GIA PARTNERS

4th Quarter 2020

Highlights

- **Financial markets had another excellent quarter, boosted by encouraging vaccine news. "Risk on" prevailed even though interest rates ticked higher. Our portfolios outperformed their benchmarks;**
- **Mounting infections put the brakes on the economy's 3Q momentum. Consumers continued to spend, yet employment suffered. The outlook for early 2021 dimmed even with more government aid;**
- **Many assets delivered remarkable performance in 2020, including cryptocurrencies. While we believe these have earned legitimacy, their utility may not warrant their valuations.**

Markets

		Returns (%)			
GIA*	Average Quality	4Q20 Gross	4Q20 Net	12 Months Gross	12 Months Net
Core Plus Composite	**(A)**	**3.07**	**2.98**	**9.05**	**8.67**
Global Credit Plus Composite	**(A-)**	**3.56**	**3.43**	**9.31**	**8.76**
High Yield Composite	**(B+)**	**9.22**	**9.07**	**5.56**	**4.98**
Emerging Market Corporate Debt Composite	**(BB+)**	**7.62**	**7.45**	**6.72**	**6.09**
Benchmark Bonds					
Bloomberg Barclay's U.S. Agg. Index	(AA+)	0.67		7.51	
Treasury	(AAA)	-0.83		8.00	
Corporate	(A)	3.05		9.89	
Mortgage	(AAA)	0.24		3.87	
Government/Credit	(AA)	0.82		8.93	
ICE BofA U.S. Corporate & Yankees	(A-)	2.73		9.46	
ICE BofA U.S. Corporate	(A-)	2.99		9.81	
ICE BofA U.S. High Yield	(B+)	6.48		6.17	
ICE BofA EM Corporate Plus	(BBB)	4.05		7.52	
ICE BofA Global Gov't ex-US	(AA-)	4.30		9.80	
JPM Emerging Markets EMBI GD	(BB+)	5.80		5.26	
JPM CEMBI Broad Diversified	(BBB-)	4.44		7.13	
JPM GBI-EM Global Diversified	(BBB)	9.62		2.69	
Benchmark Equities					
S&P 500	NA	11.69		16.26	
Nasdaq Composite	NA	15.41		43.64	
Russell 2000	NA	30.99		18.36	
MSCI EAFE	NA	15.75		5.43	
MSCI Europe	NA	15.23		3.02	
MSCI Japan	NA	15.10		12.37	
MSCI Emerging Markets Equity	NA	19.34		15.84	

* Please refer to the respective factsheets for the long-term composite and benchmark returns for each strategy.

Markets

What a year, and what a quarter! The final chapter on the pandemic has not been written, although financial markets presage a happy ending. Consistent with the year's paradoxes, the worst quarter for infections was accompanied by several record high equity closes and a decisively "risk-on" attitude. During the quarter, a tumultuous presidential election was accompanied by the approval (and initial application) of effective COVID-19 vaccines, a new stimulus package and persistent central bank support. By the close of a year most of the world would like to forget, U.S. equity markets forged ahead with the Nasdaq Composite up a staggering 43.64%, the S&P 500 up 16.26%, marginally off its record high and the Dow up 7.23%. Worldwide, investors gladly took central bank liquidity and parlayed it into impressive results, especially given constrained economic performance and historically low interest rates. Global stocks were up 14.06% with emerging market equities contributing 15.84%. European stocks underperformed, yet delivered 3.02% returns in dollars as the U.S. currency devalued. Even bond markets posted healthy returns on the heels of central bank monetary stimulus. Credit markets, commodities, housing and even crypto currencies rose. Perhaps the only laggard was the U.S. dollar, and that was a function of the Fed's aggressive support for the U.S. economy and, by extension, the world.

