Advisory Notes

June 2020

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Second Quarter in Review

After three plus long months of quarantine, social distancing and Zoom meetings, we here at VASI are now able to meet with clients in person while still keeping within the Federal Government and New York State guidelines. We will try our best to accommodate your individual needs based on timing the flow of clients and staff.

The second quarter equity markets continued with volatility but they also created a base from the lows in March as the Federal Reserve added liquidity to the markets in the form of asset purchases consisting of treasuries and corporate and municipal fixed income instruments. The returns on the bond market have been slightly positive due to the extreme measures the Federal Reserve provided to lower interest rates to help prop up the economy in the face of the COVID-19 crisis. (See Market Table.)

While unemployment jumped dramatically during the quarter due to the shutdowns in certain sectors of the economy, we have seen improvements recently as certain parts of the country are beginning to reopen. All inflation remains low for the near future and interest rates linger near zero, which should help the economy get back on its feet in the latter half of 2020 and the beginning of 2021.

Many obstacles may throw the economy off course such as a large second wave of COVID-19, the presidential election, trade issues with China and other countries and the disruptions regarding the social injustice protests. We are committed, however, to making sure your portfolio is consistent with your goals, risk tolerance and preferences, while making sure you are properly diversified and resisting the urge to react to the daily headline news items that affect the near term markets.

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Market Table

Valicenti Advisory Services, Inc.
Comparative Index Period Returns
From 03-31-20 THROUGH 06-30-20

	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)
03-31-20 to 04-30-20	11.22	12.82	15.45	13.66	1.78	-1.36	5.11	0.03
04-30-20 to 05-31-20	4.66	4.76	6.75	6.36	0.47	3.46	1.60	0.00
05-31-20 to 06-30-20	1.82	1.99	5.99	3.40	0.63	0.89	2.08	0.00
Cumulative Returns 03-31-20 to 06-30-20	18.51	20.54	30.63	25.00	2.90	2.96	9.01	0.03
YTD Returns 12-31-19 to 06-30-20	-8.43	-3.08	12.11	-13.61	6.14	2.25	5.36	0.60

Director's Chair

To say we live in interesting times would be an understatement. We have seen one of the largest economic upheavals since the Great Depression due to government response to a potential pandemic. Economic data points and statistics, some that date back to the 1950s and 1930s, have hit levels pointing to economic contraction that is unparalleled. The reaction to shutter large components of the economy and only allow for essential services brought the April unemployment rate to 14.3% after hitting a multi-decade low of 3.5% set in February of this year. Unemployment figures this high were last seen in 1940 during the Great Depression right before the U.S. entered World War II. In response, the stock market fell 30.4% from year-end 2019 to the market bottom hit on March 23. The fall is even greater when viewed from the market peak mid-February, a near 34% decline.

As of June 30, the stock market is down a mere 3.1% for 2020, so what happened? The Federal Reserve's release of an unprecedented quantity of liquidity (in the trillions) into the capital markets coupled with a multi-trillion dollar rescue package from the President and Congress known as the CARES Act created one of the most amazing market turnarounds that seemed unimaginable. From the March 23 low to June 30, the S&P 500 is up 39% on a total return basis. If you want to see this much liquidity on film, just look up any movie with the word Titanic in it after the iceberg hit.

We should all be grateful for the market rebound, but should also be incredibly cautious, using this opportunity to rebalance portfolios. On June 8, the S&P 500 was actually in positive territory for the year. In effect, the stock market in June has traded at levels as if there were no virus, shutdown or high unemployment. The market is being held up by a large amount of government provided liquidity, hopes for a vaccine and belief that the economy will reopen quickly. The S&P 500 is currently trading above 20 times earnings estimates for 2020, while those estimates will have a high degree of error since we will not know how bad the second quarter was until earnings are reported in mid-July through August. An analogy can be found in the original water tunnel that feeds New York City. Built in 1917, no one dares shut off supply because it is believed that water pressure is the only thing preventing collapse.

Paring back equity positions while holding a higher percentage of cash may be a wise strategy considering the potential issues that may arise from efforts to reopen the economy. Certain questions must be asked, as in what happens if the virus reappears in force, what if there is no vaccine and what if unemployment remains high? Large portions of the country now live with social distancing guidelines that will negatively affect corporate earnings. For instance, a publicly traded restaurant company will not be able to generate the same profitability at 25% or 50% of capacity with distancing guidelines. That means less earnings for the company and less need to employ wait staff.

