

# Wealthspire Advisors 2020 Q4 Review

## 2020: Happily in Hindsight

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By the Wealthspire Advisors Investment Team

### In this letter:

- As 2020 ends, the contrast between solid financial markets and the ravages of COVID-19 continued
- Both equity and fixed income markets saw noticeable regime changes during the year
- The classic 60% equity/40% fixed income portfolio just had its best two-year return since 1997-1998

A year-end investment commentary typically talks on performance, valuations, levels of market indices and rates, to name a few common topics. It would be tone deaf of us, however, not to acknowledge upfront the profound impact the COVID-19 pandemic has had on all of us and our families: the headline number of cases, hospitalizations, and deaths; the profound economic pain suffered by many individuals, sectors, and countries. Having a longer history than our country's own, it has been reported that the UK suffered the worst economic contraction in 300 years - that covers a period of many wars, conflict, pandemics, and territories declaring independence. Closer to home, we were proud that many Wealthspire employees responded to the food insecurity faced by many of those in our communities by supporting Feeding America. Even when we get back to some sense of normalcy, all of us are likely changed forever. That said, you, our clients, partner with Wealthspire to help you meet your financial goals, so we recap 2020 and preview what we expect going forward.

The arrival of the pandemic in late Q1 was paradoxically the perfect environment for companies in growth areas, work/play from home growth stocks in particular - think Zoom and Peloton. The surge in subscribers/customers meant companies like these were simply not just surviving during the pandemic but in fact thriving. Thus began the frequently discussed narrative of "Wall Street vs Main Street" and the "K-shaped recovery," where half the people/companies do well and the other half suffers. Separately, larger companies, even those whose business model proved directly exposed to the COVID-19 pandemic largely had continued access to capital from the markets, allowing them to stay solvent through the end of the pandemic. Thus, for most of the first half of the year, larger capital stocks outperformed smaller capital stocks and growth bested value.

While there were many head fakes throughout the back half of 2020 about the "rotation from growth to value", we look back at the end of 2020 and the first half leaders were indeed second half laggards as small cap significantly beat large caps and value and cyclical stocks bested growth. Why? As news of the success of multiple COVID-19 vaccines began to circulate and decreases in death rates due to better knowledge of how best to treat patients, the market was able to look through the next few quarters and envision a country and world largely getting back to normal. Unlike typical recessions where the excesses that caused the economic downturn have to be worked through, with uncertain duration, the "fix" to this recession is largely known, even if challenging: control the pandemic via vaccines, treatments/therapeutics, and herd immunity so people can get back to their normal lives. International stocks, long lagging the performance of US equities, followed a similar pattern: underperforming domestic stocks through Q3 and then outperforming in Q4. Fixed income saw similarly stark regime shifts in 2020, namely high quality, core fixed income significantly outperforming more risky satellite fixed income during the depths of the market meltdown in Q1, followed by three quarters where the latter largely made up the deficit versus core.

It is often said that a professional athlete knows how to slow the game down. The same could be said of successful investors who avoid reacting to every headline and take emotion out of decision making. That proved especially challenging in 2020 given the extremes we witnessed. When markets were falling in Q1 and rallying as quickly in Q2 we did not make any wholesale portfolio changes, we emphasized continued balance between growth and value stocks, and we argued for time tested rebalancing. To put some context around the latter, assume you started the year with a 50/50 stock/FI portfolio. Assume your equity markets were down 35% in March and your fixed income was flat. So your 50 equity was now worth

32.5, your total portfolio 82.5 and your split had become - 40% equity/60% FI vs the desired 50/50. Buying equities and selling fixed income to get back to 50/50 at that point was emotionally tough - buying into anything down 35% is tough. And to be clear we are not patting ourselves on the back because we certainly could not have predicted that the markets would rally back so fast. However, our game plan is to re-balance when portfolios deviate from strategic levels as much as they did early in 2020 as we feel that buying a core asset class down 35% from where you were happy to own three months prior is generally a winning strategy in the long run.

## Looking Ahead

And looking forward? While we are far more interested in the long run returns that drive success of financial plans, those long run returns are a product of shorter-term decisions, market conditions, starting valuations, and decisions of policy makers. Markets also tend to be mean reverting. For that 60% S&P 500/40% Aggregate fixed income representative portfolio, these last two years have been the best performing two years since 1997-1998 and the sixth best over the last 43 years. Not to say that markets cannot continue to perform as well as they have recently, but we would caution you not to expect it. The third-party providers of Capital Market Assumptions (CMAs) that we use to inform our view of future performance are also calling for muted performance in the medium term. JP Morgan is calling for the lowest 10-year future performance of that 60/40 portfolio since their CMAs began in 2004. One silver lining is that most CMA providers are calling for lower returns to only persist for the medium term, say out to ten years, before equity valuations and fixed income interest rates assume to normalize. Thus, for clients with a time frame longer than ten years we may assume better returns over the life of their financial plan. Finally, as 2020 starkly showed us, the markets will undoubtedly confound us in some unexpected ways. Why might these the markets collective view of future performance be too pessimistic? For one, the extensive policy responses to the COVID-19 pandemic, both in the US and globally, and from both a monetary and fiscal standpoint, likely remain in place for years. This should continue to support asset price levels. So hope for better and (financial) plan for lower.

