Integer Wealth Advisors Group, LLC

Advise, Guide and Protect

Fourth Quarter 2020 Market Commentary

We start every market commentary by highlighting an observation from our previous commentary. We were almost on the mark with the following observation from last quarter:

We are also entering the last days of the most contentious political battles ever waged in modern history. It is highly probable that the results of the election will not be known for weeks or months, and the results could end up in the courts, and civil unrest continue. This will put a short-term pall on the markets even during what is usually a positive time during the holiday season. So, do not be surprised if we see a short-term market slump as a result.

Maybe contentious was not strong enough! And the market took a slight dip between November 3rd and November 29th with the Dow dipping 3%. Not a drop mind you, just a little dip as concerns about President Trump not leaving peacefully were floated around Washington. Thankfully, this does not appear to be the case and on January 20th, President-Elect Joe Biden and Vice-President Elect Kamala Harris become our new leaders.

As we go to press with this commentary the Georgia Senate races are still to be decided. For those of us living in Georgia, we cannot wait for the races to conclude so we can start watching television again without recording everything to avoid the ubiquitous political ads! How the two remaining Senate seats go will have an impact on the markets, and not in ways you would normally consider. Should the seats both go to the Democrats, the feeling is that this will be a positive for the markets because of the prolific spending that will be unleashed, despite the elimination of Trump tax cuts. On that subject it will be difficult for Democrats to do a wholesale rollback on the tax cuts since virtually everyone received a benefit due to the "jiggering" of the tax brackets.

While spending will be a short-term "sugar high," the theory is that the spending will travel from consumer to businesses. How long the high lasts will be dependent upon the mid-term elections. Recall that only one of the Georgia seats is for a remaining two-year term as former Senator Johnny Isakson was slated to go until 2022, and the remaining cycle of nationwide Senate seats will be up as well. If the tax increases are implemented, it will be hard for a Senator that supported a rise in taxes to defend his/her seat, especially one that will serve only a two-year term. Assuming a razor-thin majority by the Democrats, they must calculate how well they will do in mid-term elections with a tax-hike on their resume.

Meanwhile, should the seats be split, the Republicans will retain a majority, albeit a slim one, and can possibly "run out the clock" by blocking the Biden Administration's spending and taxation plans until the mid-term elections in two years. However, with a similar thin majority, Majority Leader McConnell will have to deal hard with his members in the event one or two of them defect on proposed legislation. The slight edge in the Senate will help those wishing to hold the line on tax increases which would be a positive for the markets.

What then are the negatives? Like we said before, Wall Street cares not about the occupants of 1600 Pennsylvania Avenue, but about the rules of the game. Markets are driven by profits, by deal making, and by innovation. They could be restrained by over-cumbersome regulations and higher taxes. Given that we are far from over the pandemic, it seems hard to believe that the new Administration would want to immediately move to raise taxes, as it would be counterproductive and hurt economic activity. Better to do some targeted rollbacks such as the SALT limitations than a wholesale revision of the tax code and to remember the following headline below:

Looking Forward – "It's the Pandemic, Stupid" and 2023 Tax Increases

We kept part of this headline in from last quarter because it really has been "the pandemic, stupid." We hope the incoming Administration will provide even more focus on the subject matter and continue programs like "Operation Warp Speed" to get the vaccines out even faster, and to continue more production. Before President-

Elect Biden starts chopping at the previous Administration's work, his singular focus needs to be the pandemic, period. If he wants to heal the nation and bring people together, let us get this thing under control and eliminated by the summer. Then let the economy get back to a normal level of activity. In fact, if we can get to "herd immunity" levels of 90%, and the economy is free to open, the growth of GDP will be immense. Getting to 90% means sometime next Fall at best.

Tax Hikes in 2023

Assuming the Biden Administration heeds our suggestion for singular focus on Covid-19, they can consider raising taxes in 2023. Why? First, once the economy reopens fully the level of pent-up demand will be enormous, unleashing a growth in GDP that will be percentage points above anticipated levels. Second, the 2022 mid-terms could give Biden the firepower he may need should the 2021 Georgia runoffs go the way of the Republicans. And finally, in 2023 the Fed would be free of their promise not to raise interest rates but would not have to do so with the Biden Administration doing their part on the fiscal side (namely raising taxes).

Therefore, the Biden Administration can think about tax increases in 2023 when people are flush with cash and have sated their appetite for travel and spending, and the 2022 mid-term elections are completed. The mistake would be to try and satisfy his more left-leaning colleagues because of their disdain for the previous Administration by implementing tax increases on Day One. That would be a disaster for the nation and would jeopardize the Democrats in the 2022 mid-terms.

