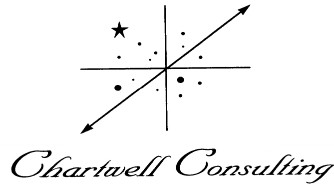

CHARTWELL REVIEW

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2020 will be remembered for many reasons - the COVID-19 pandemic, global lockdowns, end of a 12-year bull market, global recession, high unemployment, and social unrest. As we look back on a year for the record books, we are reminded that non-traditional factors can drive economic outcomes and that swift and sizeable policy responses can be effective in maintaining and restoring orderly markets. Here are the high and lowlights of a unique and unprecedented year:

- ~95% of global economies were placed under lockdown at the pandemic's peak. The US economy still remains at 67% of pre-pandemic levels.
- 92% of global economies fell into a recession in 2020, the greatest synchronized downturn since 1870.
- Coordinated fiscal policy response amounted to \$8.6T across G10 countries (6% of global GDP). Despite this, US interest expense as a percent of GDP remains at a six-decade low.
- The pandemic's "first wave" resulted in 25 million US layoffs and headline unemployment spiked to 14.7%.
- A unique bear market in the US – 1.) the volatility index (VIX) rose to an all-time high of 87, 2.) the S&P500 dropped -34% in 22 days, and 3.) a swift 5-month recovery paved the way for a new bull market cycle.
- The top five companies in the S&P500 represent 22% of US equity market capitalization. These five names rose 49% in 2020, the remainder of the index rose only 9%.
- E-commerce as a share of total US retail sales grew to 16%, increasing as much in 2020 as it did over the past 10 years. Asian countries have seen above 30% penetration.
- US credit spreads spiked to 450bps for investment grade credit and 1100bps for high yield in March. Monetary intervention helped normalize spreads.
- WTI oil futures closed negative for the first time *ever* in April. Conversely, pandemic uncertainty propelled gold price to an all-time high of \$2,064 per troy ounce.

Figure 1: Index Benchmarks

Market Index	Trailing Returns *				
	4Q 20	**1 Yr**	**3 Yr**	**5 Yr**	**10 Yr**
S&P 500	12.2	18.4	14.2	15.2	13.9
U.S. Top-cap Stocks	11.1	22.4	16.0	16.4	14.6
U.S. Mid-cap Stocks	19.9	17.1	11.6	13.4	12.4
U.S. Small-cap Stocks	31.4	20.0	10.3	13.3	11.2
Non-US Stocks (**EAFE**)	16.1	7.8	4.3	7.5	5.5
Non-US Stocks (**Emerg**)	19.7	18.3	6.2	12.8	3.6
3 mo. T-Bills	0.0	0.6	1.6	1.2	0.6
U.S. Aggregate Bonds	0.7	7.5	5.3	4.4	3.8
High Yield Bonds	6.5	6.2	5.9	8.4	6.6
Global Bonds ($Hdgd)	0.9	5.6	5.2	4.5	4.2
Consumer Prices, p.a.	*0.1*	*1.4*	*1.9*	*2.0*	*1.7*
Blmbrg Commodities	10.2	(3.1)	(2.5)	1.0	(6.5)
MSCI World REIT's	8.9	(4.2)	3.9	6.1	7.0
Chartwell 65/35 Global	10.7	8.7	7.6	9.8	7.8

Figure 2: Average Mutual Fund Returns

Fund Category	Trailing Returns *				
	4Q 20	**1 Yr**	**3 Yr**	**5 Yr**	**10 Yr**
U.S. Large-cap	13.2	16.7	12.5	13.8	12.6
U.S. Mid-cap	22.1	13.3	8.5	11.5	10.4
U.S. Small-cap	29.3	12.6	7.0	11.1	10.2
International Lg. Cap	16.3	12.8	5.8	8.7	6.1
International Sm. Cap	18.2	22.7	7.4	11.4	10.0
Emerg. Mkt. Equity	19.6	20.3	6.8	12.4	4.1
Balanced/Hybrid	9.5	12.2	8.0	8.9	7.7
General Bond	2.7	11.0	7.1	7.0	6.4
High Yield Bond	6.0	5.3	5.1	7.0	5.7
Hedge Funds, Equity	14.5	17.5	5.5	6.1	4.2

*Annualized trailing returns for periods ending 12/31/2020

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Economies, Economics, Prices, and Policy

	12.31.20	12.31.19
CPI - headline, y-o-y	1.4%	1.8%
CPI - core, y-o-y	1.6%	2.3%
Unemployment Rate	6.7%	3.6%
Labor Force (millions)	160.1	164.6
Employed (millions)	142.6	152.0
Employment/Population	57.4%	61.0%
Growth in Real GDP, (y-o-y)	(2.8)%	2.3%

At 1.6%, current *core* inflation (ex-food & energy) has dropped from 2.3% on a year-over-year basis. Sharply falling food and energy prices have pushed year-over-year *headline* inflation down to just 1.4%.

