2021 Market Outlook: It's Not How You Start, It's How You Finish

Executive Summary

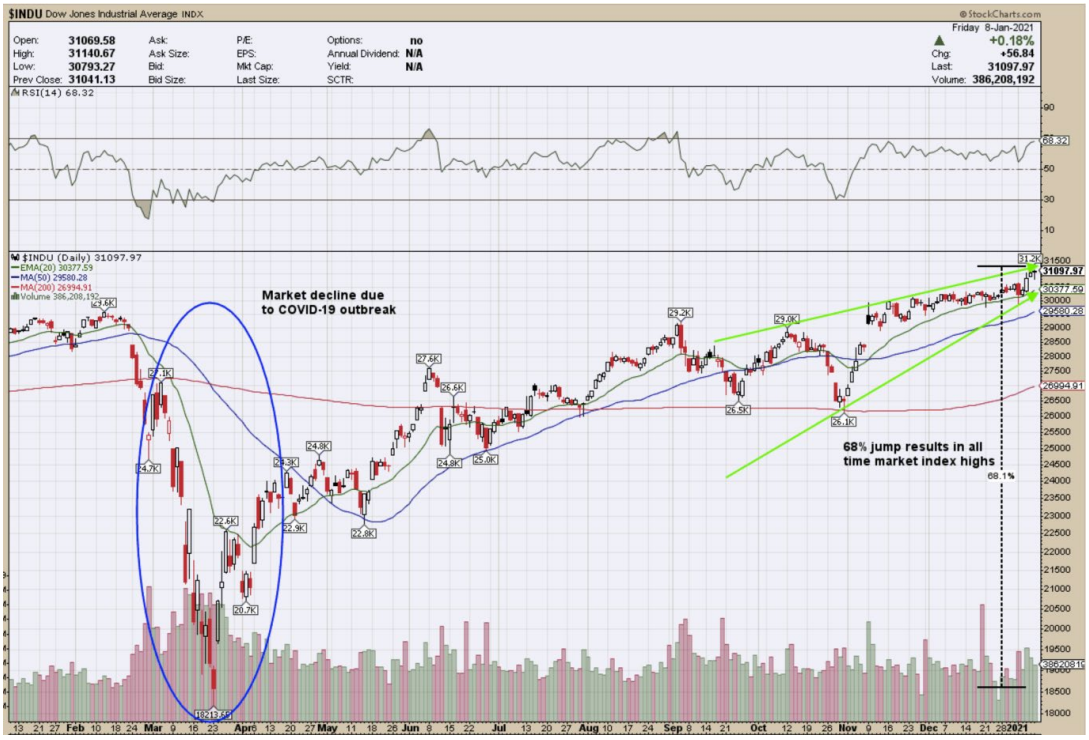
2020 Recap

Just as in sports, the start of the season does not always dictate how a team finishes the year. Recall the 2017 Philadelphia Eagles, for example; they were 4-6 just after the midpoint of the season and eventually defeated the Tom Brady-led New England Patriots in Super Bowl LII. Similarly, the Dow Jones Industrial Average (DJIA) saw a large drop in the beginning of 2020 followed by a quick recovery, exceeding the all-time high. However, the large jump in the DJIA does not necessarily suggest a continual move upwards.

2020 was a year that featured a pandemic, socio-political unrest and one of the most controversial president elections in the history of the United States. As a result, the stock market experienced its largest drop since the 2007-08 financial crisis. Beginning in February and into March, investors endured extreme volatility in witnessing the DJIA drop more than 35% in a matter of days. The coronavirus has made a tremendous global impact as it ultimately shut down economies and resulted in the loss of many lives. As the news and hope of a successful vaccine becomes more prominent, we look to 2021 with great optimism.

Uncertainty Looming

While we expect an upward trend of the overall market for the long-term, there remains speculation regarding the virus and the recovery of global economies. Throughout 2020, unemployment soared as both small and large companies were forced to close offices for months at a time, work from remote locations and in some cases, close permanently. Although there is increasing hope in a vaccine as several are in the distribution and administration phase, no one can be certain of the response that may follow. As 2020 showed us, volatility often provides great value in the market along with opportune buy points followed by quick recoveries. After the 35% drop in March, the Dow Jones moved 68% upwards in the remaining nine months in 2020. This quick recovery indicates skepticism in the short-term with securities becoming "overbought". Many analysts suggest that a correction could occur in early 2021 before a long-term upward move would occur. Thus, the recovery we have witnessed into year-end 2020 leads us into our equity forecast for the year 2021.