This is more likely to be an era where individual stock picking is preferred over passive investing. Being able to target certain industries that will do well in the current environment will provide opportunities to own equities.

Then again, the markets could continue to rise on the backs of continued stimulus from the Federal Reserve and the Federal Government. That seems like a shaky house of cards because the government's resources are finite and unchecked money printing could lead to a return of 1970s style inflation. With the Federal Government guaranteeing bad debt with recent legislation, banks using commercial loans will lend since there is little chance of losses. Money could rapidly enter the economy through this mechanism in a much more efficient process than the Federal Reserve buying bonds as it did during the Financial Crisis more than a decade ago. Such an occurrence of inflation would take years to manifest itself, however.

We continue to look for companies that will outperform and that can take advantage of the current situation while also adjusting asset allocation and cash positions to protect from the downside. Back to the iceberg, hate to ruin the movies for you, but the boat sinks in the end each time. We do not intend to go down with the ship and prefer to float away in a lifeboat of our own choosing such as targeted stocks, bonds, cash and a little gold.

Louis F. Ruize
Director of Research/Portfolio Manager

Second Quarter
(Continued from Page 1)

From our office to your home, please stay safe – social distance when appropriate, wear a mask when you cannot and wash hands regularly. If we all do our part, we will continue to stop the spread until a vaccine has been developed and distributed.

Joseph M. Valicenti
President/CEO

Investment Strategy

In the second quarter, the U.S. economy slowed at an unprecedented rate as Federal and State officials took aim at trying to flatten the curve on the spread of COVID-19 through limited movement policies with the number one goal of minimizing the loss of life. The monetary and fiscal measures taken in the first half of 2020 were also unprecedented with the goal of minimizing the impacts on the U.S. economy. These measures aided the U.S. equity and fixed income markets, which rebounded sharply from the March lows.

While uncertainty remains as states reopen from the pandemic, there is a cautiously optimistic tone that economic activity will improve in the third and fourth quarters of 2020. Currently, inflation does not appear to be a risk in the near term, rather COVID-19 has created a disinflationary environment in the short term. Unemployment claims will be watched closely over the next several weeks as the CARES act is set to expire at the end of July. There remains the possibility of a further round of fiscal measures that may need to be taken before Congress breaks for its summer recess.

While we are cautiously optimistic, our asset mix will be nimble as we continue to navigate these unprecedented times. Our equities will focus on primarily large companies with strong financials and the ability to adapt quickly to the ever-changing COVID-19 environment. As data points become available, our asset mix will remain flexible with equities 40-55%, fixed income 25-35% and 5-15% in cash. The asset mix will vary based on client specific risk levels, need for income and other specific directives.

Stay healthy and safe!

Jeffrey S. Naylor
Executive Vice President/CFO/CCO

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Analyst Corner

As we concluded the first quarter of 2020, major equity indices were largely down mid to high double digits and fixed income spread products such as corporate and municipal bonds were showing signs of weakness and were beginning to return negatively. The second quarter became a period of shifting circumstances and, as we progressed through the months of April, May and June, produced a reversal of the first quarter's market misfortune due to a variety of factors. Monetary and fiscal policies combined to become a stabilizing force. The COVID-19 pandemic spread through the country and as bad as it was in specific locations, the early worst case projections seemed to not be realized throughout the nation as a whole. In a recession, it is typical to begin to look for the green shoots of recovery, so some re-emergence optimism may have impacted sentiment over the short term. Looking beyond the intermediate term, market participants will be looking for the dust to settle in order to gain a better view of the environment in which companies are operating.

The S&P 500 rebounded 20.54% in Q2, which went a long way in erasing Q1's precipitous drop. The main index is still down 3.08% on the year; while the technology and momentum filled Nasdaq Composite outperformed the broader S&P just as it did in the selloff of Q1. This has solidified the YTD outperformance by a full 15 percentage points (S&P 500 down 3.08% vs NASDAQ Comp up 12.74%). As the domestic and global economies struggle to find robust aggregate demand at this stage, the Dow Jones Industrials have conversely lagged coming in down 8.43% on the price index.

