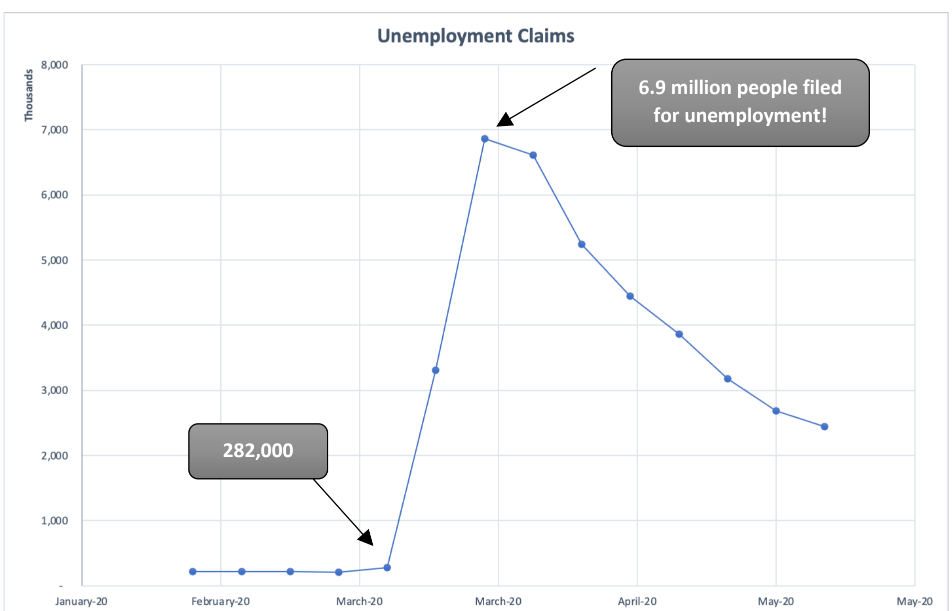
## 2020: A YEAR OF EXTREMES

What is the best way to sum up 2020? Strange? Anxiety-ridden? Tumultuous? How about “extreme”? In every facet of life -- dealing with a deadly pandemic, our home lives where both work and school have been confined to our houses, our political environment – the volume has been turned up to eleven. There has been nothing mild about these past 12 months, and the machinations of stock prices are consistent with such extreme behavior.

## WILD MARKETS

The COVID-19 crash last March caused significant damage to the stock market. Here is a look at that punishing period of trading, with some notable extremes:

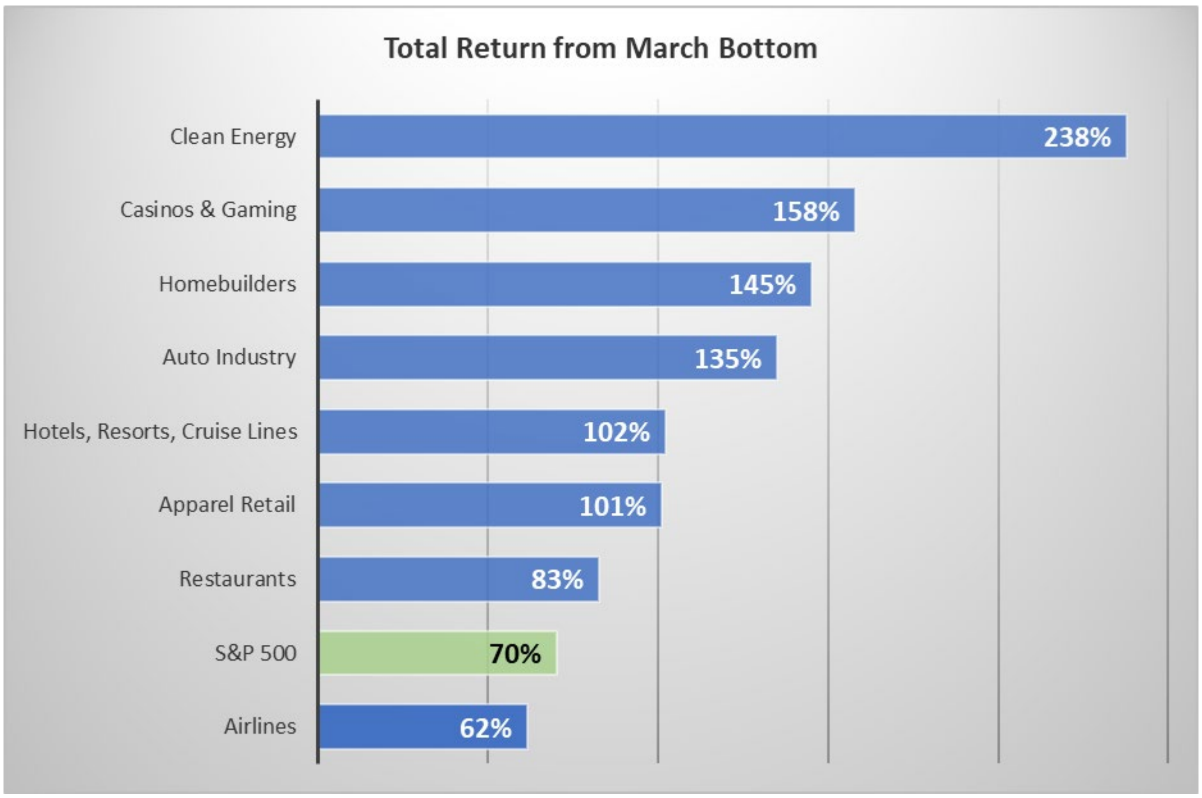
- On Monday, March 9, after a crushing overnight session in futures markets, the S&P 500 opened for trading and was halted for 15 minutes due to more than a 7% drop, eventually closing down 7.6% on that day
- Subsequently the market was halted three more times: March 12, March 16, and again in the afternoon of March 18, due to an intraday sell off greater than 7%. Stocks suffered losses of 10%, 12.9%, and 5% respectively on those days
- Since 1900, trading has only been halted on *four* other occasions:
    - July 31, 1914: as World War I broke out, the New York Stock Exchange effectively closed for four months
    - October 27, 1997: markets experienced a “mini-crash” due to an Asian banking and economic crisis (although stocks were only down 4.5% when trading was halted)
    - September 11, 2001: following the attacks on the World Trade Center and the Pentagon, markets were closed and not reopened until September 17
    - December 1, 2008: during the Great Recession as the threat of systemic bank failure started to become reality, trading was again halted
- Following the economic shutdown in March and April, unemployment skyrocketed virtually overnight. This dramatic graph shows the peak claims of nearly 7 million the week ending March 28 -- the same week that stocks bottomed.



- Oil prices collapsed due to an unprecedented dynamic. A glut in global supply was met with a steep drop in demand for oil as almost all transportation was grounded due to the pandemic; from the end of February to mid-April, the price of a barrel of crude oil dropped 60%
- The number of shares traded in March rose to levels never before seen. The volume of shares traded in SPY, the exchange traded fund (ETF) that tracks the S&P 500, rose to nearly six billion. That's a 200% increase over the average monthly volume traded, which in our estimate is roughly $1.6 trillion of valuation, in just one of the ETFs, over the span of only one month.

Clearly, investors and the broader economy suffered significant damage. The cluster of extremes during a 90-day period was historic. And this list is merely a sample of data, with little precedent.

Since the bottom in March the markets have experienced other extremes. Of particular interest, this chart shows the performance of the industries most affected by the pandemic:




With the exception of airlines, the share prices of the most economically sensitive industries not only performed well, but handily beat the broader market. Of course, these same industries were punished as the market collapsed. Air travel declined by 97% from July 2019 to April 2020.

This chart includes the index of clean energy stocks, whose returns were exceptional between March and December, as an extreme, or extraordinary, comparison.

**DATA DUMP**

A random list of other notable and thought-provoking data:

- Building permits for new construction hit a ten-year high of 1.64 million in November 2020, but were still down from the 2005 peak of 2.2 million and the all-time high of 2.4 million in January 1973

- The yield on a 10 Year U.S. Treasury was 0.93% on December 31, 2020, an all-time low; yields on that bond peaked at 14% in 1981

- Americans are either charging less or paying off credit cards faster; as of the end of September 2020, consumer debt accounted for a little more than 5% of disposable household income, down from a peak of 5.8% at the end of 2019, and down from the all-time high of 6.7% at the end of 2001, a positive trend

- 31% of wealth in the U.S. is held by 1% of Americans, which is down slightly from peak (31.4%) in 2016

- The Nasdaq market was up a massive 48.6% in 2020, with the S&P 500 up 18.4%. There has only been one other period in the past 20 years where the divide between the markets was greater, and that was 1999. That year the Nasdaq returned nearly 79% while the S&P 500 was up 14.4%. Interestingly, that was close to the top of the internet bubble, and the following year those markets returned -36% and -10.7% respectively.

