Investment Insights

2021 MARKET OUTLOOK

Editor’s note: The following is an edited transcript of a December 17, 2020, Investments & Wealth Institute Exceptional Advisor (EA) Webinar focused on insights about 2021. Participants were three Investments & Wealth Institute board members: Chair Todd Wagenberg, CIMA®, managing partner, Integrated Fiduciary Advisory Services; Treasurer Scott Welch, CIMA®, chief investment officer–model portfolios, WisdomTree Asset Management; and Board Member Brian Ullsperger, CIMA®, managing director, Andersen Investment Advisory. Investments & Wealth Monitor Editorial Advisory Board Chair Tony Davidow, CIMA®, president of T. Davidow Consulting, moderated the discussion.

This discussion builds on a previous EA Webinar held in May 2020; read an edited transcript in “Extraordinary Times: Managing Market Volatility and Engaging with Clients,” Investments & Wealth Monitor (May/June 2020): 59–64.

Davidow: We’re finishing a challenging 2020, and a lot of new things are on the horizon for 2021. I’ve asked Brian, Scott, and Todd to talk about the things they’re focused on in 2021.

Ullsperger: I think about what we can control in portfolios, first and foremost. We can manage risk through asset allocation and rebalancing. Right now, we are speaking with managers, reviewing the asset allocation, tactical opportunities, style (growth vs. value), and adding alternatives to create more consistency. And we’re always thinking about taxes.

As we go through a change to the Biden administration, we may have new tax policies to address. So, we’re trying to minimize taxes where we can. We could have some opportunities in terms of fixed income—higher tax rates could benefit municipal bonds. With fixed income, the biggest challenge we’re facing, for the second time in my career, is interest rates at zero. We’re trying to identify where we can get yield, without having to take excess risk.

COVID was unforeseen, but we should always be thinking about events around the corner. How many people will get vaccinated? Will there be a government stimulus package? How big will it be? Will we re-engage with the world and our relationships with allies? And then there’s China—that’s a big question mark. As the United States has retrenched over the past four years, China has taken the stage as, maybe, the dominant superpower. It’s going to be interesting to see how we re-engage with China.

Davidow: Scott, what’s on the top of your mind?

Welch: I tried to break it into two parts: signals and noise. Signals are those things that drive market performance: (1) economic growth, (2) earnings growth, (3) interest rates, (4) inflation, and (5) central bank policy.

The second list is “noise” or “known unknowns”—the things we know are on the horizon that may affect our outlook, but about which we don’t have current clarity.

Today’s “known unknowns” include the continued evolution of the coronavirus, the rollout of vaccinations, fiscal stimulus, and the effects of new taxes and regulations.

With the announcement of the Pfizer vaccine after the election, we saw a massive cyclical rotation back into small-cap and value stocks. So another “known unknown” is whether that rotation has legs, or is it just a momentary phenomenon?

A final “known unknown” is geopolitics. Where will we move with China, Iran, Russia, and so forth?

Davidow: We have tension with China, Iran, and in the Middle East, all of which could have an effect on our outlook and how we position our portfolios.
**Wagenberg:** I look at it in terms of what I think I need to be concerned about or what my clients need to be concerned about. What is at risk within the portfolios of my clients and how will each one of these things affect them? I have an idea of either this happens or that happens, and that helps me to set expectations for clients.

I’d be willing to gamble that capital gains rates will not go down. I would also be willing to say that the exemption from estate taxes is not going higher than the current exclusion number. We’ve spent the past six weeks trying to cram everything in, making sure irrevocable trusts are funded, and the fact is that you have a $23-million exemption for a married couple or exclusion, so you want to make sure that you take full advantage of that while you can.

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So, we look at what’s going on now and what could happen, and have taken full advantage. At the end of the day, my list is not that different from Brian’s or Scott’s. It’s more about managing the risks you have right now and trying to identify where the opportunity is going to come from.

**Davidow:** Todd, I recall we discussed whether you were telling clients anything different during the downturn, and you said you were trying to bring your clients back to basics.

**Wagenberg:** Yes, you have to help clients trust the planning that’s in place. That’s why we have an investment policy statement and an asset allocation, so when things get crazy, you have a touchstone to rebalance back to. Quite frankly, it reduces your ability to mess it up by overthinking. As advisors, people expect us to know what’s going to happen, and we don’t know what’s going to happen. We do know that a solid plan and rebalancing portfolios works in the long run, creates these compounded rates of return, which is all we can really hope for.

