

Economic & Market Overview

August 2021



U.S. Recovery Gathers Strength, Rest Of World Unsynchronized

- Fed policy and fiscal support remain key factors
- Vaccine deployment spurs reopening and unleashes pent-up demand

Inflation and Fed Policy Take the Spotlight

- Fed shift in inflation framework – Average Inflation Targeting vs. 2% “hard target”
- Powell: “Inflation higher and a little bit more persistent than expected.”
- CPI up 5.4% in June, biggest monthly jump in 30 years

Equities: Rally Continues

- Sector performance shifts back to US large growth in 2Q
- Valuations suggest lower returns ahead

Bonds: Lower Yields in 2Q Raise Questions About Economic, Inflation Outlooks

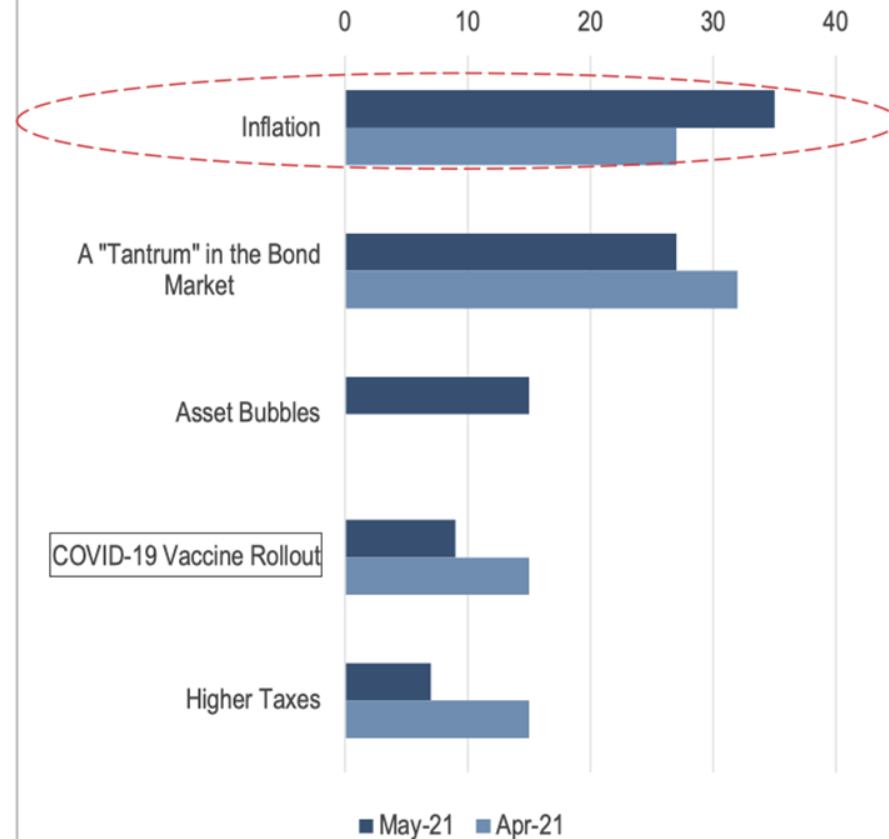
- Fiscal and Monetary policies geared toward growth, running risk of upside surprise in inflation
- No compensation for additional duration risk
- Continue to overweight credit exposure

Risks and Challenges

Potential Risks

- Inflation shocks as economies re-open amidst record stimulus
- Shift in Fed policy
- “Peak growth” in a shorter-than-usual cycle
- Richly valued assets across markets driven by massive liquidity
- COVID-19 resurgence and/or vaccine delays or uneven roll-out
- Washington DC policy uncertainty – stimulus and taxes
- Technology disruption - cyber-attacks and big tech regulation
- Geopolitical risks
 - U.S.-China tensions
 - Middle East crisis
 - North Korea nuclear ambitions
 - Post-Brexit euro-zone challenges

Biggest “Tail Risks”: Global Fund Manager Survey (%)



