

Comprehensive Investment Management, LLC Fee Only Personal Financial Planning Spring 2021

A Review of the Financial Markets at March 31, 2021

Last year on March 31st the S&P closed down -37.4% from its high set just one month earlier. The next day it dropped yet another 4%. Finally, the markets had stopped ignoring the warnings about the first global pandemic in just over one hundred years. A major shutdown to reduce the spread of the virus would mean the economy would get a lot worse before it got better. The reaction of the markets now matched what any observer would have expected. But it didn't last. Just six days later the S&P rose 7% and it hasn't looked back since. Measuring the change in stock prices from the short lived depths of last March to the new highs this past quarter results in the extraordinary one year change you see in the chart below. Of course, as we all know, long term performance is what matters. In fact, for any measurement of stock performance the starting and ending points greatly impact the results. Another example of that in the chart is the drop off between ten and fifteen year returns. It is directly attributable to the downturn thirteen years ago in 2008, the worst financial crisis since the Great Depression.

In the most recent quarter, stocks continued their climb higher, with the S&P hitting new highs five times in March. Nothing seems to slow it down. On January 6th (a day that will live in infamy) and over the two days that followed the S&P rose 3%. A March rise in interest rates presented no problem. Other than just those few weeks, the markets have not reacted negatively to a global epidemic which led to the hospitalization of millions and to over 560,000 deaths in the US alone. Since the market is already hitting highs, as vaccinations become more readily available, can we expect it to go higher? Perhaps trees can grow to the sky after all, but probably not. The stock market very often gets ahead of itself and ahead of the economy for that matter. The markets and the economy are, after all, not one and the same.

Across the US markets, small cap stocks had the best quarter. Vanguard's Tax Managed Small Cap fund was up 18.3%. However, the average return of the small cap group was dragged down by Brown Small Cap Management which had an uncharacteristically poor quarter (-6.1%). The drop

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Average Returns of Mutual Funds Recommended by CIM						
At March 31, 2021	Quarter	1 Year	3 Years	5 Years	10 Years	15 Years
Large Cap Stocks	10.2	60.9	14.8	16.7	14.3	11.1
Mid Cap Stocks	7.4	72.0	14.6	17.7	15.0	11.8
Small Cap Stocks	5.7	78.9	16.9	18.5	14.1	11.3
Healthcare Stocks	-.3	38.0	15.2	14.0	16.7	13.2
Foreign Stocks	2.6	80.0	13.8	17.1	11.7	9.2
Short Term Bonds	-.6	4.0	3.7	2.5	2.2	3.1
Intermediate Bonds	-2.6	6.9	5.6	4.1	4.3	5.0

The Financial Markets (from page 1)

can be attributed to Brown's 40% of its holdings in healthcare. Overall healthcare investments have hit a rough patch with the Covid crisis pushing aside many of its profit making segments. Among large caps, funds managed by PRIMECAP were the leaders with a double digit average (11.7%). The top mid cap fund was Capital Opportunity (8.7%) also managed by PRIMECAP and foreign funds were led by Vanguard's Emerging Markets Select (5.4%).

A surprise increase in long term interest rates over the past couple of months caused bond values to dip. The best thing about large intermediate term bond funds like the ones Vanguard has is they hold more than twenty five hundred individual bonds. As bonds mature (the average duration is 6.2 years) they are replaced with new bonds. The replacements earn the higher interest rate. So in time things will eventually even out. That said, over the last ten years bonds have underperformed, returning about 2% below their historic norm.

There's now a lot of discussion about the real possibility of inflation over the next few years and beyond. With all the stimuli and low interest rates it looks like we may be entering this century's version of the roaring twenties. Even if inflation isn't a problem, extraordinary government monetary and fiscal actions along with the Covid pandemic and its variants are going to be the driving forces for the economy and the markets for sometime to come. The following are summaries of what is dominating financial discussions these days.

It takes a Worried Man

Former Treasury Secretary and Harvard Professor Larry Summers takes note of the following: "I have to wonder about the Fed chair saying that the Federal Reserve has a new regime and is no longer sure an overheated economy leads to inflation and the administration saying we're in an entirely new progressive era where policies could differ radically from what it has been for the last forty years. It may all work out, perhaps a way will be found to bring it under control. But I see three trillion dollars of stimulus, two trillion dollars of savings overhang, a major acceleration coming from having Covid in the rear view mirror and interest rates expected by the Federal Reserve to be at zero for three years. All that even in a booming economic record growth this year with major expansion of a Fed balance sheet and much new fiscal stimulus to come. I'm worried."



Did he say Trillions?

