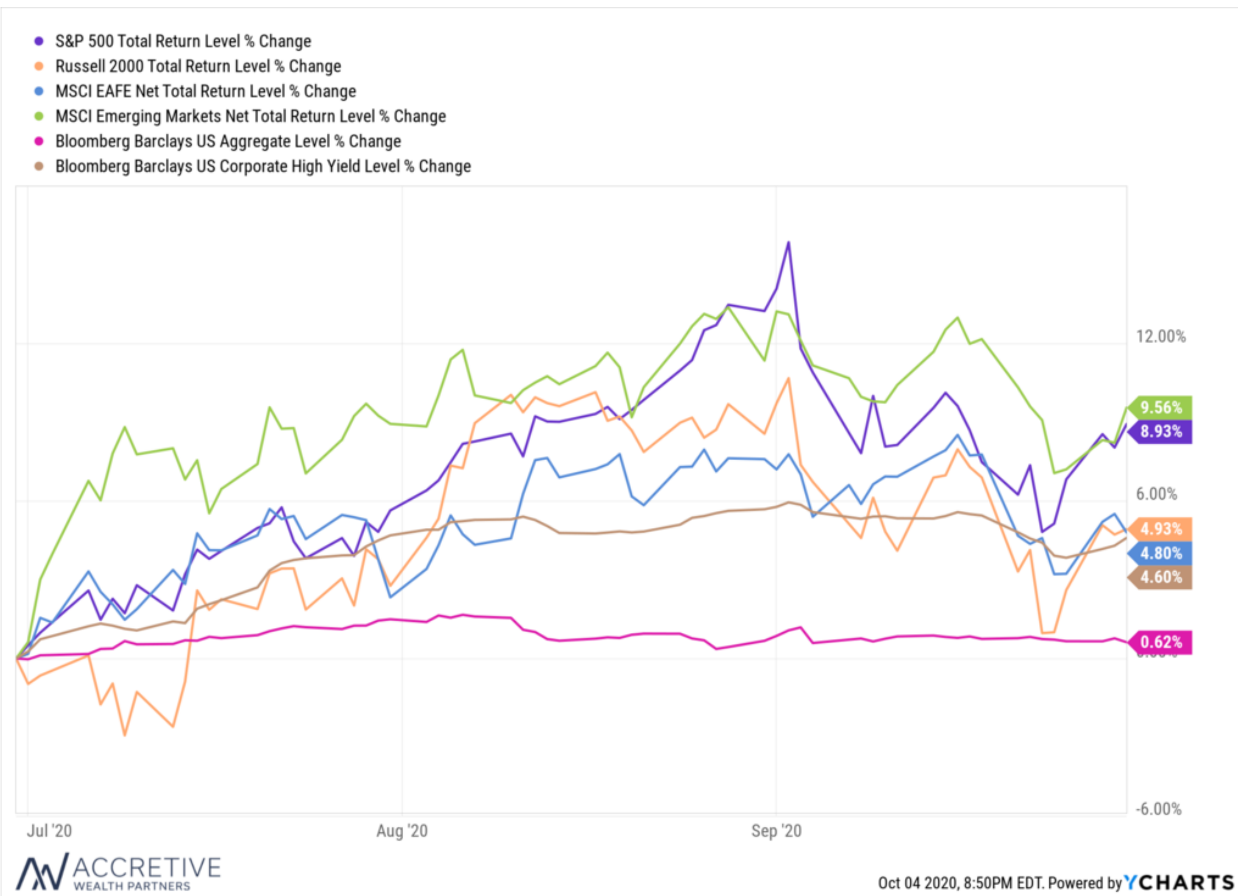
Accretive Q3 2020 Client Letter

Dear Clients and Friends of Accretive,

At the end of the third quarter, Accretive managed approximately $136 million for clients on a discretionary basis. As a result, we are waiving 2.5% of our management fee for the fourth quarter under our Client Alignment Program™ (CAP). Based on our current activity we believe that market permitting, we are on pace to cross into the next tier of the program by year-end.

In many ways the third quarter was simply a continuation of what we saw in the second quarter. As you can see below, from a stock and bond market perspective any commentary in this letter will simply be putting old wine in new bottles. There was a bit of a September selloff from the highs made earlier in the month, but corrections are normal, healthy, and to be expected. From our perspective, capital markets look to be open and functioning.



There are three main narratives attributed to the day-to-day market activity: the upcoming election, the status and timing of more stimulus, and pandemic news.

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Pandemic News
Let's take these in reverse order and start with the pandemic. There are a variety of COVID headlines that impact markets day to day: actual and potential second waves, the status of various vaccine trials and treatments, and the lifting or re-imposing of various local restrictions. But for some optimism on a vaccine coming to market relatively quickly and having a full restart of the economy a few months earlier than currently forecast, we think most of the headlines mean little to the market in the long run. To put it simply, from a market perspective only, it is mostly noise.

Fiscal Stimulus
We wrote in the last two letters that the prevailing attitude can be summarized as "do whatever it takes." It turns out that, after the most acute part of the crisis has passed, there is some disagreement over what the "whatever" should entail. Put simply, politicians are politicking over the next round of stimulus.

We think that both sides are in general agreement over the need for another round of large stimulus, but some sticking points remain. The main ones, as far as we can tell, are unemployment benefits, liability protections for businesses, and how much money can or should go to various municipal entities like cities and states. As we write this, it is unclear whether a stimulus bill will progress prior to election day. Since money is cheap for the Federal government, we expect politicians to act like politicians and spend a lot of it. We think it is also unlikely that whatever gets passed is the last round of stimulus.