**Davidow:** Sound advice. Scott, what did we learn last year?

**Welch:** Perhaps most importantly I learned that I am an optimist. As bad as it got, I always believed things would eventually get better.

What that translates into from a portfolio management perspective is patience. When the markets tanked in the early spring, we tried to identify different ways that advisors could still add value—things like tax-loss harvesting, rebalancing, swapping from mutual funds to ETFs [exchange-traded funds] for cost and tax purposes, or maybe getting out of some long-standing positions that had built up huge gains.

In our own model portfolios, we didn’t make a whole lot of changes because we built them to handle whatever came their way.

When the disruption occurred, we remained comfortable with our position—ing and we believed we would work our way through the pandemic, so we were patient and didn’t overreact.

As a counter—illustration, look at the amount of money currently in money market funds. It’s an astonishing amount, because many investors de—risked and got out of the market and haven’t gotten back in. So they missed everything that happened in the second half of the year.

**Davidow:** So, having the plan in place, staying optimistic, and being patient is really critical. Brian, I was struck in our first call how often you, in a very calm way, kept saying that you were bringing your clients back to basics. How did you keep your clients grounded?

**Ullsperger:** Aside from the basics, you must have faith in your process, starting with asset allocation and how you construct portfolios. Second, if you believe in asset allocation, by nature, I would argue that you have to embrace being a contrarian. We trim from winners and buy the “up and comers,” buying the rotation. Third, we have to be great storytellers. You must be able to paint a picture for clients to inspire them to action that they often are not inclined to. This year has been fascinating because we’ve gone through a cycle and a half since January, when we were saying this market might be a little frothy.

That froth was taken away by mid—March by a global shutdown. As we reopened, some sectors expanded faster than others. We had a rapid acceleration of technology adoption as we all learned to work from home; we all learned to do video calls versus travel. We took a contrarian view in September regarding technology stocks getting ahead of themselves and stock prices getting too far ahead of earnings.
We are always trying to predict where the puck is going, to use the Wayne Gretzky quote. I’ve had clients say to me, because I’ve used airlines as an example, “Do you really think people are going to fly as much as they did in 2018, 2019?” My reply: “I really don’t know.” What I am confident in is that if we do get a vaccine and if people get vaccinated, we’ll be flying more two to three years from now than we are today, because right now it’s shut down. Earnings for airlines should grow from this point.

Davidow: Part of our discussion in May focused on behavioral coaching, which is keeping clients from acting on their emotional impulses and heading to the sidelines when things feel uncomfortable. Brian, how do you deal with that behavioral element?

Ullsperger: It depends on the client. If you’ve had a client for an extended period of time—and I’ve had a number of clients for 10, 15 years—we’ve had a number of what I call light-bulb moments, where you’ve already experienced times when the market has appreciated, or the market has gone down and you are taking a contrarian approach; they can anticipate what we are going to do. But you do have to paint a picture for these clients, so they know that if or when this happens, here’s how we’re going to act.

We need to hold their hands and walk them through it and say, well in advance, that if this happens, this is our decision-making process. We are delivering a process. It needs to be unemotional because investors will be driven by fear and greed. Our job is to sit in the middle and provide that disciplined approach to investing.

Davidow: Scott, what have you been telling people throughout the year?

Welch: Step one: Manage client expectations upfront. Step two: Build a portfolio that can withstand tension. You may not capture all the upside with that kind of all-weather portfolio, but you should achieve some downside protection when something unexpected happens. And, step three: When that unexpected thing does happen, you overcommunicate. You don’t hide.

The early spring of 2020 is when advisors really earned their keep. It’s because (a) they did the upfront work and put the appropriate portfolios in place for their clients, and then (b) they managed expectations along the way. And when the unexpected event happened, they overcommunicated and made sure that clients stayed the course.

Now, that’s not to say that you don’t make any portfolio changes if and when they are appropriate, but if clients understand why you are recommending changes, it helps to ease adoption of those changes.

Davidow: Todd, maybe you have a slightly different twist, because you have both high-net-worth and institutional clients. Did you get different reactions?

Wagenberg: Definitely different reactions from the institutional clients. Institutional clients are more programmed to take the lead of our advice, much more so than an individual. Definitely 2020 was completely unlike anything we went through in 2008 and 2009. Most of my clients were with me back then and, frankly, they were more freaked out then than this time. They understood that by sticking to the plan they ended up coming out of it fine.

