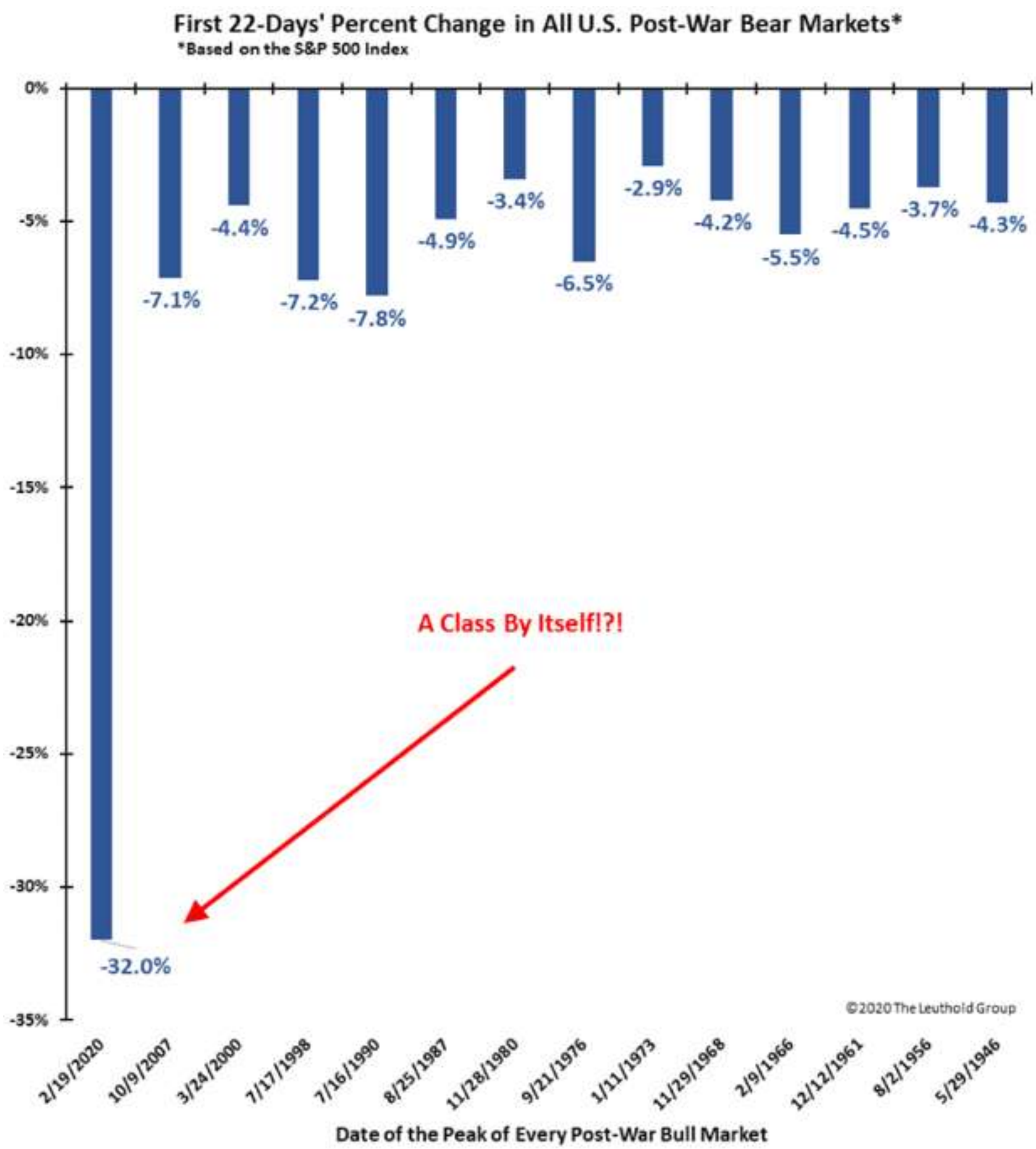
December 2020

“[Y]ou often hear financial professionals say such things as ‘forecasting market direction from here is exceptionally difficult’ in a tone conveying ‘gee, this is really strange.’ Well, I think forecasting the market over short-term horizons is always exceptionally difficult. If they said, ‘Our market-timing forecasts are mostly useless most of the time, but right now, they are completely useless,’ I suppose I’d be OK with it, but I’m not holding my breath that they will.” - Clifford S. Asness, "My Top 10 Peeves," Financial Analysts Journal, volume 70, number 1 (January/February 2014)

2020 saw the steepest post-WWII Bear Market followed by the steepest Bull Market, during the worst pandemic in over 100 years. A chart we shared in our March Newsletter:

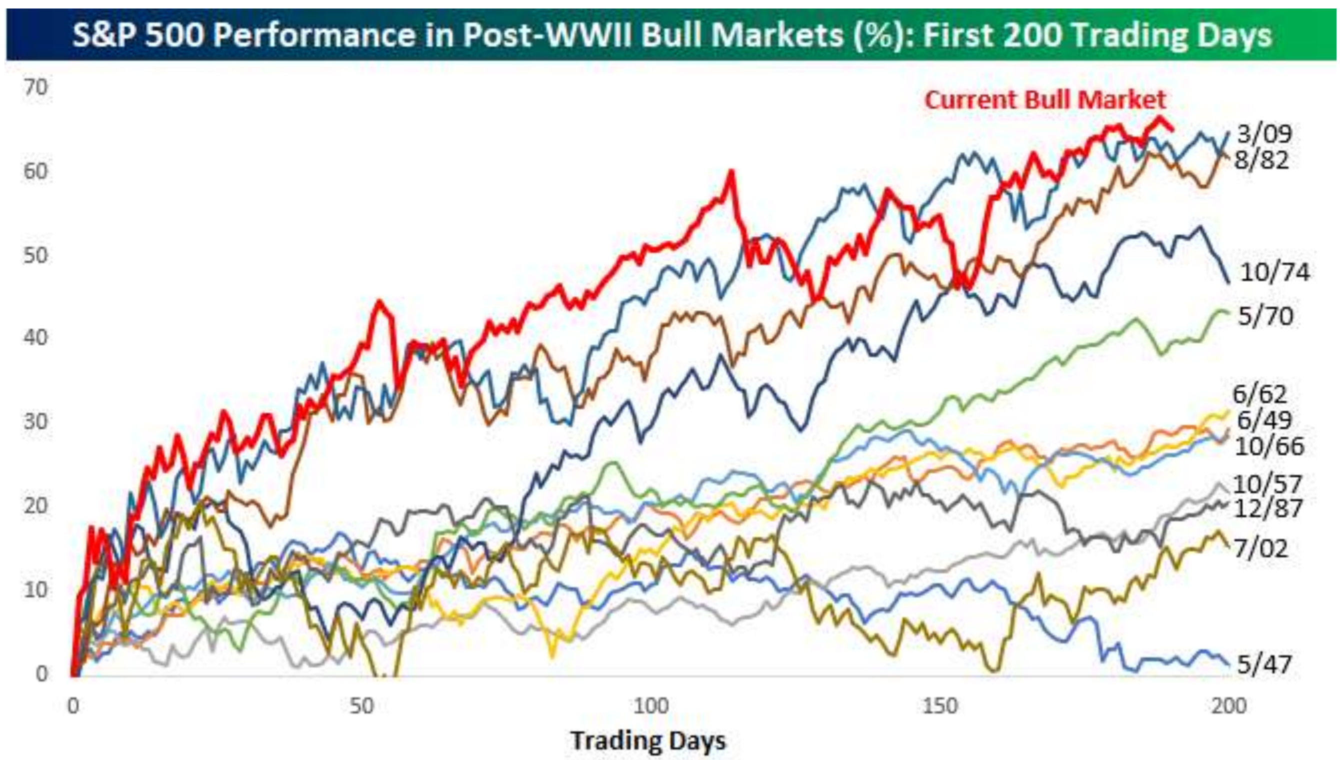


From Bespoke:

Closing in on a Record 200 Days

Tue, Dec 22, 2020

The rest of the year on Wall Street will be a time when many investors will be taking some time off, but when they return to work in the New Year, the S&P 500 will be closing out what has been a historic 200 trading days for the index. The current bull market hasn't quite reached the 200-trading day point, but for most of its existence, it has ranked as one of the strongest at that point in its life. The first 190 trading days of this rally have been the strongest on record, just edging out the rallies coming off the March 2009 and August 1982 lows.