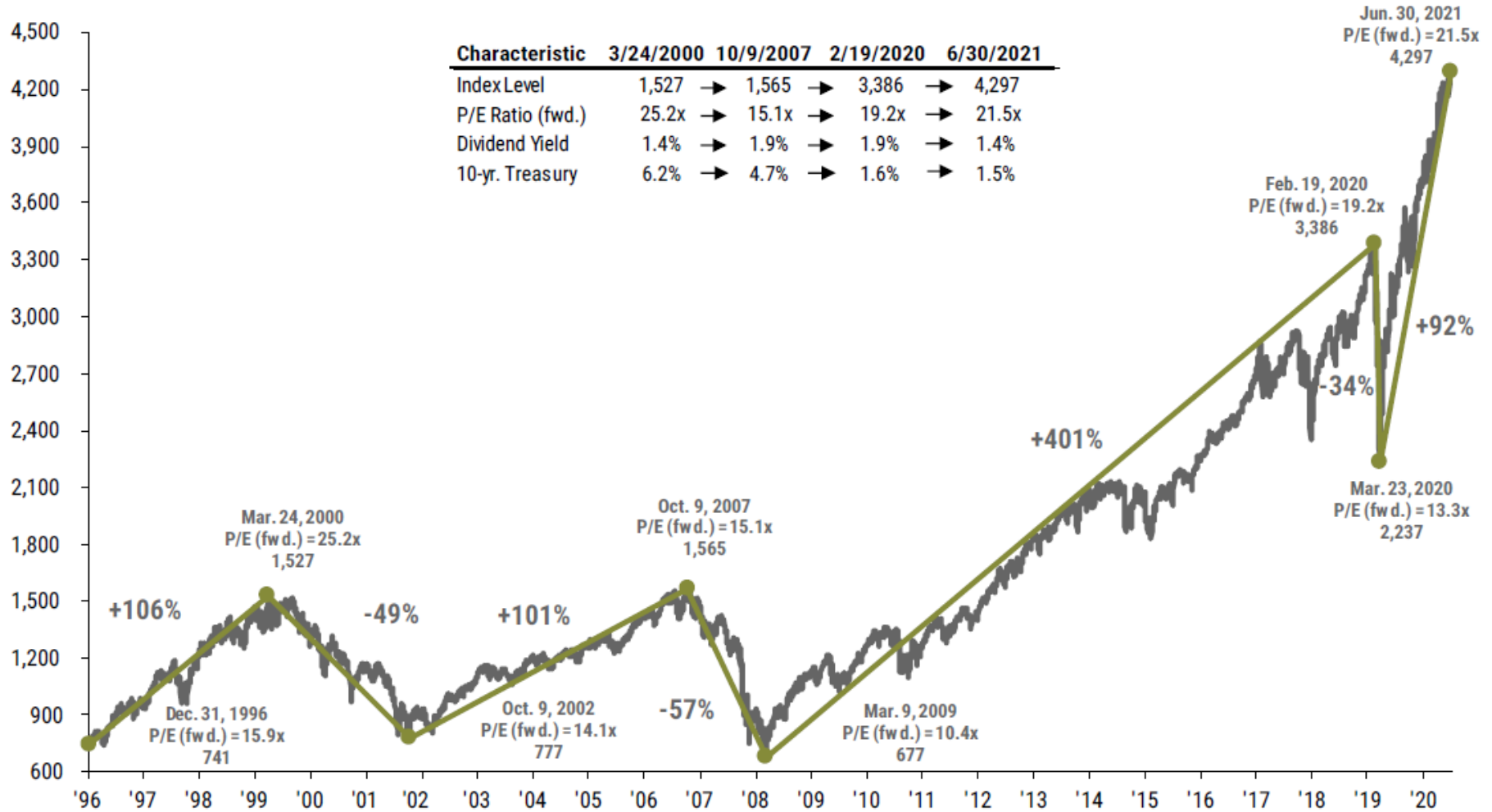
Post-COVID Rally Driven By Unprecedented Fiscal And Monetary Policy

