

Advisory Notes



JUNE 2021

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Second Quarter in Review - Post Pandemic Reopening

In the first half of this year, the S&P 500 index has delivered its best returns since 1998. This is due to the cyclical rotation and breadth of the reopening recovery and positive GDP. Last year was a



year of turmoil that focused on lower Fed fund rates, fiscal stimulus and “open economy stocks” vs. “closed economy stocks.” This resulted in 2020 being led by the market “big 5” – Apple, Microsoft, Amazon, Alphabet (Google) and Facebook. Without these five mega-cap companies, the S&P 500 in 2020 would have returned 3% rather than 18%. So far in 2021, these stocks have cooled off and energy, financials, industrials and materials companies and industries have

paved the way. The range of the market is wide and the underlying fundamentals are improving as the country continues to “unmask” and to get vaccinated. (See Market Table.)

As the fiscal spending continues to help prop up the economy, the Federal Reserve is keeping its eye on inflation. Supply/demand constraints have also created inflationary fears in housing, real estate and automotive areas. We see some of these issues subsiding in the second half of this year, but it may, unfortunately, continue into 2022. Please see more in depth articles inside this issue.

As always, we are managing your portfolios with your specific goals and objectives in mind. Wishes to you for a happy and healthy summer!

Joseph M. Valicenti
President/CEO

Market Table

| Valicenti Advisory Services, Inc. Comparative Index Period Returns From 03-31-21 THROUGH 06-30-21 | | | | | | | | |
|---|-------|---------|--------|--------------------|------------------------------|------------------------------|---------------------------|-----------------------------------|
| | DJIA | S&P 500 | NASDAQ | Russell 2000 Index | BBG Barclays AGGR Bond Index | BBG Barclays Muni Bond Index | FTSE Corporate Bond Index | U.S. Treasury Bill Index (90 day) |
| 03-31-21 to 04-30-21 | 2.78 | 5.34 | 5.43 | 2.10 | 0.79 | 0.91 | 1.24 | 0.00 |
| 04-30-21 to 05-31-21 | 2.21 | 0.70 | -1.44 | 0.21 | 0.33 | 0.32 | 0.57 | 0.00 |
| 05-31-21 to 06-30-21 | 0.02 | 2.33 | 5.55 | 1.94 | 0.70 | 0.30 | 1.84 | 0.00 |
| Cumulative Returns 03-31-21 to 06-30-21 | 5.08 | 8.55 | 9.68 | 4.29 | 1.83 | 1.53 | 3.69 | 0.00 |
| YTD Returns 12-31-20 to 06-30-21 | 13.79 | 15.25 | 12.92 | 17.54 | -1.60 | 1.15 | -1.08 | 0.06 |

The highest compliment our clients can give is the referral of their friends and family. Thank you for your trust!

Director's Chair: Freedom of Speech and Your Portfolio

In the 1972, (Golden Globe winning season) episode of *All in the Family*, *The Bunkers and the Swingers*, lonely housewife Edith Bunker responds to a personal ad in a magazine to find



new friends unaware the ad is seeking people looking for a different kind of *friendship*. Upon discovering that the couple known as the Rempley's are not there to be friends, it causes a culture clash with the Bunker family. Curtis Rempley says, "I may disagree with what you say, but I'll defend with my life your right to say it." The quote is paraphrasing a line attributed to French philosopher Voltaire, "I disapprove of what you say, but I will defend to the death your right to say it." Technically, Voltaire's biographer created the saying as a summation of his beliefs on freedom of expression.

America was once home to the free speech movement of the 1960s. Ideas that were at the time radical, counterculture and even subversive were protected and fostered as a free exchange of ideas. More recent population changes have had a less favorable opinion on freedom of speech. A Pew Research poll found that a growing number of individuals found it acceptable for the government to prevent saying things that are offensive. But what constitutes "offensive?" American apple pie can be considered to be offensive according to a story published in *The Guardian*.