- The final unemployment rate for the nation in 2020 was 6.7%; Nebraska and Vermont had the lowest unemployment rates at 3.1% each, while New Jersey ended the year with the highest rate at 10.2%, and Nevada and Hawaii tied for second worst at 10.1%

- Minimum wage rates, likely to come into focus under the Biden administration, range from the federal minimum of $7.25 an hour in 16 states, to $15 per hour for workers in the District of Columbia; here is a comparison of the highest and lowest states:

| State | Rate/Hour | State | Rate/Hour | Difference From Highest Rate |
|---|---|---|---|---|
| DC | $ 15.00 | FL | $ 8.65 | -42% |
| WA | $ 13.69 | MT | $ 8.75 | -42% |
| MA | $ 13.50 | WV | $ 8.75 | -42% |
| CA | $ 13.00 | OH | $ 8.80 | -41% |
| NY | $ 12.50 | NV | $ 9.00 | -40% |
| CO | $ 12.32 | NE | $ 9.00 | -40% |

- The pandemic actually accelerated growth in some areas of the economy, a pull forward effect where expected future sales of a product occur sooner, in a more condensed time frame. Online retail exploded, with some estimates showing ten years' worth of growth in the 90 days from March through May.

- Online sales account for almost $210 billion worth of goods sold annually, though this is still only 14% of total retail sales ($1.47 trillion as of November 2020)

- Consumption of alcoholic beverages has been steadily increasing the past few years, as the popularity of micro-brews, tequilas, premium bourbon, and other types of drinks has grown. We are in the midst of a surge in alcohol sales online: sales in 2020 were close to $5.6 billion, an 87% increase from the prior year.

- Recreational vehicle (RV) sales have soared recently. In 2020, despite a near-complete industry shutdown for two months due to the pandemic, sales are expected to top 400,000 vehicles. 2021 sales are expected to be at least 500,000, a 25% increase. In the past five years, sales of RVs are up nearly 52%. Shares of Winnebago (symbol: WGO) were up 14.2% in 2020 after a monstrous 122% return in 2019.

- And finally, according to the Social Security Administration, the most popular names for babies born in 2020 were Olivia for girls and Liam for boys, compared to the 1990s when Jessica and Michael were most prevalent. We want to see if you're still paying attention!

## INFLATING A BUBBLE

Robinhood is a wildly popular app that allows investors to easily open investment accounts and make trades commission free. It has become somewhat of a phenomenon with younger people, and there are websites dedicated to highlighting what users have been trading, which has had the effect of stratospherically increase the share price of little known or followed public companies. The app was launched in March 2015 with approximately 700,000 users. Those ranks have swelled to more than 13 million today. The financial media believes the pandemic, which temporarily halted professional sports (and consequently curtailed fantasy sports and sports betting) , opened the door for Robinhood to step in as a substitute for such activities.

As with any disruptive service or technology, there are unintended consequences. In the long term, we believe Robinhood's ability to capture a new slate of investors is a good thing. This disruption has also forced the largest brokerages – Fidelity, Schwab, TD Ameritrade – to offer commission-free trading as well. With little to curb trading behavior, liquidity has skyrocketed, as we indicated earlier. The unintended consequences, though, are excess buying and selling of shares and less "investing"; speculative behavior is nearing an extreme. History may not always repeat, but it does rhyme, and what we are currently experiencing in the stock market is eerily similar to the 1999 internet hysteria.

Should we be concerned? Speculative bubbles never deflate in an orderly fashion. However, they are historically confined to one particular sector or industry. Our research - based upon fundamentals in underlying businesses that comprise the market, the relative attractiveness of stocks versus bonds, and investor sentiment - is flashing a warning sign. Stocks are expensive, but relative to bonds we still see pockets of value.

## OUR FINAL POINT…

…regarding investor behavior, is concerning. By almost every measure we see excessive optimism toward stocks. We would welcome a market pull back and some investor humility. Our experience has informed our philosophy – moderation in investing is key. As Warren Buffett once said, "There is nothing wrong with a 'know nothing' investor who realizes it. The problem is when you are a 'know nothing' investor but you think you know something."