STATERA
ASSET MANAGEMENT

Third Quarter 2020

QUARTER IN REVIEW

Not much less eventful than the prior two, the third quarter saw global stocks rise on a mix of generally slow, often halting and occasionally reversing trends as the world further emerged from comprehensive COVID lockdowns. Equities gained a further boost here in the States as hopes rose for another round of government stimulus. With the pandemic a still-bleak backdrop, the U.S. presidential election will be the stronger focus through early November. While we'll seek to retain an upbeat stance on the potential for an orderly ballot, we expect nonetheless for markets to rumble as pockets of perspectives gain or lose confidence in their desired outcome. But as we regularly repeat, we've been here before and we'll be here again. There's little special about this election, or these potential electees, when placed in the context of history, a history that shows that we've always eventually emerged stronger on the other side of the poll.

Still in It. Still Whole.

By quarter's close, the domestic equity market was down about 6% from the peak set in early September, a level not far below where they were just prior to the onset of the pandemic. With gains in October bringing the indexes closer to record territory, we wonder just how long the fiscal juice…or, better put, the idea of said juice…will last. That investors collectively seem even more enthusiastic about the future than prior to the pandemic seems a bit odd to us, but so it seems they are. We just wonder how long it might take reality to catch up to those expectations.

Getting Used to the Hiccups

We'll counter this perhaps somewhat negative slant with the notion that very few stocks have participated in the rally (see our September commentary). Indeed, it was nice to see some heretofore unloved segments of the broader stock universe (like smaller stocks and less expensive stocks) gain a bid during the later bits of the third quarter. Could be a temporary change in the wind. However, it could also be just the sort of shift that may portend a better season for our chosen approach. Either way, we'll continue to approach equity investing with a strategy that grounds itself (far more defensibly, we believe) in empirical reviews of the past, as opposed to hopeful prognostications of the future.

Set for a New Stage

Speaking of such, whatever the outcome of the election, we have the sense that a new stage is about to be set. Still, whichever cast of characters grace the playbill, we continue to believe that investors will find themselves better served by plans that incorporate discussions regarding the potentially wide range of outcomes that might be seen over the course of their investment time horizons. For many, those horizons are likely to include many more election cycles. Just as might have been the case in every election past, substantial shifts in investment policy based on a narrow focus on this one election may lead to less-than-ideal outcomes. While it may seem tough stay the course, we continue to believe that it's the better approach for most.

Figure 1: Quarter Summary

Overall Take		
↑	↑	Equity: Stocks surged on reopenings, and withdrew on setbacks, but the trend was on balance upward for the quarter, with government support providing a late tailwind
	↗	Fixed Income: The Treasury yield curve steepened, even as short-term rates fell, while credit spreads narrowed

Equity			
↑	Domestic Still on a roll, with gains spreading across a broader spectrum of stocks	↗	International Broadly trailed U.S. stocks, but gained nonetheless, further boosted by a falling dollar

Directions and colors of arrows reflect a subjective interpretation of the quarter's market events and performance; upward (downward) and angled-upward (-downward) arrows indicate relatively favorable (unfavorable) reviews in the aggregate. They are not indicative of any specific underlying data. SOURCE: SRCM

Equity Market Review

In what turned out to be another solid quarter of gains, global stocks began Q3 on a relatively smooth march upward, along with generally more positive trends in the pandemic. U.S. stocks sprinted away from the pack over the second half of August, only to fall back to the group presumably as COVID cases resurged while Congress dithered in agreeing a second stimulus package. Big stocks led the way again, though there was an awakening of sorts within the smaller-cap and Value segments after the September peak. Small-cap stocks even topped the charts for the quarter among international stocks, but mostly from stronger gains among the growthier portion of that group.