Positive Market Influences	Negative Market Influences
Phased Reopening	Enduring COVID-19 Issues
Oil Production Cuts	Labor Market Disruptions
Pent Up Activity	Long-Term Growth Trajectory
	Geopolitical Tensions

The 10YR US Government yield stabilized and traded near 0.70% for most of the quarter with an attempt to back up towards 1% in early June, possibly portending what longer-term rates could do if a reflation and swifter recovery does take hold. The Bloomberg Barclays Aggregate Investment Grade Index was up 2.90% in the quarter due to the strong rebound in corporate credit and stability in the risk free treasury markets. A main concern for investors at this juncture is grappling with the absolute lower levels of income able to be safely purchased as the lower and reliable funding costs for borrowers seem to be a prerequisite for recovery scenarios.

As we close the door on the rather historic second quarter of 2020, the open door into the corporate earnings season will soon appear. That large parts of the economy were shut down for non-essential businesses and activity lowered significantly for essential ones in the period, the actual corporate earnings results will likely appear grim in many corridors. This, of course, will be contrary to the price recovery we just observed in market prices, though it will also allow us to hear commentary of what company leaders are currently seeing out there. The symmetry of the near term drivers may skew slightly negative given the torrid and quick pace of the nascent market price recovery that we just experienced versus the realities of the moment.

Positive Market Influences:

- **Phased Reopening** – The U.S. economy and the various states are undergoing a phased reopening of activity as the nation works through the crisis.
- **Oil Production Cuts** – Following dramatic falls in the price of oil in April, early May saw OPEC agree to a 9.7 million barrel per day production cut which was initially to run until the end of June; however, the organization has since extended the cuts until the end of July.
- **Pent Up Activity** – There is some anticipation that the reopening of the economy may see a very strong sequential uptick in demand activity on the part of consumers that have been locked in their homes and apartments through the pandemic response. If observed, it would likely be reassuring for markets in the short term; however, it would not necessarily inform the long-term growth outlook.

Negative Market Influences:

- **Enduring COVID-19 Issues** – Delays in vaccine development or lack of communication regarding effective therapy responses to COVID-19 amidst a rise in cases indicative of a second wave in the fall or earlier are a source of uncertainty and concern.
- **Labor Market Disruptions** – The payrolls, unemployment and initial claims data are key indicators to watch regarding the long-term health of the consumer. It is likely that it will take a considerable period to reach a 2019 level of activity for employment once again.
- **Long-Term Growth Trajectory** – The outlook for consumption, investment and productivity may be weaker, which is not unusual on the march out of a recession. Forecasters may have a slightly less sanguine view of the factors that will drive the economy forward even if the

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Analyst Corner

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strong pent up demand release is seen in the shorter term.

- **Geopolitical Tensions** – The retreat of global trade in the face of waning demand around the world can feed negatively back into itself, intensifying domestic response policies and those of our significant trading partners which all can add further to the imbalances and associated complex issues. The tensions may not in all cases be problematic as underlying trading systems appear to need desperate reforms, but the uncertainty of outcomes weighs heavily.

Daniel P. Burchill
Security Analyst

Inherited IRAs - An Update for 2020

The rules for inherited IRAs have changed as of January 1, 2020. When the SECURE Act passed in late 2019, it changed the rules regarding inheriting an IRA and effectively eliminated the stretch ability for non-spouse beneficiaries. These rules depend on when the original account owner died and who is the beneficiary of the IRA.

If the IRA owner dies after December 31, 2019, the beneficiaries of the IRA inherit the funds in an inherited IRA. If the beneficiary is an "eligible" beneficiary, then the old rules will apply. Eligible beneficiaries include:

1. The surviving spouse of the original account owner – this can be treated as your own IRA.
2. A minor child of the original account owner – distributions must start, but are based on the minor's life expectancy until they reach the "age of majority". At that point, the beneficiary has 10 years to withdraw the entire account.
3. Any beneficiary who is disabled or chronically ill – distributions can be stretched over the beneficiary's lifetime.
4. Any beneficiary who is not more than 10 years younger than the original account owner – distributions can be stretched over the beneficiary's lifetime.

If the beneficiary is not an "eligible" beneficiary (for example, a deceased account owner's adult child), they must completely distribute their inherited IRA within 10 years of the original owner's date of death. This new rule eliminates the stretch ability of the IRA and may create heavier tax burdens for the beneficiaries. The distributions do not have to occur evenly over those 10 years, but the inherited IRA must be fully depleted within the 10-year period. The beneficiary may decide to wait until year 10 to withdraw the entire amount or they may decide to take some each year.

For beneficiaries under the age of 59.5, there is no penalty for withdrawals from inherited IRAs, but all withdrawals are still taxed as income.

As always, if you have any questions regarding inherited IRAs, please give us a call.

