HARTFORDFUNDS
Our benchmark is the investor.®

Five Pressing Questions for 2021

Nanette Abuhoff Jacobson
Managing Director and
Multi-Asset Strategist
at Wellington Management LLP
and Global Investment
Strategist for Hartford Funds

IN MY CONVERSATIONS WITH CLIENTS AT THE END OF 2020, MANY OF THE SAME QUESTIONS KEPT COMING UP. Here are five that topped the list, along with my thoughts in response.

#1: Given last year's robust market gains and the current state of the economy, how optimistic are you about 2021?

There are always risks for investors to navigate. Notably, this latest surge in COVID-19 cases, hospitalizations, and deaths mark a tragic phase in the ongoing global health crisis. However, as we learned in 2020, markets are forward looking. I believe the recently deployed COVID-19 vaccines, gradually reopening economies, and easy fiscal and monetary policy could provide a supportive backdrop for potentially solid gains from risk assets[1] in 2021. So optimism seems in order, but given that this is the consensus view, I am only moderately bullish on global equities as of this writing.

#2: What's your take on what a Joe Biden presidency might look like?

Investors are understandably concerned about a progressive Biden agenda. However, the president-elect's razor-thin majorities in Congress and the low likelihood of removing the Senate filibuster have dimmed chances for proposals such as the "Green New Deal" and "Medicare for All." That said, any major budget legislation will have to pass through reconciliation—a process that allows a simple majority to enact legislation with spending or revenue implications, but must be budget-neutral over 10 years. Major budget legislation is also likely to include another large COVID-19 relief package focused on state and local aid, further expansion of unemployment benefits, and stimulus checks for lower-income individuals. I expect higher taxes (corporate and individual) to partially offset spending as well, but probably not until 2022 to avoid choking off the economic recovery. Biden will have more unilateral power on foreign policy.

#3: Do you think the unprecedented government policy actions have heightened inflation risks?

Inflation risks have risen amid prospects for improved economic growth, a weaker US dollar, supply-chain bottlenecks, and higher commodity prices. However, I don't expect these dynamics to result in much higher inflation and hurt markets this year because there is still substantial slack in the economy, as evidenced by higher-than-normal unemployment. I also tend to think equities would better withstand rising inflation if it were induced by stronger growth. Whatever the cause, higher inflation is likely to be more damaging to growth sectors (such as technology) than to value areas (such as financials).

[1] Risk assets (such as equities, commodities, high-yield bonds, real estate, and currencies) have a significant degree of price volatility.

Key Points

- Recently deployed COVID-19 vaccines, gradually reopening economies, and easy fiscal and monetary policy could provide a supportive backdrop for potentially solid gains from risk assets in 2021.
- Higher inflation is likely to be more damaging to growth sectors (such as technology) than to value areas (such as financials).
- A range of regions, sectors, and market caps have the potential to outperform, including international over US equities, cyclical over defensive sectors, and smaller caps over larger caps.

#4: With yields so low these days, what's the value in fixed income?

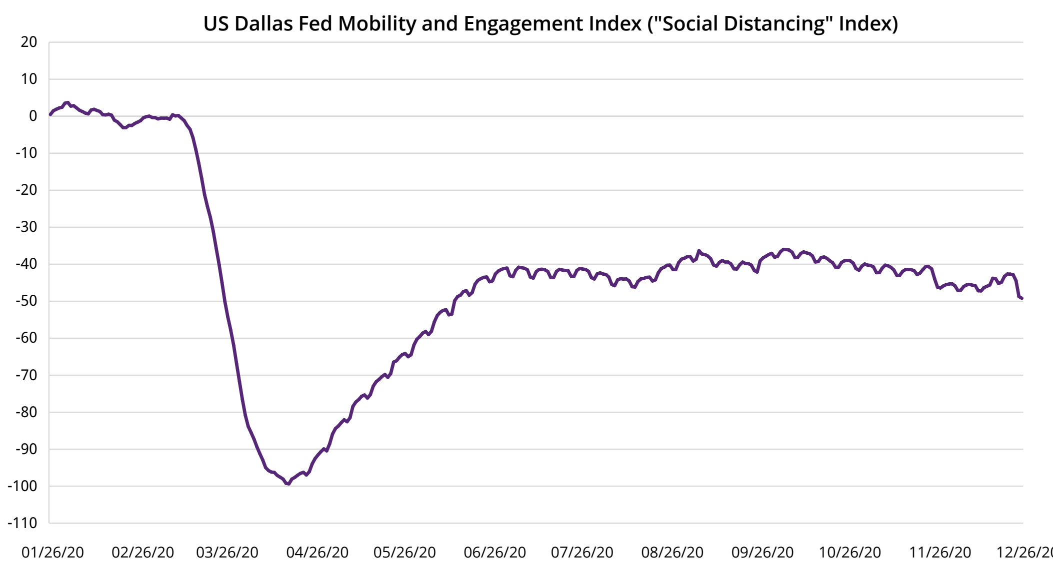
Around 75% of global government debt is negative-yielding right now, so it's not unreasonable to think fixed income offers little to no value. But I disagree. For example, fixed income would still play a valuable diversification role in the event of a large equity sell-off. Suggestions to supplement fixed-income allocations with value equities or high-dividend stocks are suspect in my opinion, as such exposures would only add more equity risk to a portfolio. I prefer widening the universe of diversifiers beyond traditional government bonds to include cash, gold, global government bonds, and high-quality credit. I expect credit spreads[2] to continue tightening.