I have a handful of newer clients that weren’t around in 2008-2009 with me. You never really know your clients until you’ve gone through a really disruptive period. Everyone says, “Yes, I can take a 20-percent drawdown.” Really? Say you lose a million dollars in a 20-percent drawdown. Right. Most of my clients were pretty open to rebalancing and putting money to work. We thought the markets were a little frothy coming into 2020, so we were a little underinvested, we had dry powder that we were able to put to work. But we had two clients that I know did not take it because they were panicking. You can lead a horse to water, but you can’t make him drink. They wanted to get out of everything, and you can only do so much. For the most part, though, our clients listened to us and we were able to get them through it, not to say that it wasn’t without a lot of stress. If you told me back in March, we’re going to end the year with all-time highs, I would have never believed it.

Welch: I think it’s important that both Todd and Brian alluded to the Global Financial Crisis (GFC) back in 2008-2009. It underscores the importance of storytelling. For many people, the GFC was perhaps the worst experience of their financial lives. Certainly one of the lessons I was reminded of was “Don’t fight the Fed.”

The massive amount of monetary and fiscal stimulus back then resulted in huge buying opportunities. I remember sitting with my team and creating an “opportunities list.” We believed the world was not going to end, and that a variety of sectors and asset classes had huge upside potential as a result.

We were mostly right in our calls, and our clients benefitted from them—if they listened. Again, you can always find ways to add value. You can add value in up markets and in down markets. So be prepared and be patient.

Davidow: Do you think the unprecedented market rally was Fed induced? Do the market fundamentals warrant the current valuations?

Welch: Back in January and February [2020], we were economically healthy heading into the pandemic. Now, much of that health admittedly was driven by massive deficit spending. But because
we were healthy, and because when the pandemic hit the monetary and fiscal responses were immediate and massive, we were able to come out of recession quickly.

A recent Wall Street Journal consensus estimate calls for 2021 U.S. GDP [gross domestic product] of around 3.5–4 percent, without making any assumptions about additional stimulus. If the vaccinations are distributed and effective in the second half of the year, we might even see the economy rip higher, due to pent-up demand and consumption.

Focusing on the “signals” I mentioned earlier, we see a mostly risk-on environment for most of 2021:

- Economic growth and earnings forecasts are positive.
- Interest rates probably are going to stay low. They might grind higher from where we are as the economy recovers, but that’s on a relative, not absolute, basis.
- Inflation seems benign. If I had to look for a negative, it might be that we get inflation that’s higher than expected in the second half of the year.
- Finally, we believe central banks will stay accommodative into the foreseeable future.

Davidow: Brian, you’re watching several negative factors. Do you think all the good is factored into the market and are we not paying enough attention to the risks?

Ullsperger: Great question. Our team thinks about portfolio construction as creating a thesis about what is going to happen and seeing if it plays out. Typically, it either plays out faster or slower than expected. The question I have right now about growth stocks or value stocks is the way they’ve rallied. At the end of this year [2020], are prices ahead of what earnings are going to be in Q1? My gut tells me yes. And so Q1, Q2 could be choppy because it’s hard to imagine earnings are going to support that kind of price appreciation, especially for COVID-affected stocks.

In terms of risks, we’re all anticipating the vaccine gets rolled out. That drives stock prices. We’re still going through a lot of pain. It’s hard to watch the number of COVID cases, the number of deaths. And there’s the separation between Wall Street and Main Street. The risks are: (1) People don’t get vaccinated and we don’t get enough people who have immunity; and (2) we don’t get a reopening as fast as people are anticipating and investors (the market) are anticipating. This is what we’ve talked about with our clients. The biggest concern I have is that if we don’t get a stimulus package that really supports small business owners, bars, and restaurants, and we get a slew of bankruptcies before the economy reopens, we’re going to be sitting in June and July in the exact same position we are today because those businesses are gone, and we’re going to have an incredible amount of unemployment that is going to hinder economic recovery.

Davidow: In the suburbs of New York City, I can tell you, the bars and restaurants are struggling. There will be a ripple effect if those businesses are not saved.

Ullsperger: Think about the economic impact of this. The people right now who are not working, or who spend all the money that they make, are the people who work at those bars and restaurants. Let’s just say they get a stimulus check again, it’s $1,200, $1,500, whatever that may be, that tides them over. But if their employer is gone and those businesses never come back, that’s the real risk to the economy because those people support the GDP growth.

Davidow: Todd, you listed taxes at the top of your list. Are you assuming that taxes will be raised even during this financial crisis?

