MONTH IN REVIEW

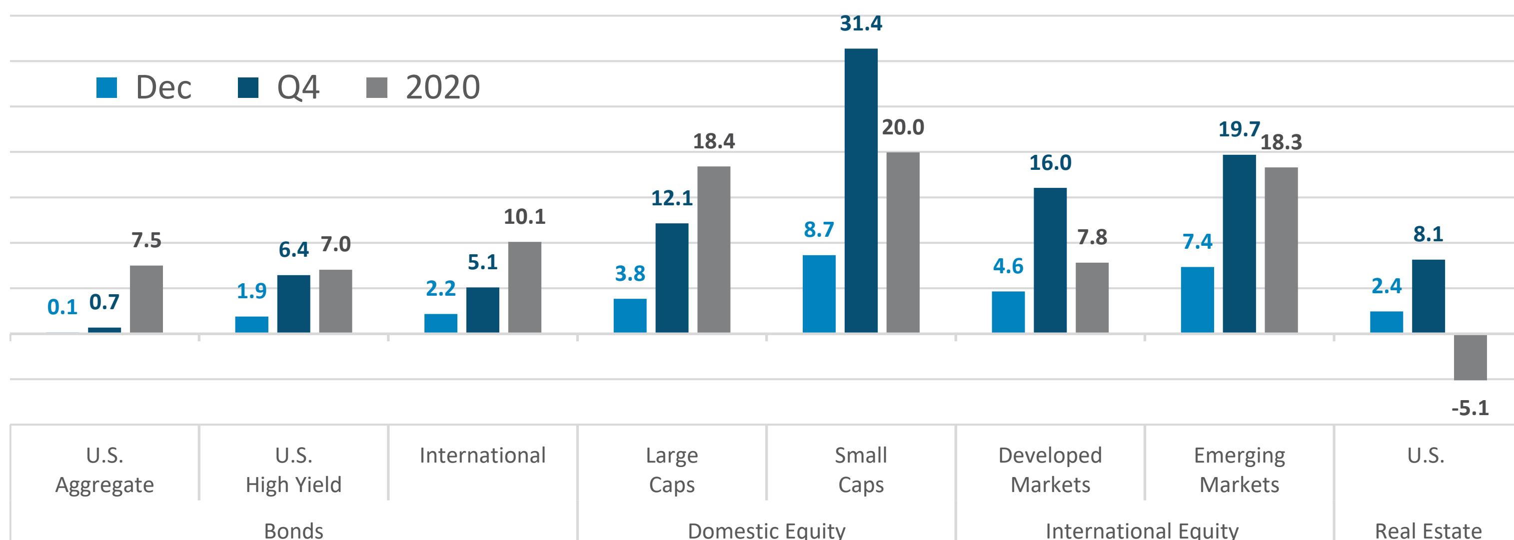
December 2020

Quick Takes

- **Finish strong.** Stocks closed the quarter, and 2020, with strong returns, despite lingering economic concerns brought on by a resurgence in coronavirus cases, challenges with the vaccine roll-out, and uncertainty around the policy implications following the Georgia Senate runoff outcome.
- **Highs and lows.** Most major stock indices finished the year at/near all-time highs while bond yields finished the year at/near record lows. Likewise, mortgage rates finished at/near record lows and Financial Conditions are the loosest on record.
- **The year of COVID-19.** Nothing defined 2020 more than the coronavirus pandemic. On that front, the year ended with global deaths from Covid-19 passing 1.8 million. New York and Florida both broke their previous daily records for cases. A new strain appeared in the U.K. and is now in the U.S.
- **Much better, but room for improvement**. The U.S. economy continued to recover, but remains below pre-pandemic levels even after record third-quarter GDP, and employment that is still 9.8 million jobs short of its total before coronavirus hit in March.

Asset Class Performance

Though not quite as high as November's levels, all major asset classes had positive total returns again in December and resulted in all asset classes being positive for the fourth quarter and all but Real Estate positive for 2020.



