FLIPPIN, BRUCE & PORTER, INC.

INVESTMENT COUNSEL

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For many of us, 2020 will be remembered as one of the most difficult years in our lifetimes. Our hearts go out to those whose lives were directly impacted by the sickness and death brought about by the global pandemic. Even if you were spared infection, every one of us was impacted by the lockdowns. Thousands lost their jobs, with the travel and restaurant industries taking the biggest hit. A first quarter collapse in the stock market was another painful fallout from the virus. Add in a disputed presidential election and you have the recipe for a truly unforgettable year, or maybe we should call it a forgettable year! While the headline story of 2020 had anxiety and fear playing key roles, hope and optimism dominated as we ended the year. The stock market reflected that positive sentiment, with broad US indexes generating double-digit percentage gains during the fourth quarter.

The optimism is due in large part to the remarkable and unprecedented scientific achievement of creating multiple vaccines to fight Covid 19, and to accomplish that task in just a few months. Both government funding and unrelenting investment of corporate resources deserve credit for vaccine development. While it will take some time to get the population inoculated, it appears that the days of rapid spread of the coronavirus will soon be over. Consequently, the limitations we have endured on economic and social activity should be short-lived as well. There is light at the end of the tunnel. Economists are already forecasting very strong GDP growth for 2021 and 2022, as expectations rise for the anticipated reopening of the economy.

Another important development witnessed last year was a dramatic shift in stock market leadership during the fourth quarter, with value stocks handily outpacing growth stocks for the first time in several quarters. Historically, value stocks perform well in the early stages of economic recovery, which it appears we are in. We would expect this shift in value leadership to continue as the economy reopens.

Some may argue that the increase in stock prices is a sort of Federal Reserve-induced "sugar high" that is not sustainable. Clearly, the monetary and fiscal stimulus implemented to aid consumers and the economy was very large. As a result, total government debt skyrocketed, and the Fed's balance sheet expanded markedly. Following the Georgia Senate runoff elections, it appears the Democrats will control the balance of power in DC, making additional fiscal stimulus even more likely, which will add even more to the deficit. At some point, high levels of government debt will become a concern for the US, but not for the foreseeable future. We believe that a growing economy will go a long way towards fixing that problem. The ultra-slim Congressional majority held by the Democratic party will make it challenging to pass some of the more progressive measures that have been discussed. Center-leaning members of Congress, such as Sen. Joe Manchin (D-WV) and Sen. Susan Collins (R-ME), will be key swing votes and might be reluctant to go along with many of these policies. No doubt there will be changes coming out of Washington, but a modified form of legislative gridlock will most likely be the outcome.

Delving deeper into the returns from the stock market last year shows a real dichotomy in performance. The coronavirus accelerated trends toward online shopping, video conferencing and streaming media. As a result, technology stocks led the market, with the Nasdaq Composite soaring more than 40% for the year. More economically sensitive stocks such as energy, consumer discretionary, and financials lagged, creating the largest spread between growth and value that we have ever witnessed. As noted, this leadership shifted to favor value late in the year, but the valuation and performance gap between growth and value is still wide. We believe there is tremendous opportunity for value stocks, as world economies rebound and the virus threat fades.

In a quarter when value beat growth for the first time since 2018, our Equity & Dividend Plus portfolio performed very well, outpacing the Russell 1000 Value index. Calendar year results for the strategy were slightly negative, however. This is emblematic of the weak performance by dividend stocks in general, which were among the poorest performing market segments for 2020. The underperformance was even evident early in the year during the market selloff, which is atypical for dividend stocks. The iShares Dividend Select exchange-traded fund, for example, dropped almost 5% for the year. That fund follows the Dow Jones Select Dividend Index, which is comprised of large-cap US stocks that have relatively high dividend yields. While total returns for dividend stocks were disappointing last year, we were very pleased that strategy cash flow, from both dividends and option premiums, exceeded our goal of 5% annually. Given that many companies suspended their dividends during March and April, the fact that dividend cash received was higher in 2020 than 2019 was encouraging. Additionally, option premiums generated as a percentage of the account were the highest since 2009, making last year very favorable from a cash generation standpoint. We continue to maintain a diversified portfolio with a tilt towards economically sensitive sectors that should perform well as economic growth picks up in 2021.

For additional firm wide information please visit our website at www.fbpinc.com or call us at 1-800-851-3804. As always, we appreciate your continued interest in our firm.

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