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John C. Robinson
Chief Executive Officer
Tel: 404-883-2577
john@consequentcm.com

Capital Markets Review and Outlook

By: Cyril M. Theccanat, Chief Investment Officer

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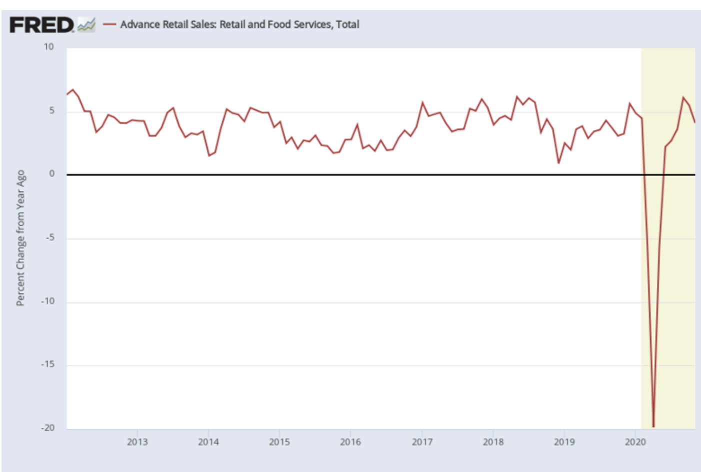
Economy and Outlook

The final month of 2020 ended on a hopeful note after what was certainly a tumultuous and unprecedented year not seen in over a century for the entire world. While Covid-19 cases continued to hit records in December with the total number of infections worldwide now exceeding 87 million and fatalities rapidly approaching the 2 million mark, a mass vaccination program also began with close to 3 million Americans vaccinated by the end of the month. Vaccinations have also started in several other countries around the world, including Canada, the United Kingdom, the European Union, Israel, and China. As more vaccines receive regulatory approval, the mass vaccination program will ramp up globally in 2021. The end to this devastating scourge is now clearly in sight. Although December marked the worst month, by almost any measure, for the pandemic in the United States, economic data remain mixed. While employment gains decelerated, leaving over 10 million Americans still out of work, economic output was sturdy with a key index for the manufacturing sector (IHS Markit PMI) registering at 57.1 in December, the 6th consecutive month with a reading above 50. The December reading reflects the largest improvement in the health of the U.S. manufacturing sector in over six years. Consumer spending, which represents close to 70% of the U.S. economy, declined in November for the second consecutive month. However, as shown in the chart above, on a year-over-year basis, consumer spending is up +4.1%.



Furthermore, a bill providing $900 billion in additional stimulus was finally approved by Congress at the end of the month providing relief for millions of people.

The global vaccination program for Covid-19 will quickly pick up speed as wrinkles in the distribution and administration of vaccines are ironed out. Post-Covid renormalization will follow suit beginning, most likely, with the developed parts of the world including advanced emerging countries. Judging by the lofty readings in investor sentiment indicators, investors appear to be anticipating a continuation of the strong gains in financial markets that accompanied the pandemic-induced recession in 2020. It is, however, important to

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recognize that markets are a discounting mechanism. Thus, the sharp rebound in asset prices following the plunge in prices in the first quarter of 2020 was based on expectations that the unleashing of massive fiscal and monetary stimulus programs together with the rapid development of successful vaccines for the Covid-19 coronavirus would result in a significant recovery in economic growth in 2021. In the near-term, therefore, volatility is likely to rise together with market pull backs, especially in the domestic equity markets which are at record highs. Some of the unique circumstances in 2020, including the near-zero cost of money, have led to excessive risk-taking as reflected in the frothy initial public offering (IPO) and special purpose acquisition company (SPAC) markets, for example. While the Federal Reserve has indicated that monetary policy accommodation is likely to remain in place for the next 2 to 3 years, faster than expected global economic recovery from the pandemic may lead to the closing of the monetary spigot sooner and lead to higher Treasury yields. While the investment thesis, in terms of strategic asset allocations, for long-term institutional investors remains mostly unchanged, volatility is likely to rise as 2021 unfolds.