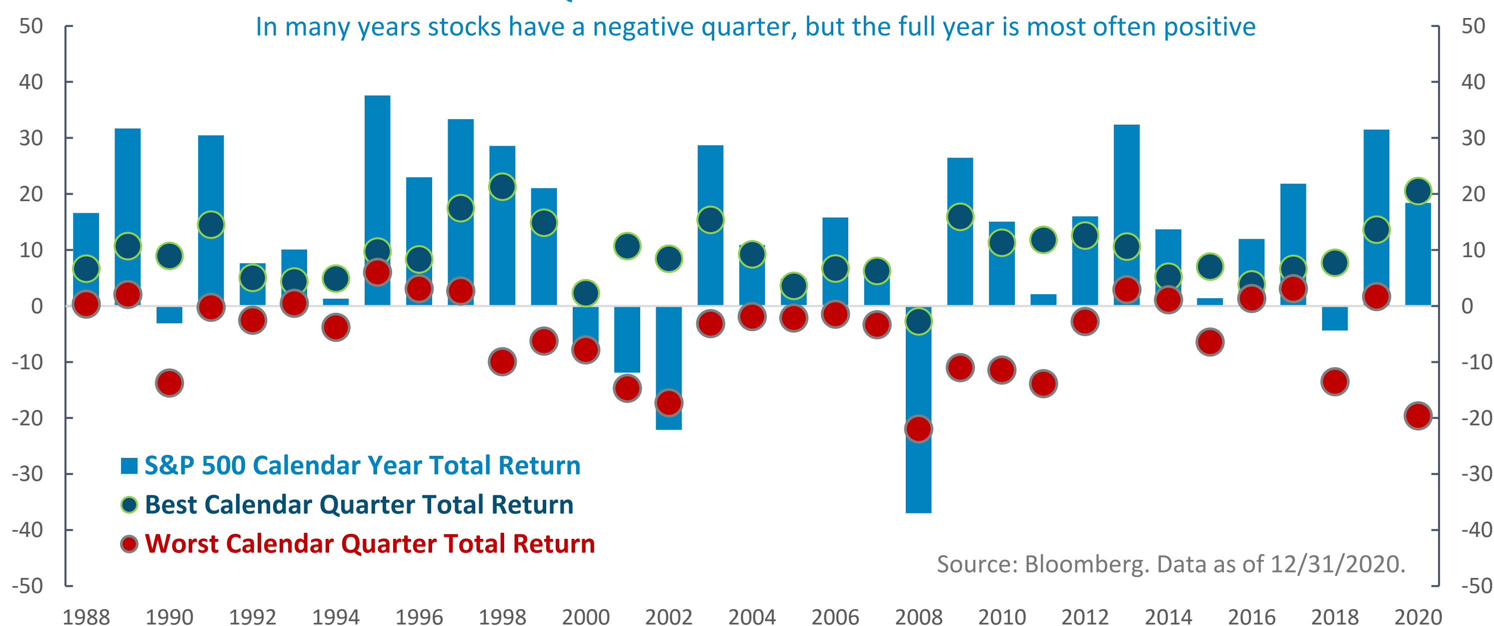
Source: Bloomberg, as of December 31, 2020. Asset-class performance is presented by using total returns for an index proxy that best represents the respective broad asset class. U.S. Bonds (Barclays U.S. Aggregate Bond TR), U.S. High Yield (Barclays U.S. HY 2% Issuer-Capped TR), International Bonds (Barclays Global Aggregate ex USD TR), Large Caps (S&P 500 TR), Small Caps (Russell 2000 TR), Developed Markets (MSCI EAFE NR USD), Emerging Markets (MSCI EM NR USD), Real Estate (FTSE NAREIT All Equity REITS TR).

MONTH IN REVIEW

2020: A year of Pandemic… and of Recovery

December capped a very strong quarter for capital markets, and an unforgettable year overall, with the continuation of a broad, robust rally. Although markets couldn't quite match November's generous returns, most major asset classes were positive again in December, and for the final quarter of 2020. That is a stark contrast to how the year started, when virtually all risk assets had substantial pullbacks as the COVID-19 pandemic spread across the globe and most economies were largely shut down during the first quarter.

was better understood, and mitigation efforts became more widespread, economies opened back up again. Equities stormed back, with the S&P 500 climbing more than +66% from its March 23 low, resulting in the shortest bear market in history. Halting the descent wasn't easy, it required decisive and massive action by the Federal Reserve and other major central banks to shore up the credit markets. It also required decisive and massive fiscal policy from government officials to shore up small businesses and consumers.