Some of you may be wondering if we have entered some brave new world. We are talking about borrowing mind-boggling amounts of money. How can the government borrow so much money at such low rates? Someone has to pay for this, right? If money is practically free for the government, then why do I pay taxes? Inflation has to rear its head at some point, right?

We think it is possible we get an uptick in inflation, but without a new permanent government program it may be more transitory in nature. Our view is the amount of borrowing actually creates a deflationary overhang as any uptick in rates brings the conditions for economic contraction and for prices to fall. The net effect, in our view, is that rates should dip lower in each successive crisis. The next step in this could be to negative level in the US. Even if the Fed policy rate is not negative, market forces could take US treasuries there in the next crisis. Putting transitory inflation aside, for the time being, we believe the path of least resistance on inflation and rates is lower. It is possible that negative rates, if they arrive in the US, could be used as a justification for a currency debasement event and/or a new permanent social program. This may be how inflation ultimately materializes, but when inflation happens is still TBD.

The Upcoming Election
Coming into 2020, we thought the election would be what brought volatility to markets. That prediction, so far, has not panned out. We have noted in recent monthly updates that the market sees the polls and is aware of the various proposals. We think that observation bears repeating here before diving into the various potential outcomes.

The biggest concern we hear from clients tends to be around whether their team wins or loses and what impact that may have on markets. There is some concern around a contested election, which seems like a possibility, but the probability of which is uncertain. At Accretive we discuss politics to the extent it impacts financial planning and/or our portfolios, but as a firm we have no horse in the race. With that

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said, we think it may be helpful to map out the three main outcomes as it relates to control of the White House and Senate, as well as their impact on markets, as we see them.

Outcome 1: Status Quo
In this scenario the current parties continue to control the same respective branches of government. We view this outcome as status quo and not much would change from an outlook/market perspective. We think this outcome is heavily discounted by markets and the polls (to the extent you think they are accurate).

Outcome 2: Change in Control of the White House, but Congress is status quo
This outcome would result in gridlock. At a high level, from a market perspective, gridlock is typically not so bad. What may complicate matters is if Congress and the White House need to agree on something quickly in an emergency, so risk is elevated from that perspective. The President also appoints heads of the various government agencies that regulate various large industries. In this scenario, the regulatory regime could become more hands on and aggressive so it could change winners and losers economically. In addition, a complete health care overhaul would be hard to do, but tighter financial and environmental regulation would likely occur. Those sectors are already down and more aggressive regulation could make them even less appealing.

Outcome 3: Complete Change in Control
From an economic perspective, we think we would get the regulation we detailed in Outcome 2 and a potential change to healthcare. The last time health care reform was enacted it also brought crony capitalism, while the sector wound up doing just fine. There could be higher corporate and individual taxes but balancing that is a desire to keep the recovery going.

We would also point out that offsetting the potential increase in regulation and taxes would be a potential increase in stimulus. We think the market would welcome the government going bigger in terms of packages and currently it is the Republicans that are arguing for a smaller stimulus package. We also think a blue wave stimulus package would include a good amount of money for states and municipalities. Without taking a stance on whether or not that is the right thing to do, we will point out that it is pretty high-powered money.

A Contested Election
This outcome is the most uncertain of all and, like the 2000 election, it is possible that we have the Supreme Court involved. We think what matters in this scenario is that one of the outcomes outlined above is clear by Inauguration Day.

Our Portfolios
The third quarter was a good one for our portfolios and we feel good about our participation in the recovery. Our conservative portfolios participated well but to a lesser degree than our more aggressive portfolios. We were also pleased with our individual stock portfolios on both a relative and absolute basis. The outcomes made sense to us, given what transpired in the market.

Earlier in the year we had an extreme level of activity for us, and we wrote in our last two letters that you should expect that to wane in the coming quarters. To that point, it has waned. We could have an uptick in activity around the election, but we do not expect it to be nearly the level we had in the late

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winter/early spring. We would expect most election related changes, should they occur, to be in our individual equity portfolios.

We have read a lot about certain tech stocks driving the indices higher and that this recovery is not broad enough. While we agree the indices are more top-heavy than normal, particularly some of the more specialized indices, we disagree with those complaining that the biggest tech companies are the only ones driving index returns. We think many of the complainers simply made active bets that did not pan out, whether they knew it or not at the time is another matter.

Even if an investor is only utilizing passive index funds or ETFs and asset allocating, decisions still need to be made on the methodology and there needs to be research into what those funds and ETFs actually own. In the end, investors own a fractional interest in all the underlying businesses those funds and ETFs hold. Those business's collective results should drive the indices over time. Our observation is that too few investors are thinking about the health and prospects for the underlying businesses in the funds and ETFs they invest in.

Conclusion

2020 has been a challenging year but we feel we have navigated it well both as a firm and in our portfolios. There is still another quarter to go, but we are pleased with our progress thus far.

Our firm is growing nicely and in a responsible way, a lot of that growth is the direct result of our clients telling a friend or family member about us. Internally, we view that as one of the best compliments we can receive. Eric, Steve, and I thank those of you who complimented us in this way, it is much appreciated.

To our clients, we appreciate the trust and confidence you have in us. If you have any questions or concerns, please do not hesitate to contact us. To our friends, if there is anything we can do to help you, please reach out to us. We would welcome hearing from you.

Sincerely,

Gary C. Ribe, CFA, CFP®
Chief Investment Officer, Managing Partner

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