It's Over

Thu, Dec 31, 2020

The 2020 market year is officially behind us, and for most of the ETFs in our Asset Class Performance Matrix is was a great year. The top-performing ETF in our matrix was the Nasdaq 100 (QQQ), which advanced 48.7% on a total return basis. Fittingly, in second place silver (SLV) posted a gain of 47.5%. Other big winners this year were large-cap growth (IVW), Consumer Discretionary, (XLY), Technology (XLK), Communication Services (XLC), and China (ASHR). All of these ETFs posted annual returns of more than 25%. On the downside, there were some big losers, though. Oil (USO) lost two-thirds of its value, while Natural Gas (UNG) dropped 45%. The only other ETFs that experienced declines of more than 20% were Brazil (EWZ) and Energy (XLE).

The middle column of our matrix shows each ETF's total return since the 3/23 closing S&P 500 low. There were some truly mind-boggling returns as SLV, India (PIN), Australia (EWA), the Materials sector (XLB), Mid

Cap Value (IJJ), Small Cap Growth (IJT), Mid Cap Growth (IJK), the Russell 2000 (IWM), the Small Cap S&P 600 (IJR), and the Mid Cap S&P 400 (IJH) all advanced 90% or more. Over that same span, the only ETFs that were down were long-term US Treasuries (TLT), UNG, and USO.

What was a very strong year for financial assets in 2020 was capped off with a strong December. In the US, every major index ETF was up at least 3%, every sector was positive, and every international ETF finished in the green. In fact, of the nearly 60 ETFs in the matrix, only three were down in December (IEF, TLT, and of course UNG).

Asset Class Performance December, Since 3/23, and YTD - Total Return (%)

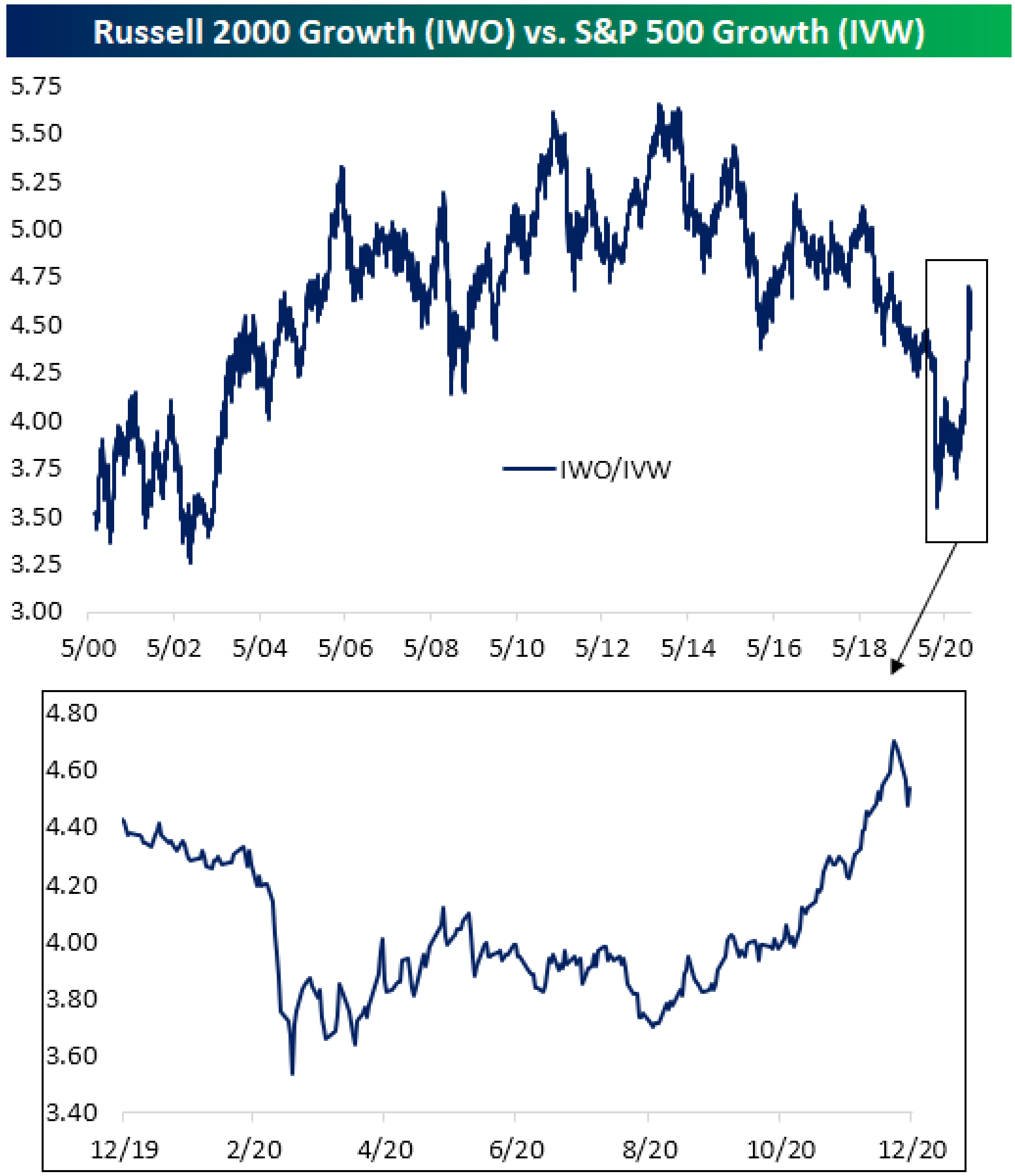
US Related			Since		Global			Since	
ETF	Description	December	3/23	YTD	ETF	Description	December	3/23	YTD
SPY	S&P 500	3.83	70.05	18.52	EWA	Australia	6.37	91.32	8.33
DIA	Dow 30	3.36	66.94	9.68	EWZ	Brazil	12.22	81.38	-20.41
QQQ	Nasdaq 100	4.97	85.09	48.71	EWC	Canada	3.48	79.31	5.88
IJH	S&P Midcap 400	6.62	92.30	13.75	ASHR	China	5.45	62.46	36.26
IJR	S&P Smallcap 600	8.31	90.10	11.34	EWQ	France	3.19	65.01	3.16
IWB	Russell 1000	4.20	75.34	20.87	EWG	Germany	5.47	75.19	10.77
IWM	Russell 2000	8.79	99.32	20.19	EWH	Hong Kong	4.54	39.23	4.21
IWV	Russell 3000	4.53	77.25	20.69	PIN	India	10.30	92.14	18.64
					EWI	Italy	4.14	59.70	1.88
IVW	S&P 500 Growth	4.08	78.55	33.30	EWJ	Japan	5.41	53.27	15.49
IJK	Midcap 400 Growth	6.49	94.01	22.61	EWW	Mexico	7.12	73.66	-3.12
IJT	Smallcap 600 Growth	8.82	92.89	19.21	EWP	Spain	3.17	51.68	-3.60
IVE	S&P 500 Value	3.40	58.77	1.26	RSX	Russia	9.35	64.14	-0.15
IJJ	Midcap 400 Value	6.87	90.04	3.78	EWU	UK	5.14	53.42	-11.55
IJS	Smallcap 600 Value	7.59	86.97	2.72					
DVY	DJ Dividend	3.39	60.37	-4.88	EFA	EAFE	5.21	60.97	7.80
RSP	S&P 500 Equalweight	4.22	80.29	12.79	EEM	Emerging Mkts	7.02	71.37	16.91
					IOO	Global 100	4.69	64.88	18.73
FXB	British Pound	2.51	18.77	2.86	BKF	BRIC	4.31	61.81	16.46
FXE	Euro	2.33	13.12	7.94					
FXY	Yen	1.07	7.38	4.62	DBC	Commodities	5.38	32.70	-7.90
					USO	Oil	6.55	-15.47	-67.80
XLY	Cons Disc	2.49	84.97	29.71	UNG	Nat. Gas	-13.30	-27.35	-45.49
XLP	Cons Stap	1.74	41.93	10.24	GLD	Gold	7.01	21.91	24.81
XLE	Energy	4.59	68.01	-32.46	SLV	Silver	16.84	99.80	47.45
XLF	Financials	6.35	69.93	-1.62					
XLV	Health Care	3.87	54.02	13.41	SHY	1-3 Yr Treasuries	0.03	0.39	3.03
XLI	Industrials	1.13	84.10	11.10	IEF	7-10 Yr Treasuries	-0.26	0.30	9.98
XLB	Materials	2.53	91.76	20.58	TLT	20+ Yr Treasuries	-1.14	-3.79	18.25
XLK	Technology	5.70	86.30	43.84	AGG	Aggregate Bond	0.12	6.81	7.51
XLC	Comm Services	3.45	68.50	27.04	BND	Total Bond Market	0.15	7.10	7.71
XLU	Utilities	0.64	43.16	0.59	TIP	T.I.P.S.	1.09	9.33	10.83

