



Investment Insights Monthly

From The Desk of Bill Hornbarger, Chief Investment Officer

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Turning of the Tide?

November was a record-breaking month for equities, with the Russell 2000 index of small-cap stocks having its best month on record (+18.4%) and most other segments of the equity market also posting strong gains. The strength was driven in large part by positive news from multiple sources on progress towards a vaccine with high efficacy rates. The potential for a widely available vaccine in the first half of 2021 and the possibility of a return to some type of normalcy from both a social and economic perspective was widely hailed by investors after nine months of various degrees of lockdowns. While some potential green shoots are currently visible, a vaccine would bolster confidence, indicating that the end of the pandemic is in sight.

By any measure, market activity in 2020 has been unique and unpredictable. The markets have experienced a short and sharp bear market, a forced recession, massive stimulus (fiscal and monetary) and subsequent new highs for the S&P 500, which was up 14% through the end of November. That strength in the widely followed U.S. equity market benchmark masks the dispersion in market performance between large- and small-cap stocks as well growth and value styles.

Viewing the market in terms of size and style (large, mid, small, growth, value) since the end of the Global Financial Crisis (GFC) shows a relatively consistent theme of U.S. growth in general and U.S. large-cap growth in particular leading the markets. These companies tend to have some of the strongest balance sheets in the world, which was widely desired by investors after the GFC and also feature some of the most innovative companies in the world. This year has seen the broader trend (large-cap



growth outperforming) accelerate and shine as many are companies that could thrive in the “work from home” environment. Through the middle of November, the Facebook, Alphabet, Apple, Amazon, Netflix, Microsoft group of six stocks had contributed more than 140% of the S&P 500’s return, a very top-heavy year where the rest of the index (490+ stocks) has detracted from the overall index performance. In terms of the growth versus value divergence, through the first 11 months of 2020, large-cap growth has outperformed large-cap value by more than 33%, and a similar spread is visible in small- and mid-cap value and growth stocks.

Buoyed by the vaccine news, previously unloved areas of the market led the way in November. Small cap and value (across the size spectrum) outperformed large cap and growth respectively. The Dow Jones Industrial Average (more representative of the old economy) also fared better than the S&P 500. While one month certainly does not make a trend, these performances were noticeable. They are also an indication that market participants are willing to look beyond the current record-setting COVID-19 cases towards increased economic activity as - and if - the vaccine is effective enough to end the

restrictions on social gatherings in the first half of 2021.

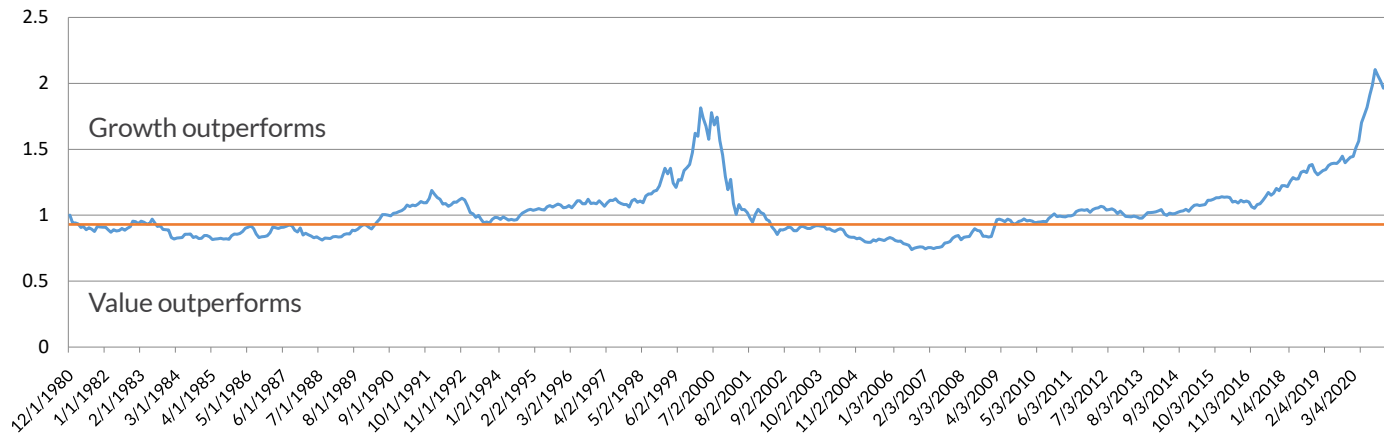
With the news that multiple companies have had some success in creating and testing new vaccines, this rotation could persist and value’s performance (relative to growth) improve. In addition to the “economic” story, there is also a valuation story. By just about any measure, value stocks, particularly small- and mid-cap value stocks, currently trade at more attractive levels relative to growth. In a recently published paper, Research Affiliates suggested the valuation gap is at the most extreme on record. It is also worth pointing out that the value universe currently has a higher dividend yield, a desirable attribute in today’s low yield world.

