NOTTINGHILL
INVESTMENT ADVISERS, Ltd.

Vol. XXIV No. 1 February 2021

An Update

SCORECARD

	2020	Three Years	Five Years	10 Years
S&P 500 Index	**18.40%**	**14.18%**	**15.22%**	**13.88%**
10-Year Treasury Note	**11.82**	**6.75**	**4.78**	**4.90**
Gold	**24.69**	**13.38**	**12.28**	**2.94**

All multi-year returns are annualized, and all returns are associated with time periods ending December 31, 2020

2020 — The Year in Review

Wow! How does one review 2020? At year-end 2019, all was well: Taxes were low; the overall economy and corporate profits were growing at healthy rates; and, unemployment was at a 50-year low. Then, the quintessential out-of-left field event. In early-February, word of a new SARS-like virus emanating from the Chinese city of Wuhan began to spread. By all accounts, the virus was highly contagious, and <u>was</u> a real danger to certain segments of the population. The contagious nature became evident over the weekend of February 22-23 when these newly-identified COVID-19 infections began spiking in the faraway lands of Italy and South Korea. Containment in the age of jet travel? Not a chance. The COVID-19 horse was out of the barn, and big changes were on the way.

No playbook for this one. But, we have to give credit where credit is due: Many governments and central banks quickly recognized the severity of the problem and the need to shut down much of the worldwide economy, and stepped up to the plate with massive economic stimulus. Then, as so often happens, investors began to pick winners and losers and to spot bargains in the midst of the chaos. The markets turned. Our value-oriented stock market indexes lagged the Growth side, however, Value or Growth, all of the stock market ground lost in the first quarter had been made up as 2020 came to an end. For the year, our Russell 1000 Value Index provided an investment return of 2.80%. Bonds? The 10-year Treasury benefited from periodic bouts of safe-haven buying, and provided an investment return of 11.82%. But actually, gold at 24.69% ended up winning the 2020 performance derby. From an investment perspective and every other perspective, 2020 was quite a year.

That's 2020 in a nutshell. Forecasting is not part of our DNA, but we do have a few thoughts on the state of affairs at year-end.

- **Worldwide Economy**
  The race is on. With economies continuing to open up, the second COVID wave is upon us, and progress toward business-as-usual clearly has slowed. <u>But</u>, these COVID times also are time of medical miracles. The vaccines are here, and more are on the way. By all accounts, the vaccines ultimately will win the race, and we ultimately will return to normal times.

- **Equities**
  QI 2020 was no picnic, but worldwide equities then spent nine months undoing all the Q1 damage. From a valuation standpoint, equities are not undiscovered, but we maintained throughout 2020 that it is a market <u>of</u> stocks, rather than a <u>stock</u> market. Granted, Growth valuations are a bit stretched; Value/Yield and emerging market valuations are not.

- **Interest Rates**
  For quite some time, the Fed has sent clear signals that short-term interest rates would stay low for an extended period of time. One base case forecast with which we are familiar defines "extended period of time" as five or six years (!) A bold forecast, in our view. By implication, however, the chances of a near-term surprise on the interest rate front are low.

In the original "Ghostbusters," the Bill Murray character, Peter Venkman, witnesses an otherworldy event, and says, "That's something you don't see every day." Well, 2020 also was "something you don't see every day," however, 2020 and COVID were no laughing matter. Light at the end of the tunnel at this point? By all accounts, yes. Here's to a return to normal in our daily lives and a return to widespread economic health as the vaccines increasingly work their magic.

* *

And now, let's take a look at the 2020-2029 decade and the balanced investment strategies.

About the Firm

Nottinghill Investment Advisers, Ltd., is a registered investment adviser founded in May 1996.

Nottinghill is owned by the seasoned professionals serving its clients, and effectively managing the assets of those clients, taxable as well as tax-exempt, is the Firm's only business. The twin results are commitment and focus.

