“A bend in the road is not the end of the road, unless you fail to make the turn.”

— Helen Keller

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COVID-19 has upended our daily lives, while the response to the pandemic has reshaped global markets and the economy. The pandemic accelerated certain market trends that were already underway prior to the outbreak while sparking new ones.

As the economy moves forward, we anticipate a convergence of trends that we did not observe after the 2008–2009 financial crisis. This includes protracted fiscal and monetary stimulus that government leaders resisted over the past decade. In the private sector, the post-pandemic recovery resembles rebuilding from a natural disaster, with strong spending on durable goods and housing. The combination of massive liquidity and private spending on big-ticket items is prompting a rotation in equity markets, shifting away from growth and high quality, which historically have characterized late-cycle markets, to a recovery with certain typical early-cycle characteristics.

Bonds will continue to struggle in today’s low- (but rising) rate environment, yet pent-up demand for commodities could spark a new bull market for the asset class. With corporate balance sheets flush with cash and equity dispersion levels on the rise, we believe the landscape is ripe for elements of active investing.

One main risk to our view is that the recovery rapidly accelerates, leaving the economy vulnerable to overheating and rising interest rates. In this scenario, markets may become highly sensitive to interest rate increases and inflation, owing to significant amounts of private and public debt worldwide.

We do not see this scenario persisting for several reasons: A significant amount of savings has been accumulated, a trend that commenced before the pandemic and intensified with the recapitalization of the U.S. consumer; a gradual recovery in employment that bodes well for a smooth transition to positive spending growth; a resurgence of trade growth that should benefit the global economy; and advances in technological innovation that should help contain inflation and keep interest rates below historical averages.

Key questions we consider in this report

| What pandemic-related trends will likely endure in the coming months and years? | How might these trends affect consumer patterns and business activity? | Which types of assets are poised to potentially benefit from these trends? | How can investors find opportunities in the post-pandemic landscape? |
Monetary and fiscal policy to the rescue

As global markets contend with the reverberations of the COVID-19 pandemic, monetary and fiscal policies are working in tandem to help restore economic growth to pre-pandemic levels. While the partnership between the Federal Reserve (Fed) and the U.S. Treasury might be noteworthy for its magnitude, the nature of this union is not new. The two entities have coordinated efforts to achieve economic stabilization during prior periods in U.S. history.

Thanks to Fed facilities established after last year’s downturn, financial markets were injected with cash while interest rates were lowered to near zero. This allowed many firms to shore up balance sheets, withstand a deteriorating economic situation and avert a potential solvency crisis.

The monetary stimulus from the Fed also allowed firms to borrow low-cost capital and employ debt to accelerate growth. Capital injections are being allocated toward developing information technology infrastructure and accelerating the digitization of the economy. Companies are investing in cloud computing, artificial intelligence, and machine learning in order to improve operations, expand online customer service, and reconfigure global supply chains.

Technology capital expenditures (capex) at an inflection point

The pandemic increased demand for remote and digital services, strengthening an existing trend of companies devoting more assets to information technology and fewer assets to transportation, industrial equipment, and real estate.

Sources: Wells Fargo Investment Institute and Bureau of Economic Analysis, U.S. Department of Commerce. Data ranges from March 31, 1980, to December 31, 2020, on a quarterly basis. Technology spending = sum of software, information processing equipment, and research and development spending divided by total nonresidential capex. Hard machinery/structural spending = sum of transportation equipment, industrial equipment, and structures divided by total nonresidential capex.
A shift in equity leadership

The convergence of low inflation, low interest rates, and quantitative easing prompted investors to reevaluate the prospects of technology-driven, high-growth companies against the backdrop of an accelerated move toward a digitized economy. Investors have extended valuations on these stocks, partly owing to lower interest rates but with the assumption that higher earnings will justify prices in the coming years.

Furthermore, investor perspective has evolved as revenue growth has become increasingly scarce within the U.S. We believe investors should consider opportunities in riskier assets including those overseas. We anticipate a low-rate environment that provides ample liquidity and promising growth prospects is now poised for a shift in equity leadership toward highly cyclical asset classes such as small-cap stocks and emerging markets.