Comparing the Path of Today's Crisis to Past Stock Market Shocks



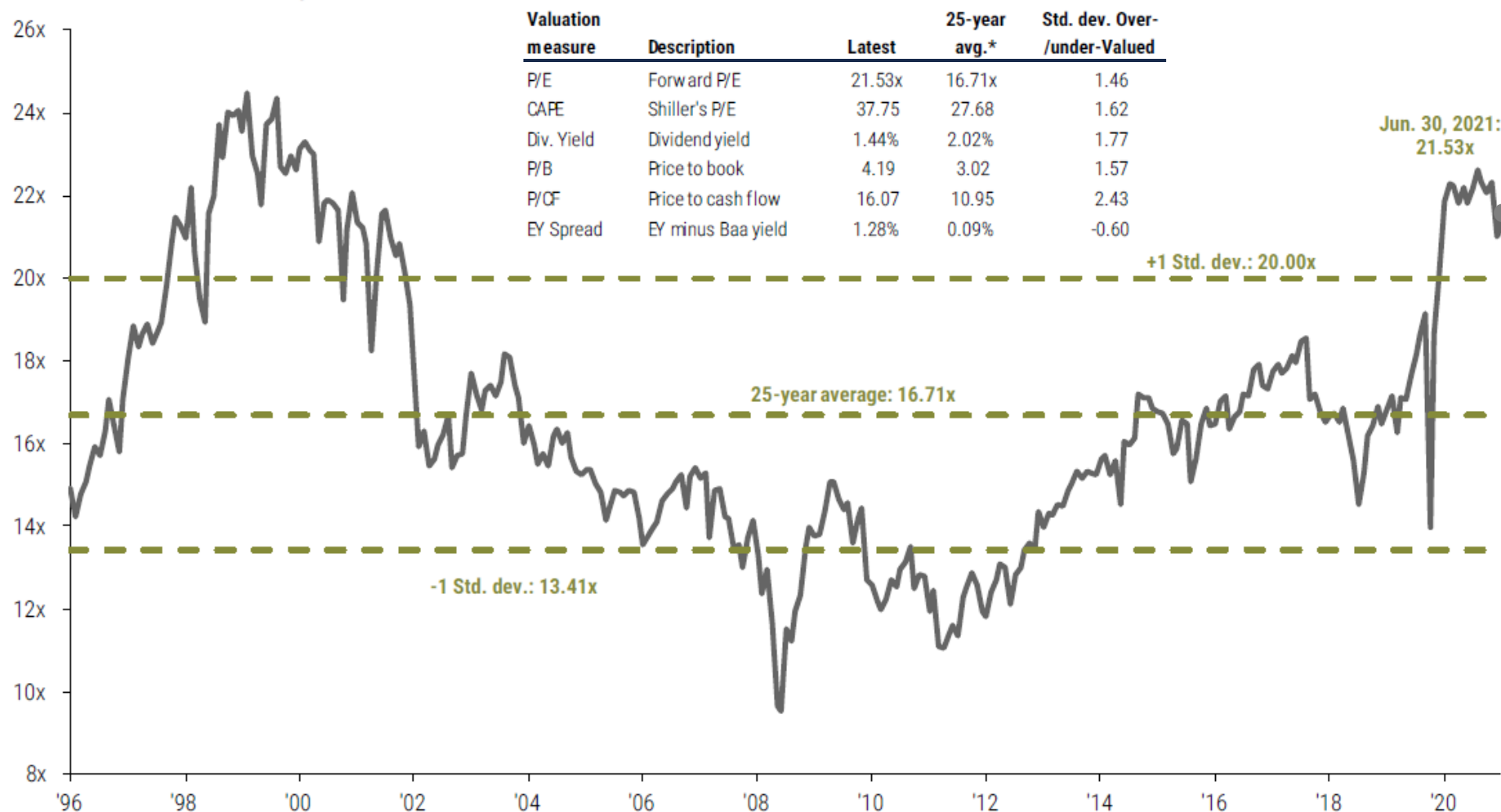
Rally Takes U.S. Equities to New High

S&P 500 Price Index



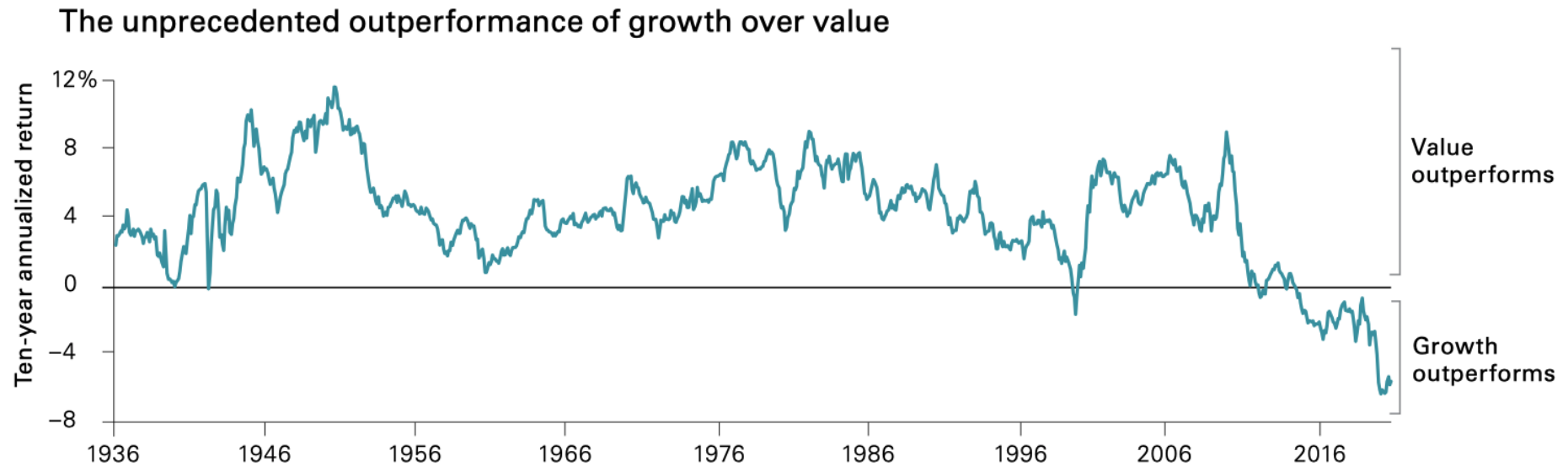
Stock Surge Leaves Valuations Extended, But Earnings Growth Mitigates Level

S&P 500 Index: Forward P/E ratio



Source: FactSet, FRB, Robert Shiller, Standard & Poor's, Thomson Reuters, J.P. Morgan Asset Management. Price-to-earnings is price divided by consensus analyst estimates of earnings per share for the next 12 months as provided by IBES since June 1996, and J.P. Morgan Asset Management for 6/30/21. Current next 12-months consensus earnings estimates are \$200. Average P/E and standard deviations are calculated using 25 years of IBES history. Shiller's P/E uses trailing 10-years of inflation-adjusted earnings as reported by companies. Dividend yield is calculated as the next 12-months consensus dividend divided by most recent price. Price-to-book ratio is the price divided by book value per share. Price-to-cash flow is price divided by NTM cash flow. EY minus Baa yield is the forward earnings yield (consensus analyst estimates of EPS over the next 12 months divided by price) minus the Moody's Baa seasoned corporate bond yield. Std. dev. over-/under-valued is calculated using the average and standard deviation over 25 years for each measure. Guide to the Markets -U.S. Data are as of June 30, 2021..

Style: Value Versus Growth Stocks – Reversal Ahead?