Investment grade credit had another good quarter driven by supportive investor flows and the Fed's liquidity back-stop. Even discontinuation of the Fed's primary and secondary market support facilities did not dent demand. With bond markets flush in liquidity, companies continued to borrow at a record pace to refinance near term maturities and lower their borrowing costs. The investment grade corporate bond index, the ICE BofA U.S. Corporate Index (C0A0), was up 2.99% in fourth quarter and 9.81% in 2020. By comparison, the U.S. treasury index returned -0.91% for the quarter and 8.22% for the year. Corporate option adjusted spreads (OAS) narrowed by 40 b.p. to 103 b.p., while the yield to worst of the index declined from 2.03% to 1.78%. The big story in investment grade credit continued to be issuance. Following record months soon after the lockdowns, and relentless volumes thereafter, 2020 borrowing shattered the previous record. For the quarter investment grade companies issued $267.2 billion in public markets taking the year's total to $2.102 trillion, surpassing 2017's $1.47 trillion by over $600 billion.

The high yield market had an excellent quarter despite renewed infections and further restrictions on travel and leisure. With economic data holding up and stressed companies finding ways to stay afloat, the demand for yield propelled the sector higher. The ICE BofA U.S High Yield Index (H0A0) was up 6.48% for the quarter, which finally brought the sector's returns into positive numbers. For all of 2020, the index was up 6.18%. Energy, the largest industry in the index, had an outstanding quarter with a 13.38% return, but still posted a -6.62% fall for the year following the challenging first quarter and a rash of bankruptcies. Spreads to worst narrowed by 151 b.p. from 539 b.p. to 388 b.p., while the yield to worst decreased from 5.70% to 4.21%. High yield retail investors added $8.3 billion during the quarter, completing a volatile, but healthy, inflow of $44.3 billion for the year. The default rate increased to 6.2% in December from 5.8% in September (6.76% including distressed exchanges). For the year, $129.6 billion of bonds defaulted, led by $49.1 billion in energy-related insolvencies. Away from energy, previously distressed telecom and retail added to the tally. Like investment grade, the new issue market remained lively with $99.6 billion pricing during the quarter. The full year marked an annual record at $449.5 billion, well in excess of 2019's $286.6 billion and the sector's prior record of $398.5 billion in 2013.

Emerging markets continued to suffer varying degrees of COVID-19-related damage. Away from China, which achieved successful containment as the rest of the world succumbed, countries were forced to withstand painful economic damage and healthcare emergencies. On the bright side, lower rates, abundant global liquidity and support mechanisms from global central banks helped ease the financial pain. Also, renewed demand from China pushed commodity prices higher aiding exporters of grains, metals and energy. Investors returned money to the sector boosting returns for the quarter, although not enough to outperform other fixed income markets. For the quarter, the JPM Emerging Markets Bond Index – Global Diversified (EMBIGD), a dollar denominated sovereign index, was up 5.80% and for the year was up 5.26%. The JPM Corporate Emerging Markets Broad Diversified Index (CEMBI BD) improved 4.44% for the quarter and gained 7.13% in 2020. The JPM Global Bond Index – Emerging Markets Global Diversified (GBI-EM Global Diversified), a local markets index jumped 9.62% for the quarter, yet was held to only 2.69% for the year.

Economy

Not surprisingly, economic analysis for 2020 revolved around measuring the impact of COVID-19. By year-end certain adjustments became evident and logical, although capturing consumer behavior remained as intractable as ever. Lockdowns and restrictions in the face of infection resurgence continued to delay recovery in many service-related industries, postponing the earlier-expected fourth quarter bounce. However, shifts in consumer behavior, along with elevated savings, provided an unexpected boost to global manufacturing. In addition, low interest rates and fiscal aid packages enabled consumers to purchase homes, autos and other capital goods. The shift from services to goods provided a welcome assist to the global economy in 2020, although we think its sustainability throughout 2021 looks questionable.

Financial markets closed the year on a positive note, boosted by the approval and initial application of vaccines. In addition, congress approved a new $900 billion relief package that extended unemployment benefits, provided cash to lower income individuals and families, added money for vaccine distribution and offered additional assistance to small businesses. While this legislation arrived too late to boost fourth quarter activity, economists lifted their first quarter 2021 numbers as a result. A few conclusions became evident as 2020 ended. The world expects vaccines to arrest the pandemic by mid-2021 and “normality” to return in the second half of the year. While those expectations seem logical, their widespread acceptance becomes a source of caution because negative surprises have featured prominently in this crisis.

