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Annual Market Insights & A Look Ahead

Never Bet Against America

2020 tested America like few other years in our history. It was as if the perfect storm made landfall and washed across the continent. The Covid pandemic, the shutdown of the economy, a contentious presidential election, fires and hurricanes, and civil disobedience.

Yet, as the economy was near the bottom, investment legend Warren Buffett reiterated, “Never bet against America.” We won’t forget this year and although we were severely challenged, optimism is embedded in our DNA.

Below are various performance numbers for the quarter and the full year of 2020.

Stock Indices	Q4 2020 Return*	Annual Return %*
S&P 500 (large)	+12.15%	+18.40%
S&P 400 (midsize)	+24.37%	+13.66%
Russell 2000 (small)	+31.37%	+19.96%
MSCI EAFE (intl.)	+16.05%	+7.82%
Bond Yields	**12/31/2020 Yield & Yrly. Change**	**Dec. 31, 2019 Yield**
3-month T-bill	0.09% (-1.46%)	1.55%
2-year Treasury	0.13% (-1.45%)	1.58%
10-year Treasury	0.93% (-.99%)	1.92%
30-year Treasury	1.65% (-.74%)	2.39%
Commodities	**12/31/2020 Price & Yrly. Change**	**Year end 2019**
Oil per barrel	$48.52 (-$12.54)	$61.06
Gold per ounce	$1,895.10 (+$372.00)	$1,523.10

*Stock indices include reinvested dividends and are not annualized for the 4th quarter.

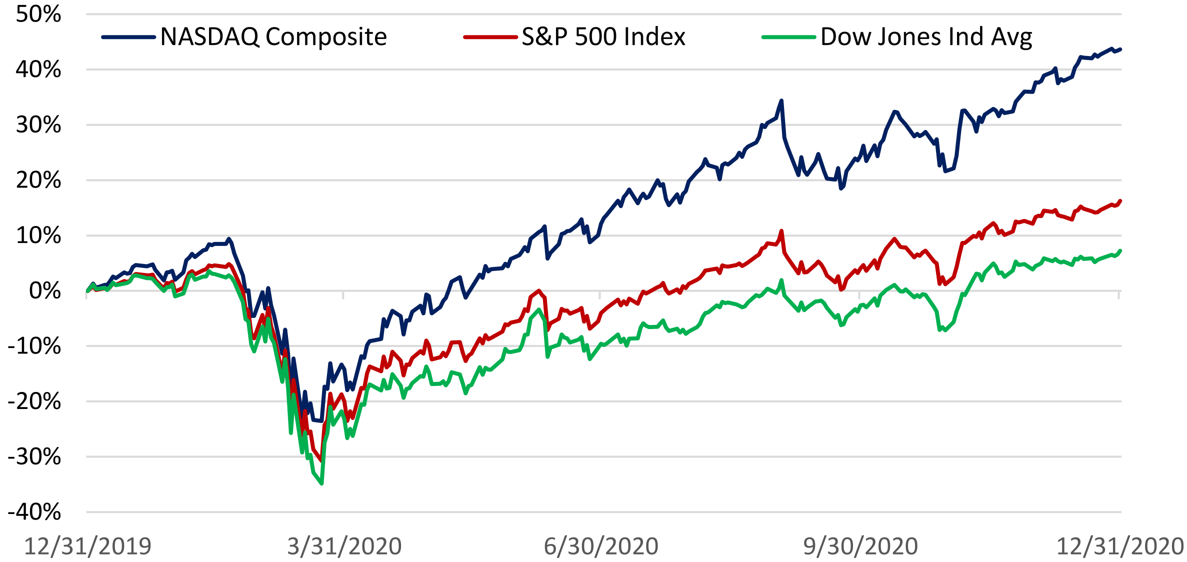
Let’s quickly look at some stats. The shuttering of the economy early in the year led to the steepest quarterly decline in the U.S. economy on record. Economic growth in the following quarter, however, rebounded at the fastest pace on record.

Despite a vicious market selloff in March, stocks recovered and set new highs during the year. “For Many Big Businesses, 2020 Was a Surprisingly Good Year,” so said a December 18th story in the Wall Street Journal. We see this reflected in equity performance for the full year.

Figure 1 highlights the steep selloff in March in the stock market, followed by the subsequent rally.

Key Index Performance Year-to-Date

Fig. 1



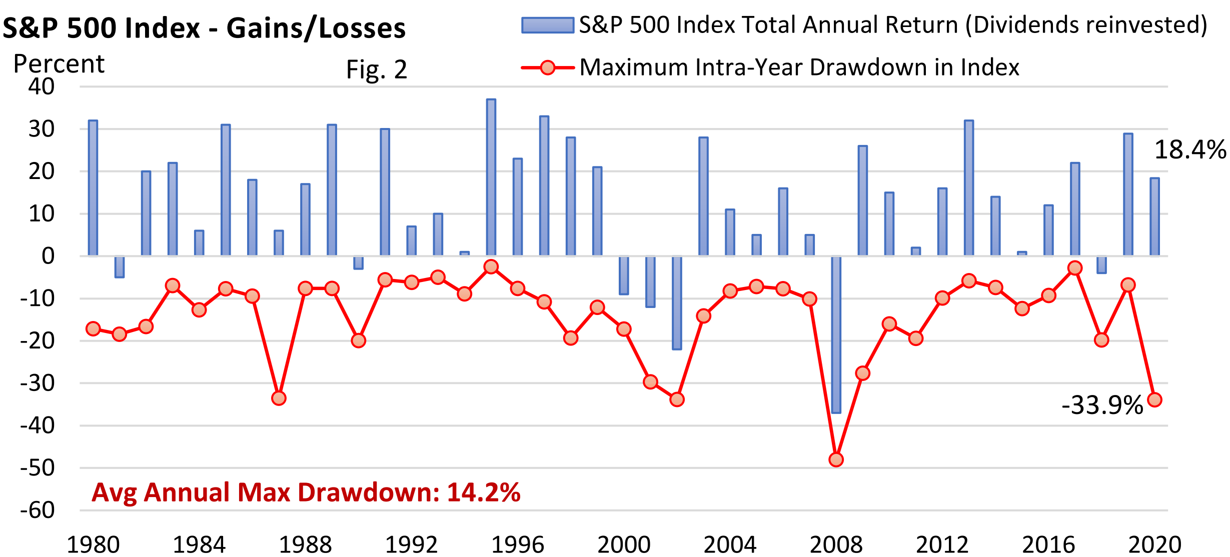
Data Source: Yahoo Finance 12/31/2020
Past performance is no guarantee of future results.
The indexes are unmanaged and cannot be invested into directly.