Free speech and a free capitalist economy go hand in hand. Americans over the past 100 years have enjoyed some of the highest levels of free speech when compared to other nations. During that time, the United States grew to have the largest Gross Domestic Product (GDP), highest income per capita for its citizens (for large countries), most competitive economy and the sole super-power status. In 1900, 85% of the world's population lived in poverty. As the number of monarchies and dictatorships declined

through the 20th century bringing with it democracy, free speech and capitalism, global poverty declined to 72% of population in 1955 and 60% by 1965. The World Bank estimates that at the dawn of the 1980s, 44% of Earth's population lived in poverty, 29% by 2000 and 16% by 2010. The World Bank defines poverty as the cost of living per person per day: \$1.91 in 33 low-income countries, \$3.21 in 32 lower-middle income, \$5.48 in 32 upper-middle income and \$21.70 in 29 high-income countries. For the U.S., it is \$33.26.

Western countries adopted both free speech and capitalism through the last century, enriching their populations. Such riches also enabled developed nations to give aid to less developed nations that lacked capitalism and free speech.

For the past sixty years, Cuba and the former Soviet Union have/had constitutions that guarantee freedom of speech, freedom of the press, freedom of assembly and pursuit of religion. They also have/had a clause that blocked rights if it interferes with the government. If you spoke against the government in the former U.S.S.R., you got a free all expenses paid trip to Siberia. In communist Cuba, you will be taken to a prison cell and beaten. Both countries have/had a low standard of living compared to any free western country. Cuba currently has the lowest rates of diabetes and obesity anywhere in the moderately developed world. This is a side effect of living on a government provided diet that provides only six pounds of rice, 20 ounces of beans, six pounds of sugar, one liter of milk (only for children under age seven), five to 12 eggs, 15 pounds of potatoes/bananas, one pound of beef mixed with soy and two pounds of chicken per month per person. For the most part, Cubans are slim, but have you noticed the ruling members of the Communist Party usually are obese.

We are all equal, some are more equal than others, as George Orwell said. The difference is freedom of speech creates the environment for a free economy and visa versa. Both create wealth. Even China has

seen increased freedoms creating increased economic growth. Over the past 20 years hundreds of millions of people have been lifted out of poverty in China, coincidentally, as the country liberalized, relatively speaking, allowing for private ownership of enterprises. From 1998-2005, China saw the highest GDP growth for the nation in the past 100 years. This was the period of liberalization, where an individual could also say things publicly that would have gotten them executed in the pre-1993 and certainly the pre-1977 periods. With the assentation of President Xi, as his administration has sought to reverse some of the policies of liberalization, what has occurred? Slowing GDP growth, using real figures not Chinese government statistics.

Another example can be seen in Europe, which has adopted legislation during the past 20 years restricting speech. During that period, the United States has easily registered greater GDP growth versus the European Union in almost every year. You do not start Amazon, Apple and Google in Europe – only the freest environments allow for transformative creations.

Your portfolios rely on the American system that implicitly link freedoms such as speech with economic gains. If the American economy is to continue to be the premier growth driver going forward, we should hope against restricting freedom no matter what side of the aisle is speaking. This obviously does not apply to speech that presents as the Supreme Court wrote, a "clear and present danger" of inciting imminent lawless action, which is a clear bright line of when speech can be restricted in America. The tribalism in today's politics is breaking the cohesiveness of the nation which, in time, if not fixed will undermine the currency and the economic underpinnings that allow for wealth creation. Imagine your portfolios denominated in Zimbabwe Dollars, Yugoslav Dinars, and North Korean Won. What will that purchasing power be? A better economic and investment environment likely lies in a world where we return to viewing those who do not agree with us as being just wrong instead of evil.

See **Director's Chair** on Page 3

Charles Schwab Update

On June 15, Schwab sent clients their annual Standing Letters of Authorization (SLOA) reminder. This notice is to remind clients of the authorization



given to their independent investment advisor. Once received, clients are asked to review the instructions for accuracy. These instructions specify the account(s) into which the advisor may transfer assets, as well as the distribution types that may be used. Distribution types include wires, journals, checks and Schwab MoneyLink transfers, which are electronic fund transfers between a Schwab brokerage account and a linked account. No action is required if the instructions are correct. If your email address is on file with Schwab, you will receive the notification that way. If Schwab does not have your email address, you will receive this notice by standard mail. If you have any questions about the notice, please give us a call.

Melissa B. Mickley, FPQP®
Administrative and Marketing Assistant

Director's Chair

(Continued from Page 2)

Much has changed in the 49 years since this *All in the Family* episode first aired. But if Rempley was looking for bigger stock market gains his view of "I may disagree with what you say, but I'll defend with my life your right to say it" appears to be the right catalyst for a unified nation with a growing economy and increasing wealth.