In fact, the "that was then, this is now" contrast between the worst quarter (Q1) and best quarter (Q2) in 2020 for the S&P 500 was itself a record – a 40 percentage point difference. As shown in the chart above, in the last 33 years, the -19.6% decline in Q1-2020 was only outdone by the -21.9 drop in Q4-2008. The quarterly period actually masks some of the damage felt in that decline. The sharp collapse in February and March, as Covid-19 spread outside of China and forced countries into lockdowns, was the most rapid -30% drawdown that the S&P 500 has ever suffered. It also marked the end of the longest bull market on record. The fact that the catalyst of the decline was not due directly to financial or economic damage, but rather damage to health, or even death, made it a truly scary and uncertain period. But in the second and third quarters, as the virus' behavior

It wasn't easy for investors along the way. Sure, the S&P 500 made 33 record highs in 2020, but it was anything but a smooth ride. The index was up or down at least 1% in 110 of the year's 253 trading days, compared to just 38 days in 2019. And those 110 daily swings included two rallies of more than +9% and a -12% single-day drop in March. However, in the end the time-tested formula of "diversification + time in the market" rewarded disciplined long-term investors once again.

Bottom Line: 2020 may have been one the most challenging years in our lifetimes. Thanks to decisive and substantial action by fiscal and monetary policymakers, stock and bond markets overcame a global pandemic to end the year near all-time highs. And although the economy still has a ways to go to surpass pre-pandemic levels it is on the right path.

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After a year like 2020, what can we expect in 2021?

According to Chinese zodiac cycles, 2020 was the Year of the Rat, which seems somewhat fitting – at least on a very superficial level. 2021 is The Year of the Ox, which could be argued is very close to a Bull, right? Perhaps that is a good omen for the continuation of the post-lockdown market rally discussed on the prior page? In all seriousness, one of the most frequent questions we hear after big market rallies and a slew of new record highs is "can this continue?" Before tackling that question, we first should acknowledge that the stock market largely got it right in anticipating the earnings and economic recovery that followed the remarkable monetary and fiscal policy responses to the spring COVID outbreak. And in that context it is hard not to remain constructive for at least the next six to twelve months. All indications are that the extremely large monetary and fiscal policy measures carried out in 2020 will likely continue in the months ahead, supporting the economy in 2021. The combination of that backdrop with vaccine progress and the possibility for herd immunity before too long should be conducive for further advances in GDP and earnings growth. JP Morgan expects S&P 500 earnings to reach new record highs in 2021.

The 2020 Year-End Rally Bodes Well For 2021

>10% S&P 500 Index Gains In November And December

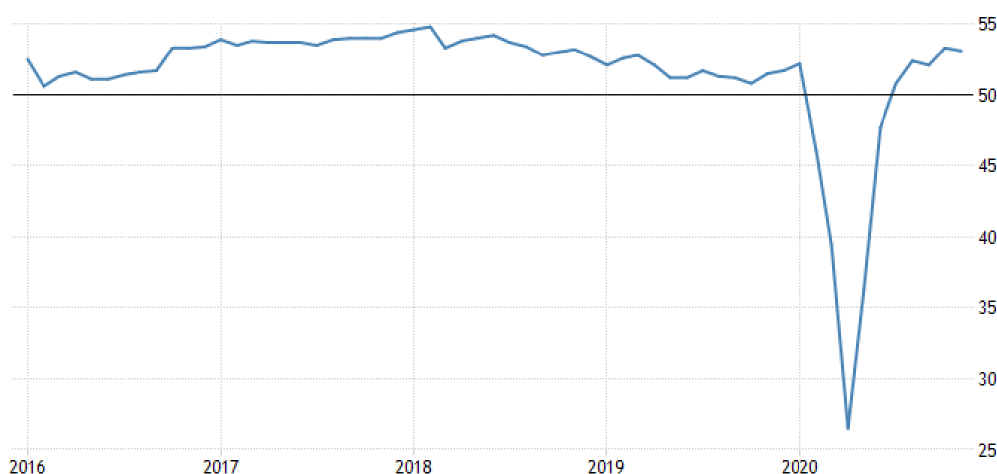
Year	S&P 500 Index Returns		
	November/ December Return	January Return	Following Year Return
1954	13.6%	1.8%	26.4%
1962	11.6%	4.9%	18.9%
1970	10.5%	4.2%	10.8%
1985	11.3%	0.2%	14.6%
1998	11.9%	4.1%	19.5%
2020	**14.3%**	**?**	**?**
	Average	3.0%	18.1%
	% Positive	100%	100%

Source: LPL Research, FactSet.

Furthermore, low rates and low inflation should continue to support asset prices (inflation expectations have jumped recently yet remain well below historical averages). As is often the case, the economic recovery has been led by the U.S., but the world is turning the corner now and most countries are showing improving economic output. For example, as shown below, the JP Morgan Global PMI has bounced back strongly from the pandemic lows and remains near the highest levels in two years. A lower U.S. dollar, higher projected growth rates, and attractive valuations should be tailwinds for international equities in 2021.