Growth Dragging on Small Caps

Wed, Dec 30, 2020

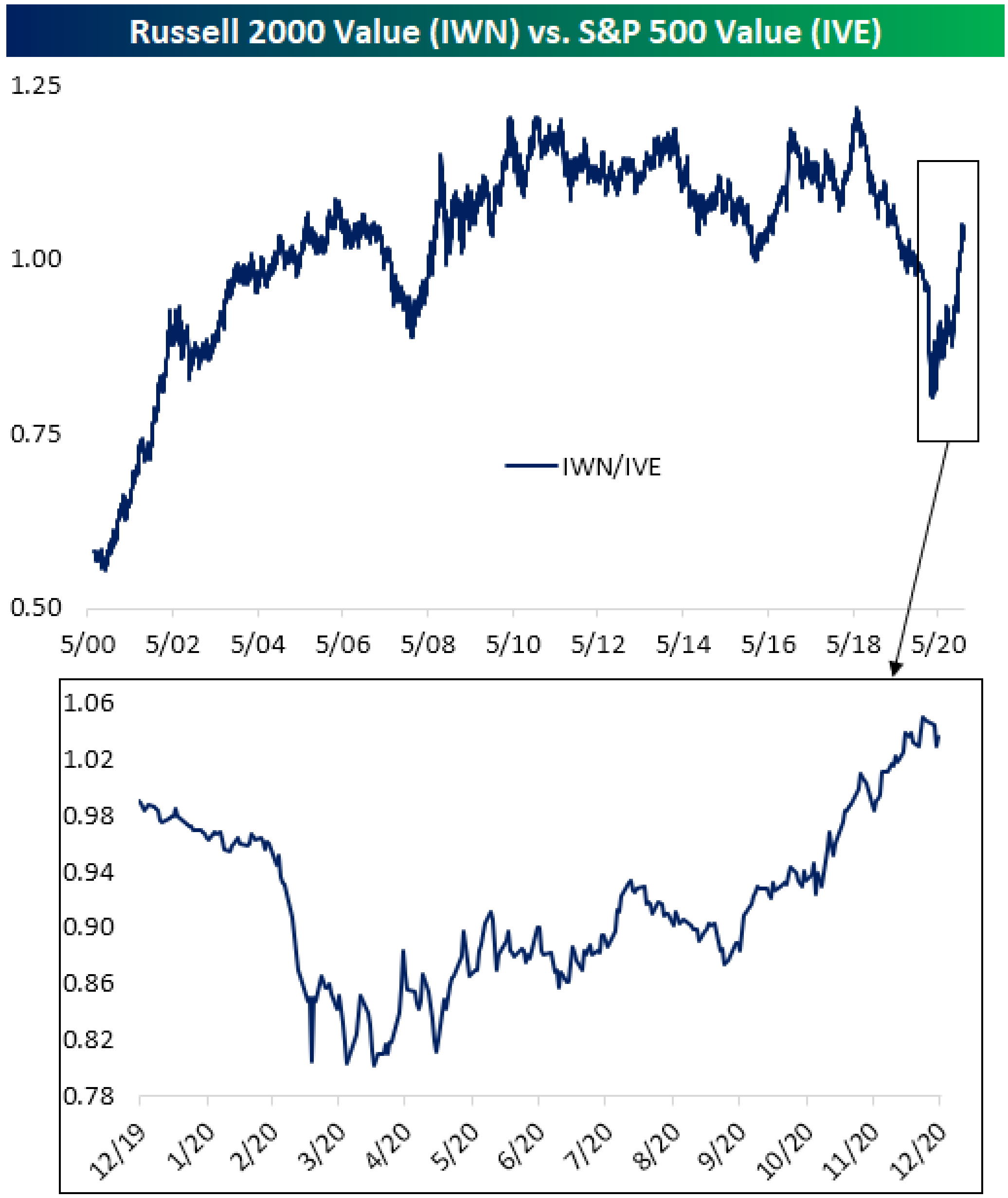
In the past couple of weeks, we have frequently been keeping tabs on small-cap equities which have been particularly strong performers of late resulting in very overbought readings as well as extended valuations. More specifically, taking a look at growth-oriented small-caps, with only a couple days left in the year small-cap growth stocks—proxied by the Russell 2000 Growth ETF (IWO)—are on pace to have outperformed large-cap equivalents in 2020. On December 10th, IWO surpassed the S&P 500 Growth ETF (IVW) in terms of YTD performance, and even after pulling back in the past week, IWO is still in the lead.

As a result of recent moves, there has been a sharp reversal on a relative basis between the two ETFs in the past week. In the chart below, we show the ratio of the Russell 2000 Growth ETF (IWO) versus the S&P 500 Growth ETF (IVW). This ratio took off beginning in the early fall meaning small-cap growth drastically outperformed large-cap growth. But the former's weakness in the past several days has put a halt to that move.



As to just how sharp of a reversal this was, in the five days through yesterday's close, the decline in the ratio of IWO to IVW was the largest since June. Before that, April and March saw declines that were even larger. Not only was this one of the biggest drops in the relative performance of small-cap growth to large-cap growth in the past few months, but that also stands in the bottom 0.5% of all readings going back to 2000 when the ETF first began trading. Outside of this past spring, the only other periods that have also experienced this type of underperformance of small-cap growth relative to large-cap growth was at various points in 2011, 2008, and a handful of times in the early 2000s.

Small-cap underperformance has not necessarily been broad though. For value stocks, small caps (IWN) have generally outperformed large caps (IVE) for the entirety of the new bull market. While there was a bit of a turn lower in recent days, it has been nowhere close to as dramatic of a move as growth stocks.

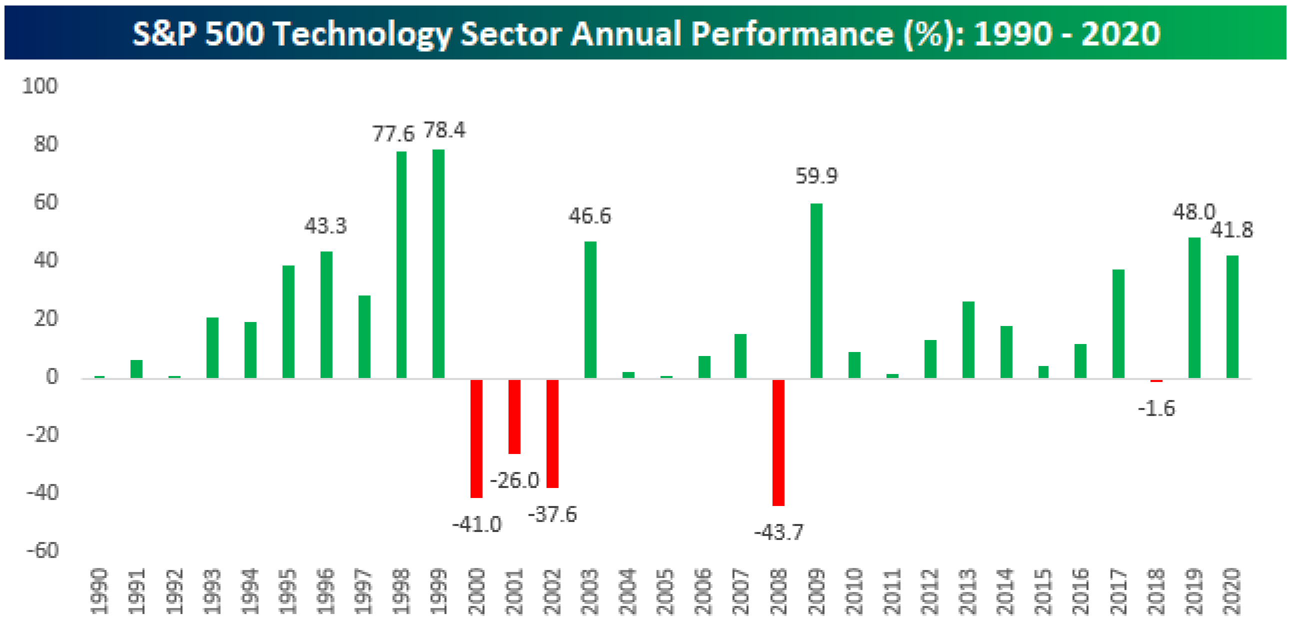


Back-to-Back Big Years for Technology

Wed, Dec 30, 2020

With just two trading days (including today) left in 2020, the S&P 500 Technology sector is on pace for its second year in a row of rallying more than 40%. Going back to 1990, the only time the Technology sector experienced back-to-back returns of more than 40% was in 1998 and 1999. Back then, not only was the Technology sector up 40%+ in back-to-back years, but it was also up over 75% in both of those years. If you think markets are pretty crazy these days, they still have nothing on the last two years of the 1990s!