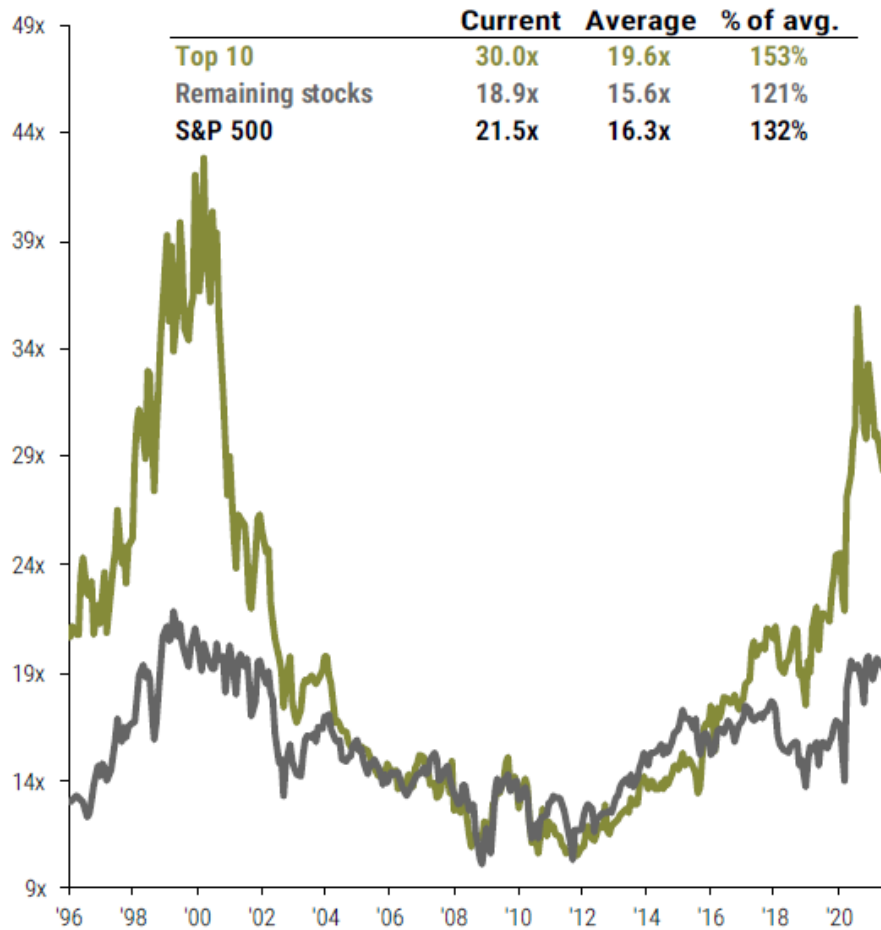


Note: The chart displays annualized 10-year trailing returns of a long-short value versus growth portfolio over the period of June 1936 to June 2021.

Size: Disparity Between Mega-Cap and All Others

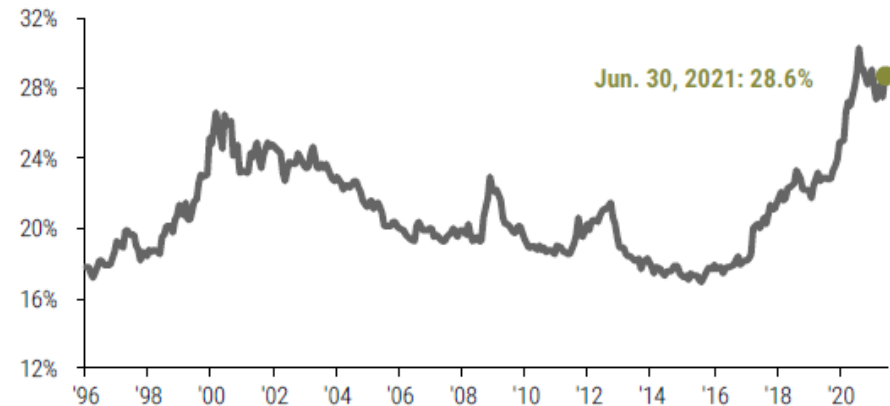
P/E ratio of the top 10 and remaining stocks in the S&P 500

Next 12 months



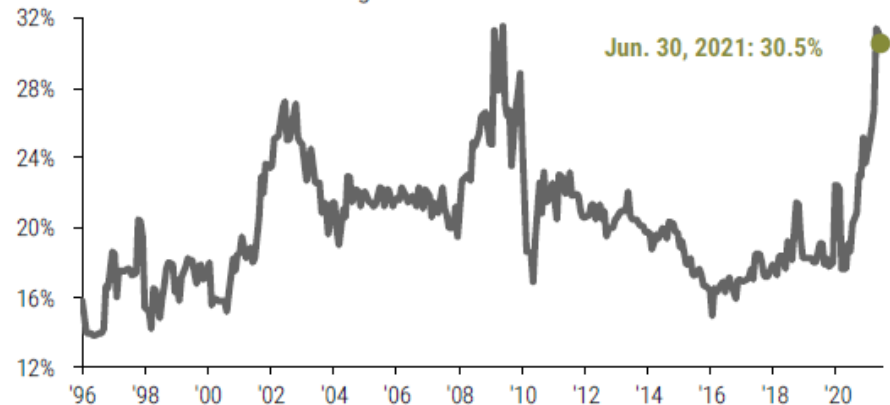
Weight of the top 10 stocks in the S&P 500

