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Market Commentary
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Introduction

2020 was a historic year that will never be forgotten. Coronavirus wreaked havoc across the globe and, in turn, impacted the economy and financial markets. Despite economic data faltering in the first half of the year, the economy has begun its path to recovery. Growth has rebounded here in the United States with GDP up 33.4% on a quarter-over-quarter basis in the third quarter, compared to -31.4% in the second quarter. The labor market has improved with the U-3 unemployment rate at 6.7% as of December compared to 14.7% in April, its worst reading in 2020. Lastly, inflation is tame with the Consumer Price index (CPI) up 1.2% year-over-year as of November. With the economy on the rocks for most of the year, loose monetary policy and immense fiscal stimulus supported a “V shaped” recovery. The Federal Reserve lowered the Federal Funds Rate to 0% and is currently purchasing Treasuries and Mortgage-Backed Securities at a rate of $120bn per month while the US Government has provided as much as $2.6tn in stimulus spending this year. While the current virus picture is grim with over 20 million total cases and over 350,000 deaths in the United States, there are some positives as we head into the new year. For one, we have gotten through election day which has provided some clarity on policy in the U.S. for the next four years. Secondly, we are distributing Coronavirus vaccines and hope to reach heard immunity by the second half of 2021. Lastly, we have another relief package which has been recently approved by Congress that we hope can help bridge the gap to economic recovery. Each of these tailwinds give us optimism as we head into 2021.

Domestic Equities

U.S. stocks took a wild ride in 2020 with the S&P 500 down as much as -33.47% from peak to trough during the selloff, however ending the year up 18.40% and up 12.15% in the fourth quarter (source: Morningstar). Investor sentiment was severely damaged by the fear of Coronavirus early in the year but was revived in the second half due to a re-opening of the economy and support from the US Government and Federal Reserve. The winning stocks on the year were technology heavy business models which had the ability to adapt when lockdowns took effect while industries that generally shoulder a greater share of employment, such as retail, transportation and energy-related companies, took the brunt of the pain. Thankfully, year-over-year earnings growth for companies in the S&P 500 improved to -6.9% in the third quarter from -30.1% in the second quarter (source: Bloomberg). However, valuations remain elevated in certain market segments due to significant stock price appreciation in the second half of the year. Despite smaller sized companies selling off harder than larger sized companies from peak to trough, midcaps and small caps ended positive for the year up 17.10% and 19.96%, respectively, as measured by the Russell Midcap and Russell 2000 index (source: Morningstar). While the Federal Reserve and U.S. Government remain accommodative and vaccines come to market, we expect stocks to grind higher over the next 12 months. Although this is our mid to long-term view, we are still aware of the risks involved with a looming virus and permanent damages from the first wave of economic lockdowns, leaving us more cautious in our asset allocation heading into 2021.

International Equities

The global economic expansion came to a halt in 2020 as the pandemic took hold and shutdowns around the world presented massive headwinds for economic growth. A second wave of virus infections in the fourth quarter has dampened the prospect of positive economic growth in the Eurozone after what looked to be the beginning of a V-shaped recovery in GDP growth in the third quarter. As the year ended, the United Kingdom finally exited the European Union, leaving Europe’s single market and customs union. Within emerging markets, China’s economy has returned to pre-pandemic output levels, as significant fiscal and monetary stimulus coupled with a more successful containment of the Coronavirus has allowed the economy to reopen at a faster pace. Despite these disruptions, foreign stocks were able to rally in 2020, with international developed equities and emerging market equities up 7.82% and 18.31%, respectively (source: Morningstar).

A successful vaccine rollout and improvement in U.S./China relations under a new U.S. administration are positive signs for economic growth in 2021, but it does not remove the headwinds facing its economy moving forward. Still, we are optimistic that global economic growth will rebound in 2021, as many of 2020’s headwinds appear likely to be resolved in 2021. The Federal Reserve looks to be on pause, which indicates the U.S. dollar may soften, trade tensions are likely to dissipate, and the U.K. may see improved growth since Brexit is resolved. As a result, we believe foreign equities may present buying opportunities in the year ahead, particularly in emerging markets.

