Horizons 2020 2Q

A QUARTERLY NEWSLETTER FOR HOMESTEAD FUNDS' SHAREHOLDERS

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Weathering the Storm

As the COVID-19 pandemic continues to deliver unprecedented losses and challenges to Americans, please know that the team here at Homestead Funds hopes for the greatest health and well-being for all of our shareholders and your loved ones.

The pandemic has brought a new level of uncertainty into our lives, both in the day-to-day sense and in what we are envisioning for our futures. The prescription — staying distant from each other and our communities — feels especially disagreeable. During a crisis, all we humans want to do is connect and support one another.

We may not be able to unite in person, but we want all of our shareholders to know just how driven we are to support you through challenging times. To start, we've dedicated this issue to weathering financial shocks.

Flip through these pages to learn a few important and actionable ways to deal with what's happening in the markets and in the economy. We offer a close look at how stock markets rebound after lows — and what the cost is to investors who miss out. We share stats on how the environment has affected American spending and investing, and tips on how to shockproof your own finances.

If there's more we can do to support you personally, whether it's offering investment guidance or a listening ear, please reach out. Helping our shareholders is our top priority.

The One Thing to Get Right in Volatile Markets

Turbulent markets can set off a strong urge to jump ship, sell off investments and move savings to cash. But if there's one thing we can learn from history, it's this: You don't want to miss a stock market recovery.

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The average recovery of the S&P 500 index following a bear-market low

In the last three bear markets, stocks posted a strong rebound in the first month following the market low.

Source: Homestead Funds' calculations.
Stocks represented by price returns of S&P 500 Index.

STILL GETTING PAPER STATEMENTS?

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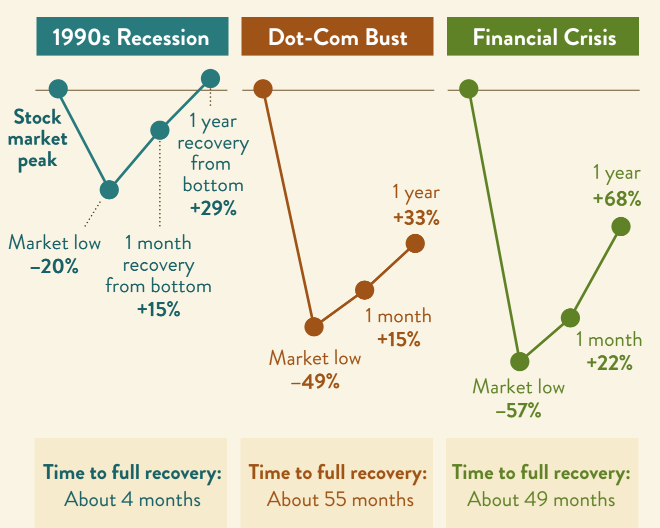
What History Tells Us

It's tough to spot the market bottom during a decline, but once the market reaches its low point, it has historically trended higher, typically with a strong move off its prior low. Remember, though, that stocks are inherently volatile. Share prices and performance will fluctuate.

We looked back at the three major "bear markets," or times when the stock market fell by 20% or more, since 1990: the early 1990s recession, the early 2000s dot-com bust and the 2008-2009 financial crisis. These market downturns were very different in nature, but they did behave similarly in one respect: Investors who did not sell during the downturn were able to participate in the market appreciation. Here are three important lessons to take to heart:

1 BOUNCE-BACKS CAN BE STRONG. First, we looked at how stocks behaved after they hit their cyclical bottom. Indeed, we saw a strong bounce-back in stock values, once the corner was turned. In all three of the bear markets we studied, stocks posted strong double-digit gains in the first month following the trough (low point). Looking farther out, stock values had recovered even more at the 12-month mark.

AFTER LOWS, STRONG STOCK MARKET RECOVERIES[1]



2 MISSING RECOVERIES IS COSTLY. The bounce-back nature of these early-stage stock recoveries has a big implication: It's quite costly for the investors who miss out. Suppose an investor moves to cash after the market starts to fall — which is exactly when most people start to ponder the idea. If you sell stocks as they are falling but fail to capture the bounce-back, you're actually just locking in your losses. Investors who stayed invested during the time period of market volatility were positioned to recover when the markets did.