After several “false positives” and a decade of poor relative performance, many investors have given up on value stocks. We strongly believe that exposure to the value factor is an important part of a well-diversified portfolio (as is exposure to small-cap and international equities). There have been long periods where value has outperformed growth, including 1981 through 2006, where the Russell 1000 Value index outperformed the Russell 1000 Growth index by almost 2% annually.



Russell 1000 Growth Divided by Russell 1000 Value

12/31/1980 = 1



Source: Bloomberg

The financial markets tend to be subject to mean reversion tendencies. There is no easily identifiable pattern or timeframe when this happens, but it is a pattern that has been repeated throughout history. That pattern, coupled with some of the aforementioned factors (valuations, economic recovery), argue that future relative returns for value could be better than what has been experienced over the past decade plus.

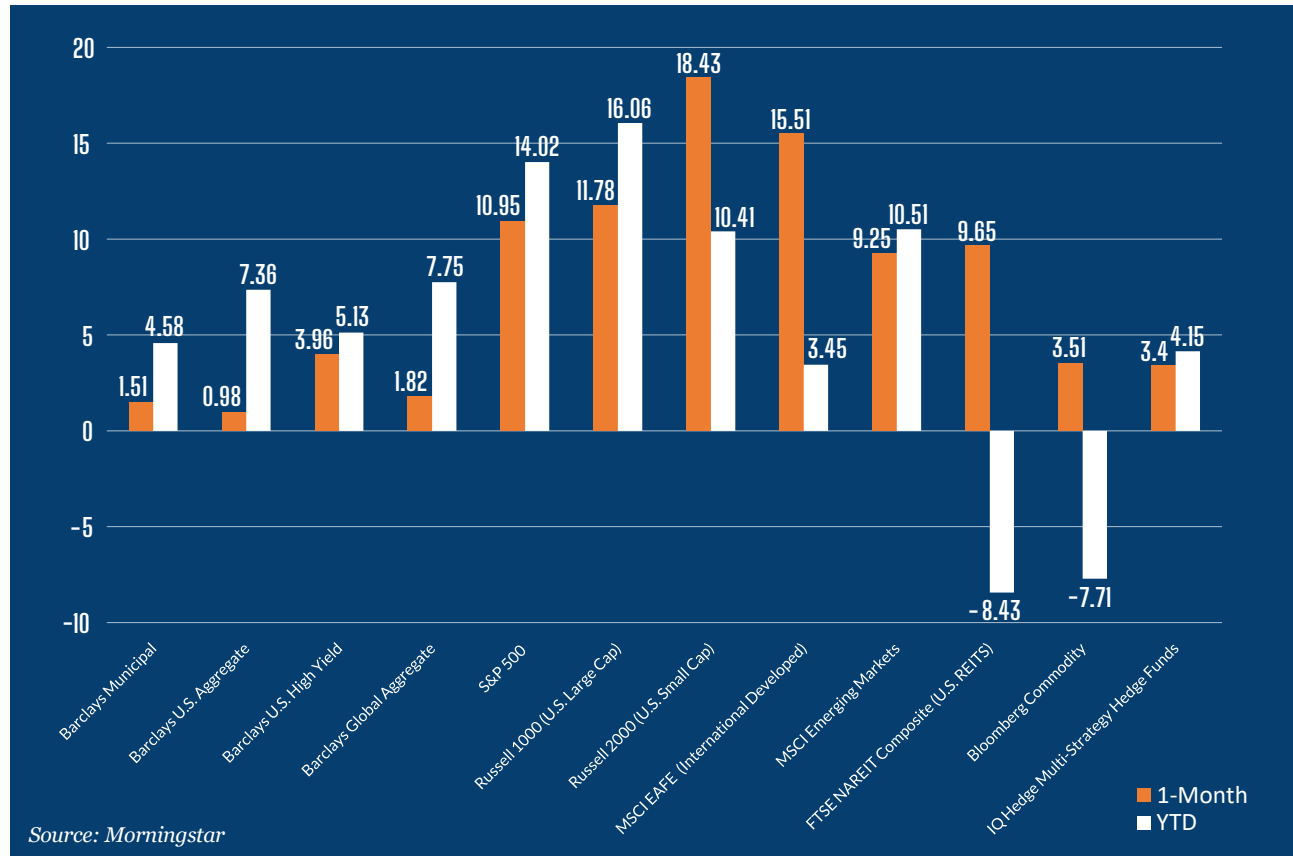


There is an adage about investing that says, “You know you are diversified when you are always unhappy with a portion of your portfolio.” Value has been that part of the portfolio that has left investors unhappy in recent years. Current conditions suggest that this could be coming to an end and value could show the positive attributes of diversification. We would advise strategic allocators to not abandon the value factor just yet.



Asset Class Returns

Comparing Recent Month and Year-to-Date Total Returns



Fixed Income

- Benchmark Treasury yields barely budged point to point. The 10-year note traded in a 25 basis point range and ended the month just two basis points lower than it started.
- Credit outperformed benchmark Treasuries by a wide margin in sympathy with the strong equity markets.

Equities

- Equity markets were generally strong.
- The positive vaccine news has raised hopes that social and economic activity will “normalize” in the first half of 2021.
- The Russell 2000 (small cap) posted its best month ever (+18.4%).
- Value stocks outperformed growth stocks on vaccine news and the ramifications for the economy to reopen fully in 2021.

Real Assets

- Real estate rallied in sympathy with other risk assets on the vaccine news.
- Oil surged on expectations that vaccines will be available in the first half of 2021. Current demand remains subdued and at current rates supply will likely outstrip demand.



