Market Commentary

December 31, 2020

GOOD RIDDANCE 2020!

As the 4th Quarter of 2020 is now history, we can't help but also reflect on the year as a whole and bid it "Good Riddance"! For better or for worse it was "a wild and crazy" ride of a year filled with uncertainty, Bulls and Bears, a pandemic, political and social unrest, a recession and a multitude of resulting events and factors too numerous to recount in this tight space. Needless to say, despite the resulting positive market performance, I believe to a person, we are ALL glad to see it end!

The quarter began with the pandemic still not under control and waiting on a vaccine, the election just a month away, and additional fiscal stimulus being debated. Three-months later we had, not one, but two vaccines in the U.S., a new president (and Democratic controlled House and Senate), and a new round of stimulus. It did, however, take until Saturday November 7th to project Joe Biden the winner of the 2020 Presidential election, and then on the following Monday November 9th, Pfizer Inc. and BioNTech announced the results of their Phase 3 Covid-19 vaccine trial had had over a 90% efficacy rate. What a couple of days! So, despite the markets beginning on a downward slide in October (S&P 500 -2.8%), these events helped "turn the tide" leading a resurgence in the markets and an increasingly optimistic outlook resulting in a +12.15% Q4 for the S&P500 Index. For the year the S&P 500 posted a somewhat remarkable return of +18.4%, despite all the turmoil and havoc wrecked by the pandemic and political and social unrest. Value stocks, world-wide, had big gains for the quarter beginning in November, reversing years of underperformance vs. growth stocks. Value outperformed growth across large and small cap stocks, and small caps outperformed large caps. Also, for the quarter, emerging market stocks (+19.7%) of less developed countries outperformed both developed or international stocks (15.9%), as well as U.S. domestic issues. On the fixed income side, interest rate changes were mixed during the quarter with the yield on the 10-Year Treasury increasing 29 bps to 0.93%, and the 30-Year Treasury bond yield increasing 18 bps to finish at 1.64%. For the quarter the Barclays US Aggregate Index returned +0.67%.

Economically, the U.S. continues to recover albeit, with a more subdued, yet still strong growth rate of +8.6%, according to year-end GDPNow's forecast, on the heels of a remarkably strong Q3 GDP +33%. Core inflation (CPI) continues to remain tame at 1.6% (Nov.) and well under the FED's stated 2% average target, where concern may start to mount. Given the additional year-end stimulus that has been injected into the economy coupled with the anticipated spending the democrats are likely to sponsor in coming months under a Biden administration, there is a growing belief that inflation may rear its ugly head, sooner rather than later. We'll be watching! On the labor front in December, the unemployment rate remained unchanged at 6.7%, as well as the number of unemployed at 10.7 million persons. Interestingly, those that are teleworking from home because of the Coronavirus pandemic continue to increase up to 23.7% of employed persons versus 21.8% in November. When or will they go back? Could have a bearing on commercial real estate in the future. We'll be watching!

Domestically all 11 S&P sectors were positive for the quarter with the top performing sectors for the quarter being Energy +25.8% (yet down the most for the year -37.3%), Financials +22.5% (-4.1% for the year), and Industrials +15.2% (+9% for the year). The worst performing sectors for the quarter were Real Estate +4.1% (-5.2% for the year), Consumer Staples +5.6% (+7.6% for the year), and Utilities +5.7% (-2.8% for the year). While stock market breadth (gainers vs. losers) improved during the year, in the end, three stocks, Apple, Amazon, and Microsoft accounted for over 53% of the S&P 500's return during the year (18.4% would have been 8.6%). Without the top 30 contributing stocks the S&P 500's return would have been negative (-0.03%) for the year.

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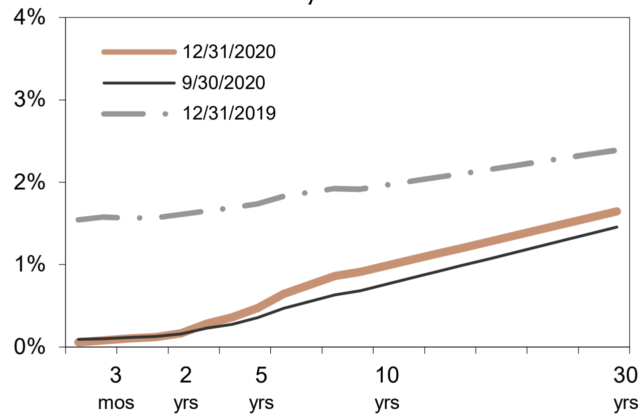
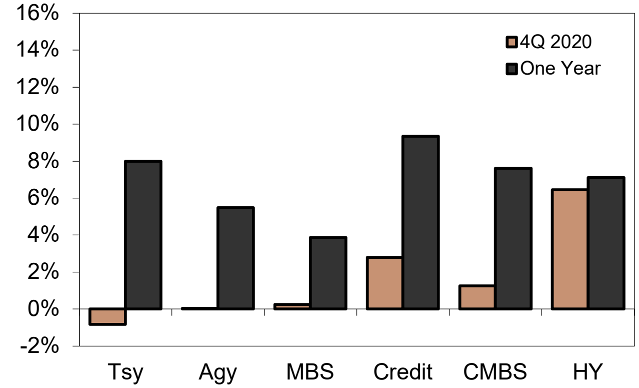
US Treasury Yield Curves



Sector Index Returns



In the world of fixed income, the combination of additional fiscal stimulus, a weaker US dollar and the Fed allowing inflation to rise above their 2% target, suggests higher interest rates. This should cause the yield curve to steepen with the largest impact occurring in maturities greater than ten years. It should also lead to greater volatility which will allow us to gradually adjust the duration of our portfolios to take advantage of the movement in rates.

Our portfolio durations ended the quarter below their benchmarks and we expect the yield curve to gradually steepen throughout the year. Credit spreads narrowed during the quarter fueled by massive central bank liquidity and now only look like fair value versus treasuries. Although we continue to maintain an overweight in credit exposure, our portfolios credit spread duration is slightly less than that of their benchmarks. We have maintained an underweight in MBS versus the index, given the uncertainty over potential defaults due to temporary layoffs and the uncertainty whether the current forbearance will be extended.

In closing, while no one could have predicted the tumultuous 2020, we are ALL certainly glad to have it behind us. The concern going forward from an investment standpoint will be what baggage are we left with? Obviously the first thing that comes to mind is the Covid-19 virus and more specifically, how quickly can the government(s) roll-out the vaccine(s) and get enough of the population inoculated? At that point – watch out! – it may be like the Roaring 20's all-over-again! If not? Watch out!! Another wave of the virus and we may be testing market lows from last March! Ouch! However, spending and more spending may then fuel inflation. It's what we'll be looking out for, and along the way we're sure to encounter more uncertainty and volatility. As always, we will remain diligent and disciplined in our approach, realizing that it's these principles that steer us to the VALUE capital markets have to offer long-term investors.

Stay safe and stay well!