Happy New Year!

From everyone here at IMG we hope you enjoyed your Holiday season and your New Year is off to a great start. We are hopeful this New Year will bring us a fresh start in many areas, especially with putting this pandemic behind us and building back our economy. While many individuals and businesses struggled in 2020, we remain optimistic 2021 will bring promise to an improved future.

There are several words that come to mind to describe the year 2020 – exhausting, chaotic, surreal, heart breaking – but then there are others – heroic, inventive, togetherness, hopeful, resilient. It was a wild ride but oddly enough, the market ended the year similarly to how it began, at all-time highs. While there are many times throughout 2020 that we want to forget, investors may find it challenging to forget how the stock market defied expectations.

Before we look ahead, let's take a moment to look back and review the market and economic activities throughout 2020 from our team of experts. For additional in-depth analysis, you may view recordings of our team as they share insights on various local and national media outlets, as well as our weekly *The Markets and the Economy* email series at www.RocklandTrust.com/Wealth&Investments.

Key Takeaways from 2020:

- The S&P 500 had one of its more turbulent years, but showed resilience in its rise to nearly 70% from its March low finishing out the year up over 18%
- Starting in March and throughout 2020, the Federal Reserve responded to the economic impact of the pandemic by implementing programs to support US households and businesses such as quantitative easing and lowering interest rates to near zero
- The FDA issued emergency use authorization for two Covid-19 vaccines expediting the approval and distribution to help combat the coronavirus disease – the path of our economic recovery will continue to be dependent on the widespread availability of these vaccines

US Economy

2020 was a year full of surprises. Just a few of the many shocks experienced throughout the year included the haste at which COVID-19 spread, the unprecedented severity of government lockdowns, and the rapid loss of 22.2 million jobs over the course of three months. This was all followed by the surprising speed and scope of extraordinary monetary and fiscal response from governments across the world and the outcome of the US election. Following a painful 33% decline in the S&P 500 from mid-February into late March, it would have been difficult for anyone to predict that the S&P 500 would then climb 70% from its low to finish the year up over 18%.

During the first half of 2020 annualized real GDP declined 5.0% and 31.4% in Q1 and Q2, respectively, as rising COVID-19 cases resulted in government lockdowns, which essentially shuttered business activity. As the country collectively bent the curve, cases began to fall throughout the spring and summer months. Economies reopened and economic activity resumed albeit unevenly – with goods producing sectors recovering to pre-pandemic highs while close contact service businesses continued to feel the negative effects of social distancing due to the highly contagious virus. Despite these headwinds, the economy rebounded strongly in the third quarter growing 33.4% as manufacturing, housing, and retail sales activity bounced back to their pre-pandemic levels. The recovery continued through year-end with the latest Atlanta Fed GDPNow forecast of economic activity predicting another 8.9% lift in Q4 real GDP. While the recovery has been trending in the right direction, we are starting to see a loss in momentum with the rise in COVID-19 cases during December. CDC data now shows that the moving seven-day average of new cases remains over 200,000 per day. This has resulted in the reinstatement of government restrictions, which continue to disproportionately impact industries such as leisure, travel, entertainment, and restaurants. Recent stimulus payments may help offset some of this pressure, but there is potential for more muted economic growth as we enter the first quarter of 2021.

Corporate Earnings

The steep decline in the economy was mirrored by significant declines in S&P 500 operating earnings. Larger publicly traded companies operating in industries that were deemed essential (e.g. supermarkets, home improvement retailers, e-commerce retailers, and auto parts retailers) showed less volatility in their earnings streams and gained share from smaller retailers who were forced to reduce their hours or shut their doors entirely. In particular, the Technology, Communication Services, Health Care, and Staples sectors were less impacted by the pandemic. Earnings recovered substantially in Q3 and look to have continued that momentum into Q4.