JPMorgan Global Composite Purchasing Managers Index (PMI)

Levels above 50 indicate economic expansion



Source: Markit, J.P. Morgan Asset Management, Trading Economics.

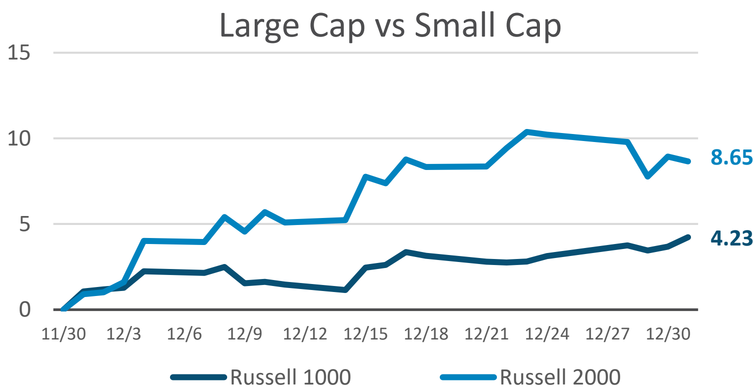
A simple historical look back also shows a favorable outlook for 2021. According to Bespoke Investment Group research, in prior bull markets when the S&P 500 exceeded it previous bull market high, the S&P 500 experienced a median gain of +38% over the subsequent 26 months before topping out. Similarly, in prior bull markets that lasted 200 trading days or more, the S&P 500's median performance over the following year was a gain of +13.4% with positive returns ten out of eleven times. LPL research corroborates the positive outlook. They looked at past instances when the S&P 500 gained +10% or more in the final two months of the year, and the average subsequent year's return for the 5 prior incidences since 1950 was +18.1% with a range of +1.8% to +26.4%. Even from a seasonal perspective, historically the S&P 500 has averaged positive returns in three of the first four months of the year.

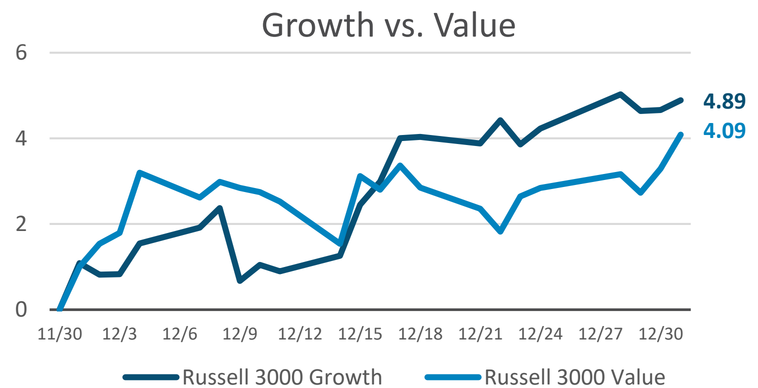
Bottom Line: The potential for vaccines and herd immunity to suppress the virus should increasingly improve in 2021. The Fed and other global central banks are likely to remain accommodative with monetary policy throughout 2021. Fiscal spending should persist, especially under a Democratic administration. All these factors should combine to provide a favorable backdrop for the continuation of the economic recovery and serve as tailwinds for capital markets in 2021.

