THOMPSON WEALTH MANAGEMENT

2nd Quarter 2020

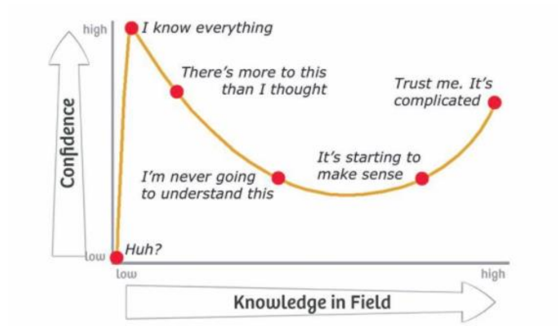
Hope you have had a happy and physically but not socially distanced summer so far! It has been an interesting ride this past quarter with markets continuing to recover, tempered by a resurgence in the virus over the last few weeks. Despite what may be in store for the markets in the near-to-medium term, here are some key insights that we believe are worth gleaning.

Investment Fund	Asset Class	Ticker	Q2	YTD	1-Year	3-Year	5-Year	10-Year
Vanguard ST Invest Grade Adm	Div Bond	VFSUX	4.84%	3.27%	4.95%	3.52%	3.03%	2.78%
Invesco QQQ Trust (Price)	LC U.S. Equity	QQQ	30.27%	16.91%	33.66%	22.63%	19.35%	20.45%
Invesco QQQ Trust (NAV)	LC U.S. Equity	QQQ	30.21%	16.81%	33.52%	22.67%	19.33%	20.43%
Vanguard SC Value Index Adm	SC U.S. Equity	VSIAX	20.78%	-21.34%	-16.48%	-2.56%	2%	9.35%
iShares Gold Trust ETF (Price)	Comm	IAU	12.74%	17.17%	25.85%	12.48%	8.42%	3.39%
iShares Gold Trust ETF (NAV)	Comm	IAU	9.82%	15.97%	25.20%	12.21%	8.32%	3.31%
Vanguard FTSE Dv Mkts ETF (Price)	Int'l Equity	VEA	16.93%	-11.11%	-4.53%	0.75%	2.45%	6.13%
Vanguard FTSE Dv Mkts ETF (NAV)	Int'l Equity	VEA	17.45%	-10.75%	-4.26%	0.90%	2.48%	6.10%
Vanguard Real Estate Index Adm	Speclty U.S. Equity	VGSLX	13.46%	-13.88%	-6.93%	2.23%	5.36%	9.71%
Vanguard Mid Cap Index Adm	MC U.S. Equity	VIMAX	24.96%	-7.18%	-0.20%	6.45%	6.99%	12.47%
Vanguard Value Index Adm	LC U.S. Equity	VVIAX	12.73%	-15.43%	-7.42%	3.88%	6.44%	11.22%
Vanguard Total Stk Mkt Index Adm	LC U.S. Equity	VTSAX	22.08%	-3.40%	6.45%	10.03%	10.02%	13.73%
Vanguard Small-Cap Index Adm	SC U.S. Equity	VSMAX	26.66%	-11.42%	-5.60%	3.99%	5.40%	11.59%
WTRISC CIT III for Metlife GAC	Cap Preservation	WWTAAX	0.58%	1.16%	2.39%	2.39%	2.34%	2.40%
Fidelity Advisor Strategic Income Z	Div Bond	FIWDX	8.30%	-0.97%	1.71%	3.27%	3.89%	4.58%
Fidelity Emerging Markets Index	Int'l Equity	FPADX	18.78%	-9.56%	-3.38%	1.86%	2.58%	N/A
Fidelity Global ex U.S. Index	Int'l Equity	FSGGX	16.78%	-10.60%	-4.48%	1.20%	2.35%	N/A
Fidelity 500 Index Fund	LC U.S. Equity	FXAIX	20.53%	-3.09%	7.49%	10.71%	10.72%	13.97%
Fidelity U.S. Bond Index Fund	Div Bond	FXNAX	2.77%	6.53%	9.01%	5.38%	4.32%	3.79%
iShares MSCI EAFE SC ETF (Price)	Int'l Equity	SCZ	20.82%	-13.03%	-3.72%	0.26%	3.74%	8.15%
iShares MSCI EAFE SC ETF (NAV)	Int'l Equity	SCZ	19.79%	-13.28%	-4.06%	0.32%	3.69%	8.01%
Target 20 Model Portfolio	Diversified	N/A	6.79%	2.72%	5.98%	4.66%	4.24%	N/A
Target 30 Model Portfolio	Diversified	N/A	8.26%	2.26%	5.92%	4.81%	4.44%	N/A
Target 40 Model Portfolio	Diversified	N/A	9.89%	1.66%	6.01%	5.21%	4.95%	N/A
Target 50 Model Portfolio	Diversified	N/A	11.81%	0.47%	5.47%	5.37%	5.28%	N/A
Target 60 Model Portfolio	Diversified	N/A	13.29%	-0.81%	4.79%	5.34%	5.46%	N/A
Target 70 Model Portfolio	Diversified	N/A	15.13%	-2.01%	4.28%	5.63%	5.95%	N/A
Target 85 Model Portfolio	Diversified	N/A	17.42%	-4.46%	2.63%	5.49%	6.19%	N/A

