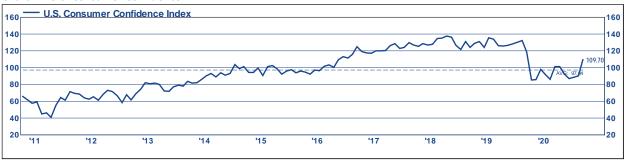
First Quarter 2021 – Investment Commentary



After the Covid-19 lockdowns last spring and subsequent reopening of state economies, there was much uncertainty as to what pace the U.S. economy would recover. Thankfully, the U.S. economy is rebounding quicker than commonly expected and it appears this trend is going to continue in 2021.

With the recent passage of the \$1.9 trillion American Rescue Plan Act, the U.S. economy is poised to see its strongest annual growth since 2005. In March, the Federal Reserve sharply raised their full-year 2021 U.S. GDP growth estimate to 6.5% from 4.2% which is a +54.7% increase. Moreover, with the approval and widespread rollout of Covid-19 vaccines, optimism surrounding a return to normalcy has blossomed as business and consumer confidence and demand are on the rise.

Chart 1 - U.S. Consumer Confidence



A consequence of the better-than-expected economic rebound and rising demand has been the development of widespread supply and demand imbalances. According to recent Institute for Supply Management surveys, these imbalances have become more evident as manufacturers, home builders, and service providers are unable to timely meet increasing consumer and business demand due to supply chain disruptions, logistic problems, depleted inventories, increasing lead times, and a shortage of parts and raw materials.

With the economy on the rebound and demand currently outpacing supply, the prospect of higher inflation has taken center stage and both the bond market and the Federal Reserve have taken notice. Since January 1, 2021, the yield on the 10-year treasury note has risen 0.83 basis points to 1.74% from 0.91%. The spike in long-term yields likely also reflects the tremendous amount of money supply growth and rising debt levels connected with fiscal policy economic relief and stimulus packages passed over the past year. Rising yields took their toll on bond market returns last quarter.

Table 1 - Bond Index Total Returns - Period Ending March 31, 2021

Fixed Income	1-Month	3-Month	YTD	1-Year	3-Year	5-Year	10-Year
Barclays High Yield	0.15	0.85	0.85	23.72	6.84	8.06	6.48
Barclays Municipal	0.62	-0.35	-0.35	5.51	4.91	3.49	4.54
Barclays Inter Gov't/Credit	-0.78	-1.86	-1.86	2.01	4.36	2.75	2.88
Barclays Aggregate	-1.25	-3.37	-3.37	0.71	4.65	3.10	3.44

While the Federal Reserve acknowledges and even forecasts that inflation is to rise in 2021 at a 2.4% annual pace, they believe the rise in inflation will be transient and move back to near their long-term target level of 2% in 2022 and 2023. Rising yields have also caused some consternation among equity investors as the prospect of record low long-term rates is likely gone and that is also too bad for someone who may owe me five bucks at year end. Although one component of stock price support has

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diminished, many of the drivers that propelled stock returns significantly higher this past year remain in place. Chiefly, the drivers are monetary policy, fiscal policy, and earnings growth.

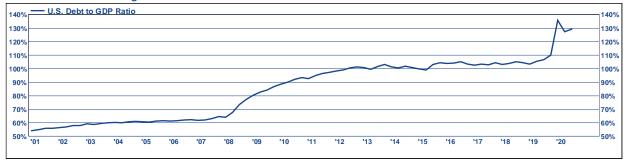
Table 2 - Stock Index Total Returns - Period Ending March 31, 2021

Equity	1-Month	3-Month	YTD	1-Year	3-Year	5-Year	10-Year
S&P 400	4.67	13.47	13.47	83.46	13.40	14.37	11.92
Russell 2000	1.00	12.70	12.70	94.85	14.76	16.35	11.68
Dow Jones Industrial	6.78	8.29	8.29	53.78	13.61	15.99	13.09
S&P 500	4.38	6.17	6.17	56.35	16.78	16.29	13.91
MSCI Developed	2.30	3.48	3.48	44.57	6.02	8.85	5.52
NASDAQ	0.48	2.95	2.95	73.40	24.54	23.44	18.22
MSCI Emerging	-1.51	2.29	2.29	58.39	6.48	12.07	3.65

At a recent press conference, Fed Chair Powell noted, "we will continue to provide the economy the support that it needs for as long as it takes." The Federal Reserve has repeatedly communicated and forecasted monetary policy will remain accommodative through at least 2023. The Federal Reserve has a dual mandate of maximum employment and price stability and it is the former that should keep monetary policy accommodative as several underlying labor market metrics remain weak, particularly for low-wage workers, minorities, and specific industries more adversely affected by Covid-19 like travel, hospitality, retail, and leisure.

Since the Covid-19 crisis began, U.S. fiscal policy support has been very strong with Congress passing six economic relief and support packages totaling \$5.3 trillion. This unprecedented level of support has boosted stock market returns and it appears the fiscal policy stimulus train is going to roll on with the rationale being "the risks of doing too little are far greater than doing too much." Despite the on-going economic recovery and strong economic and earnings growth forecasts, the Biden Administration will seek two more major fiscal policy initiatives to the tune of \$3 trillion which will push U.S. outstanding debt to GDP ratios to levels not seen since World War II.

Chart 2 - U.S. Outstanding Debt to GDP Ratio



The last and most important component that has helped advance market prices is the projected resurgence in corporate earnings growth in 2021. First-quarter 2021 (1Q21) S&P 500 earnings season is slated to kick-off in earnest the week of April 18th. According to the FactSet Earnings Insight report, 1Q21 earnings guidance has been more optimistic than normal due to increasing demand and higher revenue estimates. The report cited, "expected earnings for the S&P 500 for the first quarter are higher today compared to the start of the quarter." As of December 31, 2020, 1Q21 earnings were projected to grow y/y 15.8% vs. 23.3% as of March 26, 2021. The same holds true for full-year 2021 S&P 500

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earnings forecasts of 22.6% vs. 25.4% respectively. Much of the expected earnings growth for the next few years is already baked into the market.

Historically, the correlation between S&P 500 earnings growth and price appreciation is high. However, there are times when one component may lead the other and vice versa. The Great Recession caused considerable and widespread financial hardship and it took years for investor confidence and conviction in the economy to recover. Despite strong corporate earnings growth in 2010 and 2011, price appreciation of the S&P 500 Index lagged earnings growth and the forward price/earnings (FPE) multiple did not really begin to meaningfully expand until 2013. Today, the opposite holds true as the price of the S&P 500 Index has surged in anticipation of the corporate earnings rebound. So much so that the FPE multiple is trading six percentage points higher than the 10-year historical average (22.2x vs. 16.1x).

Typically, when the U.S. economy is coming out of a recession, earnings are rebounding, and stock markets are advancing, the penchant would be to overweight stocks but this definitely has not been, and is not, a typical environment. Stock markets have already baked in, more like overcooked, all facets of growth while the bond market is still prepping ingredients but has preheated the oven. The Fed has indicated they are comfortable with modestly higher long-term yields, above target rates of inflation, a growing balance sheet, and robust fiscal stimulus spending. The jury is still out as to whether the bond market feels the same way but there is certainly a wide disconnect right now between stock and bond markets.

Covid-19 remains the main risk to the U.S. economy as the spread and control of the virus is still uncertain and volatile. Look no further than the new restrictions recently imposed in Italy, France, and Germany.

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Sources: FactSet, The Conference Board, Institute for Supply Management, The Federal Reserve, The Conference Board

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