The unemployment rate declined to 6.7% at the end of December, down from 7.9% at the end of September. In December, job losses in leisure and hospitality and in private education were partially offset by gains in professional and business services, retail trade, and construction. Nonfarm payrolls decreased by 140,000 in December, and government jobs declined by 45,000.

The Employment/Population ratio rose from 56.6% at the end of September, to 57.4% at the end of December. The labor force rose by 450,000 persons in the quarter, but unemployment fell by 1.8 million. Though the pace of hiring slowed over the period versus the prior quarter, there remained an additional 5 million unemployed persons versus year-end 2019.

Figure 3: Breaking Down 3rd Quarter* Real GDP

% Change from Preceding Period *(seasonally adjusted at annualized rates)*				
Factor	3Q '20	2Q '20	1Q '20	4Q '19
Real GDP Growth	33.4%	(31.4)%	(5.0)%	2.1%
Nominal GDP Growth	38.3	(32.8)	(3.4)	3.5
Real Final Sales	43.7	(33.1)	(4.6)	2.7
Personal Spending	41.0	(33.2)	(6.9)	1.6
Private Investment	86.3	(46.6)	(9.0)	(3.7)
- Fixed, Businesses	22.9	(27.2)	(6.7)	(0.3)
- Fixed, Residential	63.0	(35.6)	19.0	5.8
*- Chg. In Inventories **($bn)***	*($1)*	*($298)*	*($52)*	*$3*
Export growth	59.6	(64.4)	(9.5)	3.4
Import growth	93.1	(54.1)	(15.0)	(7.5)
Government Spending	(4.8)	2.5	13	2.4

** BEA final estimate on Dec. 22, 2020*

Third quarter GDP rose 33% on a qtr/qtr basis, confirming a rebound from a sharp, but short-lived, recession. Data continues to bounce back off April and May's historic lows, with the Institute of Supply Management's services index for December registering a favorable 57.2%. Growth has been indicated for 123 of the last 128 months.

Relief spending thus far has ballooned the U.S. budget deficit. The Congressional Budget Office expects federal debt held by the public to equal over 100% of GDP by the end of FY2021. At the end of 2020, that figure was 98%.

The budget deficit was $572 billion for the first fiscal quarter of 2021 - $215 billion more than the deficit recorded during the same period last year, according to the CBO's estimates. Revenue collections were largely the same, but outlays were 18% higher than during the same period in fiscal year 2020. Unemployment compensation accounted for nearly 40% of the rise in outlays.

U.S. lawmakers, who had moved quickly in March and April to approve nearly $3 trillion in relief, continued negotiating the next stimulus bill into late December, when then-president Donald Trump signed off on a $900 billion coronavirus relief bill.

The Atlanta Fed's GDP model estimate for real GDP growth (seasonally adjusted annual rate) in the 4th quarter is **+7.5%** as of January 21st. This forecast was marked down from 8.7% earlier in the month.

For the year, the Fed's operations were one of the most successful parts of the US government's response to the pandemic. When COVID-19 first began to spread in the United States, there was a significant chance that a financial market meltdown would intensify the country's economic problems. The Fed's actions kept financial markets liquid and operating, preventing that additional level of pain.

Per the minutes of the FOMC's December meeting, the Board of Governors voted to maintain the federal funds rate target of 0-0.25%. Also during the meeting, the Committee agreed to increase the Fed's SOMA holdings of Treasuries by a minimum of $80bn per month and agency MBS by at least $40bn per month. Similar to prior meetings, the Committee indicated that they intend to allow inflation to run moderately over 2% in order to achieve their 2% target in the long-term. To reach this desired outcome, the Fed will have to maintain their accommodative stance of a low-to-zero federal funds rate until inflation exceeds 2% for some time and labor markets reach maximum employment.