Equity Markets

The major domestic equity market indices made record highs in December despite the continued surge in Covid-19 cases, hospitalizations, and fatalities from the disease. Investors, instead, focused on the start of the deployment program for coronavirus vaccinations in the United States and other parts of the world. Following a very strong November, the broad domestic equity market represented by the Russell 3000 Index added +4.5% in December bringing its return for the full year to a remarkable +20.9%. This is even after a 1st quarter loss of -21%. For the fourth consecutive month, Mid Cap and Small Cap capitalizations outpaced the gains in Large Cap (+4.2%) by +0.5% and +4.4% respectively. With its strong back-to-back relative performance, Small Cap has now made up most of its underperformance versus Large Cap. For the full year, Small Cap is up +20% versus +21% for Large Cap, while Mid Cap gained +17.1%. From a style perspective, Value's outperformance over Growth in November was reversed with Growth outperforming Value across all capitalizations by +17 bp to +143 bp. For the full year, Growth has dominated Value by a sizeable margin as shown in the table on the last page. In terms of sector performance, Cyclicals predominantly outperformed Defensives in December. Financials (+6.3%) and Technology (+5.7%) were the top two sectors for the month, and Consumer Discretionary (+2.5%) outperformed Consumer Staples (+1.8%), while Utilities (+0.7%) was a laggard. The continued rebound in crude oil prices helped the Energy sector gain +4.4% leading to a +27.8% increase in the 4th quarter. However, for the full year, Energy lost almost -34%. Highlighting the strong performance of Cyclicals in 2020, the top two performers were Technology (+43.9%) and Consumer Discretionary (+33.3%), while Utilities (+0.5%) and Real Estate (- 2.2%) lagged. The continued weakness in the U.S. dollar was a positive performance driver for international markets. The dollar index declined a further -2.1% in December which brought it to its lowest level in almost three years. The Developed Markets Index, MSCI EAFE, gained +4.6% in December driven by strong gains in Australia

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and Germany which both rose by +6%, and the United Kingdom (+5.5%). Relative laggards in the developed markets include Canada (+3.6%) and France (+2.8%). Emerging markets had a strong December with the MSCI Emerging Markets Index rising +7.4% for the month helped by double digit returns in Brazil (+13.6%), India (+10.2%) and Korea (+16.6%). While China was a relative laggard for the month with a gain of +2.8%, it was one of the standouts for the full year with an increase of almost +30%. As a result of the strong performance in the 4th quarter, the Emerging Markets Index had a return of +18.3% for all of 2020 which was more than double the +7.8% return for the Developed Markets index excluding the U.S.