November 30, 2020	MTD	QTD	YTD	1 Year	3 Year	5 Year	10 Year
Fixed Income Indices							
Barclays U.S. Treasury Bill 1-3 Month	0.01%	0.02%	0.54%	0.68%	1.55%	1.13%	0.59%
Barclays Municipal	1.51%	1.20%	4.58%	4.89%	4.80%	3.93%	4.36%
Barclays U.S. Aggregate	0.98%	0.53%	7.36%	7.28%	5.45%	4.34%	3.71%
Barclays U.S. High Yield	3.96%	4.48%	5.13%	7.24%	5.68%	7.63%	6.79%
S&P/LSTA Leveraged Loan	2.23%	2.43%	1.76%	3.38%	3.69%	4.73%	4.31%
Barclays Global Aggregate	1.82%	1.92%	7.75%	8.38%	4.50%	4.62%	2.82%
JPM GBI EM Global Diversified	5.49%	5.94%	-0.76%	3.34%	2.52%	5.52%	1.46%
U.S. Equity Indices							
DJ Industrial Average	12.14%	7.08%	6.11%	8.09%	9.37%	13.54%	13.17%
S&P 500	10.95%	8.00%	14.02%	17.46%	13.17%	13.99%	14.19%
NASDAQ Composite (Price)	11.80%	9.23%	35.96%	40.77%	21.07%	19.01%	17.18%
Russell 1000	11.78%	9.08%	16.06%	19.41%	13.66%	14.23%	14.27%
Russell 1000 Growth	10.24%	6.50%	32.40%	36.40%	21.47%	19.56%	17.31%
Russell 1000 Value	13.45%	11.96%	-1.00%	1.72%	5.25%	8.44%	10.93%
Russell Mid Cap	13.82%	14.55%	11.86%	14.43%	10.26%	11.75%	12.65%
Russell 2500	16.29%	18.40%	11.51%	13.86%	8.76%	11.06%	11.97%
Russell 2000	18.43%	20.91%	10.41%	13.59%	7.09%	10.25%	11.13%
Russell 2000 Growth	17.63%	18.53%	23.12%	25.95%	12.83%	13.19%	13.30%
Russell 2000 Value	19.31%	23.57%	-3.05%	0.35%	0.80%	6.83%	8.70%
Non-U.S. Equity Indices							
MSCI World	12.83%	9.40%	11.72%	15.11%	10.11%	11.49%	10.81%
MSCI ACWI	12.36%	9.66%	11.60%	15.58%	9.56%	11.44%	9.99%
MSCI ACWI Ex-U.S.	13.46%	11.04%	5.40%	10.00%	4.31%	7.89%	5.64%
MSCI EAFE	15.51%	10.91%	3.45%	6.83%	3.77%	6.70%	6.35%
MSCI EAFE Growth	12.29%	7.86%	13.15%	16.40%	8.95%	9.70%	8.21%
MSCI EAFE Value	18.95%	14.18%	-6.27%	-2.83%	-1.57%	3.52%	4.35%
MSCI Europe	17.03%	10.45%	1.15%	5.11%	3.11%	5.89%	6.31%
MSCI Japan	12.50%	10.70%	10.33%	12.66%	5.27%	8.23%	7.15%
MSCI AC Asia	9.69%	10.92%	14.61%	20.09%	6.40%	10.52%	6.97%
MSCI EAFE Small Cap	13.75%	9.80%	5.52%	10.14%	3.86%	8.52%	8.70%
MSCI ACWI Ex-U.S. Small Cap	13.85%	10.84%	7.14%	12.46%	3.69%	8.33%	6.63%
MSCI Emerging Markets	9.25%	11.52%	10.51%	18.83%	5.31%	11.13%	3.97%
MSCI EM Asia	7.49%	11.04%	20.23%	28.86%	7.87%	13.09%	6.85%
MSCI China	2.77%	8.21%	26.18%	36.69%	8.92%	14.32%	7.47%
MSCI EM Eastern Europe	22.37%	11.17%	-19.34%	-13.36%	2.96%	9.95%	0.94%
MSCI EM Latin America	21.90%	20.52%	-22.76%	-14.72%	-3.72%	5.94%	-3.64%
Hedge Fund Indices							
IQ Hedge Long/Short	8.06%	5.98%	9.83%	11.00%	5.17%	0.06	--
IQ Hedge Multi-Strategy	3.40%	3.23%	4.15%	6.03%	3.54%	3.63%	3.49%
Real Assets Indices							
FTSE NAREIT Composite	9.65%	6.11%	-8.43%	-7.71%	4.04%	6.39%	9.19%
Alerian MLP	23.78%	29.20%	-30.44%	-24.50%	-12.06%	-7.09%	-2.38%
Bloomberg Commodity	3.51%	4.97%	-7.71%	-3.06%	-3.15%	-0.57%	-6.00%
Other							
Oil Price Brent Crude	27.04%	16.21%	-27.89%	-23.77%	-9.20%	1.30%	-5.82%

Source: Morningstar



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