Louis F. Ruize
Director of Research/Portfolio Manager

Common Stock vs Preferred Stock

More often than not, investors talk about common stocks rather than preferred stocks. Although common stocks do carry more risk, their attraction is that their



value could increase substantially, whereas preferred stocks are a special class that are traded like stocks, but represent debt like a bond or a loan. They do not represent ownership and their distributions rarely increase so, generally speaking, you would buy a preferred stock for income rather than capital gains. Preferred stocks are first in line for dividends and are more likely to be repaid in a bankruptcy, since they are technically a loan. In addition, the dividends of preferred stocks are cumulative, so if a company does not pay the entire dividend in one quarter the difference is made up the next quarter.

Ralph H. Roberts, Jr.
Vice President of Client Services

Stock Indexes

Most of us have heard of stock indexes, but do not have a clear idea of what they are. A stock index is an average price for a large group of stocks either those on a particular stock exchange or across an entire investing sector. Indexes are developed from stocks with something in common, either on the same exchange, from the same industry or have the same company size or location.

An index based solely on stock prices is called a price-weighted index. This type of index ignores the importance of any particular stock or company size. The Dow Jones Industrial Average is a price-weighted average index made up of the stocks of the 30 most prominent companies in America.

A market value-weighted index takes into account the size of the companies involved. The price changes of small companies have less influence than those of larger companies.

There is another type of index called a market share weighted index, which is based on the number of shares rather than their total value.

The Standard & Poor's 500 Index is based on 500 United States corporations selected to represent a broader picture of economic activity.

Outside the United States, the most prominent index is the FTSE 100 Index comprised of the 100 largest companies on the London Stock Exchange.

Two other important indexes are France's CAC 40 and Japan's Nikkei 225.

Hopefully, this overview gives you a better understanding of Stock Indexes.

Ralph H. Roberts, Jr.
Vice President of Client Services



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Analyst Corner

Throughout most of the second quarter, both the market narrative and the market price action continued to favor the cyclical sectors such as Energy, Financials, Materials and Industrials as they tended to outperform driven by strong and robust economic growth numbers. Interpretations of the Federal Open Market Committee (FOMC) communications in the wake of the June meeting rendered a near-term challenge to the cyclical leadership. The main push back against unlimited fiscal and monetary dovishness was the idea that amidst the recovery in demand and with constraints to supply in some areas, continuing to maintain the emergency levels of accommodation for longer could increase the risks of deleterious inflationary outcomes. As a result, long-term interest rates fell significantly over a short period and growth names not necessarily reliant on a strong cyclical rebound found a footing once again.



The S&P 500 was up 8.6% on a total return basis for the quarter with the YTD result up 15.2% through the first six months of 2021. The Bloomberg Barclays U.S. Corporate Bond Index rallied 3.6% as the rising longer-term rates gave way to a corrective move in the opposite direction while credit concerns still seem far off. What remains to be seen now is whether or not the sectors benefitting most from the cyclical recovery regain leadership. This would likely take place alongside more yield curve steepening, strong cyclical sector outperformance and an acceptance that the cycle has much more before it runs its course. This is jux-

Positive Market Influences

Continued U.S. Recovery From COVID
Solid Growth Expectations
Earnings per Share Expectations

Negative Market Influences

Specter of Dovish Policy Abatement
Supply Constraints
ROW COVID Recovery

taped with the growth stock leadership scenario which would likely accompany a world where the sustained reflation and secular growth outcome fades towards a reality of a lower growth world facing real debt and demographic constraints.

The sharp change of circumstances regarding the growth versus cyclical value stock debate within the quarter led to Real Estate, Energy, Information Technology and Communication Services sector leadership this quarter. The more cycle-dependent Materials, Industrials and Consumer Discretionary sectors lagged the overall S&P. The concerns over the fading economic growth momentum would likely need to be ratified by continued supply and demand imbalances for key markets and possibly a resurgent COVID variant impeding progress on the re-opening front.

In regards to fiscal infrastructure spending, the path at this point is uncertain as a middling group of bipartisan legislators are still driving towards a compromise albeit a smaller and more narrow package. This in part could have been a factor in the dominance of the strong cyclical narrative stalling out temporarily. The upcoming quarter should bring news on this topic as well as reveal how the rest of the world is fairing with their re-opening and recovery efforts.