% of market capitalization of the S&P 500



Earnings contribution of the top 10 in the S&P 500

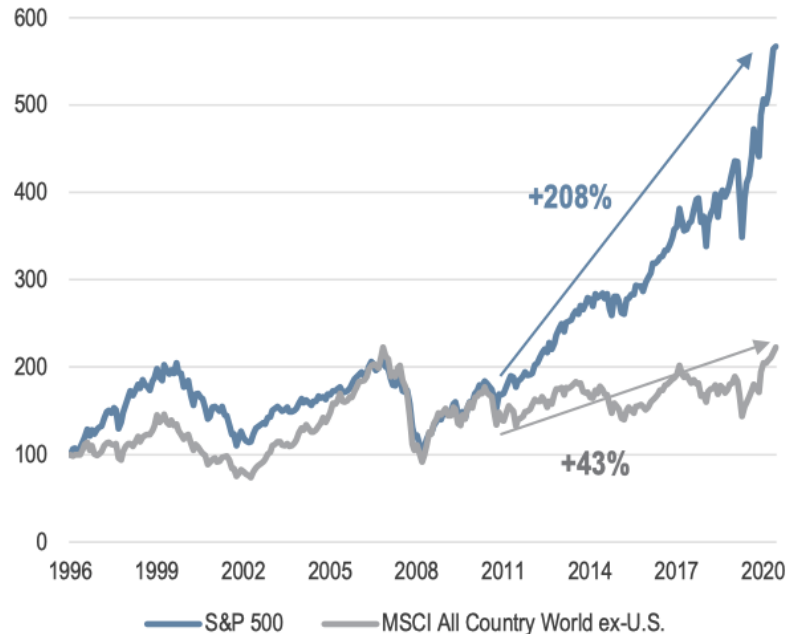
Based on last 12 months' earnings



Global Equities: Opportunities Outside U.S. Seem More Attractive

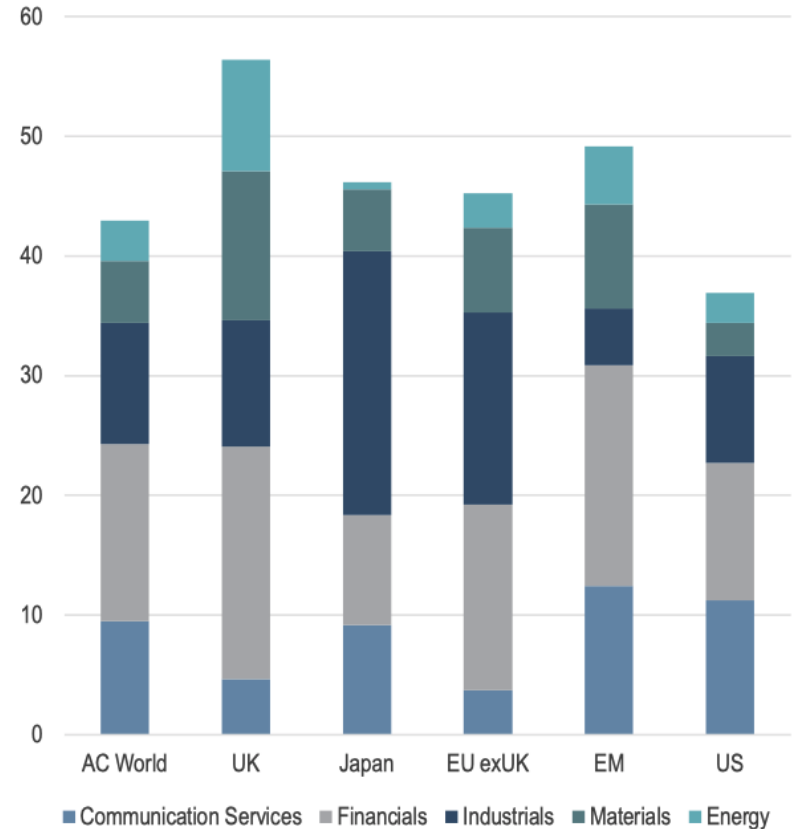
Foreign markets have more Value/Cyclical Exposure

U.S. and International Equities at Inflection Points



	P/E	20 Year Average	Dividend Yield	20 Year Average
S&P 500	22.4x	16.8x	1.4%	2.0%
ACWI ex U.S.	16.2x	13.8x	2.3%	2.9%
As % of U.S.	72%	82%	166%	145%