Total Portfolio Management, or TPM, is Nottinghill's largely passive, balanced approach to the management of a client's overall portfolio, and Indexed Total Portfolio Management, or ITPM, is the totally passive variation. In both cases, portfolios contain three sectors: Equities, U.S. Fixed Income, and the Alternatives Group. TPM and ITPM are two complete, widely diversified answers to any client's investment needs.

Seasoned investment professionals. Commitment and focus. Two complete, widely diversified answers. Nottinghill is your ideal partner.

Southampton Square
7414 Jager Court
Cincinnati, OH 45230
513.624.3000 Tel
513.624.3003 Fax
www.nottinghilladvisers.com

How Do We Get There?

A few weeks ago, a client stopped by for a portfolio review. We presented our report, and then discussed a few portfolio securities. She had warned us, though, that she also would have one of those fundamental bottom line questions: What does the future look like?

The question, of course, is not unusual, and we always begin by saying that we don't forecast, which we regard as a futile exercise. But, there is another way to approach this matter and come up with something of value. For openers, how about a little history?

A lot of research has gone into our two balanced investment strategies, TPM and ITPM, and each has a carefully constructed 2002-2020 performance data series. The data say that each strategy, if it had existed over that entire period, would have provided 7-9% per year, net-of-the management fee. So, let's be more specific, and define "the future" as the 2020-2029 decade. (Of course, one year already is in the books, but that shouldn't alter the analysis/conclusions too much.) The key question: Is TPM's and ITPM's long-term 7-9% per year achievable in the current 2020-2029 decade? If so, how do we get there? Three ways, we suspect:

Figure 1

Annualized Investment Returns
2010-2019

U.S. Value Equities	11.80%
Int. Emerging Markets Equities	3.52
Gold	2.36
U.S. Growth Equities	15.23
Bonds	4.70
Cash	0.56

1) U.S. Value Equities
As you know, the Growth style of investing, a long-time second-class citizen, has been on a tear. Over the 2010-2019 period, the Russell 1000 Growth Index provided an investment return of 15.23%, per year, over five full percentage points above the long-term trendline. Then, tack on a very good 2020, and you have an Index selling for 40x the earnings of its component companies, and yielding a paltry 0.66%. In sharp contrast, the rival Russell 1000 <u>Value</u> Index delivered 11.80% per year in the 2010-2019 period, sells at 22x component earnings, and yields 2.09%. Those are the large company comparisons; the smaller company comparisons are similar. The pendulum will swing back. U.S. Value equities are the 2020-2029 land of opportunity.

2) International Emerging Markets Equities
With the dollar strong and commodity prices weak, EM equities provided a pedestrian 3.52% per year over the 2010-2019 decade. <u>Under</u>whelming by any measure, and this despite the attractive fundamentals, i.e., real growth potential as these economies play catch up. The dollar and commodity prices? Reversion-to-the mean forces practically ensure that the former will not have the strong decade it had, and any uptick in inflation will do wonders for the latter. Then, there's the matter of valuation. The FTSE Emerging Markets Index sells at 16x the earnings of its component companies. This pendulum also is due to turn, from <u>attractive</u> valuation levels. Emerging markets equities… yet another 2020-2029 land of opportunity.

3) Gold and Real Estate
Proud members of TPM's and ITPM's Alternatives Group, these asset classes also should be meaningful contributors to that 7-9% per year in the 2020-2029 decade. Interest rates, which can be a headwind, likely will remain low, at least for a while, and inflation likely will tick up. Gold (2.36% per year in 2010-2019) should be a direct beneficiary of this, as well as any COVID-related currency problems. And, real estate (REITs) , while not undiscovered, is impacted by the same forces in many of the same ways, and should continue to chug along.

So, that's how we get to 7-9% per year. How do we <u>not</u> get there?