Ann S. Nolan, FPQP™
Administrative Assistant

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

Valicenti Receives President's Council Award

The Elmira College President's Council has announced that Suzanne M. Valicenti '00 as this year's recipient of The President's Council Award. The Award, which is presented annually each spring, recognizes outstanding Elmira College graduates who have distinguished themselves and the College by exemplary service in the College's greater community and, who, by giving generously of their time and talent, has improved the quality of the community. Valicenti, originally from Burr Oak, Michigan, graduated from Elmira College with a Bachelor of Science in Business Administration with a concentration in Marketing and Management. She was a member of the Soaring Eagles Women's Basketball team. She remained in Elmira following graduation and formed Valicenti Insurance Services, Inc. in February 2013 as President/CEO and Director of Insurance Services after spending several years as executive vice president for an insurance agency in Corning. An active member in the community, Valicenti has coached high school basketball in Corning and has been involved with numerous local organizations. She is a Founding Member of the Fund for Women, is an advocate for rescuing animals and volunteers with a number of local animal rescue groups in the Southern Tier and surrounding areas.

Please join us in congratulating Suzanne!

At Valicenti Insurance Services, Inc., we represent many insurance companies. Our role is to serve as your trusted advisor. We will work with you to help you determine your coverage needs before recommending the best combination of insurance products for your unique situation.

As your advisor, we will:

- Identify the insurance services that are right for you.
- Counsel you on matters related to your coverage or account.
- Protect what is most important to you.
- Provide prompt service with a unique personal touch.
- Guide you through the claims process for a quick and fair resolution.

IRS Update

The Internal Revenue Service (IRS) announced on June 23, 2020, that anyone who already took a required minimum distribution (RMD) in 2020 from certain retirement accounts now has the opportunity to roll those funds back into a retirement account following the CARES Act RMD waiver for 2020.

The 60-day rollover period for any RMDs already taken this year has been extended to August 31, 2020, to give taxpayers time to take advantage of this opportunity. The IRS described this change in Notice 2020-51, released June 23, 2020. The Notice also answers questions regarding the waiver of RMDs for 2020 under the Coronavirus Aid, Relief, and Economic Security Act, known as the CARES Act.

The CARES Act enabled any taxpayer with an RMD due in 2020 from a defined-contribution retirement plan, including a 401(k) or 403(b) plan, or an IRA, to skip those RMDs this year. This includes anyone who turned age 70½ in 2019 and would have had to take the first RMD by April 1, 2020. This waiver does not apply to defined-benefit plans.

In addition, to the rollover opportunity, an IRA owner or beneficiary who has already received a distribution from an IRA of an amount that would have been an RMD in 2020 can repay the distribution to the IRA by August 31, 2020. The notice provides that this repayment is not subject to the one rollover per 12-month period limitation and the restriction on rollovers for inherited IRAs.

The notice provides two sample amendments that employers may adopt to give plan participants and beneficiaries whose RMDs are waived a choice as to whether or not to receive the waived RMD.

Source: IRS.gov

Paul E. Hornbuckle, CPA
Vice President of Tax and Business Services

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Buying vs Renting

If you are considering buying a second home, you should first look at the advantages of renting first. Taking this approach will give you a better understanding of the expenses involved in having a second home. There are the questions of where the money will come from to purchase a second home. If you will be taking funds from currently invested assets, you must consider the loss of income from those assets, along with the additional premiums for household insurance, the expected expenses for a mortgage, if necessary, and all of the other expenses associated with owning a piece of property. Depending on your age, you may be tying up assets that you will need for ongoing spending and emergencies in the future. You should consider how often you would be using the second home. Renting will give you the opportunity to learn the true cost of having a second home by finding out the property and school taxes, the general upkeep, etc. and, in the final analysis, whether you really can afford the second home.

There are similar considerations when buying a boat. The cost of buying a boat can be no different than buying a car or a truck; however, the expenses of a boat really begin after the purchase. First, you have to get the boat to and from the water, which will require a trailer and a vehicle large and durable enough to handle the boat and, the more the boat is used, the more time will be spent on preparing it for use and cleaning it up afterwards. Then there is the fuel, insurance, repairs and storage. The annual cost of boat ownership is projected around 15% to 25% of its value. The cost of renting a boat depends on the location and the type, but most people can find a suitable craft for a hundred dollars an hour plus fuel.

These types of purchasing decisions should be discussed with your financial advisor before finalizing, so that there can be a clear picture and, hopefully, no surprises.

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

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