In terms of cumulative returns, the Technology sector is up 210% since the last trading day of 2018, whereas in 1999 it was up 317% in a two-year span. What's also interesting to note about the last 31 years of returns for the Technology sector is how it has only experienced five down years, while the S&P 500 has been down in ten different years during that span. Furthermore, since 2009 there has only been one down year and the decline was a paltry 1.6%. Not a bad 12-year run! (We would be remiss in not pointing out what followed Tech's last two-year outperformance.)



A Speculative Frenzy Is Sweeping Wall Street and World Markets

Bloomberg News
December 19, 2020

Animal spirits are famously running wild across Wall Street, but crunch the numbers and this bull market is even crazier than it seems.

Global stocks are now worth around $100 trillion. American companies have raised a record $175 billion in public listings. Some $3 trillion of corporate bonds are trading with negative yields.

All the while the virus spreads, the economic cycle stays on life-support and businesses get thrashed by fresh lockdowns.

Spurred by endless monetary stimulus and bets on a post-pandemic world, day traders and institutional pros alike are enjoying the easiest financial conditions in history. ...

Here are the signs of market froth in this year of death, disease and economic calamity.

IPO Boom

Nothing evokes a stock peak like a rush to the public markets. Debuts from Snowflake to Airbnb took this year’s initial public offerings volume to a record $175 billion in the U.S., data compiled by Bloomberg show.

Special-purpose acquisition vehicles that raise money for a “blank check” company to buy whatever it wants have raised over $60 billion in 2020. That’s more than the previous decade combined.

Investors still can’t get enough. The first-day return for IPOs averaged 40% this year, the highest ever other than 1999 and 2000, according to one estimate.

All that has drawn unprecedented interest in the Renaissance IPO exchange-traded fund tracking new listings, up more than 100% this year this year. Even SPACs that haven’t announced an acquisition target are up almost 20% in 2020, Bespoke Investment Group noted.

“If that isn’t a sign of exuberance, we don’t know what is!” Bespoke analysts wrote in a note.

Stock Rally

Robinhood traders have become the talk of Wall Street this year by speculating on everything from tech options to airline shares. With these retail investors chasing the equity rally along with institutional pros, the S&P 500 is trading with a sales multiple some 16% above the 2000 peak.

Everything is going up. A Goldman Sachs basket of the most-shorted stocks in the Russell 3000 has surged about 40% this quarter, triple the broader index. High-beta shares are near their highest versus low-volatility ones since 2011.

Every time the Russell 2000 has surged more than 95% off its trough, it has gone on to lose money over the next three months, according to SentimenTrader. It is now up roughly 100% from its March low.

Options Frenzy

Bullish retail investors have plunged into the complex world of derivatives like never before this year. Over the last 20 days, a record average of roughly 22 million call contracts have traded each day across U.S. exchanges.

Cboe’s equity put-call ratio has dropped near a decade low -- a sign traders have rarely ever been so hellbent on chasing upside in single stocks.

Merger Mania

Animal spirits in corporate boardrooms are another infamous sign of a market top. This quarter is shaping up to be the strongest for deal-making activity since 2016 after a record third quarter. S&P Global buying IHS Markit Ltd. and Advanced Micro Devices taking over Xilinx are among the blockbusters.

With corporate cash balances rising in recent years and deal volume as a percentage of market value still below a long-time average, it is possible the recent activity is just the start.

Europe Joins In

Even Europe’s IPO market, which is much smaller in size than the one in the U.S. and less accustomed to big first-day pops, is going bananas.

Among the 44 firms that have listed on European exchanges since Nov. 9 -- the day news of a coronavirus vaccine set off a bull run in equities -- the average gain has been 16%, according to data compiled by Bloomberg. About 70% of them are trading above their IPO price. ...

Credit Rebound

In a world of almost $18 trillion negative-yielding debt, investors have been forced to gorge on risky corporate bonds at record valuations.

In the U.S., yields on junk bonds have tumbled far below levels at which high-grade borrowers could issue earlier this year.

Even Carnival, the fallen-angel cruise ship operator, has progressively cut funding premiums this year. The stockpile of negative-yielding corporate debt now stands at over $3 trillion.

Emerging Markets

Naturally it's boom times for emerging-market nations selling more than $730 billion in dollar and euro bonds in 2020, more than in any previous year.

Even with political turmoil, Peru sold the lowest-yielding century bonds ever from a developing-economy government. Ivory Coast priced euro-denominated debt with a lower yield than last year, despite its participation in a G-20 debt relief initiative and an ongoing International Monetary Fund program.

Bitcoin's Back

To diehards, Bitcoin's more than 200% surge this year on a wave of new money shows crypto's time has come. To many on Wall Street (and us), it's just the latest sign of irrational exuberance.

"We view it and other cryptocurrencies as 'digital tulips.' We have no way to value them," Yardeni Research analysts including Ed Yardeni wrote in a note. "We do watch Bitcoin's price action as a gauge of speculative excesses."

Its volatility is a hard pill to swallow for most but the likes of JPMorgan Chase & Co. and Nomura Holdings have noted plenty of interest, from family offices to trend-following quants.

The virtual currency is surfing a wave of speculation for long-duration assets, from solar energy to Tesla Inc. shares, as investors seek a stake in a technology of tomorrow -- valuations be damned.

Follow-ups

From the NYT's Kara Swisher's annual predictions published Friday:

Speaking of the end, many of the multitude of "special interest acquisition companies" that have popped up in recent years and raised giant piles of money will fold in 2021 and 2022. (These SPACs are a financial maneuver seen as a back door to taking a start-up public, an alternative to a traditional I.P.O.)

There have been 165 SPACs in 2020, double the number the year before and five times more than five years ago. Back when there was a rush of new venture capital flooding the market, I used to say that there were not enough ratholes to shove all the money down. Guess what? There are also not enough rathole companies to merge into these SPACs.

From the front page of Friday's WSJ:

U.S. IPO Market Reaches Record Total

Few see signs of letup after companies raise more than $167 billion despite pandemic

By Maureen Farrell

Defying expectations, investors piled into initial public offerings at a record rate in 2020, and few expect the euphoria to wear off soon.

Companies raised $167.2 billion through 454 offerings on U.S. exchanges this year through Dec. 24, compared with the previous full-year record of $107.9 billion at the height of the dot-com boom in 1999, according to Dealogic.

The pandemic turned the typical rhythm of the IPO market on its head, with $67.3 billion raised in the fourth quarter. That amount is roughly six times the total for the first three months of the year.

As a result of the scramble, stalwarts of the 21st-century economy including Airbnb, DoorDash ... are now publicly traded, accessible to the average investor.

When the pandemic began shutting down swaths of the U.S. economy in March and the stock market swooned, veteran IPO watchers braced for another disappointing year after activity in 2019 fell short of expectations.

Following a brief pause, new-issue activity resumed in late May after the Federal Reserve signaled it would take extraordinary measures to shore up the economy, and the stock market rebounded from a steep decline.

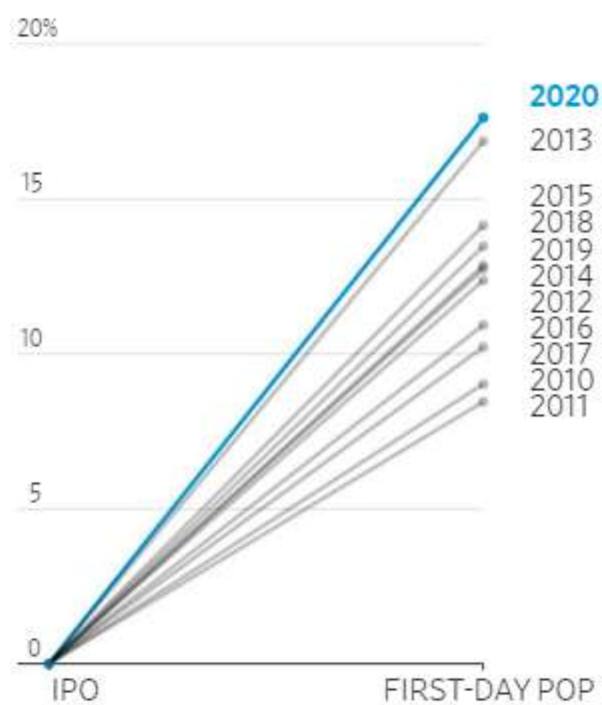
Several stocks that made their debuts around then soared, setting the stage for a race to the public markets that after a brief holiday pause is expected to pick up again in the new year.

The IPO market got a boost from a surprising surge in special-purpose acquisition companies, or SPACs, empty vehicles that raise money through listings and then look for businesses to merge with. They represent a bet that a yet-unknown business will generate steep returns and typify the risk appetite that is fueling new issues and markets more broadly.

Nearly half of all fundraising in the IPO market was for SPACs, and the total raised through SPACs this year is almost six times as much as the vehicles raised in 2019, the previous record-setting year.