Figure 2: Trailing Broad Equity-Market Performance

Best-performing index for each period is shaded in blue; worst-performing in grey. See index details at the end of this report

	3 Month	1 Year	3 Year	5 Year	10 Year
Global	8.11	9.57	6.47	9.97	8.47
World ex. U.S.	6.80	3.51	1.13	6.31	4.17
World ex. U.S. Large-Cap	5.91	2.94	1.27	6.26	3.89
World ex. U.S. Mid-Cap	7.73	3.26	0.69	6.10	4.48
World ex. U.S. Small-Cap	10.50	6.97	0.93	6.80	5.31
U.S.	9.23	15.01	11.68	13.71	13.53
U.S. Large-Cap	9.88	18.53	13.50	14.96	14.15
U.S. Mid-Cap	8.12	6.65	8.54	11.05	12.46
U.S. Small-Cap	5.01	-0.57	2.12	7.93	10.46
Developed Markets	5.56	1.38	0.73	5.55	4.97
Emerging Markets	9.79	10.14	2.03	8.43	2.34

From 09.30.10 to 09.30.20. Total return data are annualized for periods greater than 1 year. Past performance is not indicative of future results. Investing in securities involves risk, including risk of losing some or all the invested capital. There is no guarantee that any investment or investment strategy will achieve its objective. Indexes are unmanaged. One cannot directly invest in an index. Index performance reflects the reinvestment of dividends, but does not reflect the expenses associated with the management of an actual portfolio. Please see additional important information regarding indexes at the end of this report. SOURCE: SRCM using data from Bloomberg

Figure 3: Trailing Equity-Market Performance

The tables below display the relative performance of different indexes representing U.S. and international stock markets. Broad market performance is shown in the upper left of each group (3-month and 1-year periods). The remainder of the table displays the performance of various indexes, including large-, mid- and small-cap stocks, Value and Growth stocks, and combinations of each. Indexes that outperform (underperform) the broader market are shaded in blue (grey) in depth according to their respective relative performance.

U.S. Stocks

3-Month Period ended 09.30.20

		Value	Growth
All Stocks	9.2%	5.2%	12.9%
Large	9.9%	5.4%	13.9%
Mid	8.1%	6.2%	10.0%
Small	5.0%	1.4%	8.4%

1-Year Period ended 09.30.20

		Value	Growth
All Stocks	15.0%	-6.3%	38.0%
Large	18.5%	-4.2%	43.2%
Mid	6.6%	-10.6%	24.4%
Small	-0.6%	-17.2%	17.3%

International Stocks

3-Month Period ended 09.30.20

		Value	Growth
All Stocks	6.8%	3.0%	10.5%
Large	5.9%	1.5%	10.3%
Mid	7.7%	5.7%	9.7%
Small	10.5%	7.8%	13.1%

1-Year Period ended 09.30.20

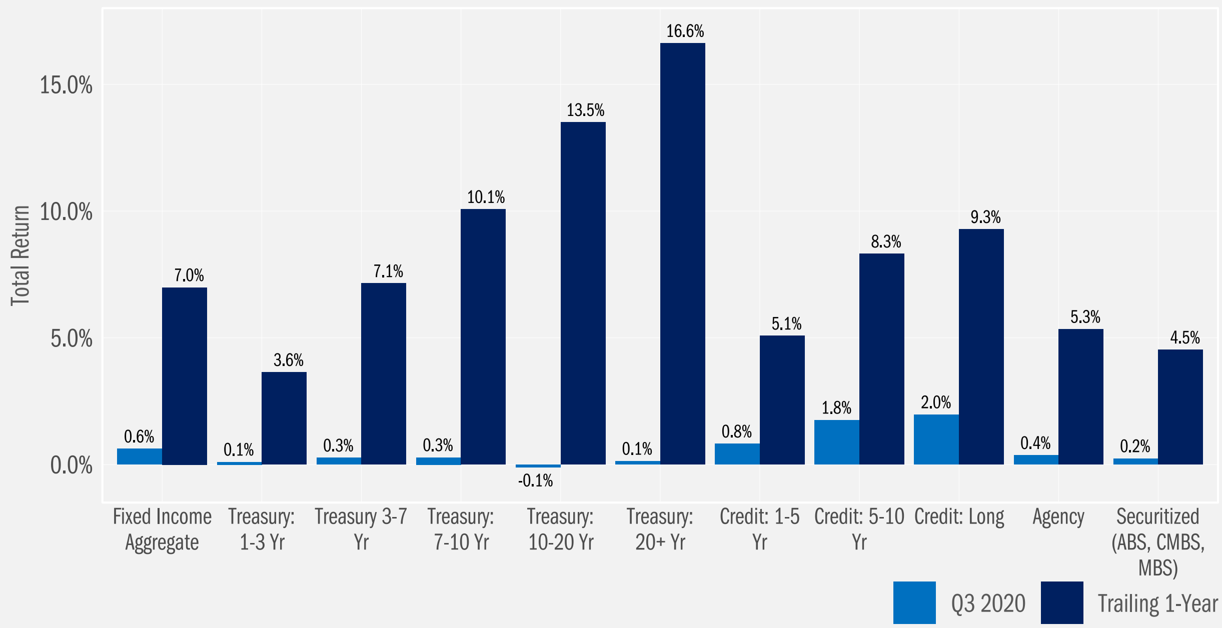
		Value	Growth
All Stocks	3.5%	-10.0%	17.7%
Large	2.9%	-11.4%	18.9%
Mid	3.3%	-8.5%	12.3%
Small	7.0%	-4.2%	18.4%