Fixed Income Markets

The continued rally in the equity markets finally weighed on the Treasury market pushing Treasury yields higher especially for maturities greater than 5 years. The yield on the 10-year Treasury note rose 9 bp to 0.93%, while the 30-year Treasury bond's yield increased 7 bp to end the year at 1.65%. On the other hand, the 2-year Treasury yield declined by 3 bp to 0.13%. As a result, the Treasury yield curve steepened with the 2-year/30-year Treasury yield spread widening by 10 bp in December. For 2020, the Treasury yield curve steepened by 71 bp to end the year at +152 bp. The corporate bond market mirrored the positive tone in the equity markets and investment grade corporate bond spreads narrowed by 8 bp leading to +79 bp of outperformance over duration-matched Treasuries. The Bloomberg Barclays investment grade corporate bond option-adjusted spread (OAS) ended the year at +92 bp, almost unchanged to the +90 bp level at the end of 2019 despite all the volatility in the earlier part of 2020 which pushed the spread past +250 bp in March. Net issuance of corporate bonds in 2020 hit a record of over $1 trillion. By way of comparison, the average annual net issuance for the five years ending 2019 was only half as much: $515 billion, and the previous record was $701 billion back in 2009. As is typically seen in a rallying credit market, the corporate quality curve and credit curve both flattened in December. BBB-rated bonds outperformed Single-A rated issues by +58 bp, while long-maturity corporate bonds outperformed short and intermediate issues by an average of +78 bp. Airlines (+209 bp) and Energy (+05 bp) were among the best performers in terms of excess return, while Telecommunications (+30 bp) lagged. For the month, the investment grade sector had a total return of +0.5% which brought its return for 2020 to +9.4%. The High Yield corporate bond sector continued its strong performance with the OAS of the Bloomberg Barclays High Yield index tightening by 52 bp to end the year at 360 bp, which, in turn, led to +190 bp of excess return for the month of December. Similar to the investment grade market, investors gravitated to risk in the high yield sector which led to a flattening of the high yield quality and corporate curves. On a total return basis, the BB sector gained +1.5%, while the single-B sector rose +1.7% and the CAA sector climbed +3.2%. The best performing high yield sectors included oil field services (+11.6%) and airlines (+4.8%), while home construction (+0.7%) and health insurance (+0.8%) lagged. The High Yield index generated a total return of +1.9% for month, and +7.1% for the full year 2020. While intermediate and long maturity U.S. Treasury yields rose in December, yields in foreign developed government bond markets declined or were little changed for the month which resulted in

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a relative underperformance for the U.S. government bond market. This was additionally impacted by the continued weakness in the U.S. dollar in December. As a result, the FTSE non-US World Government Bond Index (WGBI) rose +2.3% in December, while the U.S. government bond index declined -0.2%. After lagging the U.S. government bond market for much of this year, the ex-US WGBI's +10.8% return for 2020 is now well ahead of the +7.9% return for the U.S. government index.

		Returns as of 12/31/20 (In %)				
		Month	Q4	1 Year	3 Years	5 Years
Russell 3000®	US AllCap Equity	4.5	14.7	20.9	14.5	15.4
Russell 1000®	US Large Cap Equity	4.2	13.7	21.0	14.8	15.6
Russell 1000® Growth	US Large Cap Growth	4.6	11.4	38.5	23.0	21.0
Russell 1000® Value	US Large Cap Value	3.8	16.3	2.8	6.1	9.7
Russell Midcap®	US Mid Cap Equity	4.7	19.9	17.1	11.6	13.4
Russell Midcap® Growth	US Mid Cap Growth	4.8	19.0	35.6	20.5	18.7
Russell Midcap® Value	US Mid Cap Value	4.6	20.4	5.0	5.4	9.7
Russell 2000®	US Small Cap Equity	8.7	31.4	20.0	10.2	13.3
Russell 2000® Growth	US Small Cap Growth	9.3	29.6	34.6	16.2	16.4
Russell 2000® Value	US Small Cap Value	7.9	33.4	4.6	3.7	9.7
MSCI ACWI ex-US	Global Equity ex-US	5.4	17.0	10.7	4.9	8.9
MSCI EAFE	Global Developed Mkts Equity	4.6	16.0	7.8	4.3	7.4
MSCI EM	Emerging Mkts Equity	7.4	19.7	18.3	6.2	12.8
Bloomberg/Barclays US Agg	US Core Fixed Income	0.1	0.7	7.5	5.3	4.4
Bloomberg/Barclays US Interm. Agg	US Intermediate Fixed Income	0.2	0.4	5.6	4.4	3.5
Bloomberg/Barclays US Credit	US Corporate Bonds	0.5	2.8	9.4	6.8	6.4
Bloomberg/Barclays US MBS	US Mortgage Backed Securities	0.2	0.2	3.9	3.7	3.1
Bloomberg/Barclays US Corp HY	US High Yield	1.9	6.5	7.1	6.2	8.6
FTSE Non-US WGBI	Global Fixed Income ex-US	2.3	4.8	10.8	4.6	5.2