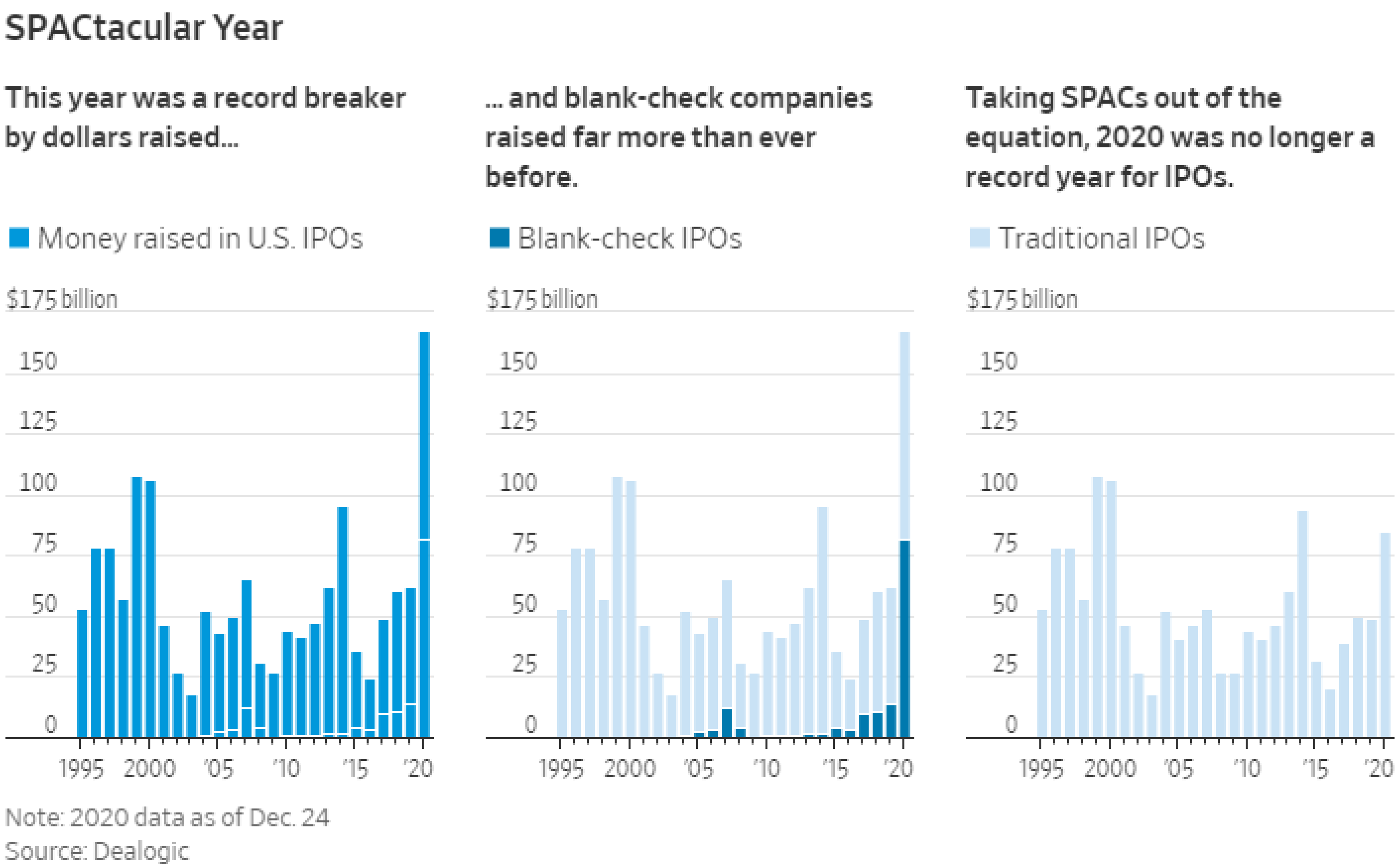
The IPO frenzy reached its height in the second week of December, typically a quiet time for new offerings as year-end approaches, when Airbnb and DoorDash soared in early trading. That gave the two companies, which have yet to

Average first-day IPO performance



Note: 2020 as of Dec. 23
Source: Dealogic

produce consistent profits, valuations stretching well into the tens of billions of dollars.



Those gains raised eyebrows among some who worry the IPO market is overheating and drew parallels with the period before the internet bubble burst in early 2000. They point to a surge in interest among individual investors, many of whom use a brokerage app run by Robinhood Financial. If history is any guide, they say, such investors are liable to run for the exits as soon as markets reverse course. ...

Few bankers predict the current pace will abate soon.

“With interest rates near zero, there are few asset classes out there that offer a return above inflation. And U.S. equities is one of those, including IPOs,” said Jeff Zajkowski, head of Americas equity capital markets at JPMorgan Chase & Co.

A slew of billion-dollar-plus startups, like Robinhood itself, bitcoin exchange Coinbase Global and grocery-delivery service Instacart, are waiting in the wings. ...

And the SPAC frenzy will likely continue. Noted technology investor SoftBank Group filed paperwork for a potential SPAC in late December. The Japanese conglomerate is considering plans to bring at least two more to market in 2021, according to people familiar with its plans. ...

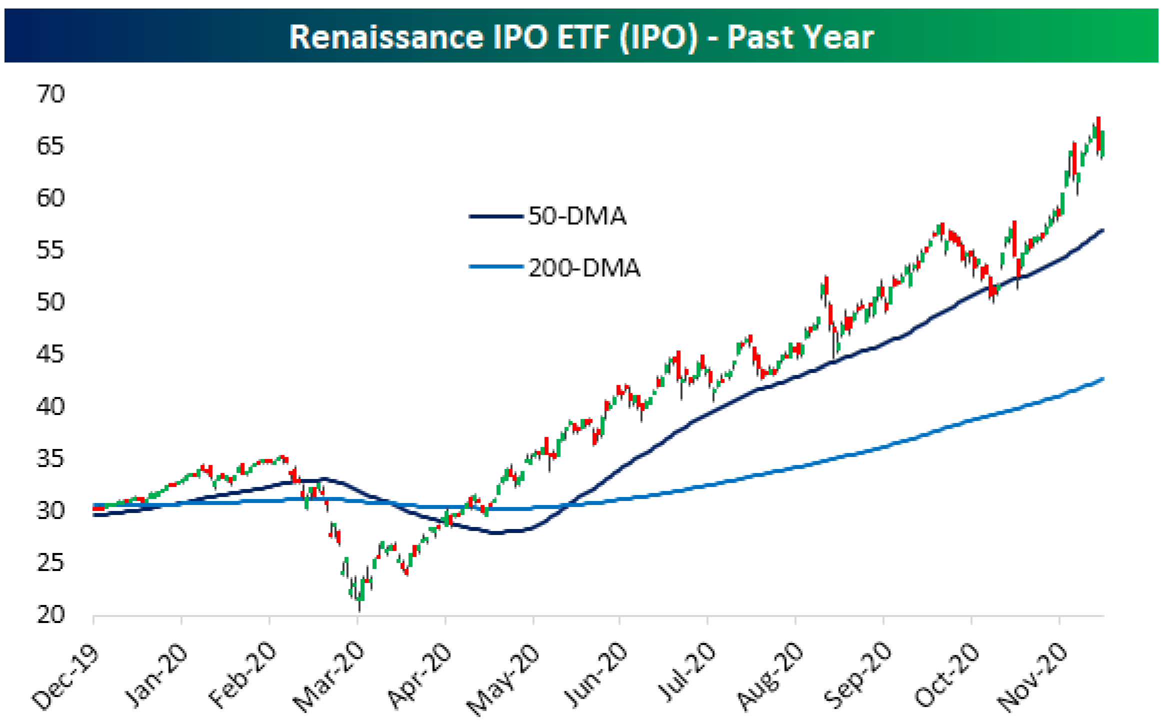
This year’s technology IPOs—the backbone of the new-issue market—have posted the biggest gains on their first day of trading since 2000, at 34% on average compared with 65% then, according to Dealogic. (Overall, IPOs have jumped roughly 18% on their first day of trading; excluding SPACs, the average first-day return of operating companies is about 36%.) On average, 2020 IPOs have risen roughly 48% from their original prices. ...

