



## JANUARY - FEBRUARY 2021 COMMENTARY

Put simply, we found ourselves intrigued by capital market behavior in January. After robust equity market gains towards the end of 2020, particularly in US stocks, some pull-back was justified. Higher interest rates (the yield on the benchmark 10-year US Treasury climbed 14 basis points from 0.92% to 1.06%) forced prices of longer-dated US bonds downward in January. And yet, riskier segments of the world's equity markets outperformed in the face of climbing Treasury yields. We actually view this as an encouraging development because it appears that the global equity market rally is broadening, or at least rotating to areas such as US Small and Mid Cap equities as well as to Emerging Markets that tend to thrive in improving economic growth regimes.

There is still a considerable amount to be concerned about both domestically and abroad, though. Conditions in the US labor market remain dire with initial and continuing jobless claim registering stubbornly persistent high levels. But, the US ISM (Institute of Supply Management), which produces several influential surveys of their members, has released key reports on the impact of COVID-19 on US business trends. The December surveys on US Manufacturing New Orders and Business Production suggest that purchasing managers are optimistic. In fact, the New Orders reading stands at a level not seen since 2004. This is a critical development because, if business optimism remains elevated, eventually staffing will have to expand, bringing job seekers back to work. A lot needs to occur for the economy to fully recover. States need to allow businesses and schools to reopen, vaccines need to be distributed in mass and be effective, and people need to feel comfortable re-engaging in economic activity. We interpret these signals as suggesting supply managers are seeing beyond the significant near-term challenges to an economic recovery in the quarters ahead.

### US Institute of Supply Management

Manufacturing New Orders and Production Surveys Suggest Optimism





Investors are concerned that US equity market levels are reaching new all-time highs and valuation readings continue to be stretched. Several months ago narrow leadership within US stocks was the reason to justify underexposure to the asset class. Market participation has broadened considerably since the pandemic-caused nadir of 2020 as equity prices have climbed. One measure of greater market participation is the percentage of stocks trading above their long-term trends, depicted as the dotted line in the chart, revealing 89% of the S&P 500 universe trading above their 200-day moving average.

The high current level of participation can persist for prolonged periods as it had over the past decade. The 2010s were a period of slow economic and job growth post-Financial Crisis, and yet equity prices delivered robust gains during times of high participation, only temporarily interrupted by bouts of Euro-related uncertainty, the US Treasury debt downgrade, and the “Taper Tantrum”. Given the amount of monetary and fiscal support pledged by the Fed and Congress, our sense is that US stock prices could maintain their general upward trend even in the face of more near-term challenges.



This leaves us in a “be optimistic yet alert” mode of thinking and investment positioning. The near-term headline and other risks are real, but signs of prosperity are ahead in the US and other parts of the world, particularly Asia. We are also approaching the one-year anniversary of the pandemic-caused market rout.

The following page details a summary of our portfolio positioning and the major risks we are following:

*See the WCM website for more market commentary or contact us with any questions.*



## PORTFOLIO POSITIONING

After some level of clarity arose post US national elections we deployed our cash stock piles to US equity and fixed income. We now have a slight overweight allocation to equities overall and modest overweight to fixed income. We are underweight cash. Within global equities, we are overweight with respect to the U.S., modestly overweight to Asia x-Japan and neutral with respect to Emerging Markets. We are neutral with respect to Eurozone stocks and underweight Japan. Within fixed income, we are overweight in the U.S. with a preference for mortgages, investment grade corporate credit. We have little to no exposure to non-U.S. fixed income, although there is more exposure to non-U.S. through Green Bonds in our ESG series portfolios. All portfolios holding fixed income maintain lower duration than the benchmark.