3 MARKET TIMING IS RISKY (and nearly impossible to get right). These points may have you wondering, So how do I spot the market bottom? If I could just catch that, I can avoid some losses but get reinvested in time to catch the gains!

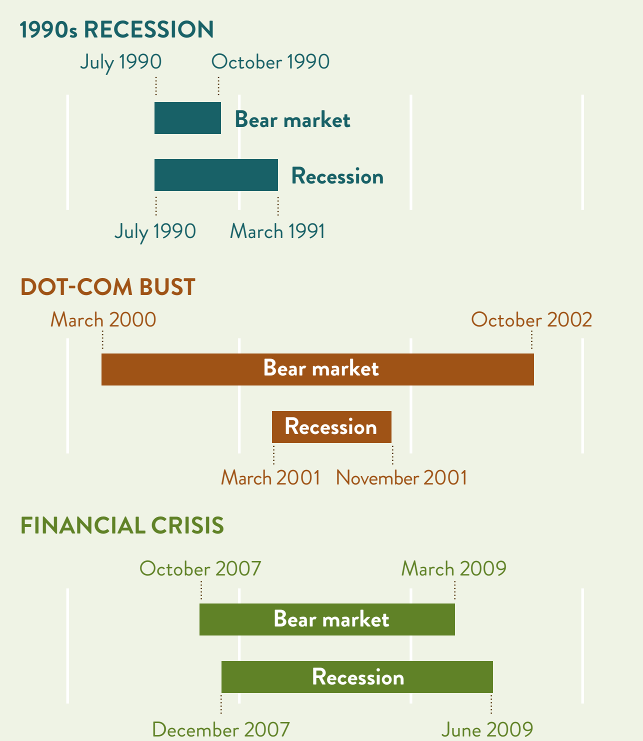
The answer is that you can only see the market bottom in hindsight. Stock markets are supremely unpredictable. In the case of the 1990s downturn, the stock market fell for about three months before hitting bottom. In the dot-com bust, stocks took 2 ½ years to hit the bottom; in the financial crisis, it was about 1 ½ years. Looking at the current pandemic-driven downturn, we may have hit the bottom already, or it could be yet to come.

Stock Markets Do Not Exactly Track Recessions

History also demonstrates another important point: Stock market downturns and recoveries do not usually sync up with recession start and end points. Most of the time, the stock market starts to tumble before a recession begins, and often it starts to recover before a recession ends.

This is because the price of a stock is driven by a company's outlook. Stocks are forward-looking assets; investors and analysts are always trying to gauge what the future holds for a company, and that drives the price investors will pay today.

BEAR MARKETS AND RECESSIONS DO NOT MATCH UP[2]



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Using History as a Guide

A range of factors will continue to sow uncertainty about the COVID-19 pandemic over the months and quarters to come: how long the global and local threats will linger, how the economy will fare in the meantime and what an eventual recovery will look like. With these unknowns, it's too early to say what the stock market could do next. The stock market losses may be behind us, or markets may face further stresses in the months to come.

With that in mind, it's especially useful to keep this historical trend in perspective — that once stocks have hit their turning point, an upward rally typically follows. Given the unpredictable timing of these turning points, having a well-diversified portfolio based on your risk tolerance and investment objectives is important.

[1] Source: Homestead Funds' calculations. Stocks represented by price returns of S&P 500 Index.

[2] Source: NBER, Yahoo! Finance

Looking for Silver Linings

In times of hardship, one coping mechanism is to be on the lookout for silver linings. Market downturns are "a feature, not a bug," as the saying goes; markets have throughout history bounced back after steep declines. With that in mind, we asked our certified financial planners to point out positive developments that can accompany such periods of market stress.

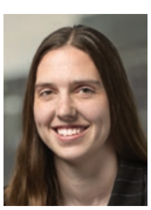
RAYMOND SCOTT, CFP®, RICP®

Institutional Sales Consultant

When I step back from the day-to-day news in the markets, I actually see this stock market pullback as an opportunity to time travel.