#5: Which equity style is likely to win this year—value or growth?

A commonly asked question for the past 15 years! I expect the cyclical upturn this year to favor value-oriented markets and assets over their growth counterparts, and the Democrats' narrow Senate win increases my conviction. A range of regions, sectors, and market caps have the potential to outperform in my view, including international over US equities, cyclical over defensive sectors, and smaller caps over larger caps. Why now? Because we have a catalyst in the form of safe, effective COVID-19 vaccines that could help persistently cheap valuations to "mean revert"—return to their long-term average. Growth assets still deserve a place in client portfolios over the long term, but I think the "reopening bounce" will be the dominant theme of 2021 and should benefit value more than growth.

FIGURE 1

There Is Pent-Up Demand To "Get Back To Normal"



Source: US Federal Reserve. Chart data as of 12/31/20. The US Dallas Fed Mobility and Engagement Index summarizes the information in seven different variables based on geolocation data collected from a large sample of mobile devices to gain insight into the economic impact of the pandemic.

[2] Spreads are the difference in yields between two fixed-income securities with the same maturity, but originating from different investment sectors.

Investment Implications

- **It pays to be optimistic, despite the risks.** The potential tailwinds from COVID-19 vaccines, accommodative policy, and reopening economies make me more confident in taking a pro-risk stance this year. That suggests favoring equities over bonds. I also expect longer-term yields to drift higher.
- **Within equities, favor value-oriented sectors, regions, and market caps.** Sectors with value-oriented characteristics that are worth looking at include financials, real-estate investment trusts, materials, healthcare, aerospace/defense, and transport.
- **US politics should present less market risk this year.** The Biden administration will be hemmed in by slim majorities in the House and Senate, so I don't anticipate any major progressive legislation that would be market-negative.
- **Higher-than-expected inflation leading to higher interest rates is a growing risk.** While not my base case, equities and bonds would be vulnerable to any sharp spikes in inflation and interest rates. I recommend exposures to inflation-linked bonds and gold as hedges against this potential scenario.

The views expressed here are those of Nanette Abuhoff Jacobson. They should not be construed as investment advice. They are based on available information and are subject to change without notice. Portfolio positioning is at the discretion of the individual portfolio management teams; individual portfolio management teams and different fund sub-advisers may hold different views, and may make different investment decisions for different clients or portfolios. This material and/or its contents are current as of the time of writing and may not be reproduced or distributed in whole or in part, for any purpose, without the express written consent of Wellington Management or Hartford Funds.

Subscribe to Nanette's commentary at hartfordfunds.com/nanette

Important Risks: Investing involves risk, including the possible loss of principal. • Foreign investments may be more volatile and less liquid than US investments and are subject to the risk of currency fluctuations and adverse political and economic developments. These risks are generally greater for investments in emerging markets. • Small-cap securities can have greater risks and volatility than large-cap securities. • Investments in particular sectors may increase volatility and risk of loss if adverse developments occur. • Investments in the commodities market and the natural-resource industry may increase liquidity risk, volatility and risk of loss if adverse developments occur. • Fixed income security risks include credit, liquidity, call, duration, and interest-rate risk. As interest rates rise, bond prices generally fall. fall. • The value of inflation-protected securities (IPS) generally fluctuates with changes in real interest rates, and the market for IPS may be less developed or liquid, and more volatile, than other securities markets. • Diversification does not ensure a profit or protect against a loss in a declining market.

Mutual funds are distributed by Hartford Funds Distributors, LLC (HFD), Member FINRA. Certain funds are sub-advised by Wellington Management Company LLP. HFD is not affiliated with any fund subadviser.

221434 MFGS_010821