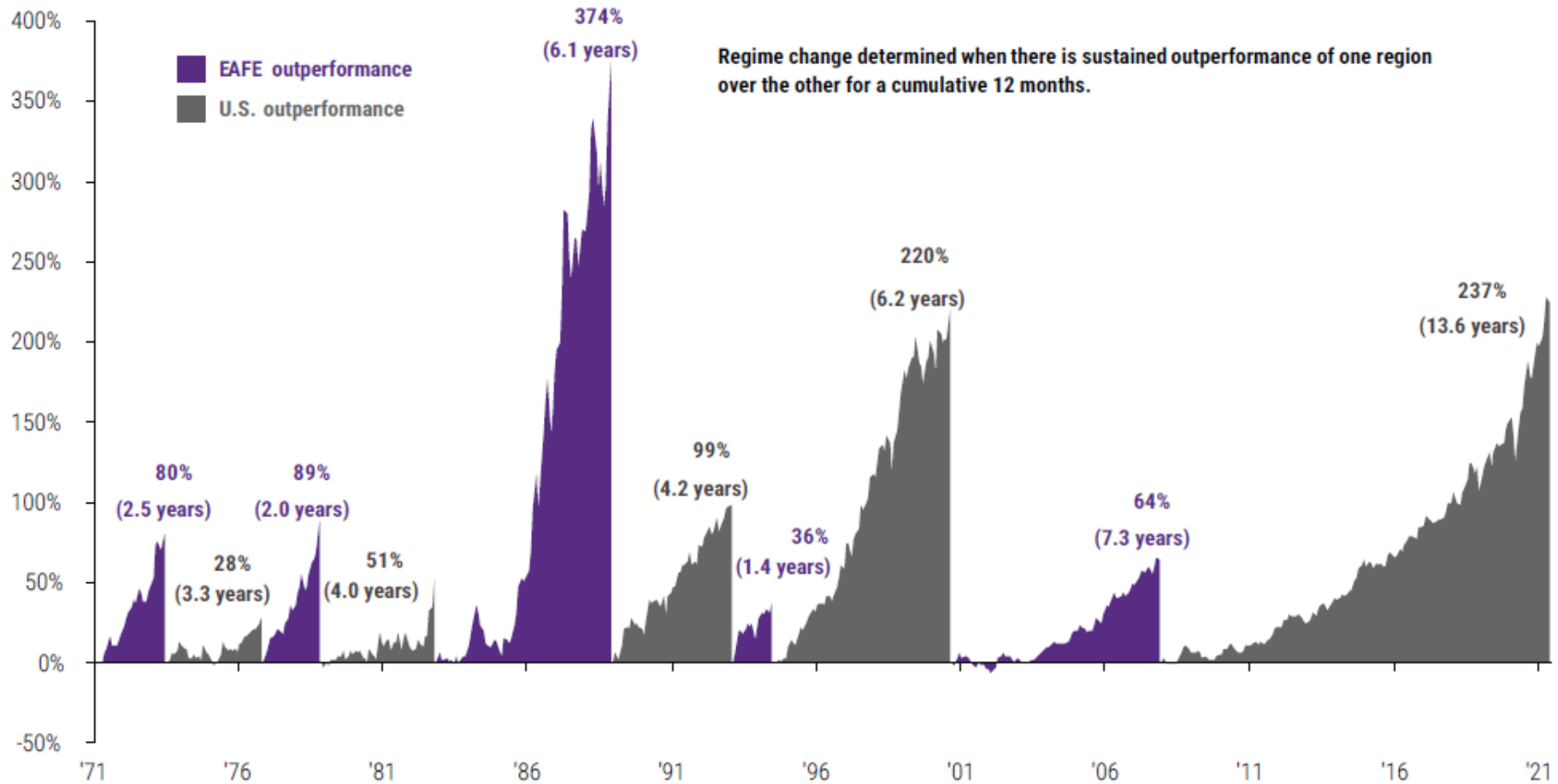
Weight of Value Sectors (%)