Before the COVID-19 crisis, stocks were trading at record highs. We don't advise our shareholders to "time" the markets. We wouldn't say, "Quick, buy now!" or "Wait, stocks are too expensive." We firmly believe that saving and investing is a long-term routine, where you keep saving and investing regularly.

Still, when you look at a market with record highs, it's easy to wish that you had put your money to work a year ago to capture those gains. Well, now it's like going back in time. You have the chance to add investments at a lower price. That might not do much for you in the short term, but looking out over the span of years, it could position you to take advantage of stock price appreciation if it occurs.



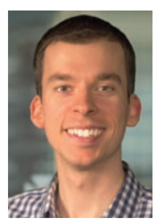
MEGAN MCFARLAND, CFP®

Senior Client Relationship Advisor

Downturns actually give us really important information about the risk tolerance of our shareholders.

When markets are going up, it's hard to tell how much portfolio volatility you would be comfortable with. This matters a lot, because potential higher-growth investments such as stocks are more volatile than more moderate investments such as bonds.

If a shareholder calls me in a panic and wants to sell everything because his or her portfolio is falling, I have to consider whether that individual needs a more conservative portfolio as a baseline. Maintaining a diversified portfolio based on your risk tolerance and investment objectives is an appropriate approach during market volatility.



JOHN SCOTT, CFP®

Client Relationship Advisor

I think we won't really know how this period will change our society for many years to come, but it seems very possible that we could see positive changes. For younger adults, this time will affect their decisions throughout adulthood. It might mean that families put aside more in savings as a rule or choose to take on less debt. Those would certainly be good things.

When you hear of stories in your family about your earlier generations getting through wars or other hardships, those times brought them together. And of course, we've seen throughout time that large-scale changes or disruptions often lead to new ways of doing things, spurring innovation or sparking demand for new products. What industries might be reshaped by this? Might those changes ultimately make some services more affordable or more widely available?

5 No-Panic Ways to Make Your Finances Shock-Ready

The COVID-19 pandemic has proven to be an economic shock like no other. Within a matter of weeks, millions of American jobs evaporated and countries across the globe were in various degrees of lockdown. Governments are now puzzling out how to guide their populations safely back to work, school and society. Though these difficult times will improve eventually, the challenges could continue for a while.

If you're among the many Americans who need to reevaluate your finances, now is the perfect time to shore up your situation. Here are five things you can do — starting today! — to improve your finances.

1 Take emotion out of your investment decisions.

If you follow your heart, you'll be selling everything on the way down (oops!) and only buying at the top (oops again!). Indeed, you'd need a will of steel to do exactly the opposite.

Instead, take emotion out of the equation completely. Choose a long-term diversified portfolio mix that is right for your goals and tolerance for risk, and allow it to work for you through the highs and lows of the market.

Need help with portfolio design?
Check out our prebuilt portfolios.
homesteadfunds.com/prebuilt-portfolios/

2 Stash more in your emergency savings.

One small upside to the lifestyle changes of a pandemic: Most people have cut back on dining out and other discretionary expenses. If you're ending the month with anything extra, put whatever you can into your emergency fund, which should hold three to six months of living expenses for emergencies.

Emergency savings don't have to sit in the bank.
Consider putting your savings to work in a conservative investment mix. Check out our model portfolios here.
www.homesteadfunds.com/make-a-plan/

3 Be quick to cut back.

If you're not "accidentally" finding yourself with surplus cash at month-end, consider an alternative. Perhaps you've thought, If I ever needed to get by on less, I would cut out ___________. Well, it might be time to cut out ___________. Whether that's subscriptions for entertainment or a fancier-than-needed car, give some serious thought to putting those emergency measures into place now.

Good news: Being thrifty is back, big time.
Check out our Q4 2018 issue of *Horizons* where we looked at the Rebirth of Frugal.
www.homesteadfunds.com/wp-content/uploads/2018-Q4-Homestead_Horizons.pdf

4 Get out of debt (or don't take it on in the first place).

Debt is usually the straw that breaks the camel's back, driving more Americans to file for bankruptcy when household incomes fall during recessions. Nearly 1.6 million Americans filed for bankruptcy[1] in 2010 following the financial crisis; by 2019, that number was down to less than 800,000. With the severity of job losses in recent months, experts expect bankruptcies to spike again.