The number of small-cap firms with negative cash flow has begun to shrink as easy access to low-cost debt has helped fund growth and innovation. Our outlook for global reflationary support from continuing dollar weakness, and likely pickup in global trade, should provide tailwinds for international markets. Additionally, improving year-over-year global production could boost emerging markets’ economic activity in the coming years. In contrast, we anticipate developed market equities may continue to struggle—especially in Europe because of ongoing structural challenges (for example, demographics, euro-skepticism, and a burdensome government role in the economy in some parts of Europe). Political dissension about government finance is likely to intensify, straining European relations between northern and southern countries and derailing policies to enhance productivity and earnings growth.

Disruption creates opportunity

1.26 million

U.S. new business applications, November 2020 – January 2021

In January 2021, there were 560,000, an increase of 55% over January 2020.

Sources: McKinsey and U.S. Census Bureau, census.gov, December 15, 2020

Continued dollar weakness has led to emerging market outperformance

A weaker U.S. dollar has historically made emerging market earnings more attractive to dollar-based investors by increasing the currency component of returns. Comparing the performance of emerging market stocks with the U.S. Dollar Index (DXY) shows the historically inverse relationship.

Accelerating technology trends will help propel the economy

The COVID-19 pandemic accelerated certain technology trends that were already in place prior to the outbreak, as businesses and individual consumers swiftly adapted to extraordinary circumstances. In our view, the shift from brick-and-mortar retail to e-commerce, the transition of online entertainment from cable to streaming services, and the growing use of telemedicine and online education are consumer trends that will likely persist. Business trends include the adoption of machine learning and artificial intelligence in business operations, and the reconfiguration of supply chains, while the transition to a more flexible workplace model allows individuals and businesses to retreat from costly coastal cities for more moderately priced locales.

Technology and innovation are essential components of productivity and economic growth and, as such, we look for many pandemic-related business adjustments should drive earnings in the coming quarters. If the transformation to a more digitized economy accelerates as we expect, innovative firms are poised to gain prominence in the new business landscape. Big Tech firms with vast repositories of data and intellectual property will help drive greater earnings growth and efficiencies across existing sectors and industries. Disruption also may create opportunities for entrepreneurial pursuits, and that, perhaps, has contributed to the recent bump in business applications.

Productivity increases

<table>
<thead>
<tr>
<th></th>
<th>Q2 2020</th>
<th>Q3 2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Productivity increases</td>
<td>9.6%</td>
<td>6.5%</td>
</tr>
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</table>

Due to the use of high-tech equipment and innovations such as cloud computing and telemedicine during the post-pandemic recovery, increases in U.S. productivity in the second and third quarter represented the largest six-month improvement since 1965.


Productivity is the amount of value a company creates per dollar of investment or hour of worker labor. It is one of the main ingredients of economic growth, along with labor and capital.

Virtual office space

20%

McKinsey Global Institute estimate of global workforce that could work away from office and be as productive.

Source: McKinsey and Company, January 2021

E-commerce as a percent of monthly spending on the rise

The COVID-19 pandemic accelerated existing trends as businesses and individual consumers adapted to changed conditions. One such trend is the shift from brick-and-mortar retail to e-commerce.

Pre-pandemic

<table>
<thead>
<tr>
<th></th>
<th>Customers whose 0%–50% of monthly spend is attributed to e-commerce</th>
<th>Customers whose 51%–100% of monthly spend is attributed to e-commerce</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pre-pandemic</td>
<td>24%</td>
<td>76%</td>
</tr>
</tbody>
</table>

During pandemic

<table>
<thead>
<tr>
<th></th>
<th>Customers whose 0%–50% of monthly spend is attributed to e-commerce</th>
<th>Customers whose 51%–100% of monthly spend is attributed to e-commerce</th>
</tr>
</thead>
<tbody>
<tr>
<td>During pandemic</td>
<td>47%</td>
<td>53%</td>
</tr>
</tbody>
</table>