From Bespoke:

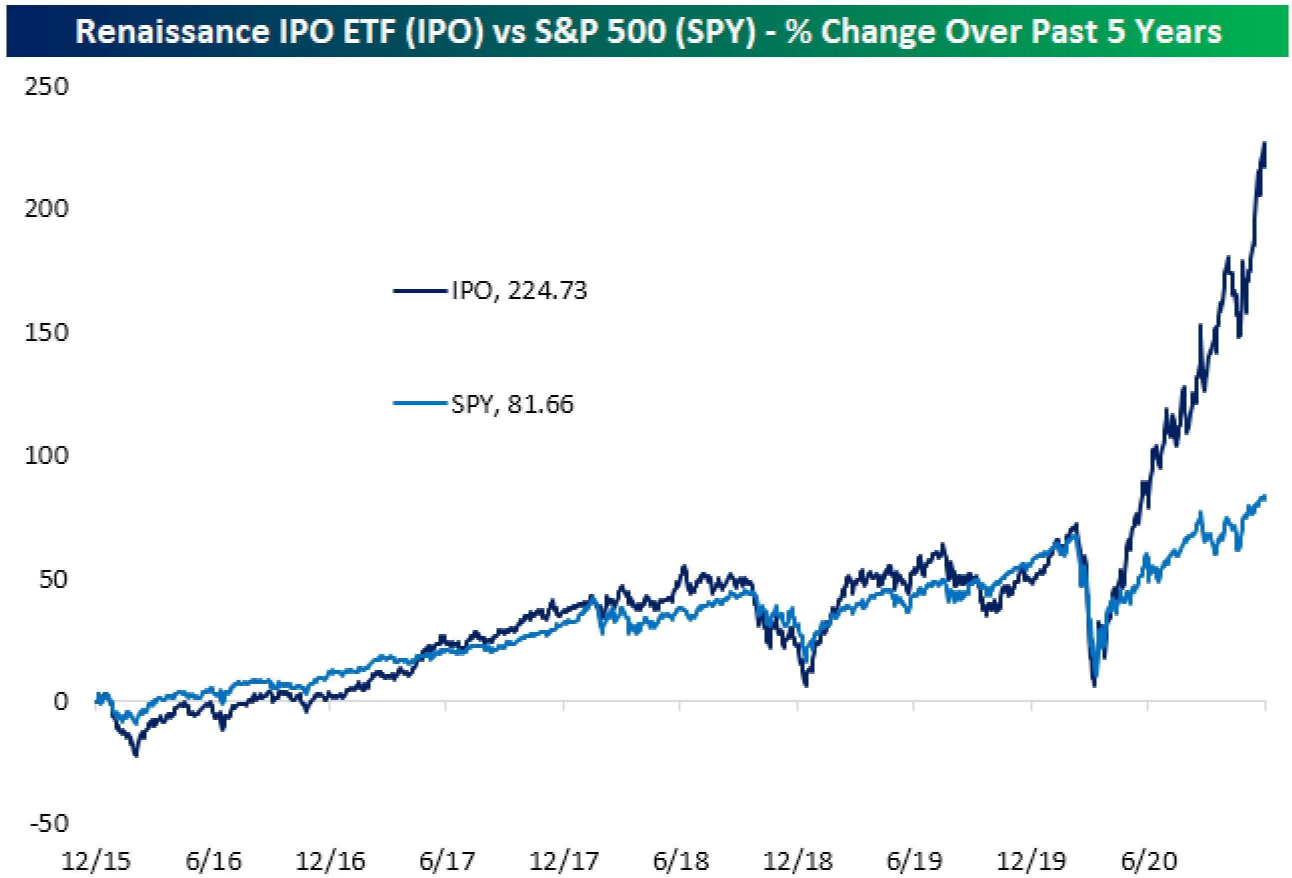
IPO Craze

Fri, Dec 11, 2020

It has been a big week for IPOs with DoorDash (DASH) and Airbnb (ABNB) both hitting the secondary market. These two stocks saw massive first-day gains of 86% and 113%, respectively. Generally speaking with the two aforementioned stocks as a case study, recent IPOs have been welcomed with open arms. As a result, the IPO ETF (IPO) has seen a sizeable rally having gained over 30% since the low at the end of October. While neither DoorDash nor Airbnb are current holdings of this ETF, this week saw some volatility with a 3% drop on the day of DoorDash's debut and a 2.5% rally yesterday when Airbnb debuted. IPO currently sits just off its highs after the past month and a half's rally, but that is at some of the most overbought levels of the past five years ....



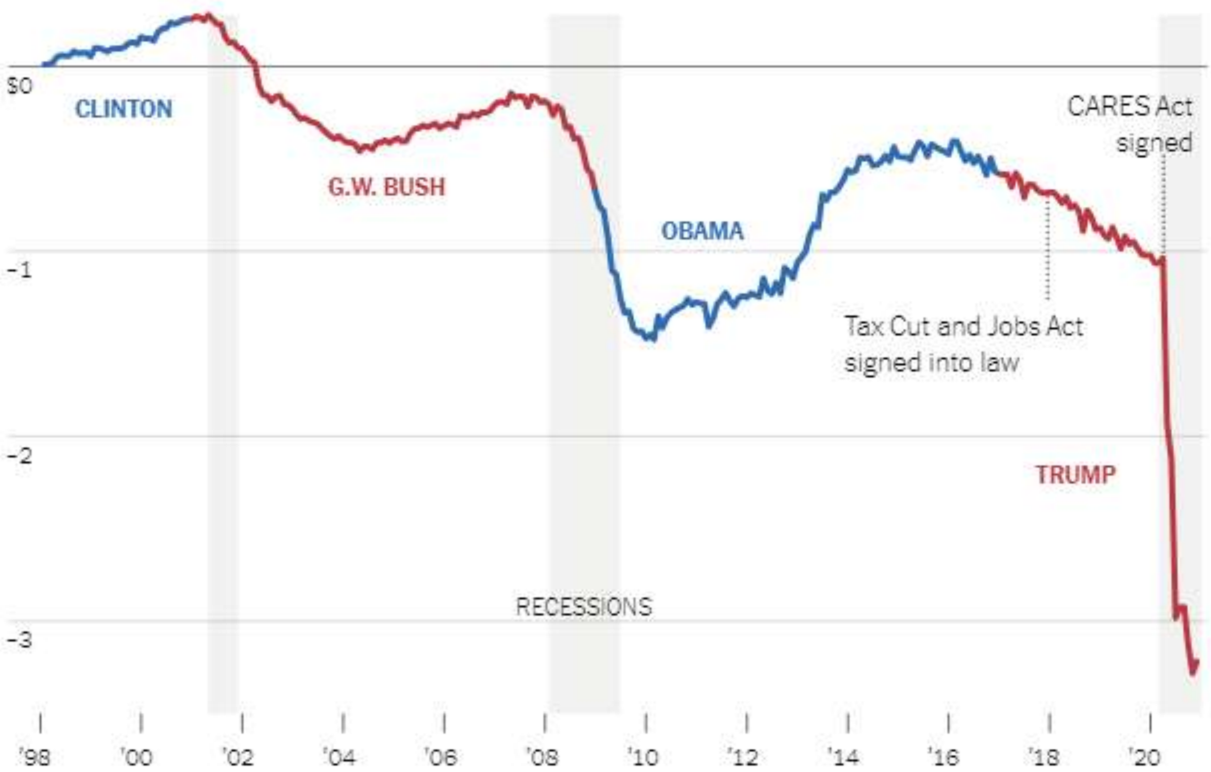
Relative to the S&P 500 (SPY), IPOs have seen massive outperformance since the bear market lows. In the chart below we show the performance of the Renaissance IPO ETF (IPO) versus the S&P 500 (SPY) over the past five years. From 2016 through the pandemic lows in March, these two tracked each other very closely, but IPO has skyrocketed versus SPY over the last nine months.



Thursday's NYT's **The Year in Charts** by Steven Rattner highlighted one of our two longer-term, and often repeated, concerns:

... Well before the coronavirus upended the economy, Mr. Trump had put the country on track for a return to trillion-dollar deficits, a terrible policy when unemployment was near record low levels. His administration promised that the 2017 tax cut would pay for itself; it never came close. He enabled huge spending increases. Then came Covid-19.

Federal budget balance, 12-month sum, in trillions



Source: U.S. Department of the Treasury

Federal debt held by the public as a percentage of G.D.P.

Source: Congressional Budget Office, Committee for a Responsible Federal Budget · "Pre-pandemic projection" is based on a C.B.O. March 2020 baseline forecast. "Current trajectory" is a September C.R.F.B. forecast that assumes $1 trillion of fiscal support, extension of various expiring tax provisions, and appropriations growth in proportion to that of the economy.

The resulting stimulus bills were essential to keeping the American economy together, but coming on top of an already huge deficit, the additional spending sent the nation's ratio of debt to gross domestic product soaring past 100 percent for the first time since World War II. As with so much else, Mr. Trump is leaving this mess behind for others to fix.

Steven Rattner, a counselor to the Treasury secretary in the Obama administration, is a Wall Street executive and a contributing opinion writer.