Consumer spending was strong over the past quarter, due in part to greater savings by individuals early in the pandemic, when even the unemployed were saving more than usual thanks to an additional $600 supplement to the standard benefits which expired in July. Meanwhile, the housing sector outperformed the broader economy as work-from-home, low mortgage rates, and rising home equity lifted homebuilder confidence to higher levels than before COVID.

The promise of a vaccine raises the question of how consumers will behave once the coronavirus is no longer a threat. It is possible that consumers will remain wary for some time. If so, households will maintain higher levels of savings, and consumer services spending will recover at a slower pace.

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Bonds – Rates Rise, Spreads Fall

Global risk momentum continued through the quarter, despite a number of short-term headwinds brought on by a surge in virus cases and revived lockdowns. Still, risk assets in fixed income posted outperformed for the quarter, drawing optimism from vaccine approvals and clarity on the US election results.

In late December, a $900 billion stimulus package was signed, sending immediate aid to individuals and businesses, providing a substantial boost to risk sentiment. US investment grade credit spreads further tightened from 128bps to 92bps, outperforming like-duration Treasuries by 3.8%. The rate of compression in US credit spreads was on pace with the prior quarter, representing lower levels of risk premia encouraged by continued fiscal and monetary support.

Central banks remained accommodative via near-zero policy rates, but there was interest rate volatility toward the far end of the curve. The US 10-year Treasury yield rose, ending the quarter at 0.91% and the 30-year at 1.65% - up 22 and 19bps, respectively.

Per Figures 5 and 6, developed market yield moves were broadly mixed over the quarter, but remained anchored at lower levels amid ongoing support from central banks. The US Treasury curve steepened by 22bps in the quarter, as the 30-year yield rose 20bps and the 3-month yield fell 2bps. At 0.91%, the US 10-year is 1.00% lower than it was year ago. The Fed's accommodative posture has taken 3-month to 2-year rates down even further, by 1.5% y-o-y. The yields on German and Swiss government bonds fell further into negative territory while those of British government bonds rose.

TIPS exhibited a positive return for the quarter, rising 1.6% as the November core PCE print came out 1.4% higher year-over-year. Though still short of the Fed's historical average 2% target, the monthly data points provided some momentum to the market. The 10-year breakeven inflation rate rose from 1.63% to 1.99% over the quarter.

Agency mortgage-backed securities (MBS) returned 0.59%, outperforming like-duration Treasuries. The sector continued to recover as volatility subsided and steady Fed purchases supported the market. Non-Agency MBS spreads tightened further and commercial MBS returned 1.40%

High Yield credit spreads continued to tighten meaningfully during the quarter (down 150 bps) to end the quarter at 386 bps. This represents a full retracement into pre-pandemic levels of spread over like-duration treasuries, though dislocations are still present across sectors and credit ratings. Within high yield, the lower-rated CCC bonds outperformed higher-rated credits during the quarter. Though yields continue to grind lower, these bonds remain some of the most sensitive to negative macro headlines and equity market volatility.

Figure 4: Primary Bond Sector Returns (%)

Index	4Q '20	1 Yr	3 Yrs	5 Yrs
US Aggregate Bond index	0.7	7.5	5.3	4.4
US Gov't/Credit: (1-3yrs)	0.2	3.3	3.0	2.2
US Treasury: Long	(3.0)	17.7	9.9	7.9
US TIPS (1-10yrs)	1.6	8.4	4.9	4.1
Mortgage-Backed (MBS)	0.2	3.9	3.7	3.1
Commercial MBS	1.3	7.6	5.6	4.8
Asset-Backed (ABS)	0.4	4.5	3.6	2.9
Inv. Grade US Credit	2.8	9.4	6.8	6.4
Leveraged Loans	2.9	(2.0)	2.3	3.6
US High Yield Credit	6.5	6.2	5.9	8.4
Municipal Bonds, broad	1.8	5.2	4.6	3.9
Global Agg., ($ hdgd)	0.9	5.6	5.2	4.5
Global Credit, ($ hdgd)	2.5	7.8	6.3	6.0
Emerg. Mkts Bonds (US$)	5.8	5.3	5.1	7.1