## RISK OUTLOOK

- Any time government changes hands, even to successors within the same party, this introduces new uncertainties about legislative priorities, infrastructure, social programs, regulation and other areas influenced or outright controlled by government. The mix of governorships and State houses remained more or less the same after the 2020 election, but the Presidency and the US Senate switched party leadership. One-party control of Washington might suggest a dramatic agenda, but the party advantage in the House narrowed, and Senate control rests only with the VP tie-breaker. With the possible exception of additional COVID-related stimulus which will be supportive of capital markets and enjoys broad support outside of DC, not a lot is likely to happen as far as bold policy initiatives. We expect to see smaller changes at the margin, in some cases walking back Republican priorities and in others advancing Democratic ones. We expect the market to be satisfied with stimulus plus incrementalism, and the risks will be found in targeted areas of the market and economy rather than at the headline level.
- Big questions about the social contract will continue to play out in the months ahead. The ratio of constructive to destructive discourse and activism will weigh heavily on the impact to investors and the economy. Advancements in diversity, equity and inclusion, civil debate about justice reform, building back better and stronger as part of the COVID recovery, and improving participation in the US (and global) economy will be positive drivers. Putting that at risk, and with it capital formation and job creation, would be more violent and destructive actions that focus attention and resources away from serving and supporting the individuals and communities and their families, businesses and livelihoods who are struggling everywhere from the urban Northeast to the rural Southwest.
- As the “long, dark winter” as it has been variously described by public health officials grinds on, we appear to have passed the transmission peak. Whether this is the byproduct of changing public policy, ramped up vaccine distribution, or personal behavioral adjustments, or likely some blend of all three, there is reason to believe the opportunity exists to begin thinking about a post peak-COVID world. We say “post peak” and not “post COVID” because we see a



lack of certainty about the global community's ability to put the coronavirus completely behind us as new variants circulate that are more transmissible and more infectious, such as the "UK" and "South Africa" strains which move more quickly and seem to beat social measures as well as the vaccines that are being deployed. At the same time, necessity being the mother of invention, businesses, schools, governments, and houses of worship are learning to function in the environment which is available to us, which means using a blend of immunization, public health programs, and behavioral adjustments like masks and social distancing to get to what may be a near-term "normal" where education, business, worship, entertainment and leisure can resume with strictures. We see the risk to achieving this near-term normal coming from strong resistance to participating in immunizations or simple lack of access to same, new and dangerous virus mutations, and other conditions which perpetuate the current Hobson's choice of health and safety vs. education and a functioning economy.

- One of our long-term risk themes continues to be our focus on Chinese Communist Party actions which have not materially shifted for the better in the COVID era. From aggression in the Asia-Pacific region to military tension along the border with India to suppression of Hong Kong citizens' rights and the interests of the Uighur population and the lack of contrition for their early role in failing to stop COVID-19 in its tracks, all may contribute to China-directed backlash or retaliation. There does seem to be regional coherency in the response as nearly all Pacific nations have aligned with the US against Chinese aggression. From lack of respect for intellectual property rights to involvement in global criminal drug trafficking to financial crimes and human rights abuses bordering on genocide, the country is finding it harder to get the global community to look the other way. We view this as a risk to investment in China and investment in companies reliant on a Chinese supply chain, but likely bullish for other parts of the Asia Pacific interested in usurping China's role as the manufacturing floor for the world.
- Accelerating and likely permanent changes to consumer behavior and global supply chains that in many cases were already under way and have been amped up by CoV-2 are likely to create further near- and long-term disruption but also opportunity as more local, sustainable and safe sources of goods and services emerge. 2020 has fundamentally reordered what it means for businesses to be resilient and what is required to operate reliably and efficiently under a variety of externalities. In main street terms, the "old ways" are not coming back and markets will need to process and reorient capital around the new order.

## ESG CONSIDERATIONS

With the changing of the guard in Washington, it is time to look again in ESG terms at the opportunities and uncertainties. When examining the ESG attributes of an investment, it can often be the case that government, legislation and regulation will be deemed externalities. That is to say, these are factors and forces that are largely outside the control of the direct stakeholders of the investment. In the case of a company, it is possible to manage with and around these externalities, but usually not possible to change them. Such efforts as lobbying can put a heavy thumb on the



scale to tilt matters in favor of the company, but that is far less certain than choosing suppliers, hiring employees, funding R&D, or changing branding.

A regime change at the national or state/local level can present these companies with an environment that is more or less conducive to business. A President can come into office and, within the limits of the law, regulate, deregulate, or re-regulate in ways that can help or hinder business prospects. New legislation can establish subsidies for emerging technologies and remove subsidies from legacy industries. The larger point is that the assumptions around operating a business in environmental, social and governance terms can shift rapidly.