1) U.S. Growth Equities
See "U.S. Value Equities" above. In the interests of diversification, the Growth style of investing deserves a seat at the table; but, make it a smaller seat, and, absolutely, don't count on Growth delivering another 15% per year. Growth has become a "crowded trade," and this decade's starting valuations are way too high. (See "U.S. Value Equities" above.)

2) Bonds
Make no mistake, we expect bonds to do <u>some</u> of the investment return lifting, but that is not their primary role. Instead, bonds are expected to provide <u>sanctuary</u> during periods of equity market stress and, therefore, to <u>stabilize</u> the pattern of investment returns. When bonds do contribute meaningfully to investment returns, well, that's gravy, and bonds <u>have</u> contributed in recent times. Over the past decade, we're talking 4.70% per year for the 10-year Treasury, and we're talking 6+% per year in the decade before that. Can we see 5-6% in the 2020-2029 decade? Not likely. At the beginning of the decade, the 10-year Treasury yield stood at 1.92%, and, in the midst of the COVID chaos, had declined to 0.80% by year-end 2020. Bonds belong in the portfolio for the above reasons, but we'd be surprised if they are major portfolio contributors in 2020-2029.

3) Cash
Don't laugh. Once upon a time (the bad old 70s), 90-day Treasury bills had a decade-long investment return of almost 7% per year. Imagine...at that rate, the investor doubles his/her money every 10 years, with almost-zero risk. But, that also was the decade of 7% inflation, so we're glad those cash yields were a one-off. To us, cash is ideal for the Rainy Day Fund where the return <u>on</u> one's money takes a back seat to the return <u>of</u> one's money. Cash making a meaningful contribution to that 7-9% per year in 2020-2029. Won't happen.

* * * * * * * * * * * * *

A lot of data say that, looking out 10 years or so, the single most important determinant of asset class investment return is starting valuation. So, what's it gonna be...U.S. Value equities and EM equities at 22x and 16x earnings, respectively, or U.S. Growth at 40x earnings? Gold after a 2% per year decade, or a 10-year Treasury yielding all of 1%? How about cash yielding a miniscule 0.05%? Actually, we <u>can</u> get to a TPM or ITPM 7-9% per year in 2020-2029. The keys are to emphasize asset classes with low starting valuations and to take advantage of the markets' strong reversion-to-the mean tendencies, i.e., to emphasize the prior decade's <u>under</u>performers.

Total Portfolio Management

Portfolio Structure

Total Portfolio Management, or TPM, is a largely passive, balanced approach to the management of a taxable individual's or tax-exempt institution's overall portfolio. TPM portfolios consist of three sectors: Equities, U.S. Fixed Income, and the Alternatives Group. An active approach governs the large company component of the Equities sector, which also includes three other, passively managed ETF components. The U.S. Fixed Income sector is a combination of three actively managed bond mutual funds and intermediate Treasuries. And finally, positions in three alternative asset classes (ETFs) constitute an Alternatives Group that adds yet another layer of diversification. The result: a complete, largely passive destination for all of the taxable individual's or tax-exempt institution's investment needs.

Investment Objectives

- **A positive inflation-adjusted investment return** — A Life of the Strategy investment return greater than the inflation rate of the overall U.S. economy
- **A structure-consistent investment return** — A Life of the Strategy investment return consistent with the component investment returns weighted in accordance with the portfolio's asset allocation structure
- **Low, structure-consistent volatility** — Life of the Strategy investment return volatility consistent with that of a low-volatility structure and one weighted in accordance with the portfolio's asset allocation structure

Investment Return Summary

	2020	**2011-2020**
TPM Baseline*	**8.40%**	**9.12%**
S&P 500 Value Index	1.36	10.74
Bloomberg Barclays US Aggregate Bond Index	7.51	3.84