Figure 5: Fixed Income Yields – 4th Quarter 2020

(YTM, % p.a.)	Dec-20	Sep-20	Jun-20	Dec-19	*1-Year Change*
US Treasuries					
3-month	0.08	0.10	0.14	1.55	*(1.47)*
2-year	0.12	0.13	0.15	1.56	*(1.44)*
5-year	0.36	0.27	0.29	1.68	*(1.32)*
10-year	0.91	0.68	0.65	1.91	*(1.00)*
30-year	1.65	1.45	1.41	2.38	*(0.73)*
BarCap Aggregate	1.14	1.19	1.27	2.31	*(1.17)*
BBB Credit	2.1	2.47	2.59	3.17	*(1.07)*
AA Credit	1.37	1.44	1.52	2.35	*(0.98)*
Agency MBS	0.98	1.29	1.36	2.54	*(1.56)*
US High Yield	4.18	5.77	6.85	5.19	*(1.01)*
UST 10yr - 3Mo	0.83	0.58	0.51	0.36	*0.47*

Figure 6: Sovereign Bond Yields, selected countries

10-year yields (%)	Dec-20	Sep-20	Jun-20	Dec-19	*1-Year Change*	*1-Year Currency Change*
Germany	(0.6)	(0.5)	(0.4)	(0.2)	*(0.3)*	*9.8*
Switzerland	(0.5)	(0.5)	(0.4)	(0.5)	*(0.1)*	*10.1*
Japan	(0.0)	0.0	0.0	0.0	*(0.1)*	*5.8*
Britain	0.40	0.28	0.22	0.81	*(0.3)*	*2.7*
Spain	0.10	0.28	0.48	0.44	*(0.3)*	*9.8*
United States	0.9	0.7	0.7	1.9	*(1.0)*	*nil*
Italy	0.5	0.9	1.4	1.4	*(0.8)*	*9.8*
Australia	1.0	0.9	0.9	1.4	*(0.4)*	*9.2*
Greece (new bonds)	0.6	1.1	1.3	1.5	*(0.9)*	*9.8*
Poland	1.3	1.4	1.4	2.1	*(0.8)*	*3.0*
Brazil	2.2	2.6	2.1	4.6	*(2.4)*	*(21.8)*
China (5 year)	3.0	3.0	2.6	2.8	*0.1*	*7.2*
India	5.9	6.0	5.9	6.5	*(0.6)*	*(2.8)*
Russia	6.2	6.5	5.9	6.4	*(0.2)*	*(15.9)*

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US Stocks – A Year for the Record Books

Despite a "second wave" surge in COVID-19 cases, US equity markets soared in Q4 as multiple vaccines were approved. Congress also passed a $900B coronavirus relief and stimulus bill to help offset some of the pandemic's economic impact. Major market indices advanced to record levels. Small cap stocks posted their best quarter *ever*, lifting the Russell 2000 index 31%. For the year, the S&P500 advanced 18.4%, midcaps gained 17.1% and small caps erased three quarters of negative lagging performance and closed the year up 20%.

Small cap stocks began outpacing their larger cap counterparts in September, and that continued through Q4. The performance differential between the Russell 1000 and 2000 in Q4 was 17.7%, and 11.5% versus the Russell Midcap index. The value style also began outpacing growth in September across all capitalization ranges. But for the year, growth stocks dominated value (Figure 7, below). The gap between top performing large growth and the weakest segment, large value, was 35.7%. For *growth* stocks, large-caps have outperformed small-caps over trailing 1-, 3-, 5-, and 10-year periods at a differential we have not seen in the 25 years we have been writing this review. For *value* stocks, the trailing 5-year returns round to 9.7% across all capitalization ranges.

Whether the growth style will continue to outperform next year may depend on the returns from a very narrow range of companies. The largest five stocks in the S&P 500 Growth index composed 40% of the total index by weight (highest annual reading ever). By contrast, the S&P 500 Value index has seen a decrease in the combined weight of its five largest positions in recent years.