Post pandemic

<table>
<thead>
<tr>
<th></th>
<th>Customers whose 0%–50% of monthly spend is attributed to e-commerce</th>
<th>Customers whose 51%–100% of monthly spend is attributed to e-commerce</th>
</tr>
</thead>
<tbody>
<tr>
<td>Post pandemic</td>
<td>46%</td>
<td>54%</td>
</tr>
</tbody>
</table>

Sources: Wells Fargo Investment Institute and Capgemini Financial Services Analysis, World Payments Report 2020
A new normal

Despite the profusion of pandemic-related changes in the economy, not all of the recent trends will become permanent ones. Working from home likely will evolve from its current form to a hybrid model as employers and employees compromise on attendance rules. Firms will continue to invest in proprietary real estate, but they may add warehouses and distribution centers, particularly in lower cost-of-living areas. Although the retreat from traditional brick-and-mortar retail and dine-in restaurants has been offset by e-commerce and curbside pick-up, many consumers are likely to return to stores and restaurants once the virus is mitigated. Businesses also could adapt to shifting consumer patterns by offering multiple service options.

We believe businesses will strive for greater flexibility in their production processes, but global competition will pressure them to do so in a cost-efficient way. Some overseas supply chains may selectively reshore to the U.S. as companies weigh the costs of dispersed supply networks against the value of more stable production capabilities. Businesses can also increase flexibility through technology that uses less office space, reduces travel, and automates customer service processes. We expect more, not fewer, jobs; however, employers will demand new skill sets and flexibility.

Today, fundamentals remain strong for cyclically oriented sectors of the U.S. equity markets. We look for the Information Technology sector to outperform the broader market, offering exposure to high-quality stocks with potential for strong growth prospects. Sectors such as Industrials and Materials are poised to benefit from the economic momentum and underlying stimulus support, possibly including greater infrastructure spending.

Potential headwinds

Aggressive fiscal and monetary stimulus could lead to economic overheating, higher inflation, and dollar depreciation. Interest rates could rise faster than expected, reversing the push toward high growth rates as borrowing costs increase. An unanticipated inflation shock could hinder growth companies with weak cash flows as well as dividend-paying stocks. Furthermore, a rapidly rising money supply poses a long-term risk for inflation and dollar devaluation. Increasingly large bailouts in response to economic crises may cause private firms to expect external support and underestimate the risk of taking on more debt.

Other potential headwinds include higher taxes that could reduce a firm’s expected revenue, potentially decreasing the willingness for capex investment, slowing growth. The evolving trend of democratization in financial markets by social media platforms may also create periods of intense market volatility.
The Fed remains accommodative

We believe that monetary policy will remain accommodative for an extended period and should benefit risk assets as the economy mends. The Fed has stated that it does not plan to raise interest rates until its unemployment and inflation targets are achieved and that it will continue purchasing Treasury bonds to ensure near-term liquidity. Additional fiscal stimulus is also augmenting liquidity levels, providing ample support for asset prices.

Coordinated monetary and fiscal stimulus could be a defining feature of economic policy in the wake of COVID-19, helping combat low inflation and lingering disruptions from the pandemic. A historical context may illustrate how monetary and fiscal stimulus have helped bolster a fragile economy in the past and why policymakers are relying on a similar approach today. In the 1920s following World War I and the 1918 Spanish flu pandemic, in the 1930s after the Great Depression, in the 1940s after World War II, and most recently after the global financial crisis, we have observed a common pattern of policymaker intervention. In each case, higher issuance from the U.S. Treasury to fund fiscal stimulus was combined with the Fed’s low-rate interest rate policy and government securities purchases to successfully reinvigorate the economy.

Stabilizing the financial system: available funds and low rates

Consistent with its responsibility to promote stability in the financial system, during major economic crises the Fed increased its balance sheet to provide liquidity and has suppressed interest rates to lower borrowing costs.

Sources: Federal Reserve Bank of St. Louis and Bloomberg, as of February 1, 2021
New administration should bring a change in fiscal policy

We expect the Biden administration to take a more active role in managing the economy; rolling out COVID-19 vaccines and growing the economy are among the administration’s highest priorities. Yet, history has shown that once the economy has rebounded, conflicting macroeconomic forces may intrude. Higher inflation, larger government deficits, and asset bubbles often are consequences of easy financial conditions. Policymakers typically respond by reversing course and tightening, leading to asset-price corrections. At present, we believe that the economy is far from that point and likely has reached a point in the cycle that typically has been advantageous for asset performance, albeit with some assets performing better than others (see table below).