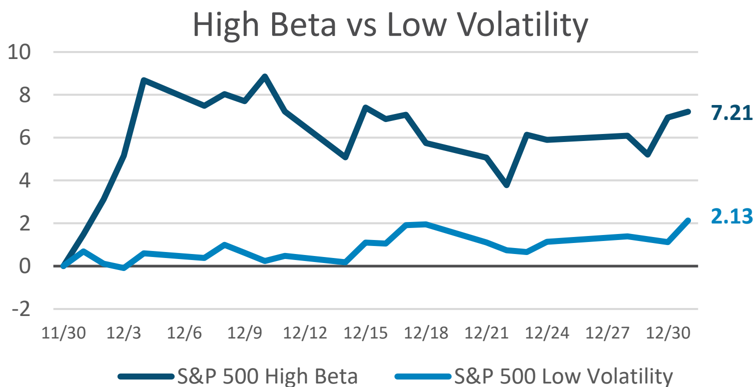
Equity Themes

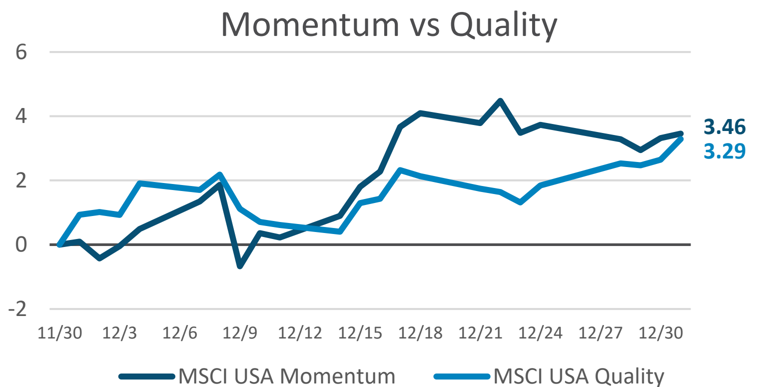
What Worked, What Didn't

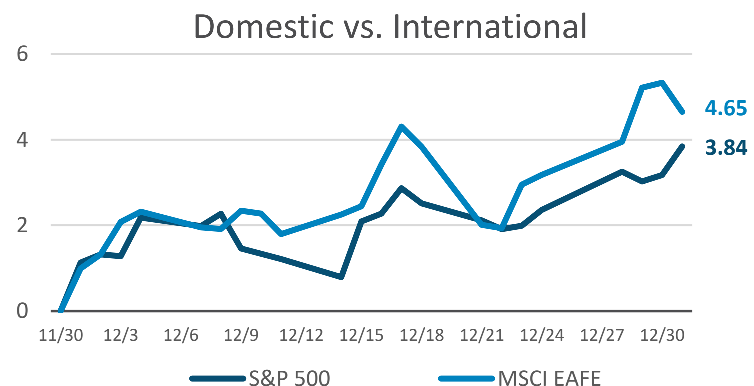
- **David & Goliath, round 3.** For the third straight month **Small Caps** beat **Large Caps**, resulting in their largest quarterly total return in history, +31.4%, as well as their largest quarter of outperformance over Large Caps in history at +17.7%. Despite the impressive showing Small Caps still finished 2020 -1.0% lower than Large Caps.
- **Emerging Markets prevail.** For the third month in a row Emerging Markets were up, giving it a quarterly total return of +19.7%, the best quarter since September 2009. 2020's +18.3% gain nearly matched 2019's +18.4%.
- **High Beta pays again**. Though it was far behind November's blistering +25.9% total return, **High Beta** was up +7.2% in December, its third consecutive positive month and best quarter (+32.1%) since June 2009 (+35.9%).

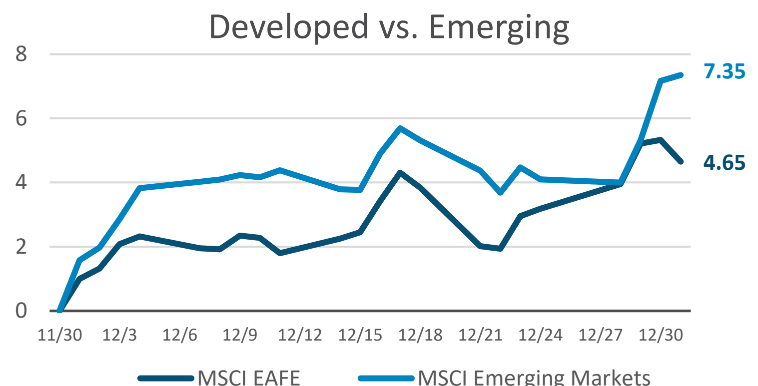












Source: Bloomberg.

