Portfolio Manager Commentary

December 11, 2020

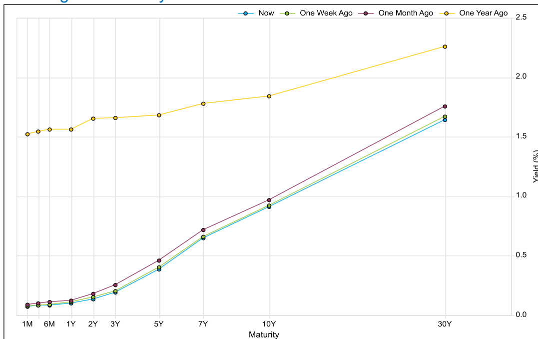
Economic Outlook

Consumer Prices rose by 0.2% in November after having been flat for October. Final Demand Producer Prices rose 0.1% for November after having been up 0.3% in October.

Fixed Income

The Federal Reserve is casting a long shadow over the world's biggest bond market, underscoring how an era of central -bank intervention will reverberate through the markets for some time to come. The Fed's outsized presence in the markets, which began with the 2008 financial crisis and shows no signs of ending, is distorting traditional trading strategies: It's limiting volatility, adding fuel to a record-setting rally in stocks, leaving credit markets priced to perfection, and curbing Treasury yields at levels that no longer fully reflect market sentiment or investor's belief in the economy. Were it not for Fed policymakers frequently affirming that they will do whatever it takes to prop up the economy, along with comments made over the past several months that they are willing to let inflation move above their target of two percent, the ten-year yield would likely have already bounced back above one percent. Perhaps well above it, some traders say. Instead, it has edged lower every time it has come close to that level since March, dragged down by traders worried that the Fed could adjust its bond purchases as soon as this week. Policymakers have said a hard cap on rates remains an option they haven't used previously in their efforts to keep interest rates accommodative for economic growth. "It's hard for a trader to have any conviction, when you are just one announcement away from the Fed crushing your trade," said Patrick Leary, senior trader and chief market strategist for Incapital, a Chicago -based underwriter and distributor of corporate bonds. "You don't want to put it all out there or ride a trade for too long." Higher yields are a double-edged sword for the Fed. On the one hand, they can signal greater confidence in the recovery and policymakers might even welcome them if they are accompanied by rising inflation expectations. But the flip side is that rates that climb too much raise long -term borrowing costs, one of the last things the economy needs with the pandemic raging and millions of Americans still out of work. Speculation is rampant that the central bank will either offer guidance on or adjus t its bond-buying program as early as this week's FOMC meeting. The majority view is that the Fed will ultimately shift its current buying program, which now totals about $80 billion a month, more to longer maturities, if needed, to support economic bright spots such as housing.

Change in Treasury Yield



Current Generic Bonds Yields

Treasuries		Agencies		Corporates		Municipals	
3 mo.	0.06%	3 mo	0.00%	3 mo	0.21%	3 mo	0.22%
6 mo	0.08%	6 mo	0.05%	6 mo	0.22%	6 mo	0.23%
1 yr	0.08%	1 yr	0.01%	1 yr	0.23%	1 yr	0.23%
2 yr	0.12%	2 yr	0.12%	2 yr	0.29%	2 yr	0.25%
5 yr	0.37%	5 yr	0.44%	5 yr	0.71%	5 yr	0.36%
10 yr	0.90%	10 yr	1.15%	10 yr	1.50%	10 yr	0.81%
30 yr	1.63%	30 yr		30 yr	2.52%	30 yr	1.52%

Equity

U.S. Equity finished the week lower as the S&P 500 notched a -1.00% return. Highlights continue to include fiscal discussion and COVID-19 vaccine progress, in which the Fiscal stimulus discussion has reached a stalemate with the liability protections the big sticking point. It is expected that talks could go past Christmas. On the vaccine front, headlines were mixed as the FDA advisory panel recommended the vaccine from Pfizer and BioNTech as expected; however, Sanofi and GlaxoSmithKline have delayed the rollout of their attempt.

Energy (+1.18) was the only sector to finish higher this week as Financials (-1.79%) lagged the most. Growth (-1.09%) underperformed Value (-0.47%), which points to the weekly sectors becoming more of a mixed bag, as Financials can be lumped into more of the va lue group.

Index Returns	Last Week	YTD
Dow Jones Industrials	-0.58%	7.32%
S&P 500 (LCap)	-0.96%	13.39%
S&P 400 (MCap)	-0.22%	8.58%
Russell 2000 (SCap)	1.02%	14.58%
NASDAQ Composite	-0.69%	37.95%
MSCI EAFE (Int'l)	-0.50%	5.18%
iShares Real Estate	-2.54%	-7.97%

Source: FactSet Research Systems

Asset Allocation

Current Sentiment

Cash	Favorable
Short FI	Neutral
Intermediate FI	Neutral
Inflation-Adjusted FI	Neutral
High Yield FI	Unfavorable
International FI	Unfavorable
Equity Income	Neutral
Large Cap Equity	Favorable
Mid Cap Equity	Neutral
Small Cap Equity	Unfavorable
International Equity	Unfavorable
Emerging Markets Equity	Unfavorable
Real Estate	Neutral
Commodities	Unfavorable

Summary below - Current stance on most asset classes:

Cash - Overweighting due to market volatility and uncertainty from Covid-19.

Short Term Bonds - Relative to Intermediate Bonds, the reduced duration is preferable given the oversold long -end of the curve.

Intermediate Term Bonds - The current trading range of intermediate bonds warrants a neutral position with limited upside potential. Some opportunities still remain in certain sectors.

Inflation-Adjusted Bonds - Low inflation expected in near-term providing zero real return.

High Yield Bonds - Spreads are rising given the market turbulence and exposure to unnecessary credit risk when compared to Treasuries would not be advised.

International Bonds - Foreign bonds offer good diversification qualities and higher yield opportunities, however, risks have been elevated recently and investment should be made cautiously.

Equity Income - High quality and higher-dividend-paying companies remain attractive for long-term investors given their favorable risk-adjusted profile and current yield curves.

Large Cap Stocks - A favorable weighting is recommended. Growth continues to be a more favorable style and should continue to be overweighed versus Value.

Mid Cap Stocks - Mid cap exposure remains neutral - more attractive than small caps but not as attractive as large caps.

Small Cap Stocks - In broad market corrections, small cap stocks will suffer most with increased volatility. Underweight until a clearer picture of recovery ensues.

International Stocks - Given most foreign investment is in developed markets and European countries, until sovereign debt concerns are alleviated, a n underweight is recommended.

Emerging Market Stocks - Stronger balance sheets, less debt, and better growth potential make emerging markets more fundamentally attractive than deve loped countries longer-term. However, trade uncertainty and dollar strength provide a headwind for EM in the near term.

Real Estate - Pricing has begun to stabilize and long-term valuations appear attractive. Real Estate should continue to be a strong altern ative to other asset classes.

Commodities - Global demand should support higher prices if the global recovery remains on track. Volatility will be higher, and commodities will be susceptible to short-term price shocks, however, if used in conjunction with other asset classes, risk can be reduced substantially within a diversifie d portfolio. Used alone though is not recommended as the short-term outlook is not favorable.

Sources of statistical information are Bloomberg and Ned Davis Research.
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