Labor Market

One of the hardest hit areas of our economy this year was employment. Its recovery has been slower and more uneven as compared to other parts of the economy. After losing 22.2 million jobs earlier in the year, through November we have recovered nearly 60% of the jobs lost early in the pandemic and concurrently saw the unemployment rate slide from its 14.7% peak in April, back down to 6.7%. While this number may be understated in the sense that we saw nearly 4 million people leave the workforce altogether, the hope is that we will continue to see this rate move closer towards the 3.5% level we saw pre-COVID as economies return to normal and job growth rebounds.

Despite the loss of employment, consumer balance sheets remained strong as personal income levels were supported by wage gains for those still employed. In addition, pandemic relief measures ranging from one-time stimulus payments to extended unemployment benefits helped to shore up personal finances. Many consumers chose to pay down debt, while others added to their savings safety nets. This drove the US savings rate to 12.9% in November, up from 7.5% a year ago. Elevated savings rates and healthy consumer balance sheets may provide dry powder to fuel a services led burst of economic activity in the second half of 2021.

Vaccine Distribution in 2021

Looking ahead into 2021, our economy's path to normalization is inextricably dependent on the widespread availability of effective vaccines to inoculate our citizens against COVID-19. Continued accommodative monetary policy from the Fed and the potential for additional fiscal stimulus will support current levels of activity and could act as a tailwind to the economy later in the year. To date, we have distributed over 4M vaccinations in the US and plan to distribute tens of millions more doses per month. Assuming that other vaccines are approved, testing continues to improve, immunity improves, and we see the same seasonal decline in infections we experienced last spring and summer, there is optimism for a return to more normal economic and consumer behavioral patterns in the back half of 2021. However, the course of vaccine distribution and case counts will continue to dictate how quickly the full rebound will happen.

Traditional Asset Class Returns Q4 2020

Asset Class	Benchmark	Q4	2020
US Stocks	S&P 500	12.15%	18.40%
US Gov't Bonds	BbgBarc US Govt Intermediate	(0.22%)	5.73%
Cash	BbgBarc US Treasury Bill 1-3 Mon	0.02%	0.54%

US Stocks

The S&P 500 finished the fourth quarter up 12.15%, following a post-US election rally. Effective Phase 3 vaccine trials, the continued development of new vaccines, and the approval and administration of the Moderna and Pfizer-BioNTech vaccines gave investors hope that there is light at the end of the tunnel and that the pandemic could finally draw to an end in 2021. This caused sectors negatively impacted by COVID-19 such as Energy, Financials, and Industrials to significantly rally in the final quarter of the year as the market began to price in a return to normal. Finally, a year-end agreement on additional pandemic relief helped continue to push markets to record highs as we ended the year.

For the year, the S&P 500 finished up 18.40%. This follows a 31.49% return in 2019. Eight out of 11 sectors in the S&P 500 posted positive returns for the year. The Technology sector was the best performing sector in 2020 up 43.89% as earnings remained resilient, while the Energy sector was the worst performing down 33.68% as demand for oil decline due to the pandemic.

Recent news that Democrats won both run-off Senate elections in Georgia, which means Democrats will now have control of the Senate, has created optimism around additional stimulus and fiscal spending. This pushed the US 10-year yield above 1% for the first time since last March, causing interest-rate sensitive industries such as banks, life insurance, and consumer finance companies to rally.

From a market capitalization standpoint, Large and Mid-Cap stocks (Russell 1000 +20.96%) slightly outperformed Small Cap Stocks (Russell 2000 +19.96%) in 2020. From a style perspective, Growth stocks (Russell 3000 Growth +38.26%), or stocks that are expected to grow sales/earnings faster than the market but tend to trade at higher valuation multiples, continued to significantly outperform Value (Russell 3000 Value +2.87%) stocks in 2020.

US Bonds

The Fixed Income markets in 2020 were driven by the Federal Reserve taking considerable measures to help bolster the US economy amidst the coronavirus pandemic. In March, Fed officials held emergency meetings bringing interest rates to zero range, a new round of quantitative easing was implemented and several lending facilities were created to support liquidity within money market funds, corporate and municipal bond markets. Chairman Powell reiterated several times throughout the year the Fed was willing to use its full range of tools available to support US households and businesses.

