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PORTFOLIO UPDATE – NOVEMBER 12, 2020

What a year this week has been. We are dealing with a bipolar environment of exuberance and the depths of despair punctuated by the more ritualistic and cyclical parts of society and markets. Through it all, markets have been approaching or touching all-time highs. For this reason, we have taken steps to embrace more market exposure in our model portfolios, adding modestly to US equities and more generously to US corporate credit to establish overweights to both and an underweight to cash as compared to our blended benchmarks.

A few headlines and a lot of fundamentals have brought us to this decision. In terms of headlines, what seems increasingly likely to be a Biden presidency, a slimmer Democratic majority in the House and a likely (although thinner) Republican majority retained in the Senate combine to present split governance and probably a fair amount of gridlock for two years. From a policy point of view this might not be very exciting, but it makes pricing risk a lot clearer for the markets, and that certainty seems to have buoyed performance. The second major headline came from Pfizer announcing their COVID-19 vaccine may be as much as 90% effective. That was followed shortly thereafter by news out of Eli Lilly that their monoclonal antibody therapy received a FDA emergency use authorization. Not a headline yet, but we expect with the jockeying for power this cycle coming to a conclusion there will be a turn in Washington to focusing on some form of yet-to-be-determined relief package that will bring some stimulus to the economy as we move into the holiday season.

In terms of fundamentals, and as we have written in our blogs and newsletters, economic news at least in the US has been serially positive with a powerful rebound over the last quarter. We are still behind where we were this time a year ago but markedly ahead of the depths of the pandemic crisis when the world went into lockdown. Our expectation is that equities in the US will hold their ground, with some rotation of leadership, but the general trend will be to grind higher, and high-quality corporate bonds will continue to be attractive and provide greater economic reward than Treasury securities that pay very little.

We take this step with a healthy respect for the risks still surrounding us. Europe, after a fairly quiet Summer, appears to have lost its grip on the propagation of the virus and has settled back into varying degrees of lockdown which will unquestionably drag on economic activity. Asia taken as a group has been more exacting about its pandemic controls and is still enjoying (relative) normalcy although hotspots do keep emerging. The US is making new coronavirus records every day, and parts of the community healthcare system nationally are feeling the strain, which is different than the highly concentrated outbreaks in New York and New Jersey that marked the Spring months. The US' small-L libertarian mindset means it is highly unlikely we will return to sweeping lockdowns as Europe is doing, and we are more likely to see targeted tactical moves like restaurant and bar curfews and limits on social gathering sizes but allowing business generally to continue which is supportive of jobs and economic activity. The numbers are all trending in the wrong direction, so from an investor's point of view a certain trust has to be placed that the pharmaceutical industry in partnership with academia, NGOs and governments will come through with the necessary preventatives and therapies to head the pandemic off.

Other risks include the degree to which parts of the economy have been impaired for the long term like retail, in-person dining, travel and entertainment and the drag that will apply on a return to normalcy. Thousands of businesses and millions of jobs may have been irreversibly lost, which has implications everywhere. We will be looking for efforts from municipal, state and federal government as well as private institutions to stimulate capital formation, housing stability, and job creation in the damaged parts of our communities and economy to continue the path to restoration that has brought us to this point and raised our conviction.

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Diversification and strategic asset allocation do not guarantee a profit nor protect against a loss in declining markets. All investments are subject to risk, including the loss of principal.

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