From Morningstar:

5 Questions to Ask a Financial Advisor

Inquire about areas of expertise, compensation arrangements, and credentials before signing on for financial help.

Christine Benz
Dec 10, 2020

Investment guru Bill Bernstein once quipped that by the time you know enough to select a high-quality financial advisor, you could probably manage your assets on your own.

Sadly, that's not all that far from the truth. The financial-advice industry features a bewildering array of titles, designations, and compensation schemes. Some advisors are fiduciaries (like HCM), some aren't.

And even though advisors must obtain licenses if they're selling securities, and pass tests and log work experience if they want to earn certain credentials ... there aren't any minimum standards in place for calling yourself a financial advisor. You could work your whole life selling cars and no one would stop you from hanging out a shingle as a financial advisor tomorrow; you'd be competing head-to-head with advisors with years of experience and prospective clients wouldn't necessarily know the difference.

It's no wonder so many investors shortcut the process, opting for recommendations from friends and family members with limited financial backgrounds. Nor should it come as a surprise that lesser advisors who happen to be strong salespeople can rake in clients, while skilled but less slick financial professionals toil in obscurity.

People skills *are* important when it comes to getting financial help; financial matters are highly personal, so you need to have a basic comfort level with any individual you're entrusting to help you out. But you also need to conduct due diligence before signing on with an advisor. The process can be broken down into two, rather manageable, steps. The first involves taking stock of your needs in the realm of advice consumption: What are you really looking for? The second step ... is to take what you just learned about your own needs and goals to identify an advisor who can help you meet them.

Here are the key questions to ask of prospective advisors.

1. Are you primarily a financial planner or an investment advisor?
This is one of the first forks in the road that investors will encounter when surveying the universe of financial advisors: There are wealth managers/investment advisors, and there are financial planners.

The former type of advisor has a narrower purview--investments--than do financial planners, who consider all major aspects of a financial plan, not just investments: insurance, estate planning, and household budgeting, to name a few. However, it's worth noting that the best investment advisors think holistically about their clients' plans ....

If you're seeking an investment advisor: Ask about investment strategy: Does it jibe with your own philosophy? Does the advisor use basic portfolio building blocks like low-cost mutual funds, or dabble (HCM doesn't) in more arcane investments like futures and options? Is the strategy readily understandable? (If not, ask every question you can think of until it is. If the advisor gets exasperated, you're not a match.) The gold-standard designation for this type of advisor is the chartered financial analyst (which I hold).

Softer, but no less important, does the advisor approach his or her job with a healthy dose of humility? You can get at that by asking about what he or she expects a balanced portfolio to return over the next decade. Any advisor who’s promising portfolio returns higher than the mid-single-digits over the next decade isn't being realistic and/or may be taking excessive risks.

2. Are you a fiduciary?
Here's another key question to ask of prospective advisors. Being a fiduciary simply means that the advisor must put their clients' interests ahead of their own when consulting on portfolios and plans. It seems fairly obvious that anyone proffering financial advice should adhere to such a standard, but as things stand today there is no uniform standard.

The good news is that many financial advisors already adhere to a fiduciary standard. Investment advisors who are registered investment advisors (again HCM)--or work for firms organized as registered investment advisors--are already fiduciaries. ... Your job is to ask the question outright: Are you a fiduciary, and will you be one in every context in which you'll serve me?

That's not to suggest that financial professionals who aren't fiduciaries are automatically unethical hacks, by the way; many non-fiduciaries uphold high ethical standards and treat clients with every bit as much care as their fiduciary counterparts. But investors who work with a fiduciary have a higher level of legal protections than if they work with an advisor who’s held to the lower "suitability standard." The latter type of advisors need to be able to defend their recommendations as being appropriate/suitable for you, versus fiduciaries, who are legally obligated to recommend the "best" products for you given your situation.

3. How do you charge for your services?
Advisor compensation can get messy. One of the first questions to ask is whether the advisor is fee-only (HCM), fee-based, or commission-based. Fee-only means that the advisor is compensated by charging fees for various services and is never compensated with commissions. Commission-based advisors obviously accept commissions for recommending products. Fee-based advisors may charge primarily fees for services they provide, but may also accept commissions. (People frequently confuse "fee-only" and "fee-based"; there is a difference.)

As with the fiduciary discussion above, advisors who accept commissions shouldn't automatically be marked with a skull and crossbones. But receiving commissions for products can introduce conflicts of interest, incentivizing advisors to recommend products that aren't necessarily in clients' best interests. The fee-only model is cleaner. And while the commission model is often touted as a way for investors with smaller portfolios to gain investment advice, that's a straw-man argument, in my opinion. ...

Percent of Your Assets: Many investment advisors charge in this fashion (often called the assets under management, or AUM, model), taking a percentage of the client's assets under management on an ongoing basis. The average rate is 1% for a $1 million portfolio, though clients with larger portfolios will generally pay a lower percentage. (After all, managing a $2 million portfolio isn't necessarily double the work of a $1 million portfolio.) Such fees are usually on top of whatever the investment fees are; for example, if an advisor charges 1% and puts the client in a portfolio with average fees of 0.35%, the client's fees are 1.35%. Advisors who employ the AUM model often have minimum portfolio thresholds; $1 million is a common level.

Best for: The AUM model is best for delegators who expect to need a fair amount of ongoing help and would also like to be able to be able to contact their advisors with questions or concerns on a regular basis. These consultations are baked into the ongoing fees you're paying, so you should be the type to take advantage of them. ...

4. What designations/credentials do you have?
In addition to getting clear on how you're compensating the advisor, it's also worth asking about designations the person has earned. Don't be blinded by a long list of letters after the advisor's name; some designations, such as the following, carry more heft and have heavier requirements than others. ...

If you're seeking investment advice, first and foremost, look for the following:

Chartered Financial Analyst (CFA): Individuals with this designation qualify as financial experts accredited by the CFA Institute. In order to use the CFA designation, advisors must log substantial work experience involving investment decision-making and take courses on subjects such as economics; financial reporting and analysis; ethical standards; equity and fixed-income investments; and portfolio management. They also must pass a series of 3 rigorous exams (the 2nd & 3rd of which are only given on one day a year) requiring substantial study time (they did).

5. What's your backup plan?
Even if your advisor is young, it's still worth asking about backup planning. Who would step in and offer assistance if the advisor could not do so for a period of time, due to death, illness, or even a long vacation? Especially if you're hiring an advisor on an AUM or retainer basis--but even if you're not--there should be individuals in place to serve as backups if your primary advisor isn't available. (that would be my Father)

Positions

As a general rule we sell any individual stock with a 20% or greater loss that we no longer consider a buy at the end of the year in all accounts, and may do so in taxable accounts even if we still consider the stock a buy and there is an equally attractive opportunity, or we believe it is likely that we will be able to profitably reenter the position after the 30 day wash-sale rule has expired.

FUN - On 12/28 we sold all positions in this Amusement Park REIT for 3 clients @ 39.49. The Insiders Forum, which we subscribe to, recommended selling on 6/26/20, with FUN closing @ 28.23.

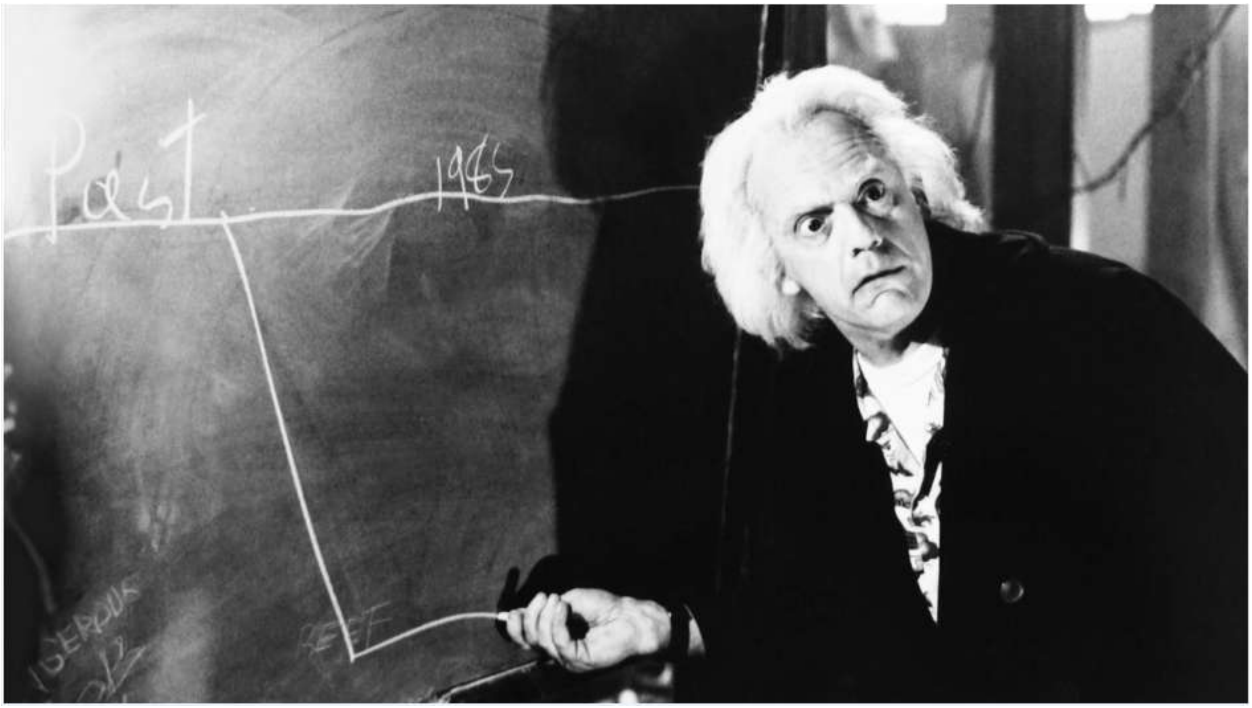
HPR - On 12/28 we sold all positions in this E&P for 3 clients @ 10.75. HPR is being acquired by Bonanza Creek Energy.