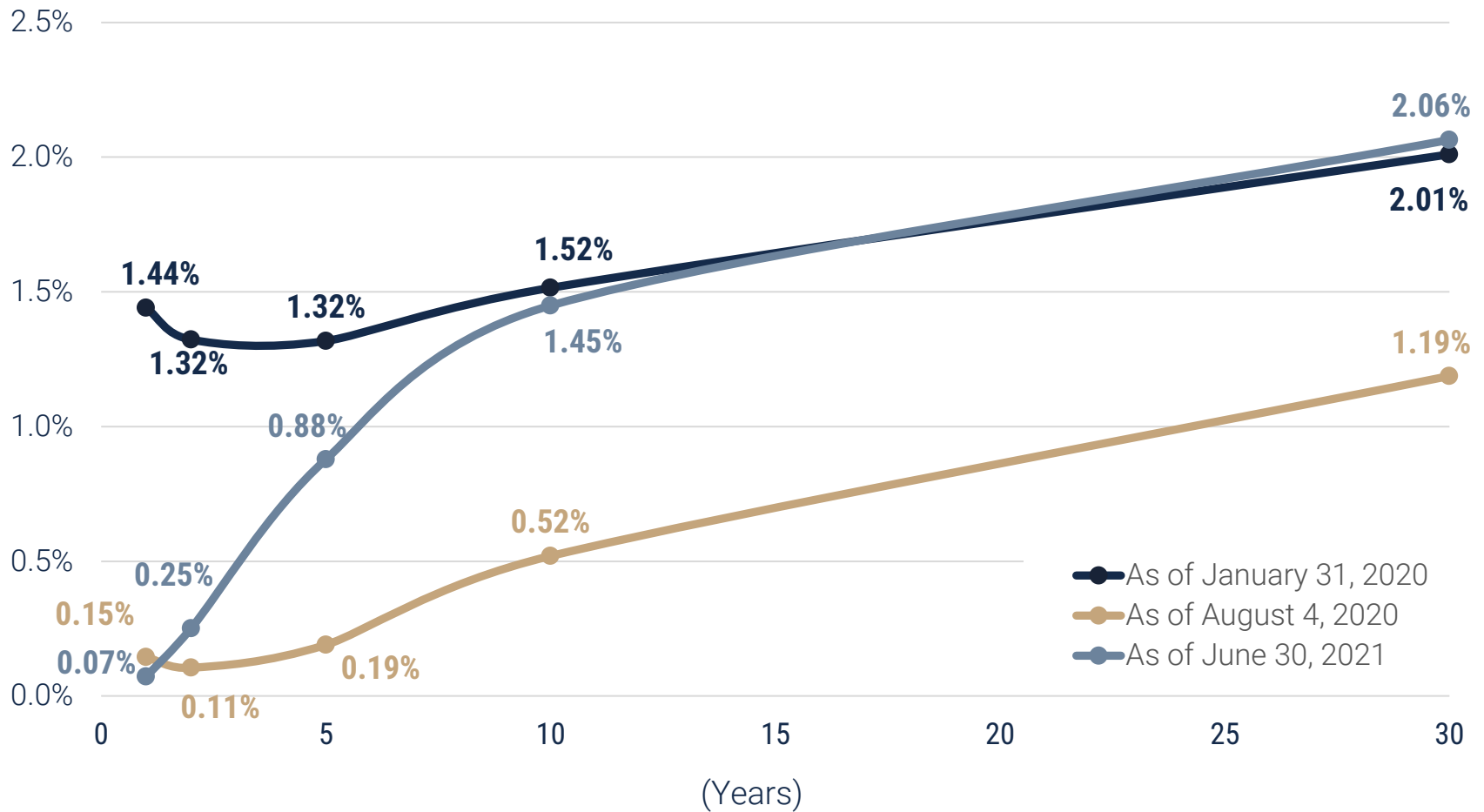
Performance Cycles by Geography

MSCI EAFE and MSCI USA relative performance

U.S. dollar, total return, cumulative outperformance*



U.S. Treasury Yield Curves



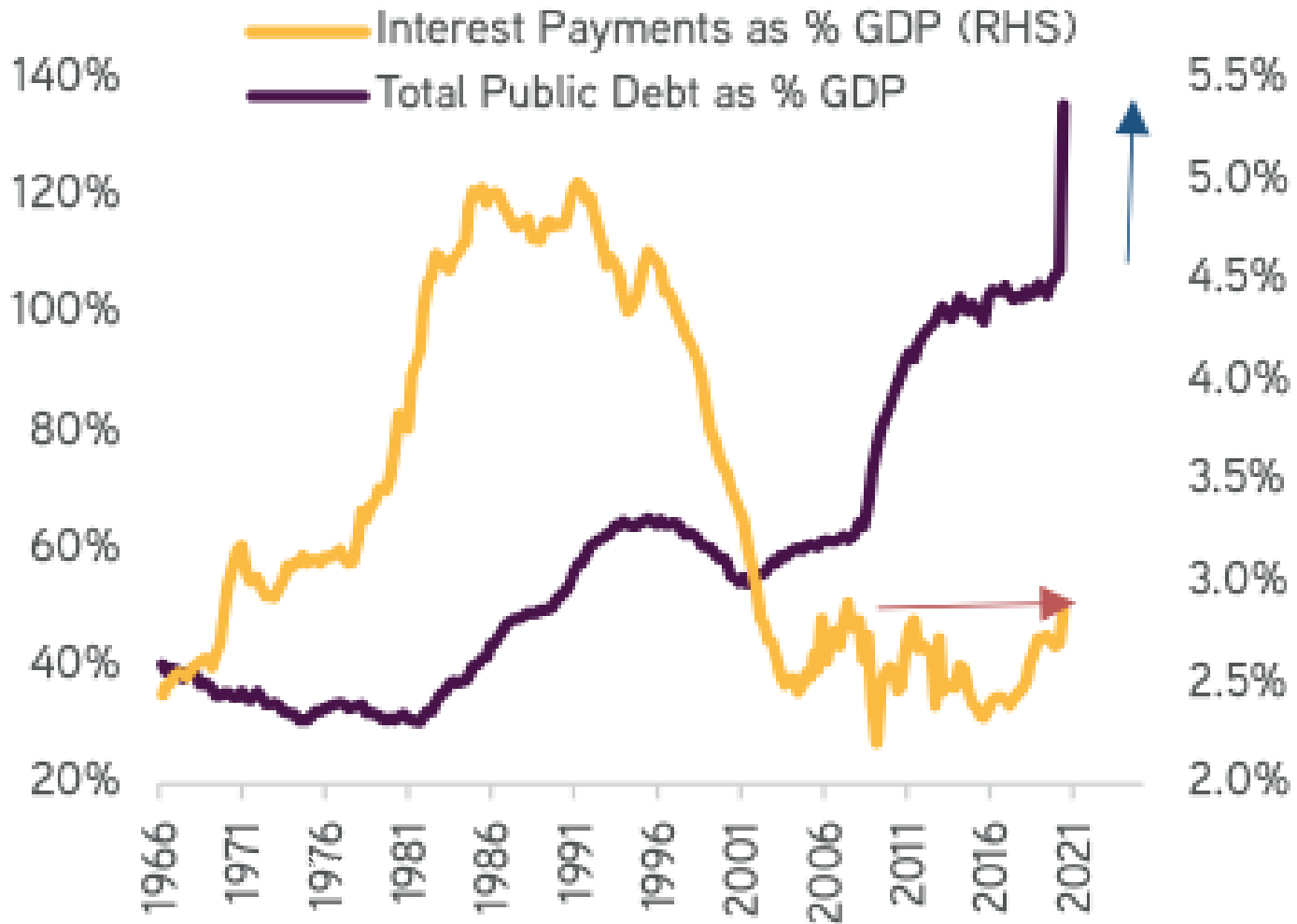
Source: Factset. US Treasury yield curves as of 1/31/2020, 8/4/2020, and 6/30/2021.

Three scenarios for 10-year bond yields

U.S. 10-year Treasury note



Cost of Debt Will Grow As Interest Rates Rise



Asset Class	Scenario 1	Scenario 2	Scenario 3
Equities	RISE	FALL	FALL
Defensive Fixed Income	RISE	FALL	FALL
Gold	FALL	RISE	FALL
Yield Curves	FLATTEN	STEEPEN	FLATTEN
Industrial Metals	?	RISE	FALL

- **Scenario 1 – The Fed (Powell) view is correct:** the coming rise in (2021) inflation is a one-off change in the price level, but does not lead to second-round effects. So, price pressures diminish again in 2022 – and those who argue that the fiscal easing is “right-sized” prove to be correct.
- **Scenario 2 – A regime change occurs – with inflation “taking off”:** Inflation expectations “move up a gear” and policymakers remain “behind the curve” – leading to a “return to the 1970s” in some form: i.e. higher inflation hurting both equities and bonds.
- **Scenario 3 – Central banks belatedly becoming aggressive** – with central banks deciding they need to act aggressively (if late) to earn credibility. They therefore hike, pushing the economy into a recession. Again, a poor outcome for equities.