Among the major asset category benchmarks, international stocks performed the best with a 9.7% return in June, boosted by an 11.5% jump in emerging markets. Valuations were a little more reasonable and many European & Asian countries have been more effective in containing CV-19. The total US stock market returned 4.7%, led by large cap growth stocks (+7%). The total bond market produced a return of .65%, and there we saw somewhat of a rebound in the more credit sensitive (as opposed to interest rate sensitive) funds. For the year so far, the US equities are down about 5%, international equities are down about 10%, intermediate bonds are up 6% and short-term bonds are up 3%.

In the US we've benefitted from aggressive monetary and fiscal responses (see article: [Federal Reserve's $3 Trillion Virus Rescue Inflates Market Bubbles]). The accompanying liquidity and "animal spirits" narrative has resulted in a "V" shaped recovery in the stock market, at least for now; but the regional and sadly politically charged management of the virus almost guarantees a "U" shaped and possibly a "|_____|" shaped economic recovery, creating an anxious disconnect between Wall Street and Main Street. We have included an article by Robert Schiller, [Understanding the Pandemic Stock Market], that discusses how the market has been moving inversely to trends with CV-19 due to the idea that the govt will continue to provide stimulus/liquidity. This is why we point out that current market driving narratives are really superfluous to longer-term outcomes.

As much as we try to wrap investing in data and logic, an essential skill for long-term investors is the ability to accept and live with uncertainty – how much we don't know. Where are we on the road to recovery as far as the pandemic is concerned? Given recent trends, we may be fighting regional flare-ups for the duration of this particular phase of the virus. This scenario seems to be playing out as we speak. Current uncertainty is also exacerbated by political risk with the almost tribalization of the pandemic response and the anticipation of the upcoming election.



All of this played into our calculation to rebalance the portfolios at the end of March (almost at the bottom of the market) and then the target models again at the end of June when equity valuations were back to inflated levels. This had the effect of moving some money into equity when valuations were low and then paring it down a bit when back to inflated levels. Rebalancing is typically done once a year in order to keep target allocations properly aligned. That calculation changed on our part given the high volatility being experienced now. In this type of environment, markets tend to work within a more binary paradigm, meaning large swings either way.

Another thing we want to highlight is how well index funds have performed relative to asset class peer groups. There has been a lot of discussion as of late about how the market downturn might turn the tide against equity indexing and in favor of active management strategies. The implication is that research-based security selection strategies have an advantage in a down market. But that certainly hasn't been the case! *In each and every equity and fixed income asset class, the mutual fund category average underperformed the return of the index fund.* For example, in the mid-cap category, for the year to date period the difference is about 7%, and about 3% per year over the last ten years. Maybe you think this isn't a fair comparison because, well, how hard could it be to pick a mutual fund in each of 12 categories that outperforms the average? The Morningstar data lists 419 mid-cap funds, but only 29 or 7% of those funds beat the Vanguard Mid-Cap Index Admiral fund. Over the last five years, only 12% beat the index fund.

But picking an index beating fund is even harder than those numbers imply because there is low persistence in active manager performance over time -- the list of index beating funds isn't the same for the one, three, five, and ten-year periods – therefore, the actual odds of picking an index beating fund are well below 10%. And that doesn't take taxes into account, which would favor the low turnover index funds even more.

To continue to reinforce the emphasis on maintaining a long-term time horizon, we also included an article by Murray Coleman, Time in Markets (Not Market Timing) is Key to Building Wealth. This is especially true in times such as these, when there is tremendous volatility.

Enjoy the rest of your summer and continue to stay safe!