Wagenberg: I’m pretty confident that we’re not going to see lower tax rates. So maybe it’s not a bad time to take some of your capital gains right now. You know, you have two weeks left till the end of the year. You take half your gains now and half after the first. And it’s not such a bad thing because most likely capital gains rates are not going down.

The reality is a lot of people are doing really well right now. Expenses have gone way down. I wouldn’t want to be a retail space or a strip mall owner right now, trying to collect whatever you can get from anyone. I believe there’s a ton of stimulus coming down the pike, as much as $900 billion. That’s just shy of 5 percent of GDP dropped into everyone’s hands. I’d be shocked if there’s not another stimulus plan out by February or March, and you just can’t fight it. We saw it in March 2020, the snapback of this whole thing was unbelievable. We’re seeing it right now in the fourth quarter.

Ullsperger: I look at tax management as a tremendous opportunity for advisors. Based on the policies that Biden has proposed, most likely we are going to see higher corporate tax rates, some sort of higher capital gains rates, and some sort of higher ordinary income tax rate. What can we do to add tax alpha to clients’ portfolios? We can harvest losses when we have the opportunity using the loss to offset gains. What asset classes are going to be impacted? Well, clearly, municipal bonds should benefit, and municipal bonds have not rallied anywhere close to what we’ve seen in Treasuries.

We are exploring high yield municipal bonds because they’ve had fewer historical defaults and less risk than corporate bonds. Another place where I would suggest advisors can add tax alpha is portfolio location. If you’re building a portfolio, where do you put certain
investments? For example, an emerging market strategy, or let’s say a REIT [real estate investment trust] or infrastructure or something with a yield, how can you minimize the tax impact of those investments? Consider an IRA [individual retirement account]. Roth or traditional. It is another way you can add a lot of value for clients.

**Davidow:** What about the international markets? China and emerging markets?

**Welch:** My investment committee sat down a few weeks ago and developed a handful of primary investment themes for 2021:

- Cyclical rotation back toward value and small caps
- Reflation
- A focus on quality and income, in both equity and debt
- Disruptive growth
- Emerging markets, in both equity and debt

In our portfolios, we remain overweight the U.S. and emerging markets and underweight EAFE relative to the MSCI ACWI index. Why? (1) Many of the Asian countries did a better job of managing the pandemic and therefore came out of recession faster; (2) we believe the dollar will remain relatively weak; and (3) if we are correct in our views, there should be a global economic expansion. That would be positive for commodity exporters. So we believe there are several tailwinds behind emerging markets throughout 2021.

**Ullsperger:** Scott and I have talked about emerging markets a lot. We’ve been so far ahead in this rotation that I really want it to last as long as it possibly can, because it feels so good when you actually do see it playing out.

We’ve tended to lean toward international and have been rotating money into the asset class. It’s less expensive. It has a better dividend yield. And it also appears that the rest of the world has dealt with COVID better than the United States has, so they may not have as long a time to reopen. We see a lot of opportunities in stocks that are more value oriented. We have been shifting money into value, and it seems to be paying off. I think we’re all historians of the market, if you go back and look at what happened right around 1999 and 2000, and I’m not going to say this is exactly like the tech bubble. The following four to five years after that, the best-performing asset classes were emerging markets, value, REITs—and it feels like this could be similar. Now, it could become a very crowded trade quickly, which means you just have to trim back on it as it runs up. But right now it seems like it’s a fantastic opportunity.

**Davidow:** What are your thoughts about China and what are your thoughts on what potential policy may be with China in the coming administration?

**Ullsperger:** With U.S. isolation, the only place that a lot of these countries could go was to China. We have to deal with China specifically in terms of technology and sharing of information. But the fact is that it will put pressure on China to be fair, to play fair. If not, no one’s going to deal with China. They’re going to work with the United States or other countries. I think there are tremendous opportunities in China. The question that usually comes up when speaking with money managers about China is how much of profits will be kept by the government. What’s the government going to take, and how much growth do investors receive from the publicly traded companies?

**Welch:** With respect to China, I think it’s a fairly common misperception that a Democratic administration is going to be nicer to China than was the previous Republican administration. There is bipartisan antagonism toward China, though perhaps for different reasons. There will be continued tensions between the two countries, and it will affect trade relations.

It will be hard for the Biden administration to say “Never mind” to some of the trade restrictions the Trump administration put into place, because China does steal intellectual property and it doesn’t follow World Trade Organization rules.

There are tremendous opportunities in China, but you have to be careful. We may not call it a cold war, but that is exactly what our relationship with China looks and feels like.