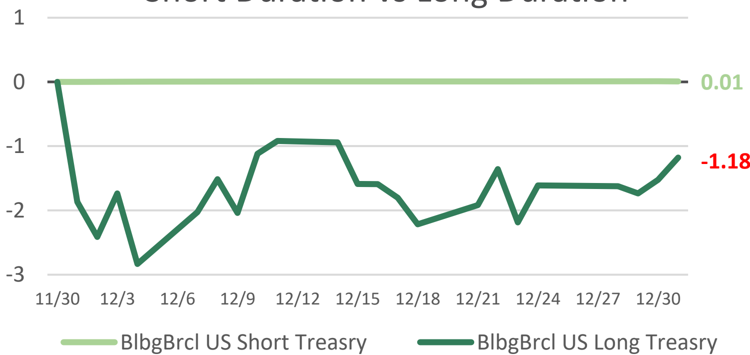
December 2020

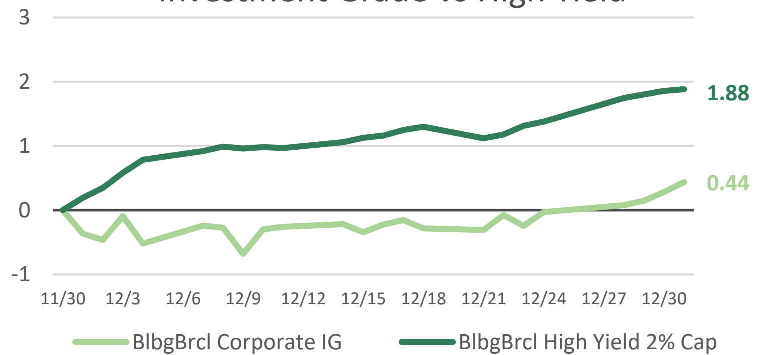
Bond Themes

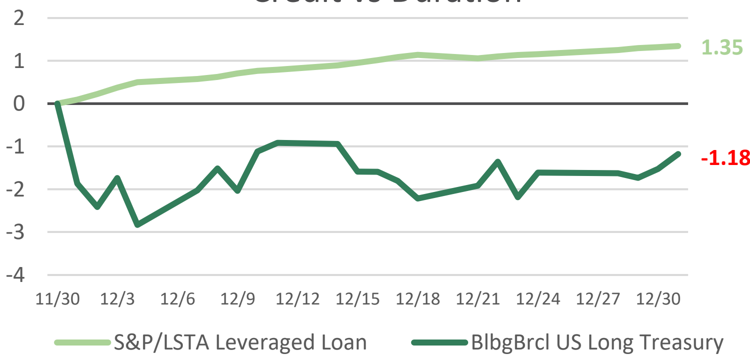
MONTH IN REVIEW

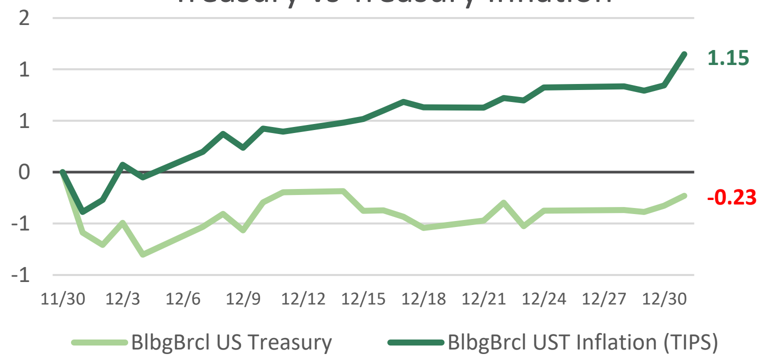
What Worked, What Didn't

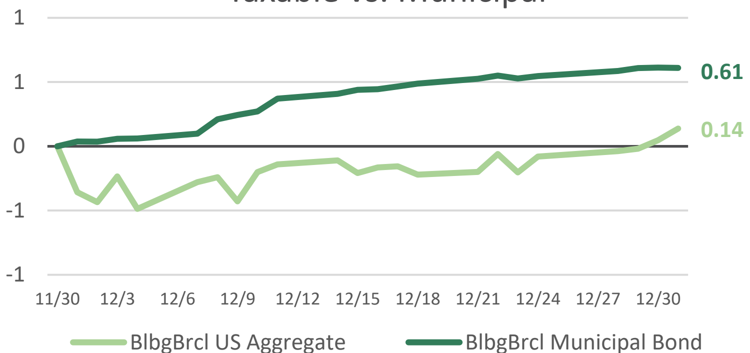
- **Dollar down, non-US Bonds up.** The US dollar has been down 7 of the last 9 months and non-US bonds have outperformed domestic bonds in 7 of the last 9 months, including December's +200 basis point advantage.
- **Risk still on, credit still up.** Credit sectors continue to benefit from the risk on environment and **High Yield** tacked on another +1.9% to November's +4% gain and has outperformed **Investment Grade** the last 3 months.
- **All-Time Lows.** November ended with **High Yield** and **Investment Grade** bonds at record low yields… but they weren't low enough apparently. Yields continued to sink throughout December, and on Dec. 30 High Yield set a new record low of 4.18% while Investment Grade followed on Dec 31 with its own record low of 1.74%.