Figure 7: U.S. Equity Market - Size/Style Returns

		Trailing			
	4Q '20	**1-year**	**3-yrs**	**5-yrs**	**10-yrs**
Growth					
Large Cap	11.4	38.5	23.0	21.0	17.2
Mid Cap	19.0	35.6	20.5	18.7	15.0
Small Cap	29.6	34.6	16.2	16.4	13.5
Value					
Large Cap	16.3	2.8	6.1	9.7	10.5
Mid Cap	20.4	5.0	5.4	9.7	10.5
Small Cap	33.4	4.6	3.7	9.7	8.9

Despite the strong finish for the value in 2020, six of the seven value risk factors posted negative returns for the year, led by High Dividend (-11.6%), Low Volatility High Dividend (-9.7%) and Enhanced Value (-10.2%) and Low Volatility High Dividend (-9.7%). The top performing risk factors in 2020 were Growth (33.5%), Pure Growth (29.7%) and Momentum (28.3%).

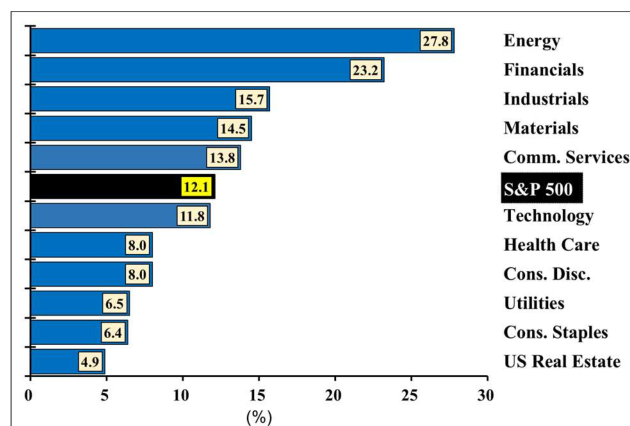
While the most dominant feature of the US equity market returns in 2020 was the dramatic COVID-linked selloff and swift recovery to new all-time-highs by August, this was a year of *two reversals*. Recent years have seen a strong trend against the original "Fama-French" factors of value, market beta and smaller size. In Q4, as well as during the strongest phase of the Q2 recovery, all three of these multi-year trends started to turn. Given the length and strength of the growth "regime" it is too early to say with confidence that the market factors dynamics have changed.

All eleven sectors of the S&P 500 posted positive returns in Q4, with five outpacing the broad index return. Top performing sectors were those that had suffered the biggest losses earlier in the year -

- **Energy** – energy gained 28% on hopes that a successful vaccine rollout leads to a resumption of travel and greater demand for oil. WTI crude prices rose from $40.22/bbl at the end of Q3 to $48.52;
- **Financials –** rose 23% after the Federal Reserve announced it would allow the largest banks to resume share buybacks;
- **Industrials & Materials –** rose 16% and 14%, on expectations for a economic rebound in 2021.

As cyclical sectors advanced in Q4, lagging sectors were the more traditionally defensive – real estate, consumer staples, health care.

Figure 8: US Sector Returns –4th Quarter 2020



In this challenging economic environment, companies have fallen into two groups: businesses with net revenues that are less impacted by the pandemic (COVID defensive) and those that have been hit hard by the global shutdown of economies (COVID cyclical). Approximately 70% of the S&P 500 is represented by COVID defensive businesses, which are dominated by big box retailers, work-from-home solutions, food takeout and anything virtual or streaming. The COVID cyclical sectors are 30% of the index and include travel and leisure businesses, airlines and hotels, banks, much of the service economy and most of Main Street America.

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International Markets Finish 2020 Strong

Global stocks finished 2020 strong, despite COVID-related spikes and new lockdown restrictions in some countries. Developed markets advanced 16.1% in Q4; yet even with that gain the full year return of 7.8% lagged the double-digit advances of emerging and US equity markets. Emerging markets posted their strongest quarterly gain in more than a decade (19.7%) and caught up with US equity markets for the year (18.3%). In Q4, the value style outpaced growth in developed and emerging markets and across all capitalization ranges. In currency markets, the US$ continued to weaken versus most developed and emerging markets. By sector, energy and financials led, as investors moved into sectors that suffered the largest losses earlier in 2020. Industrials and materials also rose sharply amid expectations of a robust economic rebound in 2021. As cyclical sectors took the lead, consumer staples and health care stocks lagged the broad market.

Developed markets (MSCI EAFE) rose 16.1% in Q4, its best quarterly gain since 2010. Within developed markets, Europe (15.6%) rose as COVID-19 vaccines became available and a Brexit trade deal was hammered out with the European Union. Gains were tempered by rising infection rates that prompted a new round of lockdowns in some European cities. Economically sensitive stocks posted the largest gains, highlighted by a 26% rise in the previously hard-hit energy sector. BP, Royal Dutch Shell and Total experienced double-digit gains as global oil demand slowly recovered. Financial stocks also rallied, led by HSBC, Banco Santander and Allianz. The euro rose 4% versus the US dollar.