Here's Howard Marks, Co-Chair of Oaktree Capital Management. "I am concerned about inflation and therefore increased interest rates. Last year we added six or seven trillion dollars to the debt. This year we're on pace to probably do five or something like that. The infrastructure package is less of a worry because those trillions are spread out over at least a decade. Last year was the first time when trillion came into common use. I don't think we're used to that. You don't want a country adding that much to its debt and print that much money and have to borrow that much to cover and refinance the debt. Now the Fed claims not to worry about any of that. I hope they're right. We've never had stimulus like this. I always say that if you've never seen something happen before you can't say how it will end."



Not that long ago people started to say: "That's billion with a B". They wanted to make sure you knew they didn't say millions. Soon you will hear: "That's trillion with a T".

Next it will be: "That's quadrillion with a Q."

What, Me Worry?

Paul Krugman, NYU Distinguished Professor of Economics, Nobel Prize winner: “The \$1.9 trillion American Rescue Plan will, without question, deliver a lot of economic stimulus. Just about everyone, from private forecasters to the Fed itself, expects an economic boom, with the U.S. economy growing at rates not seen since the 1980s. There will almost surely be a rise in inflation, too, possibly well above the Fed’s target rate of 2 percent a year. The key thing to understand is that there are really two kinds of inflation. The prices of some goods fluctuate all the time. Many other prices, however, including the prices of labor, that is, wages and salaries, change much less frequently. Most workers’ wage rates are adjusted just once a year. The point is that short-term fluctuations in volatile prices tell us little about whether stagflation* is becoming a risk. So what’s going to happen in the months ahead? We’ll probably see a number of transitory price increases, not just because the economy is booming, but also because the lingering effects of the pandemic have produced some unusual disruptions. The question will be whether these price increases are a blip or something more dangerous. Smart observers will look past the headlines. My bet is businesses will not set prices and wages based on expectations of high inflation. It’s certainly possible that the American Rescue Plan will turn out to have been too much of a good thing. But don’t let the usual suspects seize on a few months’ inflation data as evidence of looming disaster.”



**Stagflation is a combination of stagnant economic growth, high unemployment and high inflation. It’s unusual because inflation and weak economies are not compatible. It occurs when government policies disrupt normal market functioning. The US experienced stagnation, and periods of negative growth through much of the 1970’s. Stagflation finally ended with a recession that lasted two years.*

Just In from the Personnel Department

CIM recognizes that periodically, perhaps every fifteen years or so, it is important to bring in new blood, so to speak. Consequently, CIM is pleased to announce a new hire, Mercedes McCullough Petrellis, our CEO’s daughter. Over the last several months Mercedes has familiarized herself with CIM’s internal operations. As a long time client she is well informed about the company’s services, policies and strategies. She has extensive technical and financial business experience. In regard to personal finance, she recently earned the designation of Wealth Management Specialist, which is granted by the College for Financial Planning, a premier provider of graduate-level financial education. Initially Mercedes’ responsibilities will be primarily in a support role while she completes the requirements for licensure as a Registered Investment Adviser. Mercedes can be reached at mercedes@cimontheweb.com. and her phone number is 610-960-1068.



Return of Vanguard Balanced Funds With Opposing Bond/Stock Allocations						
At March 31, 2021	Quarter	1 Year	3 Years	5 Years	10 Years	15 Years
Wellesley 65% bonds	1.1	18.4	8.4	7.4	7.6	7.3
Wellington 65% stocks	3.5	32.8	11.4	11.1	9.8	8.5

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Personal Financial Planning Services

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Recent market activity can be newsworthy, and is certainly that at the present time. However investment returns over longer periods, while not predictive, are significantly more meaningful.

We Get Letters

Q: Almost everything is political these days. Is it possible that's the case with investing in ESG funds?

A: It seems so. ESG funds invest in companies after taking into consideration their environmental, social and governance policies. Environment criteria includes energy use, and policies on waste, pollution, and resource conservation. Social considers how a company supports local communities and its regard for health and safety. Governance covers stockholder rights and the opportunity to vote on important issues.

An example of the opposite of ESG? RJ Reynolds, which at one time was the US top performer over a twenty year period, even as its ads were outlawed and smoking got a bad reputation.

The environment component gets the most attention. There is the obvious connection with climate change which most people agree is happening, but don't agree on what causes it or what to do about it, if anything.

The Department of Labor oversees ERISA, a law that established minimum standards for company retirement plans. In October 2020, under a Republican administration, the DOL announced regulations that forbid plans from offering investments that increase risk or decrease returns in pursuit of "a social or political end". The point: maximizing return should be the only consideration.

There is widespread agreement among investment professionals that ESG bolsters financial performance. If everybody agreed on that, then the regulations would be moot. But any assessment of performance can be challenged and there has been ongoing disagreement about what ESG policies are, let alone how to evaluate their efficacy. In any case, the current DOL administration says it will not enforce the new ESG regulations and the White House has announced plans to "conduct significant outreach to determine how to craft rules that better recognize the important role ESG integration can play".