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DOMESTIC EQUITY STATISTICS

Index	Past Three Months Thru 12.31.2020
S&P Small Cap	30.8%
S&P Technology Sector	11.52%
MSCI EAFE Index	16.27%
Dow Jones Average	10.17%
S&P 500 Index	11.69%

(Period Ending 12/31/2020. Source: S&P Dow Jones Price Weighted Indices)

SECTOR	PERCENTAGE WEIGHT	Past Three Months Thru 12.31.2020	Full Year Returns
S&P 500		11.69%	16.26%
Energy	2.3%	26.34%	-36.46%
Materials	2.6%	13.92%	18.1%
Industrials	8.4%	15.19%	9.01%
Consumer Discretionary	12.7%	9.43%	28.3%
Consumer Staples	6.5%	5.44%	7.2%
Health Care	13.5%	7.55%	11.43%
Financials	10.4%	22.52%	-4.1%
Info. Technology	27.6%	11.52%	42.21%
Communication Services	10.8%	12.08%	36%
Utilities	2.8%	5.7%	-2.83%
Real Estate	2.4%	4.09%	-5.17%

Source: Standard and Poor's (www.spindices.com), price returns as of 12/31/2020.

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Style Return Box 4Q 2020

	VALUE	CORE	GROWTH
LARGE	14.44%	11.69%	10.62%
MID	28.62%	23.93%	20.99%
SMALL	32.92%	30.83%	29.74%

Source: Morningstar, Price Returns 12/31/2020

Domestic Markets

It was a powerful fourth quarter that finally put the Dow, S&P 500, and Nasdaq at all-time highs. The Dow finished at 30,606, the S&P 500 finished at 3,756 and the Nasdaq finished as 12,888. From the chart above you can see that it was a great quarter for all types and sizes. What is notable, however, is that the value side of the ledger finally outperformed the growth side, something we have not seen in years.

Several things combined to drive value-oriented stocks higher. First, there is the wide chasm that was performance in 2020. Growth was beating Value by 25-30% during the year and that is something not seen before in the markets. Investors recognized that and starting a rotation into the cheaper areas of the market. The second item that really lit the fire on value stocks was the pronouncement that banks, starting in the first quarter of 2021, could buy back their stock. The stress tests conducted by the Fed were so stringent that even in the worst possible economic environment imaginable, the banks had sufficient capital. That news sent bank stocks, which are found in the value sector, soaring.

Domestically there was not a lot to report about for the general economy because of the continuing Covid-19 pandemic. GDP rebounded in the third quarter as expected but with the re-emergence of increased infections, and the PPP stimulus programs shutting down, there was little to cheer about for the economy. Despite the gloomy outlook, vaccines began shipping out which gave the markets a "shot in the arm" as a possible end to the pandemic sometime next year. That was good enough news for

investors to start back into the market to power the Dow 15% higher over the November-December stretch.

With the forward-looking good news of vaccines rolling out across the country and the eventual expansion in economic activity, what could go wrong? Investors are, if nothing else, always climbing a wall of worry. So instead of trying to fight the wall of worry, we thought we would repeat a message from last quarter.

This Bears Repeating

Sometimes you write something so prophetic that it just must be repeated for good emphasis. We mention this again because we all know we are bound for a pullback. It is how the markets work. But with March 2020 so fresh in our memories, and with Covid-19 beating us about the brainbox, the following needs to be presented once again. So here we go with the emphasis on "you cannot time the markets." Early last year we mentioned the difficulty of staying fully invested when the markets are volatile. We highlighted the chart below in a previous commentary. The chart reflects the impact to an investor's return if they miss the best 10 days of a decade.

Given the environment we are moving into, namely the elections, we think it is timely to show this chart again, especially as investors consider tactical changes to their portfolios. Tactical allocation, meaning the weightings assigned within a portfolio, can move around as conditions dictate. This is different from being "all in, or all out" of the market via market-timing. An investor may wish to overweight technology as an example, but not to the abandonment of all other classes.

Excluding the 10 best days of performance per decade for the S&P 500 drastically cuts down returns

Decade	Price Return	Excluding Best 10D Per Decade
1930	-42%	-79%
1940	35%	-14%
1950	257%	167%
1960	54%	14%
1970	17%	-20%
1980	227%	108%
1990	316%	186%
2000	-24%	-62%
2010*	161%	75%
Since 1930	13,445%	72%

* 2010 Decade as of August 19, 2019.
Source: BofA Merrill Lynch Global Research. Data as of August 19, 2019.
It is not possible to invest directly in an index. **Past performance is no guarantee of future results.**
Please refer to the end of this presentation for index descriptions.