Positive Market Influences

- **Continued U.S. Recovery From COVID** – The CDC’s COVID data tracker shows new cases significantly lower relative to the height of the crisis with 65% of the adult population having received at

least one dose of the vaccine and 55% considered fully vaccinated.

- **Solid Growth Expectations** – Projections of Federal Reserve Board members for real GDP in 2021 are currently north of 6.8% and for 2022 they are north of 2.8%.
- **Earnings per Share Expectations** – 2021 S&P 500 Earnings are expected to grow very strongly this year, as the base on that growth is the trough year of 2020. Earnings expectations, at present, for 2022 are still in the vicinity of +10% according to consensus estimates.

Negative Market Influences

- **Specter of Dovish Policy Abatement** – The individual projections of FOMC members of the policy interest rate showed some movement by some towards a belief that rate hikes could come a bit sooner. As the size of a potential infrastructure bill gets ratcheted down for now, the level of fiscal support baked into assumptions is similarly getting reduced.
- **Supply Constraints** – With supplies of key inputs into production into various industries such as housing and automobiles getting tighter, this serves as a limiting factor to the amount of output that can be achieved in the economy.
- **ROW COVID Recovery** – Disparities among countries in regards to new case counts, variant exposures and vaccination rates may be weighing on the odds of a more synchronous global recovery.

Daniel P. Burchill
Security Analyst

Supreme Court Upholds Affordable Care Act

By a 7-2 vote, the Supreme Court on June 17 issued an opinion upholding the Affordable Care Act, allowing millions to keep their insurance coverage. The case centered on the individual mandate, the part of the law that compelled many Americans to purchase health insurance or pay a penalty. The entire Affordable Care Act, however, was left intact in ruling that Texas, other GOP-led states and two individuals had no legal right to bring their lawsuit in federal court. Because of this, the court did not rule on



whether the individual mandate is unconstitutional as there is no current penalty for forgoing insurance. The court's decision preserves the benefits that have become part of the nation's health care system.

Those that created the law believed the mandate would help drive healthy Americans to carry coverage to balance rising costs and adverse selection for insurers. The law's major provisions include protections for Americans with pre-existing health conditions, coverage for a number of preventive health benefits, expansion of the Medicaid program that insures lower income individuals and access to health insurance markets offering subsidized plans through advance premium tax credits.

The health law is now undergoing an additional expansion under President Biden, who sees it as the foundation for moving the U.S. to coverage for all. His COVID-19 relief bill increased subsidies for private health plans offered through the Affordable Care Act's insurance markets, which also provides higher federal payments before the states that have declined the law's Medicaid expansion. Roughly, 1.2 million Americans have enrolled with HealthCare.gov since Biden reopened enrollment amid high levels of COVID cases earlier this year.

Suzanne M. Valicenti
 President/CEO
 Valicenti Insurance Services, Inc.

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Investment Strategy

The second quarter of 2021 saw the U.S. economy and markets continue to gain strength as COVID restrictions lifted. While challenges occurred in supply chains, concerns over inflation, debt and deficits and COVID variants, markets have continued to be resilient and stay on an upward trajectory. As the economic reopening continues, concerns over inflation seem to be at the forefront of investors and markets. We see many of the inflationary pressures as short-term in nature but these need to be monitored closely as we move throughout the rest of 2021 and into 2022.

Many areas of the U.S. economy are showing improvement as the reopening occurs. Areas such as labor participation have revealed that people are gradually rejoining the work force. Supply chains also are improving as restrictions are removed. Technology innovation is still improving at a steady pace. Congress is currently working on a multi-year infrastructure investment bill that should further help labor markets and the U.S. economy as a whole.

With the economy continuing its reopening, we see the second half of 2021 continuing to show modest growth in corporate earnings. As such, we will focus on those companies with improving fundamentals and will use pullbacks in the market as buying opportunities. Our asset allocation remains flexible as we work through this unprecedented period. Currently, our asset mix is 40-60% in equities, 20-30% in fixed income and 5-10% in cash. This asset mix will vary based on client specific goals, risk tolerances and income needs.



Jeffrey S. Naylor
Executive Vice President/CFO

Time to Refinance?