*65% equities

Nottinghill Investment Advisers, Ltd., is an independent investment adviser utilizing a number of large capitalization equity and widely diversified balanced strategies. The above Total Portfolio Management - Baseline performance data are associated with the Total Portfolio Management - Baseline model portfolio. While the data associated with the strategy incorporate the model and actual investment returns associated with strategy components, such data, even when combined in accordance with the Baseline structure, do have certain inherent limitations. First, unlike an actual performance record, such data do not reflect actual trading. Second, since trades have not actually been executed, results may contain an under– or over-compensation for the impact, if any, of certain market factors. These data are provided net-of-assumed transaction costs and net-of-assumed management fees. Furthermore, the data are associated with time periods ending December 31, 2020, are annualized for the multi-year period, are expressed in U.S. Dollars, and are compared to the value-oriented, all equity S&P 500 Value Index and the all-fixed income Bloomberg Barclays US Aggregate Bond Index. Whether simulated or actual, past performance is no guarantee of future results. A complete list of Nottinghill performance composites and model portfolios and additional information regarding the calculation and reporting of Nottinghill performance are available upon request.

Investment Strategy Advantages

- A seasoned team of investment professionals
- The complete, largely indexed answer
- Low, fully disclosed investment expenses
- Solid performance at a low level of risk

Now, ITPM...

Indexed Total Portfolio Management

Portfolio Structure

Indexed Total Portfolio Management, or ITPM, is a totally passive, balanced approach to the management of a taxable individual's or tax-exempt institution's overall portfolio. ITPM portfolios consist of three sectors: Equities, U.S. Fixed Income, and the Alternatives Group. A total of nine components within those sectors, and all nine consist of ETF positions performing in line with an associated equity market index, bond market index, or commodity price. ITPM portfolios combine the traditional performance advantages of passive management, along with ultra-low transaction costs and management fees. The result: a complete, totally passive destination for all of the taxable individual's or tax-exempt institution's investment needs.

Investment Objectives

- **A positive inflation-adjusted investment return** — A Life of the Strategy investment return greater than the inflation rate of the overall U.S. economy
- **A structure-consistent investment return** — A Life of the Strategy investment return consistent with the component investment returns weighted in accordance with the portfolio's asset allocation structure
- **Low, structure-consistent volatility** — Life of the Strategy investment return volatility consistent with that of a low-volatility structure and one weighted in accordance with the portfolio's asset allocation structure

Investment Return Summary

	2020	2011-2020
ITPM Baseline*	**12.33%**	**7.23%**
S&P 500 Value Index	1.36	10.74
Bloomberg Barclays US Aggregate Bond Index	7.51	3.84

*65% equities

Nottinghill Investment Advisers, Ltd., is an independent investment adviser utilizing a number of large capitalization equity and widely diversified balanced strategies. The above Indexed Total Portfolio Management - Baseline performance data are associated with the Indexed Total Portfolio Management - Baseline model portfolio. While the data associated with the strategy incorporate the model and actual investment returns associated with strategy components, such data, even when combined in accordance with the Baseline structure, do have certain inherent limitations. First, unlike an actual performance record, such data do not reflect actual trading. Second, since trades have not actually been executed, results may contain an under– or over-compensation for the impact, if any, of certain market factors. These data are provided net-of-assumed transaction costs and net-of-assumed management fees. Furthermore, the data are associated with time periods ending December 31, 2020, are annualized for the multi-year period, are expressed in U.S. Dollars, and are compared to the value-oriented, all equity S&P 500 Value Index and the all-fixed income Bloomberg Barclays US Aggregate Bond Index. Whether simulated or actual, past performance is no guarantee of future results. A complete list of Nottinghill performance composites and model portfolios and additional information regarding the calculation and reporting of Nottinghill performance are available upon request.

Investment Strategy Advantages

- A seasoned team of investment professionals
- The complete, fully indexed answer
- Ultra-low, fully disclosed investment expenses
- Solid performance at a low level of risk

mcpeek@nottinghilladvisers.com, jem@nottinghilladvisers.com, lmason@nottinghilladvisers.com, and bmcpeek@nottinghilladvisers.com