**Davidow:** In the next issue of Investments & Wealth Monitor, we are focusing on geopolitical risks and nationalism versus globalism. I don’t think that we can ignore China—it’s a formidable player and wants to eat our lunch.

**Wagenberg:** One counter flashpoint is on the Chinese–Indian border and the Indian–Pakistani border; however, the South China Sea is a very dangerous area. I would also agree that the average Chinese person is very entrepreneurial. Unfortunately for China, it’s run by communists. I don’t think that China cares what we do; quite frankly, they control what they want, when they want. I do agree that there’s still a lot of opportunity there. The problem with China is that when an opportunity starts to do really well, the party decides they may want a piece of it. If it starts doing too well, then you have nationalization risk, which is a very big risk. Talk to the oil companies in Nigeria or in Venezuela. Those investments did well, and all of a sudden they went to zero. I’m not saying that’s going to happen in China, I’m just saying that I think that we’re not as knowledgeable about what goes on in China as we think we are.

**Davidow:** Scott, I know you wanted to go back and make a point, and then I want to pick up on the value versus growth discussion.
Welch: EM historically has been a good place to invest as we come out of recessions in the United States. Same thing is true for small-cap and value stocks. They tend to lead in an early economic recovery cycle. I think that’s part of what we are seeing. People priced in economic recovery as news of the vaccinations came out back in early November, and small caps, value stocks, and EM have rallied strongly since then.

If you combine where we are in the economic recovery cycle with the extreme valuation gap between large and small cap and growth and value stocks heading into Q4, it’s no surprise that we’ve seen this huge rally, not just in EM but also in small cap and value stocks.

The question is: “Can or will that continue?” That’s a fair question, especially if the recovery slows down or the vaccinations don’t come out as fast or as effectively as we expect.

I think that the valuation differentials were so extreme that there’s room for multiple expansion, even if earnings don’t keep up with expectations. So another of our primary investment themes for 2021 is that this cyclical rotation is real and can continue.

Ullsperger: One other comment I’ll make about market cycles is that there are always hiccups. If you go back to the recovery we had coming out of 2008, 2009, 2010, we had some big hiccups.

I remember in June, July, and August 2020, when they were talking about downgrading the Treasury, and we had some real volatility. I think if you look at it from the economic cycle standpoint, we’re at the beginning stages of a recovery. We have zero interest rates. We have incredible stimulus that’s coming. We have attractive stock prices other than tech stock prices. We have, I would say, reasonable P/E [price-earnings] ratios. The challenge on the PE ratio is earnings—there’s no forecasting being done. More and more companies have said, we are not going to provide estimates going forward. So nobody knows what the P/E is.

Welch: Growth is still going up, but value shot up. So a third major investment theme for us is disruptive growth. We think the pandemic fundamentally changed—perhaps forever—the way we work, communicate, stay healthy, and entertain ourselves. We believe there are industries and companies that are well positioned for these societal changes and will continue to show explosive growth rates.

We are rotating from growth to value, large cap to small cap and international, and from passive to active managers investing on fundamentals not market cap.

Davidow: You’ve talked about themes, but what sort of tactical decisions have you made for 2021?

Ullsperger: We are rotating from growth to value, large cap to small cap and international, and from passive to active managers investing on fundamentals not market cap.

We are exploring adding more alternatives. It could be event-driven strategies. It could be long–short strategies. It could be real asset strategies that we’re adding into client portfolios to get consistency of return. Managed futures have also done very well, providing a nice low–correlated vehicle. We are looking for strategies to provide consistency of return and even some yield that you’re not going to get out of bonds. As I said earlier, that’s, to me, the biggest challenge. Stocks are going to do what stocks are going to do. And there’s a lot of different ways for companies to grow their earnings—bond opportunities are fleeting.

There are very few high–quality, high–credit–quality opportunities in fixed income. So we’re trying to find some opportunities to get consistency of return in that space, whether it’s high yield munis or high yield credit, to provide a low correlation to equities but also consistency of return and some yield. If you really want to make a tactical play and—I hate to use gambling terminology—make a bet, you’ll buy REITs, because that’s going to be a challenging place.

Wagenberg: I agree with Brian. Equities are going to do what they say they’re going to do. We believe that active is the place to be, specifically in international and small-cap value. Those indexes are not very good, and most active managers should be able to outperform them.

The one area we haven’t talked about much is fixed income. Fixed income is very important to most portfolios, mainly because of the liquidity that it provides. We’ve historically always been pretty plain vanilla, intermediate fixed income guys. We’ve never really looked for return out of it; if we get it this time, great. My biggest surprise of 2020 was the rates of return that you got out of your fixed income.