### Asset performance during recent Fed easing cycles

<table>
<thead>
<tr>
<th>Start date</th>
<th>End date</th>
<th>Fixed income (%)</th>
<th>Equities (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>6/6/1989</td>
<td>9/4/1992</td>
<td>44.30</td>
<td>43.21</td>
</tr>
<tr>
<td>7/6/1995</td>
<td>1/31/1996</td>
<td>5.98</td>
<td>16.31</td>
</tr>
<tr>
<td>9/18/2007</td>
<td>10/31/2003</td>
<td>41.45</td>
<td>55.04</td>
</tr>
<tr>
<td>7/31/2019</td>
<td>9/16/2020</td>
<td>9.35</td>
<td>16.17</td>
</tr>
</tbody>
</table>

Sources: Bloomberg and Wells Fargo Investment Institute, as of February 1, 2021. Equities are represented by the S&P 500 Index TR; fixed income is represented by the Bloomberg Barclays U.S. Aggregate Bond Index TR. An index is unmanaged and not available for direct investment. Past performance is not guarantee of future results. Please see page 19 for index definitions and descriptions of asset-class risks.

A new tacit Fed-Treasury accord

The Fed and the Treasury typically have followed their own approaches for supporting a sluggish economy, which often has led to conflict. Even so, the disinflation and deep slumps of the past 15 years have made it easier for the Fed to align with fiscal policy. The greatest threat to this alignment is that the Fed might unintentionally unravel what we believe it is most effective at — inflating asset values — with consequences similar to those we observed a decade ago.

Eventually, the accord could break if inflation returns and the Fed tightens. Once interest rates start to rise, concerns will shift to how far bond prices will drop. We expect this most likely will happen when public debt has swelled, the Fed has ceased easing, and its balance sheet starts to normalize. The first cracks in the accord may appear once the Fed begins tapering its bond-buying activities. However, unlike the abrupt tapering signal the Fed gave markets in 2013, this signal is likely to be conveyed cautiously and with ample lead time.

Fed’s average inflation target

2.0%

Negative real yields may be more successful in driving asset-price appreciation — which could benefit riskier assets — than achieving the Fed’s average inflation target of 2%.

Fed’s average inflation target
The future for fixed income may not resemble the past

For nearly 40 years, fixed-income markets have enjoyed a bull market with equity-like performance and considerably less volatility risk, as returns were driven principally by price appreciation rather than by yields. During the pandemic, interest rates teetered near all-time lows — not only for Fed policy rates but also for yields on 10-year and 30-year Treasury securities. In addition, many global bond yields marched further into negative territory. We believe global rates will remain low as the economy recovers from the pandemic-induced slowdown. But the U.S. may see a greater recovery in interest rates than many other developed market economies as the risk of disinflation dissipates in the U.S. unlike other developed economies where fiscal and monetary stimulus have been difficult to enact.

One consequence of low interest rates is that bond duration has increased, notably on longer-dated securities, increasing bonds’ sensitivity to changes in interest rates. Although we expect the yield curve to steepen somewhat this year, we expect interest rates to remain below longer term averages. The natural rate of interest, the interest rate at which gross domestic product (GDP) can achieve its full potential, is currently near zero. The average 10-year Treasury yield for the past decade has been near 2.4% and is currently below that. It is unclear if the economy can tolerate higher rates as it recovers.

Will the bond bull market finally come to an end?

We anticipate that bond market returns will be more tempered in the future than in the recent past. Yields have little room to fall before slipping into negative territory. We do not anticipate U.S. yields to fall as low as those in other developed market economies.
Investment implications

Intermediate fixed income, which combines positive yield and roll-down return, currently is the most attractive fixed-income maturity range in our view. Portfolio duration should not deviate significantly from that of the benchmark index. We believe a neutral stance on duration can help reduce downside exposure — a portfolio hedge against losses in riskier assets during periods of volatility or if our macroeconomic and equity outlooks turn negative.