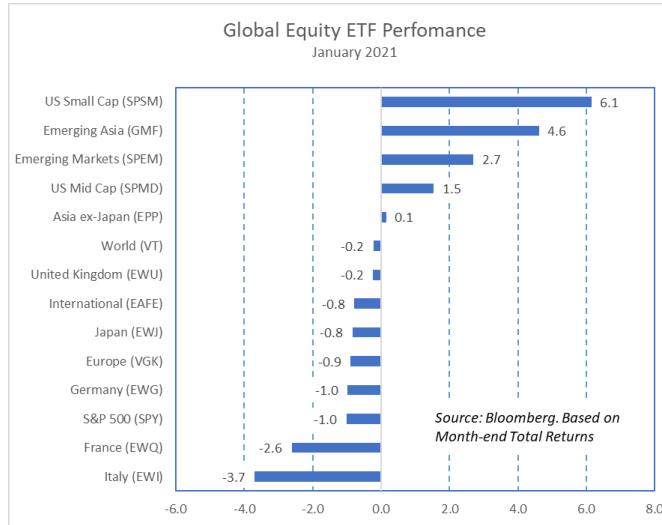
A perfect example to hold out is the Keystone XL pipeline, a central part of the strategy for moving Canadian tar sands oil through the US for refinement and distribution. The project has been fraught with challenges ranging from carbon and clean water concerns to operational safety to the property rights of farmers to the interests of indigenous peoples. The Obama administration halted KXL, the Trump administration reversed the call, and the Biden administration is expected to halt it again, possibly permanently. It is easy to see the deep environmental and human rights controversies that are, while external to the business of pulling tar sands oil out of strip mines, processing it and transporting it to Cushing, OK, directly affecting the direction of public policy and even election outcomes which change the operating environment for the business. In the 70+ days from the day before elections to inauguration, KXL went from viable to dead on the tracks.

In large and small ways, ESG-oriented investments are evaluated for these externalities and discounted according to the real possibility that an off-balance sheet and unpriced risk like climate change becomes material to the viability of the investment. Government, legislation and regulation become the mechanism for operationalizing and pricing in environmental and societal impacts on behalf of the community and the commons.



## JANUARY 2021 CAPITAL MARKET REVIEW

Overall, global stocks took a pause to start off the year, but certain riskier segments of the world's equity markets surprised to the upside. Fixed income did not fare as well in most cases.



### Equity Markets\*

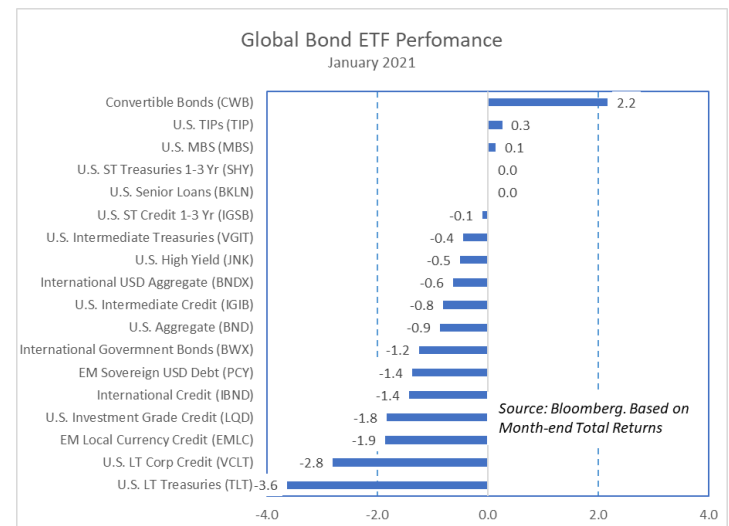
Global equities shed 0.2% in January after strong gains in November and December. US Large Caps, Europe and Japan underperformed, declining 1%, 0.9% and 0.8% respectively.

There were strong results in US Small Caps and Emerging Asia which vaulted 6.1% and 4.6% for the month while Emerging Markets overall delivered a respectable 2.7% total return in US Dollar terms. US Mid Caps resisted the downward draft in Large Caps, climbing 1.5% for the month.