From 09.30.19 to 09.30.20. Data are total returns for the period shown. Past performance is not indicative of future results. Investing in securities involves risk, including risk of losing some or all the invested capital. There is no guarantee that any investment or investment strategy will achieve its objective. Indexes are unmanaged. One cannot directly invest in an index. Index performance reflects the reinvestment of dividends, but does not reflect the expenses associated with the management of an actual portfolio. Please see additional important information regarding indexes at the end of this report. SOURCE: SRCM using data from Bloomberg

Fixed Income Market Review

Gains were meager in Treasuries, concentrated among shorter-duration exposures as yields on bonds with maturities below the 10-year mark fell while yields ended the quarter higher on longer-dated bonds. Corporate bond exposures fared better on account of a further reduction in spreads.

Figure 4: Bloomberg Barclays U.S. Aggregate Bond Index and Sub-Index Performance



From 09.30.19 to 09.30.20. The Bloomberg Barclays U.S. Aggregate Bond Index is a broad-based benchmark that measures the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market. Components of the index include Treasury, Corporate, Agency and Securitized bonds. Indexes are unmanaged. One cannot directly invest in an index. Index performance reflects the reinvestment of dividends, but does not reflect the expenses associated with the management of an actual portfolio. Please see additional important information regarding indexes at the end of this report. SOURCE: SRCM using data from Bloomberg

SRCM Portfolio Context

While tilts toward our preferred stock characteristics among our U.S.-focused holdings detracted from benchmark-relative performance during the quarter, the gap was smaller than had been the case in earlier quarters. Meantime, the tilts worked quite well outside the U.S. offsetting the relative weakness within domestic stocks, though this beneficial impact was detuned on account of our broader U.S. bias.

Within fixed income, the compression in credit spreads, and to a lesser extent the relatively better performance among shorter-duration exposures, boosted benchmark-relative performance. This was further aided by inflation-hedged exposures where they have been incorporated into the target allocation.

Historical performance details relevant to each model may be found on our Composite Fact Sheets. Past performance is not indicative of future results. Individual client portfolios may maintain exposures different from, sometimes materially so, the models for which performance is discussed above. Actual portfolio performance thus may differ from that shown on the Fact Sheets.

Important Information

Investing involves risks including the possible loss of principal. Past performance is not indicative of future results.

One cannot invest directly in an index. Index performance does not reflect the expenses associated with the management of an actual portfolio.

Asset classes and their respective indexes mentioned in this report include the following:

Domestic (U.S.) fixed income (Fixed Income Aggregate): The Bloomberg Barclays U.S. Aggregate Bond Index is a broad-based benchmark that measures the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market. Components of the index include Treasury, Corporate, Agency and Securitized bonds. The Bloomberg Barclays U.S. 1-5 Year Government/Credit Bond Index is a broad-based benchmark that includes investment grade, U.S. dollar-denominated, fixed-rate Treasuries, government-related and corporate securities with maturities between 1 and 5 years.