We often close these year-end letters thanking you, our clients, for the trust you place in us. Perhaps more so than any other, year-end 2020 is one where such thanks is most sincere.

## Markets

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total
Higher Return ↑	FIXED INC 1.92	FIXED INC 1.80	FIXED INC -0.59	US SM 14.55	US SM 7.39	EM MKTS 7.51	EM MKTS 8.97	US LC 7.19	MUNI 0.10	US SM 1.81	US SM 16.29	US SM 7.61	US SM 19.99
	MUNI 1.29	MUNI 0.72	MUNI -2.52	US LC 12.82	US LC 4.76	INTL 4.36	US LC 5.64	INTL 4.58	HEDGE EQ 0.02	EM MKTS 1.80	INTL 13.50	EM MKTS 7.39	US LC 18.40
	STOCK/BOND -0.28	STOCK/BOND -4.62	STOCK/BOND -9.64	EM MKTS 9.61	STOCK/BOND 3.80	US SM 2.89	INTL 4.53	US SM 4.53	FIXED INC -0.05	MUNI -0.22	US LC 10.95	INTL 5.62	EM MKTS 18.39
	HEDGE EQ -0.33	HEDGE EQ -3.83	HEDGE EQ -9.58	INTL 8.15	INTL 3.63	HEDGE EQ 2.21	US SM 3.98	STOCK/BOND 3.55	EM MKTS -1.61	FIXED INC -0.45	EM MKTS 9.71	US LC 3.84	STOCK/BOND 11.44
	US LC -0.04	EM MKTS -5.46	US LC -12.35	STOCK/BOND 6.47	REAL ASSET 3.03	STOCK/BOND 2.09	STOCK/BOND 3.59	HEDGE EQ 2.71	STOCK/BOND -1.82	HEDGE EQ -0.54	REAL ASSET 8.84	HEDGE EQ 3.60	INTL 11.12
	REAL ASSET -1.93	REAL ASSET -7.19	INTL -15.11	REAL ASSET 5.43	MUNI 2.60	US LC 1.99	REAL ASSET 3.53	REAL ASSET 2.66	INTL -2.30	REAL ASSET -1.03	STOCK/BOND 7.92	STOCK/BOND 3.14	FIXED INC 7.51
	US SM -2.03	INTL -8.08	EM MKTS -16.19	HEDGE EQ 4.49	HEDGE EQ 1.22	REAL ASSET 1.03	FIXED INC 1.49	EM MKTS 2.00	US SM -2.59	STOCK/BOND -1.39	HEDGE EQ 4.59	REAL ASSET 2.89	HEDGE EQ 4.58
	INTL -2.74	US LC -8.23	REAL ASSET -18.61	FIXED INC 1.78	EM MKTS 0.92	FIXED INC 0.63	MUNI 1.18	MUNI -0.20	REAL ASSET -3.45	INTL -2.22	FIXED INC 0.98	MUNI 0.39	MUNI 4.23
Lower Return ↓	EM MKTS -4.59	US SM -8.39	US SM -21.70	MUNI -0.34	FIXED INC 0.47	MUNI 0.43	HEDGE EQ 0.82	FIXED INC -0.81	US LC -3.80	US LC -2.66	MUNI 0.81	FIXED INC 0.14	REAL ASSET -7.52

### LEGEND

<span style="background-color: #f4a460; padding: 2px;">US LC</span> Domestic Large Cap	<span style="background-color: #c47a3b; padding: 2px;">US SM</span> Domestic Small-Mid Cap	<span style="background-color: #f4d03f; padding: 2px;">INTL</span> International	<span style="background-color: #95a5a6; padding: 2px;">EM MKTS</span> Emerging Markets	<span style="background-color: #95a5a6; padding: 2px;">REAL ASSET</span> Real Assets
<span style="background-color: #2980b9; padding: 2px;">FIXED INC</span> Taxable Fixed Income	<span style="background-color: #d9ead3; padding: 2px;">MUNI</span> Tax-Exempt Fixed Income	<span style="background-color: #2980b9; padding: 2px;">STOCK/BOND</span> 60% Global Stock/40% Muni	<span style="background-color: #95a5a6; padding: 2px;">HEDGE EQ</span> Hedged Equity	

- U.S. Equities continued to rebound in Q4, bringing returns well into double digits. Looking beneath the numbers, technology (+44%) led the way in the U.S. with only three sectors finishing in negative territory (energy, financials, and real estate).
- U.S. small-mid cap markets along with markets overseas rebounded strongly in Q4, to finish 2020 in positive territory. Positive vaccine developments translated into investors rewarding more cyclical businesses, which make up a larger portion of U.S. small-mid cap and international stocks.

- In fixed income, credit markets continued to rebound despite rising defaults, as many borrowers were able to tap the corporate credit markets over the summer and into the fall to extend debt walls. Municipal bond investors benefited from reduced new issuance of tax-exempt bonds (more and more municipalities are issuing taxable bonds) and renewed demand for tax-free income.
- Alternative investments put up reasonable numbers in Q4. Those with significant equity exposure performed well. Strategies with tilts to lesser liquid parts of the fixed income market also rebounded, and many have moved back into positive territory for the year.

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