The aggregate is up 7 percent on the year. I tell clients we’ll probably never see that again anytime soon. We’ve added quite a bit of gold, 3–5 percent, and we’ve actually taken it out of fixed income because the cost to carry gold is not as bad as it has been historically. Gold doesn’t give you any kind of income, but if you’re taking it out of cash or fixed income, you’re not really giving up a lot. I believe the dollar is going to weaken, and I’m concerned about what Congress is going to do—I’m already afraid of what they’ve done. The debt levels in this country are going to be pretty ridiculous.
Davidow: Let me set the stage for the alternate investment discussion. All the capital market assumptions (CMAs) I have reviewed are projecting substantially lower equity returns than the long-term historical average (10.2 percent). Most CMAs are projecting 5–7–percent traditional equity returns over the next 10–20 years, and bond yields are at generationally low levels. We have also seen correlations across most traditional asset classes rise over the past decade. So, it would seem to be an environment for alternative investments.

Welch: I believe in diversification, and I believe alternatives can play an important role in that diversification. I agree that the alternative credit space may present opportunities to generate enhanced yield, if you find the right sponsor and have the ability to tolerate some illiquidity.

Then there’s gold, if you consider that an alternative. We took a tactical position in gold in the spring of 2020 and it did pretty well. Recently, we expanded our allocation beyond just gold to a broader, more diversified basket of commodities. If you believe in global expansion, a weakening dollar, and potential reflation, then commodities might be interesting.

Wagenberg: I’m sure you’ve all seen what’s going on in the college world these days, they’re under a lot of duress. Colleges and their endowments are going to have to funnel a lot of money to help the operations of these schools. I consider endowments way overinvested in illiquid investments. There’s going to be a fire sale coming. You may want to take a look into some of these secondary offerings that are out there.

Davidow: I’m a big fan of private equity, private credit, and real assets, but advisors need to consider some of the structural trade-offs in accessing these long-term investments. I would also recommend that we consider the role of each investment in a client’s portfolio, and in which type of environment they work best. Advisors should make informed decisions about allocating appropriately.

Ullsperger: The role of fixed income and alternatives in a portfolio is to allow investors to stay invested in long equities. Long equities are going to provide the best returns in the boom times. You’re very rarely going to see a hedge fund beat the S&P.

The area that will probably become attractive at some point, particularly if investors start to chase yield, is going to be distressed debt. It will get bid up because people are desperate to get yield, and that might create problems similar to what we saw in the financial crisis. I hope they’re not the same problems, where we start to see some of those artificial strategies that come up that were overly levered.

We have some exposure in real assets. We have some exposure to timber and farmland. We have managed futures. There’s going to be a lot of M&A [mergers and acquisitions]. I will push back on one thing that Todd said. I have found, particularly in the past five years, there is a benefit to illiquidity. There is risk; I don’t disagree with that. I’m advising people to make sure that they understand what kind of illiquidity they can afford, because it helps remove the volatility, those investments from the retail high-frequency-trader market.

Welch: I think what Brian said just underscores strategy versus structure. I agree that event-driven or merger arbitrage might be very interesting strategies. I agree that long–short strategies can play a role in diversified portfolios. But a lot of the performance in those spaces comes down to illiquidity and leverage, which are functions of structure.

Davidow: What’s the one thing that maybe people aren’t paying enough attention to that could have an impact on the market?

Ullsperger: It’s the great unknown: We’re going to get through this pandemic and there’s going to be something else on the other side. I don’t want to be this doomsayer, but there is always something out there to deal with. I am generally very optimistic about where we’re going. If investors are not ready for the shocks, it may create bigger swings. I have some concerns that as we get into fourth–quarter earnings, they’re not going to support the current prices, and you’ll have what should be a run of the mill 15–percent market correction that becomes a 25–percent correction because of the lack of sophistication from new investors.

Welch: Investor sentiment currently is in a euphoria stage. If you look at various investor sentiment indicators, there’s a lot of optimism priced in. So at the retail level, we’re in a risk–on environment, and I agree with much of that optimism. But a potential shock might be that there’s too much optimism built into the market. If we get an event that turns sentiment around, and people begin to de–risk, it could happen quickly and dramatically.

Wagenberg: I would say the shock that I’m going to be the most concerned about is a change in Fed policy.

Davidow: Gentlemen, this has been fantastic. Thank you for your leadership on the Investments & Wealth Institute board, and thank you for participating here today.

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