It appears U.S. GDP will decline approximately -3% to -4% in 2020, a welcome result compared to the -6% or more forecast as the pandemic began. Europe will likely decline more although the region, like much of the world, will witness broad disparity between countries. Emerging economies will be the hardest hit, collapsing between 7% and 10% due to a more limited capacity to control the virus and provide fiscal support. China will be the only major country showing respectable growth (around 2%), although that too falls well below the country’s potential. Altogether, the world will suffer the worst decline in over 70 years. The key question becomes how soon do we recover?

For the U.S., economists responding to the WSJ December Economic Survey expect, on average, a 2.7% decline in 2020 followed by a 3.7% recovery in 2021 leading to a recapture of 2019 output by the end of this year. Away from them, in October reports, the IMF presented a weaker outlook that left world output down around -4.4% for 2020. By their projections, even a robust recovery of 5.2% in 2021 would still leave global GDP well below 2019’s year-end level.

Scenarios

We propose three scenarios for the U.S. economy over the next 6 months:

1. Our most likely case has the economy growing about 2.0% at an annual rate in 1Q, and accelerating to a 4.0% rate in 2Q 2021. 2020’s third quarter U.S. GDP exceeded most expectations, and the fourth quarter appears to be defying downwardly revised forecasts. However, with slow vaccinations and further drag from prolonged restrictions, the economy will likely slow in 1Q 2021. Even the recent stimulus package will only prevent an outright contraction because, instead of incentivizing employment, much of the money just keeps the currently unemployed afloat. Recent employment data confirmed the damage from the latest infection wave and that wave will not likely end until the second quarter. The rest of the world is in the same boat, fighting mounting infections while vaccinating as quickly as possible. Results should improve by April or May, with a big economic boost likely over the summer. PROBABILITY 60%

2. A second scenario has the economy deteriorating due to a losing battle between mounting infections and vaccinations. The recently passed stimulus may keep the economy from collapsing, but consumers may moderate their purchases of higher ticket items as debilitating restrictions drag on. Furthermore, the incoming

administration's stimulus plans may face resistance and take longer than expected to become law. In the meantime, unemployment may rise causing the economy additional stress. In this scenario, similarly affected regions like Europe and Latin America also struggle to contain the jump in infections. With decelerating momentum from 4Q, the global economy struggles to register any growth in 1Q. The U.S. turns in a near-zero growth first quarter and experiences a muted 2% to 3% recovery in 2Q. PROBABILITY 20%

3. A third scenario has the economy recovering faster than expected as favorable events come together. The third wave crests in January and is accompanied by accelerating and effective vaccinations. In addition, the Biden administration passes an additional stimulus package that puts money directly in people's accounts for rapid spending. In this scenario, 1Q GDP is boosted to about 3% at an annual rate with the momentum and renewed consumer confidence taking the second quarter to a 5.0% or better result. PROBABILITY 20%

Market Outlook

The incongruity of stellar financial market performance in a global economy racked by a health pandemic can only be squared by assistance from monetary and fiscal authorities. While the world appears to be on a path to conquer the virus, asset valuations rely on two critical assumptions: 1) the vaccines will successfully mitigate COVID-19 by around mid-2021, and 2) fiscal and monetary policy support will remain forthcoming and effective. Although we often prefer to disagree with broad-based consensus, we fall solidly with the crowd and, therefore, retain a preference for higher risk positioning in the portfolios. The "carry trade" continues to make sense in fixed income as long as the Fed continues to subsidize rates, which must occur to enable massive fiscal spending. In time, the U.S. Treasury's absolute level of debt and the Fed's ownership share of that debt will become a challenge. As long as the world remains gripped by the virus, these stimulus efforts will be welcomed by financial markets. For now, the overarching priority remains to control the virus.

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Important Information

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Index Definitions

Bloomberg Barclays U.S. Aggregate Index
The Barclays U.S. Aggregate Index represents securities that are SEC-registered, taxable, and dollar denominated. The index covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities. These major sectors are subdivided into more specific indices that are calculated and reported on a regular basis.