Lessons Learned Revisited

The full version, which is posted on our website, was shared on 5/17/20. As usual, our parenthetical updates are in red:

Lessons Learned

“It is difficult to make predictions, especially about the future.” – A Danish Proverb, often attributed to Niels Bohr



With the market bottom likely behind us (it was) and less market uncertainty now than in the past two months, I wanted to directly provide my thoughts on where we are and the important takeaways from the crisis.

What looks obvious now with hindsight was largely unthinkable three months ago. For example, the Spanish Flu in 1918 was a public health catastrophe that killed 50,000,000 people worldwide and 675,000 in the US. While the current COVID-19 crisis is not over yet, it is relatively safe to say that the Spanish Flu was much worse. However, from peak to bottom the Dow Jones Industrial Average (DJI) fell just shy of 11% in reaction to the Spanish Flu pandemic. In contrast, the DJI fell 37% from the peak on February 12th to the bottom on March 23rd. Large swaths of the world and US almost completely shutting down for more than a month did not seem politically possible, yet looking back it appears inevitable.

I did not see the full scope of the crisis until it was too late. (Most experts were predicting far fewer than the current 20,600,000 confirmed cases, and 350,000 deaths from Covid-19, with the IHME model now projecting 567,195 deaths by April1st. Recognizing the incompetence of the Trump administration wasn't difficult, but predicting that he would purposely "down-play" the seriousness of the pandemic, and politicize mask wearing was far beyond my prognosticating ability.) That being said, even if I had I would not have changed much. In order to successfully predict a market crash, you have to be able to first see the economic calamity coming before the rest of the market, and then predict precisely how the market will react to said calamity, as the economy and stock market are not perfectly correlated (in fact, they have very little correlation, if any at all).

Being right once is hard enough. Being right twice, and getting the timing perfect is exceptionally challenging. While being a perma-bear and waiting a decade for each new panic to say "I told you so" looks prophetic when everybody is bailing, missing out on long stretches of market gains makes such a strategy suspect at best. In the long run, staying the course tends to work better.

In the midst of a panic, moving to the sidelines and missing the rebound is a greater risk than staying the course or being too early when buying. However, roughly timing the bottom is possible, but acting too late can be very detrimental. On March 20th I felt that the market would likely bottom the following week, and more precisely that it would bottom that Tuesday. It bottomed on Monday. While "close" in terms of time, the S&P 500 ended up 6% higher by the end of Tuesday. Despite being a day late, adding positions on Tuesday rather than wait for the Market to retest the low appears to have been the right call (it was) ....

The economic news is not as bad for stocks as it appears on the surface. While breathless media coverage proclaims that we are seeing the worst unemployment numbers since the Great Depression, a large portion of this is due to the Government (rightly) changing the definition of unemployment to include people who are merely furloughed, or are independent contractors who aren't actively seeking another job. That's not to say that the situation for millions of people around the country isn't dire, because it is. However, the massive suffering at the individual level is unlikely to translate fully to further stock market losses. There is significant pent up demand for products and services that wasn't present during times such as the bottom of the Great Recession. Further, there likely won't be the political will to lockdown the country once more in the event of a COVID-19~~'s~~ second wave (we are currently suffering the 3rd wave, with the consequences of Christmas gatherings and New Year's celebrations yet to hit overwhelmed hospitals.) .... Looking ahead, while we could still see a retest of the March lows (we didn't), I don't see that as likely. In March the market was pricing in Armageddon, and while the news has been catastrophic from a public health perspective, uncertainty surrounding the bad news has decreased substantially, and it is uncertainty that most often results in sustained market downturns.

Reducing downside risk is hard while still trying to justify a management fee, and many of the instruments designed to do so don't. In my admittedly short investing career, QMNIX remains (see below) my biggest mistake, which we have covered ad nauseum in previous Worth Sharings. In short, QMNIX offered a Factor-based approach with 0 beta, which worked until it didn't. While potentially viable in the long run, managing maximum drawdown risk is very much an immediate term concern. Unfortunately, none of the alternatives we had invested in to fulfill the risk mitigation role functioned properly either in the midst of the panic. While most have recovered somewhat, the point of these funds was to mitigate the initial drawdown, which they didn't. Fortunately, many of our "risky" funds such as MTUM performed better than expected during the crash, which helped cushion the blow.

This isn't to say that products don't exist that reduce risk. For example, there is currently a Goldman Sachs Certificate of Deposit (CD) that yields 1.6% annually and, being FDIC insured, is functionally risk free. However, it is not possible for me to justify a 1% (for clients with individual positions) or even a 0.5% (for clients with funds only portfolios after the first year) management fee while investing a client in a product with such small potential upside. As such, in the future for clients with low risk tolerance, HCM will be recommending setting a portion of the portfolio outside of HCM's direct management that can be invested in such a product to reduce risk. HCM will then manage the "risky" portion of the overall portfolio. This will allow the client's risk tolerance to be met, while avoiding prohibitive management fees on low yielding products.

For somebody with a measurable risk tolerance, individual stocks do not appear advisable. It's too early to tell whether I will continue investing in individual stocks even for clients who are solely focused on capital appreciation, as the market needs to fully recover before determining whether individual IVA System picks (that rely on the Insider Buying and Value Factors, combined with analyst estimates) are worth the additional drawdown risk. (As our IVA System picks having performed very well, we will continue to offer individual stock selection to those clients with a suitable Risk Profile.)

Expertise is paramount. ... My expertise is in equities and crafting a portfolio to meet a client's risk profile, and particularly in times of uncertainty and panic that expertise is crucial to not making rash decisions that are financially ruinous. Knowing the limits of that expertise (such as trading futures in the oil market) is also critical to avoid making bad decisions.

Finally, patience is a very valuable investing skill, yet in the short term can seem indistinguishable from stubbornness paired with confirmation bias. Factors can underperform the broader market for decades at a time (such as the Value Factor currently), yet over the very long-term still significantly outperform. The inherent problem with such a long time horizon is that it can take an entire career to find out at the end that a Factor was no longer functioning. This is why it is critical to diversify across Factors.

Thank you for your trust during these troubled times,
Devin

From our March 2020 Newsletter:

QMNIX - On 3/23 we sold the remaining positions in this OEF for 2 clients. We will be providing further analysis of this failed Alternative Fund in a future Worth Sharing. We have added the S&P 500, via SPY, the largest tracking ETF, to Morningstar's chart:

Morningstar first rates a Fund for performance 3 years after inception. QMNIX's initial performance rating was 5 stars, with an initial analyst rating of Bronze. By that time it was already closed to new investors, with 2.2 billion in Total Assets (see our 11/18/17 Worth Sharing.) Not anymore, as shown below. As of Friday's close:

AQR Equity Market Neutral I QMNIX ★ Neutral

Analyst rating as of Jul 10, 2020

Quote Fund Analysis Performance Risk Price Portfolio People Parent Crowd Sense

NAV / 1-Day Return	Total Assets	Adj. Expense Ratio	Expense Ratio	Fee Level	Longest Manager Tenure
6.31 / **0.00**	48.6 Mil	1.320%	1.760%	Average	6.24 years
Category	**Alt Style Correlation / Relative Volatility**	**Min. Initial Investment**	**Status**	**TTM Yield**	**Turnover**
Market Neutral	Low / Medium	5,000,000	Open	0.00%	263%

USD | NAV as of Dec 31, 2020 | 1-Day Return as of Dec 31, 2020, 5:44 PM GMT-06:00