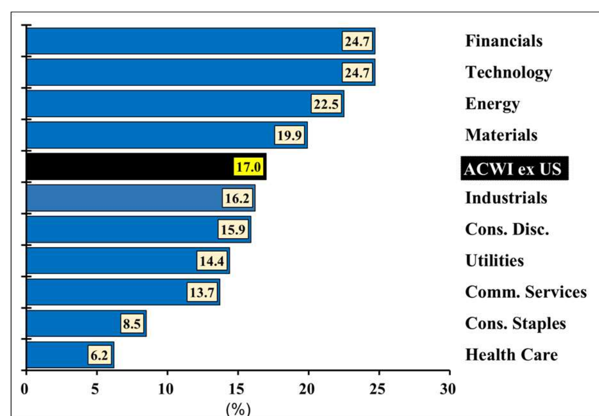
Figure 9: International Equity Markets – Returns

	U.S. Dollar Returns (%)		Local Currency Returns (%)	
thru 12/31/20	4Q '20	1-Yr	4Q '20	1-Yr
World ex-USA	**15.9**	**7.6**	**11.1**	**1.1**
- MSCI Growth	*12.6*	*18.4*	*8.1*	*11.1*
- MSCI Value	*19.3*	*(3.2)*	*14.3*	*(8.9)*
- Europe	15.6	5.4	10.3	(2.2)
- Pacific, ex-Japan	20.1	6.6	14.3	0.3
- Japan	15.3	14.5	12.8	8.8
- United Kingdom	16.9	(10.5)	10.6	(13.2)
Int'l Small Caps	**17.6**	**12.8**	**12.3**	**6.0**
Emerging Mkts	**19.7**	**18.3**	**16.0**	**19.1**
- EM Asia	*18.9*	*28.4*	*16.2*	*25.5*
- EM Europe	*22.5*	*(12.5)*	*16.9*	*(1.4)*
- EM Lat Amer	*34.8*	*(13.8)*	*23.9*	*2.3*
- EM BRIC	*15.3*	*17.7*	*13.6*	*21.5*

The Pacific region rose 16.7% during the quarter. Japan, the largest economy in the region (15.3%), rose as economic expansion offset weaker exports. GDP rose an annualized 22.9% in Q3 from the prior quarter, the first expansion in a year. Exports fell 4.2% in November, the 24th consecutive month of year-over-year declines. Sectors which rose most were materials, technology and consumer discretionary. The Japanese yen rose 2% versus the US dollar.

Australia (+22.9%) was the top performer in the region. Ending their first recession in nearly 30 years, its economy expanded 3.3% in Q3. Hong Kong's (+15.5%) economy showed signs of stabilizing, with the IHS Markit Hong Kong PMI rising to 50.1 in November, the highest reading in three years. Retail sales posted the smallest decline (-4%) since mid-2019. New Zealand (+13%) advanced as Prime Minister Jacinda Ardern was elected to a second term. Singapore rose 19%, as their economy is also showing signs of expansion.

Figure 10: Ex-USA Sector Returns – 4th Quarter 2020



Emerging markets (+19.7%) posted their strongest quarterly return in more than a decade, boosted by China's economic rebound, stronger commodity prices and a weaker US dollar. Asia rose 18.9%, powered by semiconductor companies as supply chain concerns grew. Korean technology giant Samsung jumped 51% and Taiwan Semiconductor gained 27%. In China, the biggest gains came from internet services platforms (Meituan, Pinduoduo). Technology giant Alibaba slid 21% amid government scrutiny regarding the business practices of large internet platforms. The Government also nixed the IPO of Alibaba's fintech affiliate Ant Group, a deal that was expected to be the world's largest IPO ever.

Latin American markets rose 34.8% on stronger commodity prices and a rebound in financial stocks. Brazil posted its largest quarterly gain since 2009 (+37%), led by energy giant Petrobras, iron ore supplier Vale, Unibanco and Banco Bradesco. Overall, commodity-exporting Latin American countries rallied after lagging most Asian countries in 2020.