Bloomberg Barclays U.S. Treasury Index
This index is the U.S. Treasury component of the U.S. Government index. Public obligations of the U.S. Treasury with a remaining maturity of one year or more.

Bloomberg Barclays U.S. Government/Credit Index
The Government/Credit Index includes securities in the Government and Credit Indices. The Government Index includes treasuries and agencies. The Credit Index includes publicly issued U.S. corporate and foreign debentures and secured notes that meet specified maturity, liquidity, and quality requirements.

Bloomberg Barclays U.S. Credit Index
This index is the U.S. Credit component of the U.S. Government/Credit index. Publicly issued U.S. corporate and specified foreign debentures and secured notes that meet the specified maturity, liquidity, and quality requirements. To qualify, bonds must be SEC-registered.

Bloomberg Barclays U.S. Mortgage Backed Securities Index
This index is the U.S. MBS component of the U.S. Aggregate index. The MBS Index covers the mortgage-backed pass-through securities of Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC).

ICE BofA U.S. Corporate & Yankees Index
The ICE BofA U.S. Corporate & Yankees Index tracks the performance of US dollar denominated investment grade debt publicly issued in the US domestic market by US and non-US corporations and non-US quasi-governments.

ICE BofA U.S. Corporate Index
The ICE BofA U.S. Corporate Index tracks the performance of US dollar denominated investment grade corporate debt publicly issued in the US domestic market. Qualifying securities must have an investment grade rating (based on an average of Moody's, S&P and Fitch) and an investment grade rated country of risk (based on an average of Moody's, S&P and Fitch foreign currency long term sovereign debt ratings).

ICE BofA U.S. High Yield Index
The ICE BofA U.S. High Yield Index tracks the performance of below investment grade US dollar-denominated corporate bonds publicly issued in the US domestic market.

ICE BofA Global Government Excluding the U.S. Index (N0G1)
The ICE BofA Global Government Excluding the U.S. Index tracks the performance of publicly issued investment grade sovereign debt denominated in the issuer's own domestic currency. N0G1 excludes U.S. government bonds.

JP Morgan Corporate Emerging Markets Bond Index Broad Diversified (CEMBI Broad Diversified)
The CEMBI tracks total returns of US dollar-denominated debt instruments issued by corporate entities in Emerging Markets countries. Two variations are available: CEMBI Broad and CEMBI. The CEMBI Broad is the most comprehensive corporate benchmark followed by the CEMBI, which consists of an investable universe of corporate bonds. The CEMBI Broad Diversified limits the weights of those index countries with larger corporate debt stocks by only including a specified portion of these countries' eligible current face amounts of debt outstanding.

JP Morgan EMBI+ Index
The EMBI+ tracks total returns for U.S-dollar-denominated debt instruments of the emerging markets: Brady bonds, loans, Eurobonds. The EMBI+ currently covers 104 instruments across 15 countries.

JP Morgan Government Bond Index-Emerging Markets (GBI-EM)
The GBI-EM is the first comprehensive, global local Emerging Markets index, and consists of regularly traded, liquid fixed-rate, domestic currency government bonds to which international investors can gain exposure. Variations of the index are available to allow investors to select the most appropriate benchmark for their objectives.

S&P 500 Index
An index of 500 stocks chosen for market size, liquidity and industry grouping, among other factors. The S&P 500 is designed to be a leading indicator of U.S. equities and is meant to reflect the risk/return characteristics of the large cap universe.

Nasdaq Composite Index
An index that tracks the change in the total market value of all companies listed on the Nasdaq Stock Market.

Russell 2000 Index
An index measuring the performance of the 2,000 smallest companies in the Russell 3000 Index, which is made up of 3,000 of the biggest U.S. stocks. The Russell 2000 serves as a benchmark for small cap stocks in the United States.

MSCI EAFE Index
The index is a capitalization weighted index that monitors the performance of stocks from Europe, Australasia and the Far East.

MSCI Europe Index
The index is a free-float weighted equity index measuring the performance of Europe Developed Markets.
MSCI Japan Index

The index is a The MSCI Japan Index is a free-float weighted equity JPY index.

MSCI Emerging Markets Equity

The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets.