VAHANIAN & ASSOCIATES
FINANCIAL PLANNING INC.

60 Railroad Place, Suite 104, Saratoga Springs, NY 12866

(518) 583-0891 (518) 583-1617 vahanian@vahanian.com www.vahanian.com

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Dear Friends and Financial Advisory Clients:

Three months into the New Year, I want to remind you of an expectation we shared at the start of January that is now not only a reality, but one that is important for investors to note and understand. It has to do with a process called "Sector Rotation," an investment decision making strategy that can happen quite suddenly. And it is one we want to explain since it is so much a part of what is happening right now.

Bear in mind, in January, we observed that with a potentially recovering economy, a cyclical shift and "potential rotation towards more value-oriented companies – ones that have been beaten down by this pandemic" could be underway. Basically, investors might sell their stay-at-home stocks and embrace companies that should more directly benefit from the reopening of our society. Travel, Construction, Restaurants, Infrastructure, Industrial Production companies…Firms in sectors that have been out of favor, might now be ready to roll. Well, this process actually began to trickle along before the beginning of the year. But now, it has picked up steam.

So, what does this mean and what do we do? Well, for many of you, in the 4th Quarter of 2020 and in January of this year, we began to initiate a bit of a value tilt to some of these sectors. And now, as challenges of the Covid Pandemic appear to be abating – and with the U.S. economy showing more resilience in its recovery - we expect to do a bit more rotating as well.

But here is where an important historical lesson must be kept in mind. There is such a thing as over rotation. That is where investors drop what was working and chase what they think comes next. Indeed, they rush out of one area, into another, thus creating imbalances in their holdings that are uncalled for. For instance, just because the economy is recovering, it doesn't mean the process of ordering products online has come to an end. Just because many of us have been vaccinated doesn't mean everyone will be returning to their office or place of work in one fell swoop. No, in truth we are adapting and that is all. We are adjusting and navigating our way through this time.

We want to make this observation to you now, because as financial markets have shown strength in recent days, many great companies that performed well in 2020 and early 21, are falling dramatically, while the less glamorous cyclical companies are rising. We have what is truly a bifurcated market. And it may be that way for a while. And just like an economic and then financial market downturn can lead investors to panic and sell without thinking things through, sector rotations can lead investors to make equally unhealthy decisions. That is what happens if everyone runs out of one area and over rotates to another.

Bottom line, it is one thing to adjust your portfolio based upon sound strategic thinking. But if that process is overdone, then you are participating more like a gambler betting on what will next be hot or cold. That is not a healthy approach to investment thinking, which ideally serves us best in a context of longer periods of time.

When sector rotations occur, it can actually happen that what gets “chased” becomes overpriced, despite sector friendly conditions. And what gets “abandoned” can actually fall so far that it becomes the better deal, despite being in the less obvious or appealing sector.

What does this all mean? Once again, even as life appears to be on its way to more “normalcy,” as investors, we have to still proceed with poise. This is not race. It is a journey. A long one where a steady, balanced approach, even with mild tactical adjustments, is likely the healthiest way to travel.

Wishing you all a wonderful spring season,

Jeffrey C. Vahanian

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