Mortgage refinance means paying off an existing home loan with a new one. Even though mortgage rates may no longer be at the rock bottom pandemic lows, rates remain very fair and something to consider.

Most people refinance because the market interest rates are lower than their current rate. Reducing an interest rate not only helps save money in the end but also can decrease the size of the monthly payment. Interest rates in the past few months have been at historic lows, but that is not the only advantage to mortgage refinance. Refinance can shorten the term of the mortgage, provide additional cash from equity in your home for a larger purchase, a remodeling project or a need or change from an adjustable rate mortgage (ARM) to a fixed-rate mortgage. While ARMs often start out offering lower rates than fixed-rate mortgages, periodic adjustments can result in rate increases that are higher than the rate available through a fixed-rate mortgage. When this occurs, converting to fixed-rate mortgage results in a lower interest rate and eliminates concern over future interest rate hikes.

Rule of thumb is that refinancing is a good idea when the interest rate will be reduced by at least 2%.

Keep in mind, though, refinancing can cost approximately 3 to 6% of a loan's principal balance because an appraisal, a title search and application fees are again



required. A homeowner, therefore, must determine whether refinancing is an overall wise financial decision.

As with any financial decision, consider personal goals and spending habits when deliberating a mortgage refinance. Often homeowners access the equity in their homes for home remodeling, which usually adds value to the home, making the refinance a prudent decision. While a refinance to consolidate debt into a lower-interest mortgage, which at first glance appears very sensible, may not end well if the homeowner simply cannot resist generating additional debt on the now available credit resulting in higher debt, loss of that built-up equity and the spent expenses of the refinance process.

Experts generally recommend refinancing to a shorter-term loan. If a homeowner has already paid on the existing mortgage for some time, for example 10 years on a 30-year mortgage, they should try to avoid refinancing for the same term all over again – extending the overall length of finance from a 30-year mortgage to 40 years!

Is it time for you to refinance? Do you plan to stay in the house long enough to recover the closing costs and more? How much money will you save or will you meet your true objective by refinancing? If you review your financial goals and determine it best to refinance your house, shop around and compare mortgage rates and costs. Now might be a good time to secure the best rate for you!

Kelly S. Diehr, FPQP®
Administrative Assistant

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Tax Planning

Tax planning is the analysis of a financial/tax situation to ensure that all elements work together to allow you to pay the lowest taxes possible. Proper annual planning may help minimize one's federal income tax liability and planning could take a more in depth look into lowering your taxable income as well as boost your income into retirement. Annual tax planning allows you to break down past tax returns and find opportunities to lower the amount of taxes owed going forward. Planning also helps assure that you are paying your responsible share of taxes during the year.

For many individuals looking to save more for retirement, tax planning can take a more in-depth look at saving in a retirement account to help minimize the gross income by the amount contributed. As an example, for 2021 a filer under age 50 that meets the requirements can contribute up to \$6,000 to their IRA (\$7,000 if over the age of 50). Contribution amounts for retirement accounts can change from year to year, so making sure you are contributing enough is important.

Taxes should not be something you only think about in March and April, as you file your tax return for the year. Changes such as new marriages, growing families, change in jobs, unemployment or retirement, etc., happen throughout the year that may change your situation going forward. Proper planning can help avoid feelings of not knowing what to expect at "tax-time." We pride ourselves in having the ability to have our tax team work closely with our investment team to ensure the best planning possible for our clients.

IRS Updates

About the Advance Child Tax Credit

The expanded and newly-advanceable Child Tax Credit was authorized by the American Rescue Plan Act, enacted in March. Normally, the IRS will calculate the payment based on a family's 2020 tax return, including those who use the Non-filer Sign-up Tool. If that return is not available because it has not yet been filed or is still being processed, the IRS will instead determine the initial payment amounts using the 2019 return or the information entered using the Non-filers tool that was available in 2020.

The payment will be up to \$300 per month for each child under age six and up to \$250 per month for each child age six through 17.

To make sure families have easy access to their money, the IRS will issue these payments by direct deposit, as long as correct banking information has previously been provided to the IRS. Otherwise, people should watch their mail around July 15 for their mailed payment. The dates for the Advance Child Tax Credit payments are July 15, August 13, September 15, October 15, November 15, and December 15. You have the ability to opt out of receiving these funds early by visiting [IRS.gov](https://www.irs.gov).



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