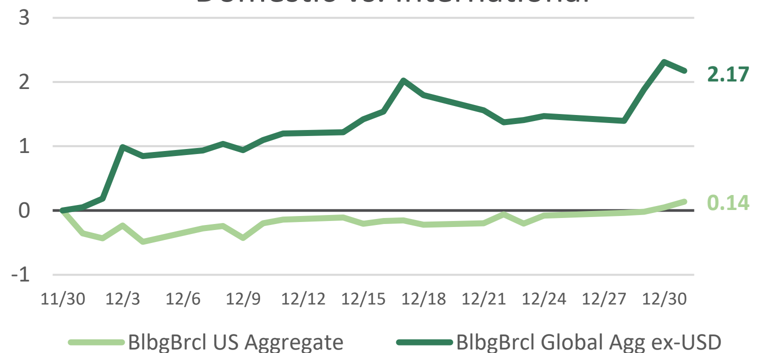












Source: Bloomberg.

December 2020

Asset Class Performance

MONTH IN REVIEW

The Importance of Diversification. From period to period there is no certainty what investment will be the best, or worst, performer. Diversification mitigates the risk of relying on any single investment and offers a host of long-term benefits, such as less portfolio volatility, improved risk-adjusted returns, and more effective compounding.

	Dec-01	Dec-02	Dec-03	Dec-04	Dec-07	Dec-08	Dec-09	Dec-10	Dec-11	Dec-14	Dec-15	Dec-16	Dec-17	Dec-18	Dec-21	Dec-22	Dec-23	Dec-24	Dec-28	Dec-29	Dec-30	Dec-31	Dec
High	IEQ 2.35	SCV 0.74	EM 1.15	SCV 2.79	SCG 0.53	SCG 1.75	IEQ 0.14	SCG 1.51	MCG 0.16	SCG 0.80	SCV 2.79	LCG 0.54	SCG 1.65	MCG 0.56	SCG 0.48	SCG 1.79	SCV 1.62	RE 0.79	RE 0.91	EM 1.49	EM 1.33	RE 1.06	SCG 9.30
	EM 1.97	LCV 0.52	RE 0.75	SCG 1.88	LCG 0.35	SCV 0.99	IBD -0.11	EM 1.29	USB 0.11	LCG 0.32	SCG 2.21	EM 0.48	MCG 1.61	SCG 0.20	USB 0.00	MCG 0.95	IEQ 1.08	LCG 0.47	LCG 0.83	IEQ 0.64	SCV 1.24	LCV 0.77	SCV 7.99
	SCV 1.48	HYB 0.28	MCG 0.74	MCV 1.56	USB 0.15	MCG 0.76	MCV -0.14	MCG 1.08	RE 0.05	MCG 0.30	MCV 1.95	IEQ 0.39	RE 0.98	HYB 0.08	LCG -0.07	RE 0.79	EM 1.02	LCV 0.28	IEQ 0.82	IBD 0.32	SCG 1.13	MCV 0.50	EM 7.13
	MCV 1.15	IBD 0.27	SCG 0.59	RE 1.47	IBD 0.11	LCG 0.37	USB -0.14	SCV 0.46	HYB -0.10	IBD 0.21	RE 1.93	MCG 0.34	LCG 0.93	USB -0.05	MCG -0.09	LCG 0.46	MCV 0.97	HYB 0.21	EM 0.28	60/40 0.03	MCV 1.09	LCG 0.23	IEQ 5.02
	RE 1.14	EM 0.14	SCV 0.56	LCV 1.28	MCG 0.07	IEQ 0.35	HYB -0.15	IBD 0.37	LCG -0.15	IEQ 0.06	LCV 1.51	RE 0.15	IBD 0.90	LCG -0.09	IBD -0.12	SCV 0.32	LCV 0.76	60/40 0.12	60/40 0.26	USB 0.02	IBD 0.54	HYB 0.08	MCG 4.75
	LCG 1.00	MCV 0.07	IBD 0.54	MCG 1.14	EM 0.00	LCV 0.35	SCV -0.16	LCG 0.31	60/40 -0.16	HYB 0.02	MCG 1.17	60/40 0.08	SCV 0.89	EM -0.12	HYB -0.36	USB 0.14	HYB 0.45	USB 0.09	LCV 0.24	HYB -0.13	MCG 0.54	USB 0.08	MCV 4.58
	LCV 0.93	IEQ 0.01	MCV 0.49	EM 1.03	HYB -0.05	60/40 0.22	LCV -0.19	60/40 0.30	LCV -0.20	USB -0.06	LCG 1.16	USB -0.04	IEQ 0.70	IBD -0.13	MCV -0.41	HYB 0.13	60/40 0.32	MCV 0.07	SCV 0.22	LCG -0.21	LCV 0.48	SCV 0.05	LCG 4.45
	60/40 0.84	60/40 -0.01	60/40 0.31	IEQ 0.85	60/40 -0.16	MCV 0.20	60/40 -0.41	USB 0.25	IBD -0.21	60/40 -0.13	EM 1.08	HYB -0.15	MCV 0.70	60/40 -0.26	60/40 -0.46	60/40 0.00	SCG 0.30	MCG 0.05	IBD 0.21	LCV -0.28	RE 0.45	60/40 0.00	LCV 3.73
	IBD 0.79	USB -0.11	LCV 0.21	LCG 0.64	MCV -0.46	IBD 0.08	RE -0.76	HYB 0.18	IEQ -0.30	RE -0.46	IEQ 1.02	SCG -0.16	EM 0.65	LCV -0.44	LCV -0.50	IEQ -0.25	IBD 0.13	IEQ 0.04	HYB 0.13	MCG -0.66	60/40 0.34	EM -0.06	60/40 3.27
	MCG 0.30	LCG -0.25	USB 0.17	60/40 0.60	SCV -0.53	EM 0.04	EM -0.86	IEQ 0.14	SCG -0.34	SCV -0.50	60/40 0.85	MCV -0.23	60/40 0.54	IEQ -0.52	RE -0.64	MCV -0.26	USB -0.07	IBD 0.03	MCV 0.11	MCV -0.78	HYB 0.21	MCG -0.14	IBD 2.69
	SCG 0.30	SCG -0.33	IEQ 0.17	HYB 0.42	LCV -0.56	USB 0.01	SCG -1.33	MCV 0.05	MCV -0.55	EM -0.51	HYB 0.31	LCV -0.27	LCV 0.50	MCV -0.76	SCV -0.71	IBD -0.54	MCG -0.52	SCV 0.00	USB 0.02	RE -0.81	IEQ 0.14	IBD -0.46	RE 2.51
	HYB 0.26	MCG -0.67	HYB 0.06	IBD -0.08	RE -0.78	HYB -0.08	MCG -1.67	LCV -0.11	EM -0.70	MCV -0.79	IBD 0.21	IBD -0.40	HYB 0.15	SCV -1.25	IEQ -1.28	LCV -0.57	LCG -0.65	SCG -0.18	SCG -0.99	SCV -1.68	USB 0.06	SCG -0.48	HYB 1.96
Low	USB -0.32	RE -0.89	LCG 0.00	USB -0.27	IEQ -0.81	RE -0.49	LCG -1.72	RE -0.58	SCV -0.84	LCV -1.00	USB 0.06	SCV -0.63	USB 0.00	RE -1.80	EM -1.47	EM -0.80	RE -0.68	EM -0.44	MCG -1.31	SCG -2.25	LCG -0.07	IEQ -0.76	USB 0.09