International Markets

We continue to favor the domestic US stock market but have a less harsh sentiment on international markets. The rationale here centers on the blooming deficit spending the United States is embarking on in support of the economy. With a lot of liquidity sloshing around in the world, and with the international markets perennially behind the United States, having some increased exposure to the international markets is warranted. Besides, after 10-years of relative underperformance to the domestic US markets, you must assume there will be a turn for the better internationally. We can comfortably see portfolio exposure of 20% to the international and emerging markets collectively.

With the dollar weakened against the Euro and the Pound, dollars invested in overseas markets have the additional boost of the exchange rate helping the local foreign currency. Leaving aside the issue of currency exchange (let the mutual fund or ETF handle that), a USD investment internationally has the advantage of the growth

of the investment and the growth of the exchange. Aside from those two elements, the international markets have some exceptionally nice yields. The iShares Core MSCI Emerging Markets ETF sports a 2.8% yield, while the iShares Core MSCI EAFA ETF provides a 2.7% yield. The S&P 500, on the other hand, provides a 1.57% yield. For investors looking for a little more income in the portfolio, the international markets provide a nice yield.

This has been about as nice as we have spoken about the international markets in quite some time. We have always had international exposure in client portfolios, we are just boosting the percentage a bit more for those who have the same sentiment on diversification. The last period that international outperformed the domestic market was the stretch from 2000-2010. Since that time, we have underweighted international relative to the domestic market. To be clear, our preference is still the US market, but we can see the rationale for a bit more international to be placed in the portfolio.

Fixed Income

Nothing new to speak about regarding fixed income. Yields are low and are expected to stay there until around 2023 (according to Jerome Powell, the Fed Chairman). The low interest rates explain a great deal about why the Dow has recently hit 30,000, there is no money to be made in fixed income. Then why have it in a portfolio?

Cushion. That is the main reason why you have fixed income in a portfolio. You may not appreciate it when the Dow is cruising past crooked numbers like Usain Bolt in the 100-meter dash. But when the market decides to pullback (aka March of 2020) bonds are a genuinely nice cushion to have in your portfolio. The secret to owning bonds is to understand two especially important elements: duration and quality.

Duration is the way you calculate the risk in the bond you own. For example, take the 10-Year Treasury yielding 0.90%. That is right, 0.90% which means you give the government $1,000 and they pay you $9 per year. The duration of a newly minted 10-year Treasury is basically 10-years. The risk in ownership is if interest rates move

higher. For example, if interest rates rose 1% overnight, you would lose approximately 10% in the value of the Treasury bond. And with interest rates at historically low levels, interest rates have nowhere to go, eventually, but higher. The secret here is to keep your duration short, like 4-5 years, so that the move in rates does not wipe out the interest payments.

The second item is quality. Top-tier quality are Treasury bonds, bottom-tier quality would be a bond issued by your local used car lot. Top-tier pays less, bottom-tier pays more. Right now, you can be paid wonderfully for owning the used car lot bond while the United States pays you little. Which one do you want to own when the bottom drops out of the market? That is right, you want Treasuries, which is what everyone was clambering for back in March of 2020.

So, in the fixed income department we continue, as we have for years, to recommend short duration, high quality bond funds. You are free to mix in a bit of short-term high yield, but do not over do the recipe.

Looking Forward

Everyone likes to polish up the crystal ball to try and see what is in our future. We must admit that we used to have a crystal ball in our office just for fun but abandoned it many years ago. Seems that it was always giving us the answer "it depends" when we asked for insights and wisdom. We do not believe it takes a crystal ball to see the immediate future, just look to the two main events occurring over the next six months to get an idea of what lies ahead. The first is the eradication of the Covid-19 virus or the achievement of herd immunity that will allow us to fully re-open the economy to normal activity. Human behavior will not be the same for many years to come, if ever in the current lifetime. Expect masks to be the newest fashion trend and let us not "mask shame" people who decide to wear one when the pandemic is behind us. If nothing else, it sure helped reduce the flu!

The second will be the economic policies of the new administration. At the time of this writing, we do not know who will control the Senate, and it may be weeks before

we know the outcome. If the Republicans should hold the majority, it will be politics like we have not seen before as President Biden will have to go to the "phone and pen" like his previous boss did.

Should the Democrats take control, and this is with no animosity toward the Democrats, expect a market drop on the anticipation of higher taxes and prolific spending. And like most market drops, it will be temporary since the market always finds a bottom and begins the rebuilding process. We find it hard to imagine that the Democrats, should they gain power, would enact tax increases during a pandemic. The playbook is clear in these instances…liquidity, liquidity, and liquidity. Get the economy moving and the virus under control, then we can discuss new fiscal policies.

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