High-yield corporate bonds typically have a shorter duration than government bond indexes. In aggregate, less creditworthy corporates typically are unable to borrow for long terms. The lower duration of high-yield corporates makes them less vulnerable to capital losses from rising interest rates and poised for incremental gains from bonds moving toward their maturity date (roll-down) in the steeper intermediate part of the yield curve.

For now, we believe investors should not be tempted to diversify entirely away from bonds. Modestly higher rates should not lead to price disruptions for all fixed-income classes. And this will not be evident until interest rates begin to shift higher across the yield curve as the Fed begins a new tightening cycle. We anticipate that fixed-income returns will be lower than those of equities, but anticipate the bond market’s diversification value will continue to make them an important part of a diversified investment portfolio.

No great rotation out of bonds in sight

Historically, investors increased their cash holdings during recessions and then bought risk assets once the recovery began. Over the past 10 years, flows into fixed income increased significantly as issuance skyrocketed. We believe that investors will continue allocating capital toward fixed income classes keeping rates relatively low.
Is a new commodities bull emerging?

A washout event in 2020?
In our view, the negative $40 oil price — which we observed in April 2020 — was likely a washout event for commodity prices.

Rebounding from the bottom
Commodities have been on a steady climb since their 2020 nadir, which included oil prices falling into negative territory for the first time ever. Fundamentals for commodities at the time were broadly weak, and prices had plummeted, offering compelling values for investors. Since its low, every component of the index in the chart below has returned double digits, and some even triple digits. In fact, many commodities have reached all-time, multiyear, or cycle highs, while others are approaching key cycle highs. Is this just a tactical bounce in commodity prices, or was 2020 the beginning of a new commodity bull supercycle?

Have commodity prices reached an inflection point?
Recent strength in commodity prices could reflect a short-term bounce off the March 2020 bottom, or it could signal the beginning of a new commodity bull supercycle.

What is a commodity supercycle?
Commodity prices tend to move in overall bull and bear market cycles, some lasting decades. These protracted cycles are called supercycles. Commodity bear supercycles are characterized by chronic oversupply and poor returns, while bull supercycles show the opposite (see chart above). The current bear supercycle started in 2008 and, to date, has behaved as a typical bear. Excess supply that built up over the exuberant bull years overwhelmed demand and crashed prices from 2008 to 2016. Prices bottomed, stabilized, and then remained range-bound between 2016 and 2020. The last stage of a bear usually involves years of consistent underinvestment and then very low prices that wipe out marginal suppliers. This allows demand to overwhelm the supply response, and a new bull is born.

Demand versus supply

A number of boxes have been checked that would indicate a new bull is forming (see table below). The key for us in calling a bull supercycle is how well supply responds to demand growth and price increases. Should a surge in demand materialize, possibly associated with the pandemic recovery, a new bull supercycle could be confirmed.

Chinese demand will be key to any new bull supercycle. China is the world’s largest consumer of commodities, accounting for roughly half of the world’s demand for industrial metals. If China’s economy stumbles, we would expect a nascent commodity bull to stall. Other key demand drivers may include accelerated infrastructure spending and the global green energy transition. The question that remains is whether or not supply will ramp quickly to match demand. If it does, the bear supercycle could reassert its hold.

Is a new commodity bull forming?

What to look for ahead

The pandemic caused an unprecedented disruption to the global economy, a historic drop in commodity demand, and a washout in prices. This may have created the catalyst needed to spark a new commodity bull supercycle. But questions remain. Key to whether the bull finds its legs will be how supply responds. We currently rate the commodities asset class favorable, and evidence is growing that the commodity run could extend into the coming years.