Fixed Income
After a strong 2019, it did not appear that fixed income had the potential to continue to appreciate in 2020. However, fixed income was supported by extremely accommodative monetary policy as the Federal Reserve stepped in to shore up markets as the pandemic took hold, resulting in another positive year for bonds, with the Bloomberg Barclays Aggregate Bond Index finishing the year up 7.51% (source: Morningstar). To combat the economic devastation of the shutdowns, the Federal Reserve cut its benchmark interest rate to zero in March, launched a new quantitative easing program, and introduced several lending facilities to restore order to fixed income markets. Following these moves, short-term rates decreased from 1.57% to 0.12%, while the 10-year U.S. Treasury yield ended the year at 0.91%. This is well below where it started the year, but higher than the low of 0.50% it reached in August (source: Bloomberg). Despite the flight to quality in March, lower credit quality bonds tended to outperform for the remainder of the year, as investors sought yield amidst a risk-on environment. Over the next year, we project the path for short-term interest rates to remain neutral, but we anticipate a potential increase in longer term rates, as inflation has the potential to pick up if the economy expands at a faster pace than expected. Thus, we believe fixed income securities will continue to benefit portfolios from a diversification perspective but may offer low returns moving forward.

Alternatives
Alternative asset classes lagged global equities in 2020. While seemingly every asset class fell in tandem during the market sell off in the first quarter, unlike the equity market, alternative assets were not able to fully recover from their March lows. Oil prices went negative for the first time in history, as futures contracts for WTI oil fell to a stunning -$37.63 on April 20th on lack of demand due to the Coronavirus (source: Bloomberg). Oil prices rebounded since the April bottom, but still finished the year lower, with WTI crude ending 2020 at $48.52 per barrel, down from $61.06 per barrel at the end of the 2019 (source: Bloomberg). Liquid alternatives provided some cushion from the bouts of volatility markets experienced over the year, with the Morningstar Diversified Alternative index having a standard deviation of 13.17% in 2020 versus the S&P 500 having a standard deviation of 25.95% (source: Morningstar). Hedge fund-like alternatives will continue to play a key role in downside protection and volatility reduction within a portfolio by maintaining low correlation to equity and fixed income markets.

Real Estate
The housing sector was resilient during the recession that followed the Coronavirus pandemic. Residential real estate had one of its best years in almost a decade as a move from cities to the suburbs and historically low mortgage rates buoyed demand. Mortgage rates remain near all-time lows at 2.86% for the week ending December 18th (source: Bloomberg). The November reading on housing starts and building permits is a testament to the current strength of the housing market with the former up +1.2% to 1.547 million and the latter up +6.2% to 1.639 million (source: Bloomberg). Single family homebuilding increased to its highest level since April 2007; building permits, a proxy for future construction, rose to its highest levels since 2006. As we look forward into the new year, with several COVID-19 vaccines making their way to market along with immense fiscal and monetary stimulus, the housing market could continue its historic run in 2021.

Conclusion
The magnitude of the events that took place in 2020 cannot be understated. GDP growth plunged to depression like levels, the unemployment rate increased to double digits and the government spent over $2.6tn in economic relief because of the Coronavirus. As we close out the year, we acknowledge that many of our views at the start of 2020 did not play out as expected. This reminds us that there are no certainties in investing but the investor who is aware of the risk associated with each of their investment decisions is best equipped to navigate unexpected market events. We expect more of the same in 2021 but we believe we are through the worst of the pandemic and its impact on the economy. We would not be surprised to see a moderation or even a slight pullback in economic data in the early parts of the New Year as virus cases rise but believe our trajectory is higher over a 12-month period.