With an accommodative monetary policy firmly in place, we saw interest rates collapse across the yield curve. The 30-year US Treasury hit a record low in 2020, falling below 1% for the first time in history. The 10-year Treasury also hit an all-time low of .32% in March. Investors became cautiously optimistic with headlines of vaccine arrivals and the passage of a second round of fiscal stimulus in the 4th quarter pushing rates up marginally towards pre-pandemic levels. The 10-year Treasury ended the year at .92% versus 1.92% a year ago. The 30-year Treasury ended the year at 1.65% versus 2.39% a year ago.

US companies, supported by the Federal Reserve's programs, gained access to the corporate debt market at a record pace to bolster liquidity and take advantage of lower borrowing costs. Investors witnessed investment grade credit spreads return to pre-pandemic levels by the end of the year. The Corporate High yield market experienced a significant recovery during the 4th quarter, as well.

As bond yields move inversely to prices, we saw exceptionally strong returns across the fixed income spectrum in 2020. As we look to 2021, US officials have committed to maintaining low rates and continuing the purchase of billions of dollars in bonds as part of their quantitative easing strategy. Ultimately, the US and other global central banks will continue to analyze and assess economies hoping for a vaccine fueled economic recovery.

Diversifying Asset Classes

Many of the equity-related diversifying asset classes helped in Q4, but failed to add value relative to the S&P 500 for the year. The S&P 500 remained among the top performing equity asset classes for the year. Mid Cap Growth (+35.59%) performed well due to its heavy exposure to the Technology sector, and Emerging Market stocks (+18.31%) kept pace with US equity markets due to continued strength in Chinese stocks.

Fixed-income related diversifying asset classes largely helped in Q4, but were a mixed bag relative to Intermediate Government and Corporate bonds for the year. Inflation Protected Bonds (+10.99%) performed well as investors grew concerned about what fiscal stimulus could mean for future inflation. High Yield Corporate bonds, which have heavy exposure to lower credit quality borrowers in the Consumer Discretionary and Energy sectors, rallied back to finish the year up 7.11% as continued low rates, scarcity of yield, and encouraging vaccine news caused investors to flock back to credit.

Asset Class	Benchmark	Q4	2020
Foreign Stocks	MSCI EAFE	16.05%	7.82%
Emerging Markets Stocks	MSCI Emerging Markets	19.70%	18.31%
US Mid Cap Stocks	Russell Mid-Cap	19.91%	17.10%
US Small Cap Stocks	Russell 2000	31.37%	19.96%
REITs	MSCI US REIT	11.52%	(7.57%)
Commodities	Bloomberg Commodity	10.19%	(3.12%)
MLPs	Alerian MLP	32.45%	(28.69%)
Managed Futures	Credit Suisse Mgd Futures Liquid TR	6.56%	1.81%
Foreign Bonds	FTSE WGBI Non-USD	4.82%	10.78%
Emerging Market Bonds	JPM EMBI Global	5.49%	5.88%
US Inflation Protected Bonds	BbgBarc US Treasury TIPS	1.62%	10.99%
Floating Rate Loans	Credit Suisse Leveraged Loan	3.64%	2.78%
US High Yield Bonds	BbgBarc US Corp High Yield	6.45%	7.11%
Convertible Bonds	ICE BofAML Convertible Bonds	19.67%	46.22%

Conclusion

Even though 2020 has ended, some of the struggles we faced have not, and the effects of this global pandemic will continue into 2021 to some degree. We anticipate Covid-19 will continue to impact the market and the economy. As such, we will continue to monitor and report to you the developments effecting your portfolios as always with an eye on protecting your financial future. The course of the pandemic is looking promising, but not without continued hurdles to overcome. Stay safe. Our team is always available to answer any questions and we remain committed to ensuring your investments are appropriately positioned and well-diversified so you can meet your financial goals.

Sincerely,

David B. Smith, CFA
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