Madison
INVESTMENTS

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WINTER 2020

ECONOMIC REVIEW

How much can the stock market advance in one month? While there are no caps on either monthly rises or falls, we can look back over quite a long historical record to get a sense of the extremes. To put this into perspective, a 2% move in a month represents a 24% annual return, which would be a big year for stocks, either up or down. This year has already seen exceptional months with a -12.7% drop in the S&P 500® Index in March and a 12.5% rise in April -- rates of return which would move the Index 150% over a year. You have to review some 400 months to get back to a bigger one-month S&P 500 gain than we had in April, all the way back to January,1978. And now we have in November, with the S&P rising 10.9%, bringing the year-to-date return to 14.0%. And it was not just a banner month for the S&P. The Dow Jones Industrial Average had its best month in decades and some international and small-cap indices produced all-time one-month records for advances this past month.

This examination of historic returns is a good moment to consider the nature of indices. It is easy when talking about the S&P 500 or the Dow Jones Industrial Average to imagine them as steady, immutable standards like temperature scales or atomic weights. The recent news of the addition of Tesla to the S&P 500 this December, a company which did not exist at the turn of the twenty-first century, is a case in point. Index composition can shift due to proactive decisions such as the Tesla addition, or through changes in the value of companies and sectors. In November, one of the leading S&P sectors was Energy, which only composed 2% of the Index. Yet it had been more than 13% of the Index as recently as the end of 2008. It is important to realize that a big move in an index forty years ago or even a dozen years ago involved different companies, differently weighted sectors in materially changed economic environments. When sector returns vary as much as they have lately, the composition of an index as well as the composition of an actively managed portfolio can have a major influence on real as well as relative returns.

But back to those stellar November returns. As we have pointed out in recent letters, the best of times for the stock market does not necessarily signal the best economic times. The Covid-19 crisis continues to create huge rents in society as cases and deaths surged tragically in November, while large swathes of the economy remained virtually shuttered. The wind-down of the fiscal stimulus from the CARES Act contributed to an accelerating wave of unemployment, actual or potential evictions and food insecurity. Meanwhile other segments of the economy, particularly those related to technology and allowing remote work, seemed to be humming along. The market returns suggested a belief that this bifurcation might be mediated in the months ahead. The Energy Sector rally reflected the overall rotation of the market to more economically sensitive components which had lagged the market recovery since the steep drop this past March. This signaled a market looking down the road more than a quarter to what appears to be better times ahead.

The biggest driver of November returns was the surprisingly positive news about three different Covid-19 vaccines, all testing at an efficacy rate which surpassed expectations. The prospect of immunization, first to front-line health care workers, then to high risk populations, and eventually to the full community kept the forward-looking optimism of the stock market at its optimum. At the same time, the initially contested results of the presidential election seemed to be gravitating to more normality, which fit into the overall mood of the market. One specific announcement, regarding Biden's nomination of Janet Yellen to head Treasury, seemed to be especially well received by the market as it harkened back to her consistently dovish governance during her tenure as Federal Reserve Chair.

As we try to absorb all the latest news and market action, we are left with the feeling that the market, at or near all-time highs, is pricing in a lot of good news. Should the hopes for a steady and expeditious vaccinated end to the pandemic prove real, perhaps these valuations will hold. On the other hand, any glitch in this progression or an emergence of an unexpected geopolitical crisis could produce disappointments. When valuations are stretched market reaction to any negative events can be pitched. As a result, we continue to emphasize careful stock selection and prudent asset allocation. We will feel better about the security of near-term results when we are able to see action from Washington, particularly regarding the promised additional stimulus, and when our currently dire Covid-19 situation shows real momentum towards a resolution.

Year-end Tax Reporting: With income tax filing on the horizon, Madison Funds may send you tax forms in late January to help you complete your income tax returns. **When you receive them, keep them for your records.** The forms you receive are specific to the type of account you hold and your circumstances.

Form 1099-DIV: Reports dividends and capital gains paid to taxable accounts. **Madison Funds observes an IRS rule that allows us not to send Form 1099-DIV if your taxable ordinary dividends for any fund totals $10 or less,** however, you must still include such dividends on your income tax return. Please review the enclosed year-end investor statement to see if this applies to you.

Form 1099-B: Reports the proceeds from any shares you sold or exchanged in taxable accounts.

Form 1099-R: Reports redemptions from qualified retirement accounts such as IRAs.

Form 1099-Q: Reports redemptions from Coverdell Education Savings Accounts (ESAs).

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Form 5498 and 5498-ESA: The Fair Market Value statement mailed in May (5498) and April (5498- ESA) will report contributions made to qualified individual retirement accounts (e.g. IRAs) and ESAs through April 15, 2021 for the 2020 tax year. As of December 31, 2020, we report the Fair Market Value of these accounts on your year-end investor statement.

TurboTax® and H&R Block® Tax Software: Download your tax information from your Madison Funds account directly into your tax return if you use TurboTax or H&R Block software. You can import your fund-related information from three tax forms: 1099-DIV, 1099-B, and 1099-R. Follow the instructions provided with your tax software.

Tax Inserts: Madison Funds prepares tax inserts that may accompany your tax forms. The inserts include general information on capital gains and losses from the sale of fund shares, fund specific percentages of income derived from U.S. government obligation, and AMT tax liability for tax-free funds. We recommend you consult with your tax advisor for complete information when doing tax planning and preparing your tax return.

Feel free to contact Shareholder Services at 1-800-877-6089 if we can be of further assistance. You can reach us Monday through Friday from 8 a.m. to 7 p.m. Central Time. But please remember we cannot offer tax advice; that is best left to tax professionals who can better answer questions and advise you about your specific circumstances.

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The S&P 500® is an unmanaged index of large companies and is widely regarded as a standard for measuring large-cap and mid-cap U.S. stock-market performance. Results assume the reinvestment of all capital gain and dividend distributions. An investment cannot be made directly into an index.

The Dow Jones Industrial Average® (The Dow®), is a price-weighted measure of 30 U.S. blue-chip companies. The index covers all industries except transportation and utilities.

Consider the investment objectives, risks, and charges and expenses of Madison Funds carefully before investing. Each fund's prospectus contains this and other information about the fund. Call 800.877.6089 or visit madisonfunds.com to obtain a prospectus and read it carefully before investing.