Legend

- 60/40 Allocation (60/40)
- Large Growth (LCG)
- Large Value (LCV)
- Mid Growth (MCG)
- Mid Value (MCV)
- Small Growth (SCG)
- Small Value (SCV)
- Intl Equity (IEQ)
- Emg Markets (EM)
- U.S. Bonds (USB)
- High Yield Bond (HYB)
- Intl Bonds (IBD)
- Real Estate (RE)

Source: Bloomberg. Asset-class performance is presented by using market returns from an exchange-traded fund (ETF) proxy that best represents its respective broad asset class. Returns shown are net of fund fees for and do not necessarily represent performance of specific mutual funds and/or exchange-traded funds recommended by the Prime Capital Investment Advisors. The performance of those funds June be substantially different than the performance of the broad asset classes and to proxy ETFs represented here. U.S. Bonds (iShares Core U.S. Aggregate Bond ETF); High-Yield Bond (iShares iBoxx $ High Yield Corporate Bond ETF); Intl Bonds (SPDR® Bloomberg Barclays International Corporate Bond ETF); Large Growth (iShares Russell 1000 Growth ETF); Large Value (iShares Russell 1000 Value ETF); Mid Growth (iShares Russell Mid-Cap Growth ETF); Mid Value (iShares Russell Mid-Cap Value ETF); Small Growth (iShares Russell 2000 Growth ETF); Small Value (iShares Russell 2000 Value ETF); Intl Equity (iShares MSCI EAFE ETF); Emg Markets (iShares MSCI Emerging Markets ETF); and Real Estate (iShares U.S. Real Estate ETF). The return displayed as "Allocation" is a weighted average of the ETF proxies shown as represented by: 30% U.S. Bonds, 5% International Bonds, 5% High Yield Bonds, 10% Large Growth, 10% Large Value, 4% Mid Growth, 4% Mid Value, 2% Small Growth, 2% Small Value, 18% International Stock, 7% Emerging Markets, 3% Real Estate.

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