### Bond Markets\*

The increase in yield on the benchmark US 10-year Treasury Bond was a major headwind for longer dated US fixed income instruments and the stronger Dollar adversely impacted non-Dollar fixed income. US Convertible bonds reflected their equity-like attributes, adding another 2.2% to gains made towards the end of 2020.

US Long-term Treasuries were impacted the most by climbing interest rates, contracting 3.6% in January.



\*The returns cited reflect total return performance of exchange traded funds listed in the corresponding bar charts



## DISCLOSURES

Wilde Capital Management, LLC is a registered investment adviser. Information presented is for educational purposes only and does not intend to make an offer or solicitation for the sale or purchase of any specific securities, investments, or investment strategies. Investments involve risk and, unless otherwise stated, are not guaranteed. Be sure to first consult with a qualified financial adviser and/or tax professional before implementing any strategy discussed herein. Past performance is not indicative of future performance.

It is important to remember that there are risks inherent in any investment and that there is no assurance that any money manager, fund, asset class, style, index or strategy will provide positive performance over time.

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.

The information contained herein is based upon the data available as of the date of this document and is subject to change at any time without notice.

Portfolios that invest in fixed income securities are subject to several general risks, including interest rate risk, credit risk, the risk of issuer default, liquidity risk and market risk. These risks can affect a security's price and yield to varying degrees, depending upon the nature of the instrument, and may occur from fluctuations in interest rates, a change to an issuer's individual situation or industry, or events in the financial markets. In general, a bond's yield is inversely related to its price. Bonds can lose their value as interest rates rise and an investor can lose principal. If sold prior to maturity, fixed income securities are subject to gains/losses based on the level of interest rates, market conditions and the credit quality of the issuer.

Foreign investments are subject to risks not ordinarily associated with domestic investments, such as currency, economic and political risks, and may follow different accounting standards than domestic investments. Investments in emerging or developing markets involve exposure to economic structures that are generally less diverse and mature, and to political systems that can be expected to have less stability than those of more developed countries. These securities may be less liquid and more volatile than investments in U.S. and longer-established non-U.S. markets.

An investment in small/mid-capitalization companies involves greater risk and price volatility than an investment in securities of larger capitalization, more established companies. Such securities may have limited marketability and the firms may have more limited product lines, markets and financial resources than larger, more established companies.

Portfolios that invest in real estate investment trusts (REITs) are subject to many of the risks associated with direct real estate ownership and, as such, may be adversely affected by declines in real estate values and general and local economic conditions.

Portfolios that invest a significant portion of assets in one sector, issuer, geographical area or industry, or in related industries, may involve greater risks, including greater potential for volatility, than more diversified portfolios.

### Important Disclosures: Exchange-Traded Funds

Exchange-traded funds (ETFs) are investment vehicles that are legally classified as open-end investment companies or unit investment trusts (UITs) but differ from traditional open-end investment companies or UITs. ETF shares are bought and sold at market price (not net asset value) and are not individually redeemed from the fund. This can result in the fund trading at a premium or discount to its net asset value, which will affect an investor's value. Shares of certain ETFs have no or limited voting rights. ETFs are subject to risks similar to those of stocks.

ETFs included in portfolios may charge additional fees and expenses in addition to the advisory fee charged for the Selected Portfolio. These additional fees and expenses are disclosed in the respective fund/note prospectus. For complete details, please refer to the prospectus.

For additional information regarding advisory fees, please refer to the Fee Summary and/or Fee Detail pages (if included with this report) and the program sponsor's/each co-sponsor's Form ADV Part 2, Wrap Fee Brochure or other disclosure documents, which may be obtained through your advisor.

Certain ETFs have elected to be treated as partnerships for federal, state and local income tax purposes. Accordingly, investors in such ETFs will be taxed as a beneficial owner of an interest in a partnership. Tax information for such ETFs will be reported to investors on an IRS schedule K-1. Investors should consult with their tax advisors in determining the tax consequences of any investment, including the application of state, local or other tax laws and the possible effects of changes in federal or other tax laws.