2020: A Year of Extremes

After starting the year with the quickest bear market decline in history, the U.S. equity market subsequently recovered to new record highs during the fourth quarter. Concern about the coronavirus pandemic continues, with cases spiking as the U.S. struggles to reopen and the winter season brings colder weather. These spikes in COVID-19 cases and hospitalizations reached new highs in November and continue to increase. Despite the slow reopening of the U.S., consumer spending has not reached pre-pandemic levels, leading many investors to question the progression of economic activity. Typically, investors start to feel confident that the worst has passed when they begin to see earning downtrends turn positive. It appears that third quarter earnings have bottomed, and earnings trends may be on an upswing going into 2021.

This environment has created a wide gap between sectors that have done well despite the circumstances and those that have suffered because of government-mandated lockdowns and fear of the virus. Winners include the technology sector, which represents approximately one-quarter of the S&P 500. Conversely, sectors such as energy and financials fared worse in the downswing until news that the Pfizer-BioNTech vaccine candidate, BNT162b2, has demonstrated evidence of up to 90% effectiveness. This ignited a powerful rotation out of large-cap growth stocks and into smaller-cap stocks and traditional value sectors.

We understand that the challenging combination of circumstances this year heightens investors' uncertainty around what to do with investment portfolios. Risk assets rallied through the summer, but volatility picked up in September and early October. Despite this volatility, the U.S. stock market is surpassing prior highs. The Federal Reserve has continued its support to aid in the recovery by pumping trillions of dollars back into the economy—with talk of another stimulus package that focuses on the distressed labor market, even as headline jobs numbers have improved.

At RMB, we believe this is a good time for investors to evaluate exposures in their portfolios. Our goals in this highly unpredictable environment are to remain diversified and to continue to be incremental, buying what may become relatively cheap and trimming what may become expensive. We continue to look for additional opportunities to selectively increase risk, if/when further stock market pullbacks develop. In the meantime, we continue to focus on dislocations in various niche markets that present attractive risk/reward opportunities.

Earnings

Corporate earnings for the second half of this year continued to decline with the ongoing uncertainty surrounding the pandemic. Even so, earnings are projected to grow in the first quarter of next year.

Valuations

U.S. stock prices remain high. With market growth continuing to reach new highs, stocks do not appear cheap, given that forward 12-month P/E ratios are well above their 5-year and 10-year averages. »

Consumer Confidence

Overall, consumer confidence has risen but remains low and will likely continue to be so until there are more answers surrounding the coronavirus pandemic, such as timing of an available vaccine.

Business Confidence

Business confidence remains low due to the slow reopening in the U.S. and the potential of further shutdowns amid rising case counts. While many restrictions have been lifted, most businesses remain unable to work at full capacity.

Monetary Policy

The Federal Reserve cut rates twice in March, and interest rates remain at nearly zero, continuing to support the economy during the pandemic. The Fed has released a series of sizeable programs to support the functioning of financial markets and the flow of credit, and it plans to continue to do so in the near term.

Fiscal Policy

Fiscal policy is aimed at providing trillions of dollars to support the U.S. economy during this time of economic instability, with talk of more to come. However, with a divided government, the timing of this additional aid is unknown.

Credit Conditions

Corporations and small businesses are more challenged to access new debt or refinance current debt in the current environment. The flow of credit to consumers may also be more limited.

Volatility

In recent months, we have seen an uptick in volatility given the continued uptick in cases of COVID-19 around the world and the unpredictable impact of U.S. general election results. We expect volatility to continue as both stories play out in the new year. ■