<table>
<thead>
<tr>
<th>Condition</th>
<th>Comment</th>
<th>Condition met</th>
</tr>
</thead>
<tbody>
<tr>
<td>Duration</td>
<td>Current bear matches shortest bear on record (12 years).</td>
<td>Yes</td>
</tr>
<tr>
<td>Washed-out prices</td>
<td>Poor absolute and relative performance versus other assets has been typical this cycle (-60% versus -57% average commodity bear performance).</td>
<td>Yes</td>
</tr>
<tr>
<td>Washed-out sentiment</td>
<td>Underinvestment and fund outflows have been rampant.</td>
<td>Yes</td>
</tr>
<tr>
<td>Strong breadth</td>
<td>Nearly all commodities have participated in the rally since the 2020 low.</td>
<td>Yes</td>
</tr>
<tr>
<td>Key commodity leadership</td>
<td>Gold broke out to all-time high in 2020 while others like silver, corn, copper, and soybeans have broken out to cycle highs.</td>
<td>Yes</td>
</tr>
<tr>
<td>Price firming</td>
<td>Will prices hold consistently above long-term averages?</td>
<td>TBD</td>
</tr>
<tr>
<td>Rising production costs</td>
<td>Will production costs increase after years of efficiency gains?</td>
<td>TBD</td>
</tr>
<tr>
<td>Slow persistent investment flows</td>
<td>After over a decade of outflows, will the money start trickling back?</td>
<td>TBD</td>
</tr>
<tr>
<td>New demand</td>
<td>China, infrastructure spending, and the global green energy transition are candidates that may drive demand over the next bull supercycle.</td>
<td>TBD</td>
</tr>
<tr>
<td>Restrained supply response</td>
<td>Will demand be able to overwhelm the supply response to spark a new bull supercycle?</td>
<td>TBD</td>
</tr>
</tbody>
</table>
Elements of active investing are making a comeback

Disruptions create opportunities

Market dislocations, like those we experienced with COVID-19, often can present opportunities for active investors especially private capital and hedge fund managers. But not all disruptions look alike. Last summer, we were anticipating that a typical credit cycle would drive prospects in alternative investments. Instead, the phases of the credit cycle occurred concurrently within a subset of sectors and industries; the credit default cycle was replaced by micro cycles highly sensitive to the massive amount of liquidity injections to stave off a credit squeeze. In our view, this unusual trajectory should not diminish opportunities for investors, but it does suggest that a more selective approach is warranted.

We believe that the post-2008 era of low volatility is behind us and that a confluence of macro and geopolitical elements — including a bottoming out of low interest rates and inflation, a new U.S. administration, and a recovering global economy — could provide a rich environment for active managers. As markets begin to display upticks in volatility, individual stock performance tends to diverge. Over the coming years, we expect significant dispersion in fundamental performance among sectors, industries, and geographies. We anticipate such an environment should favor both stock and credit picking as well as strategies that capitalize on a modest economic recovery, increased corporate deal activity, and asset reflation.

Global alternative investments

More deals in 2021?

87%

Global corporate deal volume rebounded strongly in the closing months of 2020. A survey of senior corporate executives showed they expect increased M&A activity to continue — the most optimistic year-ahead view in the 16 years the survey has been conducted.

Source: Dykema Gossett, October 7, 2020

Disruptions create opportunities

Global merger and acquisition (M&A) volume has recovered from its trough

Pandemic-related uncertainties and dislocations put a temporary stop to companies’ expansion plans. M&A activity has recently returned to pre-pandemic levels, and we believe the growing amount of deal-making suggests the trend could continue, fostered by a combination of suppressed financing costs, ample cash balances, added currency from elevated stock prices, and an improved economic outlook.

Sources: Bloomberg and Wells Fargo Investment Institute, monthly data from December 1, 2018, to December 30, 2020
Uncovering post-COVID-19 prospects in alternative investments

**M&A activity:** Due to COVID-19-related pressures, by mid-2020 global M&A activity had tumbled to its lowest level in more than a decade, as companies rolled back expansion plans and focused on asset protection. Since then, M&A activity has reverted to pre-pandemic levels, while Special Purpose Acquisition Company (SPAC) IPO issuance has surged. In our view, the growing amount of optimism and deal-making suggests the trend will continue.

Looking ahead, the tremendous amount of debt issued during the pandemic will need to be deployed, with corporate deals a likely avenue. Cash on balance sheets may be used for vertical integration and supply-chain restructuring, consolidation of weaker companies to build economies of scale, and technology upgrades through purchases. If M&A volume continues to increase over the next year as we expect, both merger arbitrage and activist managers should benefit.

