Capital Market Outlook

"Learn from yesterday, live for today, hope for tomorrow"– Albert Einstein

The election and vaccine were the two themes that drove another strong quarter and a new high for the S&P 500, rising 12.15% in Q4 and 18.4% for 2020. Market leadership saw a marked shift, especially in November, with economically sensitive businesses such as Energy and Industrials leading the market higher. This shift was driven by optimism that a vaccine would eventually lead to a full reopening of the economy and that the new Biden administration would push significant stimulus through Congress. Many large technology companies and "stay-at-home" winners that had led the market through the majority of 2020 experienced less pronounced gains. This strong performance came against the backdrop of spiking Covid-19 cases worldwide, widespread lockdowns and a renewed strain on hospital systems in certain states.

The contentious Presidential election and its aftermath overshadowed much of the financial news during Q4. As the results confirmed Biden the victor, markets rallied as investors had, at the time, invested in the likely prospect of a split-Congress. However, the low-probability scenario in which the Democrats take control of Congress became a reality after the Georgia Senate runoff results arrived, which set the stage for a Democrat-controlled Congress and White House, the first time in a decade.

Both Pfizer and Moderna vaccines were approved by the FDA in November, capping a record development period for a vaccine that normally takes 5 years. Both vaccines are highly efficacious at ~95% and both require two shots 3-4 weeks apart. Although the massive ramp in manufacturing has been hampered somewhat by state and local distribution issues, we believe these are being resolved and the vaccines will go a long way to restoring something that resembles a normal way of life in the back half of 2021. We also expect up to three additional vaccines to be approved in the first half of the year. With some 23 million confirmed cases in the U.S. and many more unconfirmed, we do not need all 330 million Americans to be vaccinated before herd immunity can drive a positive inflection point.

Capital Market Outlook (cont'd.)

Technology stocks had a strong year in 2020 as they were perceived as relative safe-havens during the pandemic, especially companies which helped enable e-commerce and work-from-home. Some of the growth in 2020 was likely a pull-forward of demand from future years, and growth may not achieve similar levels in 2021. The size and dominance of these companies has become more pronounced, which is something regulators may focus on in the coming year as antitrust investigations continue under the Biden administration, adding an additional risk element.

The economic recovery that unfolded throughout Q3 in the U.S. largely continued into Q4, but did so at a much slower rate, with 1.3% GDP growth the slowest in four years. Despite a slight drop in total jobs in December, the labor market continued to improve throughout the quarter, as the most recent employment report showed unemployment at 6.7% vs. 7.8% at the end of Q3. Weekly unemployment claims remain elevated but it's important to consider that hiring has mainly slowed in categories impacted by shutdowns (restaurants, travel, and lodging, etc.) and recent fiscal stimulus provides critical support to the labor market.

Going forward, we see many puts and takes but believe the economy will be substantially better in the second half of 2021 driven by vaccines and the end of lockdowns. The increasing likelihood of direct cash payments to U.S. citizens will likely stimulate consumer spending in the near term and provide a bridge to a more normalized economy once a sizable percentage of the population can be vaccinated. In addition, massive infrastructure spending has the potential to buoy the employment market that has been so impacted by the virus. On the other hand, government spending has also led to higher inflation expectations, which have driven 10-Year Treasury yields over 1% in the early part of 2021. Democrat control of Congress increases the likelihood of higher corporate and personal taxes, which could be a headwind to economic growth. At AMI, we continue to invest for the long-term, owning a balanced portfolio of companies that benefit from current lockdowns and those that should benefit from an economic recovery.

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AMI
ASSET MANAGEMENT

Point of Contact: Matthew Dorband· 424-320-4007 · mdorband@amiassetmanagement.com
10866 Wilshire Blvd, Ste. 770, Los Angeles, CA 90024 · 424-320-4000 · www.amiassetmanagement.com