

WAINWRIGHT INVESTMENT COUNSEL, LLC FINANCIAL MARKETS HIGHLIGHTS

Fourth Quarter 2020

As time passes and memories fade, the financial logs will remain unchanged, reflecting a superb 2020 for the capital markets. As for the here and now, with vivid memories not of holiday cheer but rather of isolation, fear and political division dancing through our heads, we know that 2020 was the year to be forgotten, not reflected upon fondly as the stock market graphs would suggest.

Two lessons come to mind. First, investors' collective willingness to look past dark days towards sunnier ones provides an illustration of what this country was built on – optimism, stick-to-itiveness and a can-do attitude. In the blander parlance of finance textbooks this phenomenon is chalked up to the stock market being a forward-looking indicator. Second, attempts to time the market, to out-forecast the ultimate forecasting machine, are generally reactionary, futile and costly. The solution remains unchanged, easy to say but hard to execute – maintain a diversified portfolio with enough conservatism that one can sleep at night, stay cool under pressure and, paraphrasing Napoleon's definition of a genius, "Do the average thing when everyone else around him is losing his mind."

The global stock markets performed exceptionally well during the quarter. The large-cap, tech-heavy S&P 500 index returned +12.2%. Six companies now constitute close to 25% of the index, those being Apple, Microsoft, Amazon, Alphabet, Facebook and Tesla with an average size of 3.9%. Its remaining holdings have an average size of 0.2%, lest one wonder who is in charge of the daily ebbs and flows of the world's most watched stock index. Notably, small-cap and "value" stocks, those characterized as having relatively higher dividends and/or lower prices compared to their earnings or assets, surged during the quarter after having been persistent laggards. In fact, the small-cap Russell 2000 Value index posted its best three-month return in its 40+ years, appreciating +33.4%. On a sector basis it was Energy, Financials and Industrials that performed best, again industries whose stocks are largely, at present, characterized as having value characteristics. The MSCI EAFE Index of international developed

market equities returned +16.1% during the quarter, and the MSCI Emerging Market Index +19.7%.

Like most everything nowadays, the resurgence of value stocks is in some way connected to the coronavirus pandemic. There was plenty of bad news regarding COVID-19 during the quarter; daily-confirmed cases vaulted to new highs and deaths accelerated as the year closed (<https://covid.cdc.gov/covid-data-tracker>). While many have forecasted dark days ahead, there are reasons to be optimistic, namely progress on the vaccine and therapeutic front. In a feat of scientific ingenuity, vaccines from Pfizer and Moderna exhibited over 94% efficacy and were approved for immediate emergency use. J & J, AstraZeneca and Regeneron, to name a few, have vaccines or therapeutics well along in the approval process. According to the CDC, as of January 2nd 4.2 million Americans have been vaccinated (or received the first dose of two-dose regimen). While this represents only ~1.3% of the US population, many can point to friends or family who have received the vaccine and, as such, optimism is "punching above its weight" based on these anecdotal experiences. Effective vaccines and therapeutics will result in the pace of movement, work and play increasing dramatically, restoring the earnings and revenue of those companies that have suffered while technology assets, generally, have held up well in this brave new stay-at-home world. Indeed, the economic recovery is well underway, with third quarter GDP increasing an estimated 33.4% after falling at a record -31.4% during the second quarter. For better or for worse, the American people are not a sedentary lot.

On the political front, Joe Biden was elected the 46th President of the United States after a contentious and fiercely disputed election. The Democratic Party maintained control of the House of Representatives and took control of the Senate, whose membership is evenly split between the Republican and Democratic Parties, with Democrat Vice President Elect Harris having the tie-breaking vote. The unification of the President and Congress under one party paves the way for the Biden

Selected Index Returns (%) as of December 31, 2020 (Source: Morningstar Direct). 3, 5, 10 year returns are annualized.

	<u>Oct.</u>	<u>Nov.</u>	<u>Dec.</u>	<u>QTR</u>	<u>YTD</u>	<u>1 Year</u>	<u>3 Year</u>	<u>5 Year</u>	<u>10 Year</u>
S&P 500	-2.66	10.95	3.84	12.15	18.40	18.40	14.18	15.21	13.88
S&P 400	2.17	14.28	6.52	24.37	13.66	13.66	8.45	12.35	11.51
Russell 2000	2.09	18.43	8.65	31.37	19.96	19.96	10.24	13.25	11.20
Wilshire U.S. REIT Index	-2.46	10.35	2.78	10.62	-7.90	-7.90	3.30	4.25	8.27
MSCI EAFE	-3.99	15.50	4.65	16.05	7.82	7.82	4.28	7.45	5.51
MSCI Emerging Markets	2.06	9.25	7.35	19.70	18.31	18.31	6.17	12.80	3.63
Barclays Aggregate Bond	-0.45	0.98	0.14	0.67	7.51	7.51	5.34	4.43	3.84
Barclays High Yield	0.51	3.96	1.88	6.45	7.11	7.11	6.24	8.58	6.80

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Administration to implement its policies more easily than a Republican led Senate would allow. The knee-jerk reaction of the stock market is surprisingly positive, largely due to the expectation that fiscal stimulus will continue to be unprecedented in size and monetary policy will remain accommodative. The offset is likely higher tax rates and a more robust regulatory regime.

Regarding individual tax rates, Biden has proposed imposing a 12.4% social security tax split between employers and employees on income above \$400,000 (currently capped at income of \$137,700), raising the highest income tax rate to 39.6% (from 37%), raising long-term capital gains and dividend tax rates to 39.6% on income above \$1 million (from 20%), amongst other things. As for business taxes, Biden proposed a 28% tax rate (from 21%) and, regarding business regulation, Biden campaigned on raising the federal minimum wage to \$15 and supporting organized labor.

On the topic of monetary policy, the Fed's Open Market Committee ("FOMC") met in December and left its short-term Fed Funds rate at a range of 0.00 – 0.25%. The Committee's statement read, "it expects to maintain this target range until labor market conditions have reached levels consistent with the Committee's assessments of maximum employment and inflation has risen to 2 percent and is on track to moderately exceed 2 percent for some time." To that end, the Fed continues its program of large-scale Treasury and Agency Mortgage Backed Securities, helping drive interest rates lower and grease the skids of the lending market.

Nowhere is this clearer than the housing market. The average 30-year fixed rate mortgage declined again to a new all-time low of 2.66% on December 24th according to Freddie Mac, representing a 1 percentage point decrease from a March 19th high of 3.65%. Housing demand remains robust, supported by incredibly low rates. The yield on the 10 Year Treasury Bond closed the year at 0.93%. The Barclays Aggregate Bond index returned +0.7% during

the quarter, and +7.5% for the full year. In the commodity markets, oil rallied approximately 20% during the quarter, the dollar declined about 5% against the world's major currencies, gold fell 5% and bitcoin surged 170%.

From the Wainwright family, happy New Year, thank you for your trust, and we look forward to sunnier days ahead.

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