**Hedge funds:** We believe certain strategies can benefit from post-pandemic trends. Historically, sectors and industries facing challenges have offered some of the best long-term opportunities. We expect strong performance from relative value strategies focused on structured credit, a source of non-traditional income in a low-yield environment, or long/short credit and event driven managers focused on distressed debt. Strategies with exposure to residential mortgage-backed securities could benefit from our outlook for a strengthening housing market. The increase in dispersion should benefit equity hedge strategies, the best-performing strategy in 2020.

**Private capital:** In private real estate, the retail, hospitality, and office sectors have struggled throughout the pandemic while the industrial sector and multifamily rental properties have enjoyed strong demand. Over the next year, we believe private real estate strategies with exposure to industrial and multifamily properties should perform well. We may see some improvement in other sectors as the economy mends and the virus is contained. Private debt may offer localized opportunities, particularly in distressed and special situations strategies, but we remain cautious on direct lending strategies.

**Favored hedge fund strategies**
- Relative Value – Long/Short Credit
- Event Driven – Distressed Credit
- Equity Hedge – Directional
- Macro – Discretionary

**Favored private capital strategies**
- Private Debt – Distressed and Special Situations

**Long-term trend to watch**

One potential implication for the post-pandemic terrain is an increase in governmental intervention in economies across the globe that is already underway in the U.S. Meanwhile, globalization trends could be constrained by more nationalist-leaning policies, like “Buy American.” These crosscurrents underscore an even greater role for active managers to identify government priorities and their impact on global markets.

Alternative investments, such as hedge funds, private equity, private debt and private real estate funds are not suitable for all investors and are only open to “accredited” or “qualified” investors within the meaning of U.S. securities laws.
Positioning portfolios for post-pandemic prospects

Alter your perspective

The reshaping of the post-pandemic landscape likely will create a host of opportunities and commensurate risks for investors. We believe that investors should position portfolios to prepare for these changes.

Broaden equity asset-class and sector exposure

We expect the global economy to grow faster than the U.S. economy, so global diversification may be increasingly important to capture worldwide equity gains. We believe emerging markets will recover more quickly from the pandemic slowdown and will offer more attractive opportunities than developed markets. We suggest a barbell approach to U.S. equities that includes larger allocations to cyclically oriented large-cap stocks and fast-growing small caps.

Be selective with fixed-income holdings

The near 40-year bull market in bond prices is winding down. Interest rates are expected to rise modestly and then remain near historical lows, likely negating the opportunity for significant capital gains in fixed income. In today’s low-yield environment, income investors should consider allocations to high-yielding fixed-income classes, including corporate bonds and emerging market bonds, but investors should do so judiciously in line with their risk tolerance. We prefer active management over passive, particularly in lower-quality investments. Preferred securities offer comparatively higher yields but should be purchased with a buy-and-hold mentality, as prices may become volatile during periods of market stress.

Increase allocations to commodities

Continued improvement in the global economy should support robust commodity demand. Moreover, supply levels likely will stay constrained in the near term, in part because last year’s oil-price drops devastated weaker suppliers. The suppliers that remain may be slow to respond to increased demand, which should support higher prices. Gold and other precious metals may act as a volatility hedge to portfolios diversifying away from low fixed-income yields, and agricultural commodities’ prices may continue to climb on rising demand.
Common behavioral biases displayed by investors during the pandemic

**Loss aversion**
Strongly avoiding losses at the expense of gains. This can result in holding on to losers too long and selling winners too soon, particularly in volatile markets. When the pandemic struck, many investors sold assets out of fear. As others followed suit, this led to where many investors sold at depressed prices.

**Regret aversion**
Avoiding or delaying decision-making out of fear of making mistakes. This can lead to holding a very conservative portfolio. In the aftermath of the pandemic, many investors feared reentering the market and remained on the sidelines while markets surged to new all-time highs.

**Status-quo bias**
Resistance to change, such as when investors fail to make adjustments to their portfolios. Some investors were overwhelmed by the outbreak and resisted making investment decisions. Investors should recognize that the landscape is transforming; post-COVID-19 investment choices may differ from pre-COVID-19 ones.