Global equity (stocks): The MSCI ACWI Investable Market Index (IMI) captures large-, mid- and small-cap representation across 23 Developed Markets (DM) and 24 Emerging Markets (EM) countries. The index is comprehensive, covering approximately 99% of the global equity investment opportunity set. May be referred to as “global”, “global equity” and/or “global stocks”. “Value” and “Growth” versions of this index are constructed as described in the “MSCI Value and Growth Indexes” note below.

International equity (stocks): The MSCI ACWI ex USA Investable Market Index (IMI) captures large-, mid- and small-cap representation across 22 of 23 Developed Markets countries (excluding the United States) and 24 Emerging Markets countries. The index covers approximately 99% of the global equity opportunity set outside the U.S. May be referred to as “World ex. U.S.”, “international equity”, “international stocks” and/or “All Stocks” in a section specifically describing only international stocks. “Value” and “Growth” versions of this index are constructed as described in the “MSCI Value and Growth Indexes” note below.

International large-cap equity (stocks): The MSCI ACWI ex USA Large Cap Index captures large-cap representation across 22 of 23 Developed Markets countries (excluding the United States) and 24 Emerging Markets countries. The index covers approximately 70% of the free float-adjusted market capitalization in each country. May be referred to as international large-cap stocks, “World ex. U.S. Large-Cap”, and/or “Large” in a section specifically describing only international stocks. “Value” and “Growth” versions of this index are constructed as described in the “MSCI Value and Growth Indexes” note below.

International mid-cap equity (stocks): The MSCI ACWI ex USA Mid Cap Index captures mid-cap representation across 22 of 23 Developed Markets (excluding the United States) and 24 Emerging Markets countries. The index covers approximately 15% of the free float-adjusted market capitalization in each country. May be referred to as international mid-cap stocks, “World ex. U.S. Mid-Cap”, and/or “Mid” in a section specifically describing only international stocks. “Value” and “Growth” versions of this index are constructed as described in the “MSCI Value and Growth Indexes” note below.

International small-cap equity (stocks): The MSCI ACWI ex. USA Small Cap Index captures small-cap representation across 22 of 23 Developed Markets countries (excluding the United States) and 23 Emerging Markets countries. The index covers approximately 14% of the global equity opportunity set outside the U.S. May be referred to as international small-cap stocks, “World ex. U.S. Small-Cap”, and/or “Small” in a section specifically describing only international stocks. “Value” and “Growth” versions of this index are constructed as described in the “MSCI Value and Growth Indexes” note below.

Developed markets equity (stocks): The MSCI EAFE Investable Market Index (IMI), is an equity index which captures large-, mid- and small-cap representation across Developed Markets countries around the world, excluding the United States and Canada. The index covers approximately 99% of the free float-adjusted market capitalization in each country. May be referred to as “Developed Markets”. “Value” and “Growth” versions of this index are constructed as described in the “MSCI Value and Growth Indexes” note below.

Emerging markets (EM) equity (stocks): The MSCI Emerging Markets Investable Market Index captures large, mid and small cap representation across 24 Emerging Markets countries. The index covers approximately 99% of the free float-adjusted market capitalization in each country. May be referred to as “Emerging Markets”. “Value” and “Growth” versions of this index are constructed as described in the “MSCI Value and Growth Indexes” note below.

Domestic (U.S.) equity: The MSCI U.S. Investable Market 2500 Index is designed to measure the performance of the large-, mid- and small-cap segment of the U.S. equity market. The index represents approximately 99% of the free float-adjusted market capitalization in the U.S. equity market. “Value” and “Growth” versions of this index are constructed as described in the “MSCI Value and Growth Indexes” note below. May be referred to as “All Stocks” in a section specifically describing only U.S. stocks.

Domestic (U.S.) large-cap equity: The MSCI U.S. Large Cap 300 Index is designed to measure the performance of the large-cap segment of the U.S. equity market. The index represents approximately 71% of the free float-adjusted market capitalization in the U.S. equity market. “Value” and “Growth” versions of this index are constructed as described in the “MSCI Value and Growth Indexes” note below. May be referred to as “Large” in a section specifically describing only U.S. stocks.

