GALECKI FINANCIAL MANAGEMENT FINANCIAL SENSE

	LAST MONTH	LAST 3 MONTHS	YTD
S & P 500 Index	-3.80%	8.93%	5.57%
Russell Midcap Index	-1.95%	7.46%	-2.35%
Russell 2000 Index	-3.34%	4.93%	-8.69%
Dow Jones Industrial Average	-2.18%	8.22%	-0.91%
Morgan Stanley EAFE Index	-2.60%	4.80%	-7.09%
DJ US Real Estate Index	-2.27%	2.07%	-12.08%
S&P Commodity Index	-3.64%	4.61%	-33.38%
Barclays Aggregate Bond Index	-0.05%	0.62%	6.79%

INDEX RETURNS

Equities had a rough September but still finished the third quarter with overall gains. The S&P 500 increased 8.93% in the quarter and is now up 5.57% on the year. However, the majority of this gain can be attributed to five companies. Mid-cap stocks increased by 7.46% in the quarter, but are still down 2.35% for the year. Small-cap stocks were up nearly 5% in the quarter, but are still down almost 9% so far in 2020.

International stocks saw some growth in the third quarter as a whole. The MSCI EAFE Index was up 4.80% in the quarter, but is still down 7.09% on the year. Emerging Market stocks were up 9.5% in the third quarter and are now only down 1.16% on the year. In fact, Taiwan's market was up 17% in the quarter and is now positive.

The Barclays Aggregate Bond index had a very quiet quarter with a gain of 0.62%. High Yield bonds were up 4.26% in the third quarter and are now only down 1.14% on the year. Global bonds also rallied in the third quarter by about 2%, but are still down 0.32% on the year.

ECONOMIC REVIEW AND OUTLOOK

The U.S. economy fell by a 31.7% annualized rate in the second quarter of 2020. The National Bureau of Economic Research (NBER) declared that we entered a recession in February. Estimates for third quarter GDP are in the positive 30% range. This means that we will have recovered around 2/3 of what we lost in production in the second quarter. It is likely that growth will slow in the fourth quarter down to a more normal 3-5%.

The Leading Economic Index was up 1.2% in August to 106.5. This follows the 2% decline in July and the 3.1% increase in June. Industrial Production rose 0.4% in August for the fourth consecutive month of growth. This is still roughly 7.3% below the pre-pandemic level in February.

The Capacity Utilization rate (which measures how much slack is in the economy) was at 71.4 percent in August which is 8.4% below the long-term average.

Non-farm payrolls rose by 661,000 in September. The unemployment rate declined to 7.9% from 8.4% in August. Initial weekly unemployment claims were 837,000 for the week ending September 26, 2020 which was a decrease of 36,000 from the prior week. The improvement in unemployment is beginning to slow. Census workers will be falling off and airlines are planning major furloughs this month, so we will likely see slower improvement over the next few months.

Manufacturing fell to 55.4% on the ISM PMI index in September. This was a decrease of 0.6%. However, this does mark the fourth consecutive month of expansion. The New Orders Index came in at 60.2 percent which was a decrease of 7.4 percent from August. The ISM Services index was at 57.8% in September which was an increase of 0.9% from August. The Business Activity Index fell to 62.40%, down from 67.20 last month. Although the service data dipped a bit over the last month, it is still in expansion territory. It is likely that we see continued growth in the service sector, but at a much slower pace until we see a vaccine.

Global economies are also experiencing economic recoveries. The JPM Global Manufacturing PMI was at 51.8 in August which is up from 50.6 in July. Of the 31 territories covered by the survey, 19 recorded PMI readings indicative of growth. In fact, the UK is now at 55.1 and China is at 54.0.

EQUITY AND BOND MARKETS

Prices in equities have moved up significantly from their lows in March of this year. The problem is that earnings for most of the companies have not kept the same pace. The P/E ratio for the S&P 500 is now at 21 times earnings. The 25-year average is closer to 16 times earnings. Stocks have not been this expensive in the U.S. since 2001. The dividend yield has also declined to 1.77% from around 2.1% earlier in the year.

We are a little concerned about the lack of overall participation in equities in this recent rally. In fact, 495 of the stocks in the S&P 500 are down an average of 3.4% on the year as of September 18. So, how was the S&P 500 up 2.7% as of that date? The top 5 stocks in the index now make up roughly 23% of the overall market cap weighting. Their return this year has been more than 28%. So, although 99% of the companies in the S&P 500 are negative on the year, the returns and weightings on Apple, Microsoft, Amazon, Facebook, and Google have carried the index into positive territory. But what happens to the index when these five companies struggle?

Source: Charles Schwab, Bloomberg, as of 9/18/2020. **Past performance is no guarantee of future results.**

The P/E ratio for the Russell 2000 index is at 36.8 times earnings versus a 20-year average of 21.1. This means that they are priced at 174% of their historical valuations. International equites appear more attractive from a valuation perspective. The ACWI ex-US index is at a P/E ratio of 16.4 times earnings versus a 20-year average of 13.5. In addition, the dividend yield for this index is at 3.0%. Compare that international income yield to the S&P 500 of only 1.8% and the 10-year Treasury yield of 0.77% and international stocks are a relative bargain.