Emerging Europe rose 22.5%, as smaller constituents (Czech Republic, Hungary, Turkey) all rose over 30%. Russia gained 21.6%, as energy prices advanced and financials (Sberbank) performed well.

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The Back Page – 2021 Investment Themes

In hindsight, 2020 was a year like no other – a deadly pandemic, global shutdown and recession, a sharp market collapse followed by a surprisingly swift market recovery. The word "unprecedented" was never used more! What can we expect in 2021 – should we expect the new "roaring 20's" as we (hopefully) tame and manage the COVID-19 virus? Here we share investment themes that may shape 2021 investment markets:

Strength of Recovery Remains Vaccine Dependent

Since the onset of the pandemic, step one on the road to recovery (medical and economic) has been tied to containing the COVID-19 virus - testing, vaccine development, distribution and administration and ultimately vaccine efficacy. Growth forecasts have "looked through" the second wave of pandemic spikes and are focused on re-opening and recovery by mid-2021. While the development of the vaccines occurred more quickly than expected, administration of the vaccines got off to a slow start in the US. The pace should pick up meaningfully in 1Q21. *Pairing better vaccine availability with fiscal policy expansion and more political clarity, could drive US GDP growth above 3% in 2021 and support a stronger recovery.*

The Digital Future

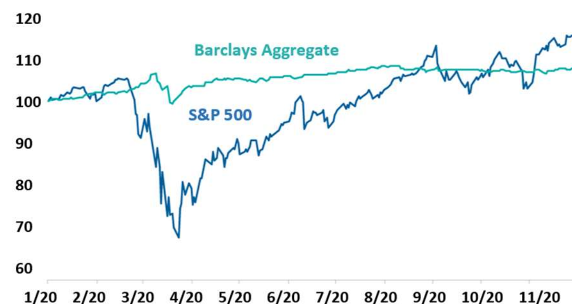
The COVID-induced shutdown accelerated the "digitization" of many sectors and services, from retailing, entertainment/fitness, working remotely and health care services. Yes, consumers were working remotely, shopping and accessing health care services online before COVID, but the pandemic has increased demand and created new opportunities for consumers and digitally savvy companies. Companies with strong online business models have an advantage and are disrupting the status quo produced by "old-economy" companies. Will these trends continue post-COVID? Lockdowns and social distancing restrictions will come to an end, but people formed new habits in 2020 and many will persist. Successful *active managers will be looking to identify growing companies that have not only benefited from the pandemic, but also have the potential to continue generating solid growth post-COVID.*

Sustainable Investing Becoming Sustainable

ESG and impact investing were gaining traction pre-COVID, and that trend has accelerated in 2020. Renewable energy, climate change, addressing social, gender and economic inequality issues, rebuilding infrastructure have become *global* priorities. *These themes will increasingly appear in US, developed and emerging markets traditional and dedicated ESG portfolios.*

Bonds for Ballast

There is a reason to hold on to core bonds even when rates are low – as a volatility buffer. When the S&P 500 index fell -34% in just 22 days in 1Q20, high-quality bonds provided a buffer to market volatility and held steady. As equities staged a swift 5-month recovery, high quality bonds held steady. Corporate bonds, investment grade and high yield, can support high quality bonds during extended periods of low interest rates. *Interest rates will likely remain low for some time and total returns in bonds may be muted; but the "buffer" benefits of diversification, capital preservation, income and inflation protection remain intact.*



Maintain Balance in Equity Portfolios

The theme of our 3Q20 Chartwell Review, "Changing of the Guard" referred to a number of investment trends which are poised for a change, including the growth style dominance over value. We are in the midst of the largest growth cycle in history. For the trailing 10-years through September 2020, the Russell 1000 Growth index outpaced the R1000 Value index by 7.3%, p.a. The growth over value gap widened in the most recent years – the trailing 1-year differential is 42.6%, the trailing 3-year differential is 19%. Given those performance differentials it is not surprising that exposure to the value style has decreased. While the environment for growth stocks remains favorable (see Digital Future above) and should not be eliminated, the factors favoring the value style are growing. *As we emerge from a recession, with interest rates expected to stay lower for longer and favorable valuations, it may be time to begin rebuilding exposure to value stocks.*

Sources: MorningStar, Capital Group, Goldman Sachs Global Investment Research, Blackrock.

Stay Safe! See you next quarter!

Natalka Bukalo
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