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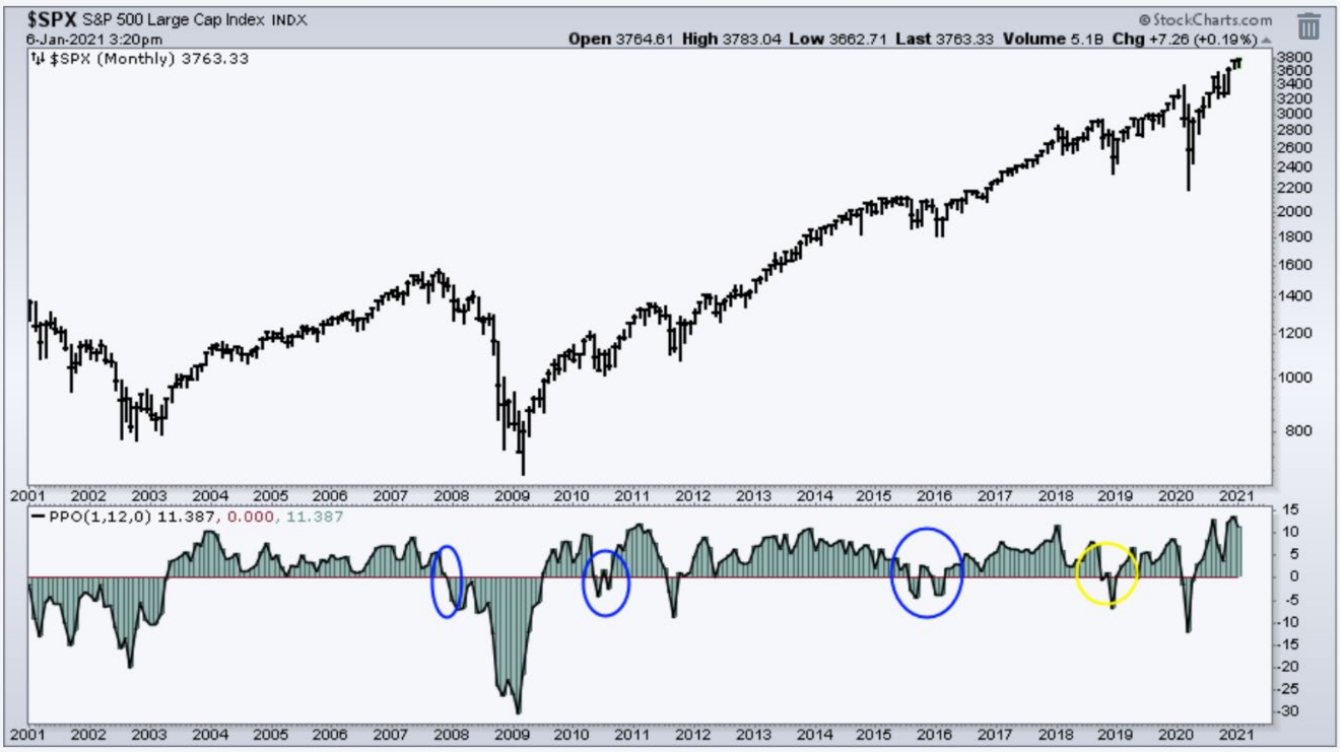
Equity Outlook

Early Pullback Expectations

As 2021 rolls in, we suspect the equity market may experience a decline in the short-term. We have been patiently waiting, once again, after the market moved to all-time highs. With the Senate race wrapping up in Georgia and President-elect Joe Biden taking office, individuals and corporations are leery of what may be in store for the economy. With the threat of income taxes rising, companies are also faced with the possibility of increased corporate taxes, which would potentially have a significant impact on their earnings. In addition, Biden's agenda includes industry-specific taxes that would have even more of a negative impact on companies' bottom lines.

As we look back on the 68% increase in the Dow Jones Industrial Average from March 2020 to the end of December 2020, we attempt to gather information on where the market may be headed through our technical analysis of charts. Comparatively, the S&P 500 Index rose 69% during the same time frame. Technical Analysis and Percent Price Oscillator (PPO) allows investors to see momentum through the relationship of two moving averages as a percentage. The graphic below depicts the S&P 500 Index, tracked monthly, over the last 20 years. Historically, when the PPO indicator line drifts above 10%, the index enters an area that has often suggested a negative price move for the market may be ahead. A correction which pulls the PPO below zero often helps resolve an overbought market scenario and promotes confidence in a long-term move higher that follows. Currently, the major indices, including the S&P 500, have drifted well above the zero line. Theoretically, the PPO would need to drop, meaning a downward move in the S&P may be near, and this would possibly correct the negative divergence. After the PPO indicator line crosses back above zero, into positive territory, a long-term move upward may be confirmed.



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Long-term Optimism

With that, there are short-term cautious signals, but after the selloff in the beginning of 2020 and the subsequent recovery, we have a positive outlook in the long-term with 37k on the DJIA as our target, based on our analysis, over the next 12-18 months. As we move further into the year, there is opportunity in areas that still have not fully recovered. The market saw many sectors experiencing negative annual returns for 2020, however, in the last quarter, we saw energy, financials and industrials undergo a significant reversal move. Analyzing rotational graphs will help to understand the possible direction of specific sectors and industries moving forward. As an entire market, we anticipate a bullish market for 2021 after we see a brief correction from the end of 2020.

Industries whose returns haven't fully recovered yet

S&P 500 Industry	2020 decline
Energy equipment & services	-37%
Oil, gas & consumable fuels	-34%
Airlines	-31%
Aerospace & defense	-17%
Banks	-15%
Gas utilities	-15%
Diversified telecom services	-12%
Leisure products	-9%
Multi-utilities	-8%
Real estate investment trusts	-4%

Source: Bloomberg. December 29, 2020.

**For further analysis, see our 2021 Market Outlook Video*

Fixed Income Outlook

The fixed income market is offering low interest rates which are expected to continue throughout 2021 and possibly into the next couple of years. In the middle of December, the Fed announced that it would keep the federal funds rate between 0 and 0.25 until the economy can recover from the effects of coronavirus. In addition, the Fed also announced that it will continue Treasury buybacks with a goal of $80 billion per month for the foreseeable future. With such low rates announced to continue through 2022, we expect the bond market to lag behind equities and to only appeal for necessary diversification purposes.

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*See page 3 for disclosures