SUMMIT
ASSET MANAGEMENT

**"Lessons (re)Learned"**

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Many investors and market pundits had a foolproof thesis for the fourth quarter. Stocks were sure to dive. After all, COVID cases were once again spiking across the country and the rest of the world. The existing political environment almost assured an ugly election dispute. On top of that, stocks looked pricey after soaring in the third quarter while the economy only limped back from shutdowns. Turns out fiscal stimulus, low interest rates and good news on vaccines are more important than any of that other stuff.

The stock markets looked through the concerns of the day and rallied hard on the hopes of a successful vaccine rollout. U.S. large cap growth stocks were finally overshadowed by other areas of investment. While the S&P 500 did post a stellar 12% return for the quarter, it was the value stocks that did most of the heavy lifting. Smaller stocks, which had spent much of the year struggling, caught fire with a 31% return for the quarter. Both large and small indices finished the year up about 18%. Developed international joined the party with a 16% quarter, bringing year to date results to 8%. Government bonds held on to previous quarters' gains and finished the year up 7%. Given what life looked like only a short six months ago, results like these are remarkable.

There has been a lot of news over the year. Recently, many questions have been answered while additional ones have been raised. The election has been decided, although with way too much strife. Now, we wonder how Democrats will use their new control. Vaccines have been discovered and approved, and distribution has started. Now, we wonder about availability and who will take them. Life is on its way back to normal. Now, we wonder how fast we can get there.

With such positive returns and negative economic and human health environments, markets did not perform like many people expected. We will not recap all the specifics that have been so obviously hard to miss. Instead, we will use the events and circumstances of this unforgettable year to review a few important investing lessons that we have learned, or relearned. Many of these have been discussed before, however, in times like these, they bear repeating.

**The stock market and the economy are not the same thing.** While the two are very dependent on one another, the differences in how Main Street and Wall Street are made up can often produce very different results. The stock market is dominated by large, multi-national corporations. Many have weathered the pandemic quite well and even prospered in these difficult times. Main Street is dominated by locally owned small and medium-sized businesses, many of which took on the brunt of the disruptions. Often, the two move in tandem, but not always.

**Do not mix investing with politics.** Investing is hard enough by itself. Inviting the emotional baggage of politics into the decision-making process only makes it harder. The truth is that politicians have far less control over the stock market than people would like to believe. Policies implemented often show up with a lag and come with unintended consequences (good and bad).

**The stock market is forward-looking.** Most of us are focused on and concerned with the world around us and its immediate conditions. This is human nature. Markets, on the other hand, tend to look past the now and towards the future. This is why we often see stocks doing poorly well before a recession occurs and doing better when it feels like things are at their worst. 2020 equity returns demonstrate how stock markets continue to look past the current lockdowns and economic difficulties and towards the time when the vaccines take hold and growth returns.

**Monetary and fiscal policies are big drivers of market performance.** As we have seen throughout history, markets react to policy changes. The precipitous freefall of February/March was quickly reversed when the Federal Reserve announced their support of the financial markets with lower rates, bond purchases and a liquidity guarantee. Congress quickly followed with their own stimulus checks, unemployment benefits and business lending programs. This increased the upward momentum. It works the other way as well. Tremendous volatility and a "taper tantrum" occurred in 2013 when the Fed announced that it would start winding down the programs implemented during the Financial Crisis. Don't fight the Fed.

**Market timing is hard.** As we mentioned earlier, investing itself is hard. Trying to time the ups and downs to maximize returns and reduce losses has always been the holy grail of investing. The major problem is that you must get two decisions correct… selling at the right time and then buying back at the right time. The "right time" to <u>sell</u> is often when an investor feels most confident about the future and wishes they had even more to invest. The "right time" to <u>buy</u> is often at the darkest moments when one wishes they had never invested in the first place. Both decisions go against human nature, and both must go correctly to be beneficial.

**Stay diversified.** It is our nature to want to own what is currently going up in price. It is also fine to concentrate or focus a portion of your portfolio in investments that interest you or in which you have high conviction. However, prudent investing requires we spread the risk around. Ideally your portfolio will have some investments zigging while others are zagging. This creates less volatility and an easier portfolio to hold through trying times. Additionally, it is difficult to know when or where the market will go next. The recent quarter was an excellent example as underperforming areas suddenly became top performing.

**We build portfolios to solve long-term problems.** We are building investment portfolios to help our clients reach their long-term goals such as saving for retirement and providing for their children's education. 2020 underscored the importance of taking a long view. Despite a pandemic, global recession, and breathtaking sell-off in most financial markets, most still ended the year strongly in positive territory. We cannot let short-term thinking and concerns affect the process of solving long-term problems.

**Outlook**

The entire world is aching to shed the fever of COVID. We want to move forward and return to normal life. This will happen in time, as more people get vaccinated and defeat the virus. Between now and then, however, things will likely get grimmer.

In the United States, most people are also aching to return to greater political stability and governmental harmony. We want to believe that this will happen sooner than later. We are also hopeful that the events at the Capitol last week will serve as both a wake-up call and a turning point for the country. Politicians need to realize the danger of their division and rediscover the virtue of coming together in a common purpose. We need to focus on building up ourselves, our neighbors, and our country, not identifying segments of the population to demonize and tear down. This country has accomplished so much in our short history by working together and emphasizing our common values. That ideal needs to make its way back into focus.

As we stand at the beginning of a new year, our outlook is fairly optimistic. The combination of effective vaccination, more stable political leadership, pent-up demand for goods and services, and large pools of cash and savings on the sidelines, should provide a prolific backdrop for economic recovery and growth. With the Democratic party gaining control of the Senate, additional fiscal stimulus and supportive monetary policy are more likely and should provide additional short-term benefits to the recovery.

The uneven recovery in the economy and stock prices have left some areas of the market very expensive and others cheap. We expect the cyclical sectors, which have been left behind in 2020's gains, to bounce back as the economy reopens. Bonds, especially longer-term government bonds, are very expensive. Short-term bonds offer little to no yield but can still serve as a defensive store of value. Corporate bonds also look expensive but improving economic conditions should allow for modest returns. We will maintain our diversification and believe progress can be made in 2021. We will also remember the lessons of 2020.

**Summit's Own Planning**

Just as we help you plan today to reach your goals of tomorrow, we manage our business the same way. We are taking steps now to build a strong future for our firm and for our clients. As part of an extended transition plan, we are putting in place measures that will facilitate the continuing transfer of ownership from our partner, Alex Thompson, to the other existing partners in the firm – Lance Hollingsworth, John Laughlin, and Peggy Adler.

Alex isn't going anywhere. The internal transfer of interest just clears the way for his retirement years from now and gives our clients assurance of our commitment to the long-term continuity of the local ownership and management of the firm. The only thing that is changing is the internal ownership structure itself.

To that note, you recently received a communication (email/mail) from Summit explaining how we need your help in this process. We need our client's signatures to acknowledge this change. It is very important that you either sign the form digitally or return the mailed document to us as soon as you can. Please let us know if you have any questions about our plans or how to complete the forms. We thank you for your help and cooperation.

Thank you again for your continued confidence and trust as we work through these extraordinary times. We welcome your comments, questions, and referrals. Please don't hesitate to contact us and stay safe and well.

Summit Asset Management LLC