10 - Year Asset Class Return Outlook

Equities	Return projection	Median volatility
U.S. equities	2.6%–4.6%	16.7%
U.S. value	3.4%–5.4%	18.8%
U.S. growth	–0.5%–1.5%	17.7%
U.S. large-cap	2.4%–4.4%	16.4%
U.S. small-cap	2.4%–4.4%	21.7%
U.S. real estate investment trusts	2.4%–4.4%	19.5%
Global equities ex-U.S. (unhedged)	5.5%–7.5%	18.9%
U.S. inflation	1.4%–2.4%	2.4%

Fixed income	Return projection	Median volatility
U.S. aggregate bonds	1.4%–2.4%	4.5%
U.S. Treasury bonds	1.1%–2.1%	4.7%
U.S. credit bonds	1.8%–2.8%	5.7%
U.S. high-yield corporate bonds	2.2%–3.2%	10.2%
U.S. Treasury Inflation-Protected Securities	0.8%–1.8%	7.0%
U.S. cash	1.3%–2.3%	1.3%
Global bonds ex-U.S. (hedged)	1.3%–2.3%	3.8%
Emerging markets sovereign	2.1%–3.1%	9.9%

- **Balanced outlook for risk assets in general**
- **Maintain core portfolio of U.S. stocks, but look for small cap and value rebound to continue**
- **Increase non-US (developed and emerging) allocations**
- **Keep bond durations short – low risk**
- **Think long term**

Market Returns Summary – June 30, 2021

Equity Index	1 Week	MTD	1 Month	QTD	YTD	1 Year	3 Year	5 Year
Dow Jones Industrial Average	1.6	0.0	0.0	5.1	13.8	36.2	15.0	16.6
S&P 500 Index	1.2	2.3	2.3	8.5	15.3	40.6	18.6	17.6
Large Cap Stocks (Russell 1000)	1.2	2.5	2.5	8.5	15.0	42.9	19.1	17.9
Growth	1.7	6.3	6.3	11.9	13.0	42.3	25.0	23.6
Value	0.7	-1.1	-1.1	5.2	17.0	43.5	12.4	11.8
Small Cap Stocks (Russell 2000)	0.7	1.9	1.9	4.3	17.5	61.7	13.5	16.4
Growth	1.9	4.7	4.7	3.9	9.0	51.1	15.9	18.7
Value	-0.5	-0.6	-0.6	4.6	26.7	72.9	10.2	13.6
MSCI All Country World Index	0.8	1.4	1.4	7.5	12.6	39.7	15.1	15.2
International Stocks (MSCI EAFE)	-0.9	-1.1	-1.1	5.4	9.2	32.8	8.7	10.8
Growth	-0.5	0.1	0.1	7.6	7.1	31.3	12.8	12.8
Value	-1.4	-2.3	-2.3	3.3	11.1	34.1	4.4	8.4
Emerging Markets Stocks (MSCI EM)	2.2	0.2	0.2	5.1	7.6	41.2	11.6	13.4
Fixed Income Index/ETF	1 Week	MTD	1 Month	QTD	YTD	1 Year	3 Year	5 Year
Barclays U.S. Aggregate Bond Index	0.2	0.7	0.7	1.8	-1.6	-0.3	5.3	3.0
iShares 1-3 Year Treasury Bond ETF	0.0	-0.2	-0.2	-0.1	-0.1	-0.1	2.6	1.5
iShares 3-7 Year Treasury Bond ETF	0.0	-0.1	-0.1	0.7	-1.5	-1.5	4.4	2.0
iShares 20+ Year Treasury Bond ETF	0.5	4.4	4.4	7.0	-7.9	-10.6	8.0	3.0
iShares TIPS Bond ETF	0.3	0.7	0.7	3.2	1.5	6.0	6.3	4.0
iShares National AMT-Free Municipal Bond ETF	0.0	0.3	0.3	1.5	0.8	3.6	4.8	2.9
SPDR Barclays Intermediate Term Corporate Bond ETF	0.2	0.5	0.5	1.6	-0.6	2.3	6.0	3.7
SPDR Barclays High Yield Bond ETF	0.4	1.3	1.3	2.1	2.8	14.0	6.6	6.2
PowerShares Senior Loan ETF	0.1	0.0	0.0	0.8	1.0	7.1	3.1	3.4
SPDR Barclays International Treasury Bond ETF	-0.5	-1.7	-1.7	0.9	-5.7	2.4	3.0	1.4
iShares JPM USD Emerging Market Bond ETF	0.3	0.9	0.9	4.3	-1.4	7.0	6.6	4.2

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Yield to Call is the yield of a bond or note if you were to buy and hold the security until the call date. This yield is valid only if the security is called prior to maturity.

Yield to Maturity is the rate of return anticipated on a bond if it is held until the maturity date.

During the period(s) shown, there were no material market or economic conditions which affected the results portrayed. With the exception of several market corrections during the period(s), the overall market as measured by the S&P 500 was generally rising. If such trends are broken, the clients may experience real capital losses in their managed accounts.

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MSCI Emerging Markets Index: A free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets. The MSCI Emerging Markets Index consists of the following 21 emerging market country indices: Brazil, Chile, China, Colombia, Czech Republic, Egypt, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Russia, South Africa, Taiwan, Thailand, and Turkey.

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