With an election right around the corner, many investors are concerned about 2021 and beyond. If Democrats decided not to invest under President Trump, they would have missed out on excellent returns. Conversely, if Republicans would have decided not to invest under President Obama, they would have also missed out on excellent returns. In fact, from 1961-2019, $10,000 invested in the Ibbotson US Large Stock index would have grown to $3.24 million. However, if that money was only invested under Republican presidents, it would have only grown to $86,397. If it was only invested under Democrat presidents, it would have only grown to $376,010.

The moral of this story, is that it is important to stay invested for the long-term. Trying to time the market is very difficult and typically not worthwhile. Regardless of what happens this election, keep a long-term perspective and ignore all of the noise. Businesses will find a way to grow over the next five years, and earnings will follow.

PORTFOLIO MANAGEMENT

The Investment Committee continues to look at risk management within the portfolio. With the equity markets near all-time highs, and valuations extended, portfolio risk should remain within appropriate levels. We have continued to maintain our Innovator ETF position that offers downside protection. These funds held up quite well in March and April and should provide additional support if domestic markets contract.

The bond side of our portfolio continues to be an area of focus. Performance in the Barclay's aggregate index has been impressive this year, but many fixed income asset classes underperformed. With the potential for a weaker dollar over the next five years, we want to maintain our equity international exposure as well as our international bond exposure. In addition, we are adding convertible bonds into the portfolio to help improve fixed income returns over the next five years as rates eventually move off of these historically low levels.

The markets will continue to be volatile in the final quarter of 2020. Should we really expect anything different given the events of the first 9 months of this year? Election results could take weeks to determine after the polls close. This could provide increased volatility as the market digests each potential outcome. It will be important to maintain a long-term focus on the portfolio and ignore the short-term chaos of the election results.

FINANCIAL PLANNING

Health Insurance

Open enrollment season for Medicare is quickly approaching. For individuals who are already on Medicare, this is the annual opportunity to review and make changes to a prescription drug (Part D) plan and supplement plan (sometimes referred to as a Medigap Plan).

Open enrollment starts on October 15, 2020 and ends on December 7, 2020. Plans elected during this time period become effective on January 1, 2021.

Medicare coverages should be reviewed annually. It is possible that the plans that worked best at age 65 upon initial enrollment are no longer the best plans for your specific situation. If you've added or changed prescriptions or have had any changes to your health, a new plan may save you on out-of-pocket costs.

We recommend speaking with a trusted Medicare insurance agent to evaluate your Medicare policies each year.

Open enrollment for medical insurance plans through the Health Insurance Marketplace is from November 1, 2020 through December 15, 2020. Individuals and families with insurance coverage through the marketplace should be sure to verify their information and new plan rates for 2021.

If you are covered under a group health insurance plan, those open enrollment periods may vary. Contact your HR department for specific information on your options.

Income Taxes

As we've mentioned in previous newsletters, Required Minimum Distributions (RMD) from IRAs, Qualified Retirement Plans, and Inherited IRAs were waived for 2020. Many taxpayers use their RMD each year to pay their projected Federal and State tax liability for the year. This is done by withholding percentages for Federal taxes and State taxes from the gross distribution.

Taxpayers who normally withhold taxes in lieu of making quarterly tax estimates should consult with their tax professional to see if they are projected to be subject to an underpayment tax penalty.

Underpayment penalties can be avoided by paying 110% of the previous year's tax liability or 90% of the current year's tax liability. On the Federal side, the standard penalty is 3.398% of the unpaid tax. State underpayment penalties vary; Indiana's is 10% of the unpaid tax.

Company News

This summer Haley Johnston welcomed her daughter, Magnolia into the world! Magnolia was born weighing 7lbs 12ozs and was 21 ½ inches long.

Haley joined our GFM Team back in 2019. She works as our Asset Management Specialist. She assists all clients of our firm with various tasks related to their accounts. Haley also has a myriad of responsibilities behind the scenes to ensure our software and programs are running smoothly.

This year we have been migrating to a new portfolio management software. Haley has been an integral part of the team who has gotten this software up and running for our clients

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We are still offering our Initial Financial Overview (IFO) for $300 until December 31, 2020. The normal fee for our IFO is $775.

The IFO is a two-hour interactive review of your current financial situation. There is no sales pitch as we do not sell any products or earn any commissions. The IFO may cover items such as retirement cash flow analysis, education funding and planning, tax planning, insurance analysis, estate planning and investment allocation and planning. The direction of the IFO typically depends on the needs of the Client.

If you or anyone you know would like to take advantage of this offer, please contact our office directly at 260-436-8525.

- Galecki Financial Management Investment Committee

Special Note: If you would like to schedule an appointment with a Certified Financial Planner™ Professional, please visit www.galecki.com