**Overconfidence bias**
Believing that one’s judgment is better than it is. This can result in underestimating risk or overestimating expected returns. This bias can lead to attempts to time the market, which is nearly impossible to do successfully.

**Confirmation bias**
When investors look for views or beliefs that align with their own. In the post-COVID-19 environment, the two prominent views — optimism and pessimism — are becoming increasingly polarized. As investors gravitate to market views that match their own, emotions such as fear or greed may lead to suboptimal decision-making.
Keys to restarting your business

Key to a successful economic recovery in the post-pandemic world is ensuring that small businesses continue to thrive and flourish. If you are a small-business owner, we want you to know that we value the hard work you have put into building your business and would like to offer some suggestions to help you reopen your business.

It is important to remember that reopening a business is not a single event. Reopening is an ongoing process that will continue, with reclosures possible until vaccines begin to contain the virus. Owners must account for shifting legal requirements from states and municipalities as well as employee and customer concerns — all while working toward making a profit.

Just over half of Americans expect changes in the way we work, socialize, and travel to stick around even after COVID-19. Business owners may need to find more permanent ways to connect with customers from a distance.

1. Help customers experience an "in-store" environment at home via custom playlists or other thoughtful additions.
2. If you've implemented contact tracing, health questionnaires, or temperature checks, automate them so they feel routine.
3. Design a permanent socially distant offering; customers may engage more comfortably if they know the service isn't temporary.

Reopening will not happen in a single day, and it will not necessarily take a straight path forward. Keep on top of big-picture developments so you can stay two steps ahead and analyze what’s working so you can adapt as you go.
An index is unmanaged and not available for direct investment.

**Risk considerations**

All investing involves risk, including the possible loss of principal. There can be no assurance that any investment strategy will be successful. Investments fluctuate with changes in market and economic conditions and in different environments due to numerous factors, some of which may be unpredictable. Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve.

The risks associated with the representative index asset classes discussed in this report include: **Stock markets**, especially foreign markets, are volatile. Stock values may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors. **Foreign investing** has additional risks including those associated with currency fluctuation, political and economic instability, and different accounting standards. These risks are heightened in emerging markets. The prices of **small-cap** company stocks are generally more volatile than large company stocks. They often involve higher risks because smaller companies may lack the management expertise, financial resources, product diversification and competitive strengths to endure adverse economic conditions. Investments in **small-cap** companies tend to be more volatile than investment grade fixed income securities. If sold prior to maturity, fixed income securities are subject to market risk. High yield fixed income securities (junk bonds) are considered speculative, involve greater risk of default, and tend to be more volatile than investment grade fixed income securities. If sold prior to maturity, fixed income securities are subject to market risk. All fixed income investments may be worth less than their original cost upon redemption or maturity. Exposure to the **commodities** markets may subject an investment to greater share price volatility than an investment in traditional equity or debt securities. Investments in commodities may be affected by changes in overall market movements, commodity index volatility, changes in interest rates or factors affecting a particular industry or commodity. Products that invest in commodities may employ more complex strategies which may expose investors to additional risks.

Alternative investments, such as private equity, are speculative and involve a high degree of risk that is suitable only for those investors who have the financial sophistication and expertise to evaluate the merits and risks of an investment in a fund and for which the fund does not represent a complete investment program. They entail significant risks that can include losses due to leveraging or other speculative investment practices, lack of liquidity, volatility of returns, restrictions on transferring interests in a fund, potential lack of diversification, absence and/or delay of information regarding valuations and pricing, complex tax structures and delays in tax reporting, less regulation, and higher fees than mutual funds. Hedge fund and private capital investing involves other material risks including capital loss and the loss of the entire amount invested. A fund's offering documents should be carefully reviewed prior to investing.
Investment expertise and advice to help you succeed financially

Wells Fargo Investment Institute is home to more than 165+ investment professionals focused on investment strategy, asset allocation, portfolio management, manager reviews, and alternative investments. Its mission is to deliver timely, actionable advice that can help investors achieve their financial goals.

For assistance with your investment planning or to discuss the points in this report, please talk to your investment professional.

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