For the typical household, the only guarantee for staying out of that situation is having plenty of savings and little debt. Take a hard look at the options for trimming what you can.

Read more about bankruptcy and other drivers of financial "illness" in another recent *Horizons.*
www.homesteadfunds.com/wp-content/uploads/2019-Q4-Homestead_Horizons.pdf

5 Set your investment accounts to rebalance automatically.

To further strip emotion from your investment decisions, set your accounts to rebalance automatically. If your allocation upkeep is on autopilot, you may be less likely to trade when markets are volatile.

Read about our automatic rebalancing program here.
If you want to implement this for your Homestead portfolios, log in to your account, then go to the Trading tab and select Asset Allocation Modeling.
www.homesteadfunds.com/wp-content/uploads/asset_allocation_modeling_rebalance.pdf

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[1] MarketWatch, "'It's really a question of when.' The coronavirus pandemic is about to spawn a surge in bankruptcies, experts say"

How COVID-19 Has Changed Household Finances

As Americans continue to cope with life through a pandemic, their finances are seeing some changes.

SAVINGS RATE IS UP

33.0%

THE AVERAGE SAVINGS RATE IN APRIL[1]

The household savings rate shot up in April as widespread stay-at-home orders restricted spending. The 12-month average before April was 8.2%.[2]

Spending MORE on:[3]

- Groceries
- Delivery services
- Gaming and other streaming entertainment

Spending LESS on:

- Travel
- Clothing and other retail shopping
- Fitness

EXPECT RECORD DEBT LEVELS TO FALL

$14.3 trillion

THE TOTAL HOUSEHOLD DEBT IN THE U.S. AS OF THE FIRST QUARTER OF 2020, A RECORD HIGH[4]

Household debt, which includes mortgages, car loans, credit cards, student loans and other borrowing, climbed 1.1% in the first quarter of 2020.

It's common for debt levels to go higher when unemployment is low, but households usually trim debt when unemployment rises.[5]

RETIREMENT SAVINGS HELD UP RELATIVELY WELL

-11.2%

THE MEDIAN 401(K) RETURN FOR THE FIRST QUARTER OF 2020[6]

According to a large Morningstar survey, the typical 401(k) account only declined 11.2% in the first quarter, even though large-cap stocks were down about 20%. According to Morningstar's analysis, the typical retirement portfolio benefited from having a mix of bonds, not just stocks, and the allocation helped investors avoid the worst stock declines.

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[1] Bureau of Economic Analysis
[2] Source: Federal Reserve of St. Louis
[3] The New York Times, "How the Virus Transformed the Way Americans Spend Their Money"
[4] Federal Reserve Bank of New York, "Household Debt and Credit Report," Q1 2020
[5] Forbes, "Why Credit Card Debt Is At An All-Time High, While Unemployment Is At A 50-Year Low"
[6] Morningstar, "Keep Your Distance"

News Briefs

Reminder: We can help with an asset allocation plan

If you're not sure your investment mix is in line with your goals and risk tolerance, now is a good time to give us a call at **800.258.3030, option 2**. Our representatives can review your portfolio with you over the phone and talk through any questions or concerns you have. We can also follow up with an asset allocation questionnaire. Your answers here will help us further refine your fund mix to make sure it's in line with your risk tolerance and goals.

CARES Act: What You Need to Know

We have received many questions from our shareholders over the past few weeks about the impact the Coronavirus Aid, Relief, and Economic Security (CARES) Act will have on their accounts with Homestead Funds. We've summarized some of the main parts of the CARES Act to hopefully answer questions you may have about it and how it affects you. Check out our website for more information: *www.homesteadfunds.com/frequently-asked-questions-about-the-coronavirus-aid-relief-and-economic-security-cares-act/*

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Asset allocation and diversification do not guarantee a profit or protect against a loss in a declining market. They are methods used to help manage investment risk.

Investing in mutual funds involves risk, including the possible loss of principal. Past performance does not guarantee future results.

Investors should carefully consider fund objectives, risks, charges and expenses before investing. The prospectus contains this and other information about the funds and should be read carefully before investing. To obtain a prospectus, call 800.258.3030 or visit homesteadfunds.com.

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