Domestic (U.S.) mid-cap equity: The MSCI U.S. Mid Cap 450 Index is comprised of the next largest 450 companies in terms of market capitalization of the U.S. equity market and designed to measure the performance of the mid-cap segment. The index represents approximately 16% of the free float-adjusted market capitalization of the U.S. equity market. “Value” and “Growth” versions of this index are constructed as described in the “MSCI Value and Growth Indexes” note below. May be referred to as “Mid” in a section specifically describing only U.S. stocks.

Domestic (U.S.) small-cap equity: The MSCI U.S. Small Cap 1750 Index is comprised of the remaining smallest 1,750 companies in the U.S. Investable Market 2500 Index of the U.S. equity market and designed to measure the performance of the small-cap segment. The index represents approximately 11.5% of the free float-adjusted market capitalization of the U.S. equity market. “Value” and “Growth” versions of this index are constructed as described in the “MSCI Value and Growth Indexes” note below. May be referred to as “Small” in a section specifically describing only U.S. stocks.

MSCI Value and Growth Indexes: The value investment style characteristics for MSCI index construction are defined using the following variables: book value to price, 12-month forward earnings to price and dividend yield. The growth investment style characteristics are defined using the following variables: long-term forward earnings per share (EPS) growth rate, short-term forward EPS growth rate, current internal growth rate, long-term historical EPS growth trend and long-term historical sales per share growth trend. The objective of the MSCI Value and Growth Indexes design is to divide constituents of an underlying market capitalization index into a value index and a growth index, each targeting 50% of the free float-adjusted market capitalization of the underlying index. The market capitalization of each constituent should be fully represented in the combination of the value index and the growth index, and, at the same time, should not be double-counted. One security may, however, be represented in both the value index and the growth index at a partial weight.

Fama/French U.S. Book-to-Market Research Indexes: Provided by Professors Eugene Fama and Kenneth French. Index constituents are formed on book equity (BE) / market equity (ME) at the end of each June using NYSE breakpoints. The BE used in June of year t is the book equity for the last fiscal year end in t-1. ME is price times shares outstanding at the end of December of t-1. The reconstitution considers all NYSE, AMEX, and NASDAQ stocks for which we have ME for December of t-1 and June of t, and BE for t-1. The Fama/French U.S. Value Research Index includes the lower 30% in price-to-book. The Fama/French U.S. Growth Research Index includes the higher 30% in price-to-book.

Fama/French U.S. Size Research Indexes: Provided by Professors Eugene Fama and Kenneth French. Index constituents are formed at the end of each June using June market equity and NYSE breakpoints. The reconstitution considers for July of year t to June of t+1 include all NYSE, AMEX, and NASDAQ stocks for which are available market equity data for June of t. The Fama/French U.S. Small Research Index includes the lower 30% in market capitalization. The Fama/French U.S. Large Research Index includes the higher 30% in market capitalization.

Fama/French U.S. Profitability Research Indexes: Provided by Professors Eugene Fama and Kenneth French. Index constituents are formed on profitability (OP) at the end of each June using NYSE breakpoints. OP for June of year t is annual revenue minus cost of goods sold, interest expense, and selling, general and administrative expenses divided by book equity for the last fiscal year end in t-1. The reconstitution considers all NYSE, AMEX and NASDAQ stocks for which are available market equity data for June of t, (positive) book equity data for t-1, non-missing revenues data for t-1, and non-missing data for at least one of the following: cost of goods sold, selling, general and administrative expenses, or interest expense for t-1. The Fama/French U.S. Robust Profitability Research Index includes the higher 30% of stocks by profitability. The Fama/French U.S. Weak Profitability Research Index includes the lower 30% of stocks by profitability.

Fama/French U.S. Investment Research Indexes: Provided by Professors Eugene Fama and Kenneth French. Index constituents are formed on the change in total assets from the fiscal year ending in year t-2 to the fiscal year ending in t-1, divided by t-2 total assets at the end of each June using NYSE breakpoints. The reconstitution considers all NYSE, AMEX and NASDAQ stocks for which we have market equity data for June of t and total assets data for t-2 and t-1. The Fama/French U.S. Conservative Investment Research Index includes the lower 30% of stocks by profitability. The Fama/French U.S. Aggressive Investment Research Index includes the higher 30% of stocks by profitability.

The S&P 500 Index measures the performance of the large-cap segment of the U.S. equity market.

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