We counsel that market pullbacks are a natural part of investing, although we acknowledge that the 33.9% peak-to-trough decline in the S&P 500 was hard to stomach since it occurred in only <u>one month</u>.

Yet, let's take a moment to review Figure 2. Figure 2 highlights the annual return for the S&P 500 Index, including dividends, and the maximum pullback during each year since 1980.

S&P 500 Index - Gains/Losses

Fig. 2



Data Source: S&P DJ Indices, LPL Research, St. Louis Federal Reserve, 12/31/2020
Past performance is no guarantee of future results.
The S&P 500 Index is an unmanaged index which cannot be invested into directly.

Since 1980, the average annual intra-year pullback in the S&P 500 has been 14.2%; yet, the S&P 500 has averaged a 13% advance each year (including dividends).

Here are some additional data points. From 1980 to 2020 (41 years), there have been:

- 7 down years, with the average decline during a down year of -13.1%
- 34 up years, with the average increase during an up year of +18.4%

The only time that we have had back-to-back declines was 2000-2002 (stock bubble bursting).

- 21 out of 41 years, we've had pullbacks of 10% or more, or an average of every 1.95 years.
- 6 of the 41 years saw pullbacks of 20% or more, or an average of every 6.83 years.

Figure 2 illustrates the long-term upward bias in stocks. Changes in sentiment can force stocks lower over shorter periods, but favorable economic fundamentals have helped fuel longer-term gains.

A Review

The economic shutdown triggered the first bear market since the 2008 financial crisis. But there were two important catalysts that helped fuel the subsequent rally.

First, the Federal Reserve went far beyond measures announced during 2008 to help the financial markets. Second, Congress passed the $2 trillion CARES Act, which provided generous benefits for the unemployed, while aiding households, and small and larger businesses.

The CARES Act and the Fed couldn't prevent the worst quarterly decline in GDP we have ever experienced, but it helped set the stage for a sharp economic rebound in the third quarter.

Record low interest rates, coupled with economic growth, played a big role in the market's rally.

Still, the pandemic created distortions in behavior. Technology generally performed very well, which is reflected in the outperformance of the tech-heavy Nasdaq.

Autos, home improvement, online retailers, streaming services, housing, and big box retailers deemed to be essential also did very well during the pandemic.

However, oil and gas, mom and pop outfits, and traditional department stores suffered.

The same could be said of businesses that rely on person-to-person interactions, including movie theaters, sporting events, restaurants, concerts, air travel, and hotels.

It has been the tale of two economies.

A Look Ahead

While cautious optimism prevails, the path of the economy is likely to depend on the course of the virus. The likelihood that vaccines will be widely available by June could provide a significant boost to sectors hit hard by social distancing but distribution of the vaccines must accelerate soon.

Just as investors sniffed out the robust Q3 economic recovery, record highs in December suggest we will see further improvement in the economy next year, though expect the recovery to be uneven.

Of course, there are always risks:

- The Fed is unlikely to lift short-term rates in the new year. But could investors be too complacent regarding bond yields, which many believe are expected to remain low in 2021?
- Could inflation unexpectedly rise amid the heavy injections of fiscal stimulus and cash into the economy? And when stocks are priced for perfection, unexpected bad news can create volatility.

Investor's Corner

That said, we can and should acknowledge there are unknowns beyond our control.

Therefore, control what you can control. You can't control the stock market, and timing the market isn't a realistic tool. The one variable you can control, however, is your financial plan.

Among other factors, your plan should consider your time horizon, risk tolerance, and financial goals.

Investors with a long-term time horizon that adhere to a holistic financial plan, which takes multiple economic and market cycles into account, are on the best path to wealth creation and achieving their financial goals.

Final Thoughts

In our never-ending goal of continuing to improve our offering to our clients, we have a new addition to our team: **Michael Sheehan**. Mike is a recent graduate from Randolph-Macon College where he majored in business and started on the football team. He will be assisting us primarily in the investment area with a title of Portfolio Administrator. Please welcome Mike if you have an opportunity.

In addition, we are very pleased to announce that both **Joni Alt, CFP®** and **Herb Hopwood, CFP®, CFA** were both named by ***Washingtonian*** magazine as top financial advisors in the DC Metropolitan area. We feel very honored to have received this recognition and it is very appreciated.

Finally, we want to wish you a Happy and Prosperous New Year!

We are thankful and humbled that you have chosen to work with our firm, and we look forward to working with you in 2021.

Hopwood Financial Services, Inc.