Market Commentary

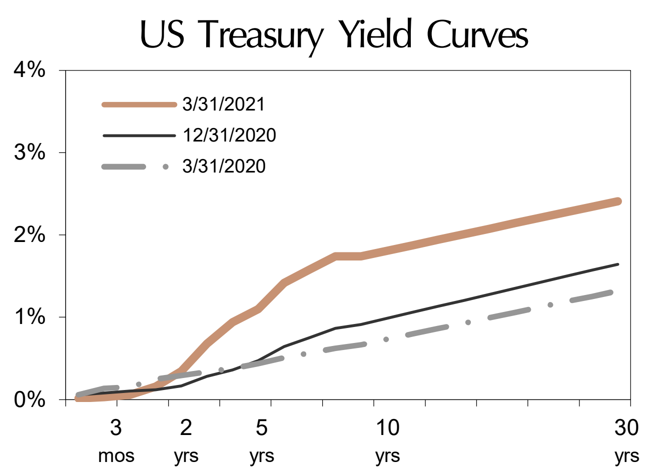
HOPE SPRINGS ETERNAL!

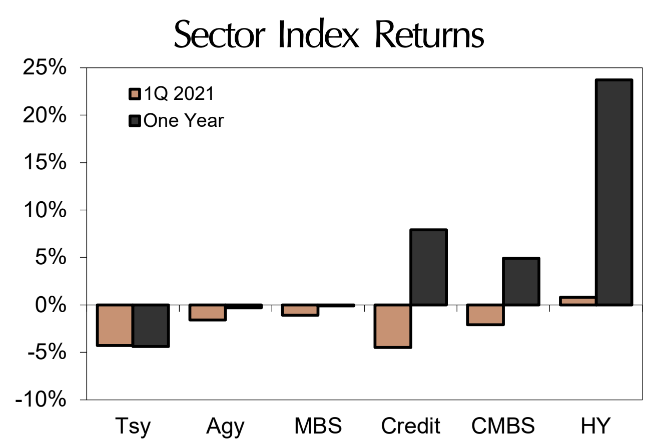
March 31, 2021

As the calendar "turns" to Spring hope fills the air as the grass greens and the trees bud, much like investors feel entering the second quarter of 2021, with vaccines in the air and economic growth budding. According to the Cambridge dictionary, hope is "something good that you want to happen in the future, or a confident feeling about what will happen in the future," and optimism is "the quality of being full of hope and emphasizing the good parts of a situation or a belief that something good will happen." As we exit the 1st Quarter of 2021, there appears to be an abundance of hope that the worst parts of the pandemic are behind us, as well as a mountain of optimism that while the economy continues to gain steam, the consumer and pockets of the hard-hit service sector are on the verge of participating – just adding to the "buds" of Spring!

The year began with a hopeful tone, as vaccines were being rolled-out, not one (Pfizer- BioNTech), not two (Moderna) but now three (Johnson & Johnson), with a fourth (AstraZeneca) still possible. The "re-opening" trade was alive and well, and value stocks continued to out-pace growth, a rotation we witnessed toward the end of 2020. But, how soon we forget, as it was just a year-ago that this all started with a BANG!...as travel bans, shut-downs, CDC and World Health Organization protocols, political bickering and miss-steps, as well as nightly recaps of hospitalizations and deaths were constant reminders of the peril, we were all faced with. Terrible! Simply terrible! Not to mention the historic sell-off we witnessed in the markets. In the 33 days between February 19th and March 23, 2020, the MSCI World Stock Market Index lost 34% of its value! Also, terrible!

For the 1st quarter we witnessed a broad-based rally across all equity sectors and indicies, as the re-opening trade continued to gain speed. The S&P 500 Index was +6.17%, and for the last 12-months/year +56.35%. A simply stellar return! Value stocks continue to out-perform growth, as the Russell 1000 Value index was +11.3% for the quarter versus 0.9% for the Russell 1000 growth index. However, the big winners for the quarter were small-cap stocks which beat large, as the Russell 2000 small-cap index was +12.7% for the quarter and a whopping +94.85% for the year! Additionally, International and Emerging Market stocks were positive, +4.0% and +2.3% respectively, and for the last year while still positive were not quite as stellar as their domestic counterparts, +45.9% and +58.4% respectively. REITS were also up nicely for both periods, according to the Dow Jones U.S. Select REIT Index +10.0% for the quarter and +36.7% for the year.





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The biggest macro event for the quarter resided on the fixed income side, as interest rates rose quite dramatically with inflation fears beginning to escalate along with economic growth, not to mention an additional $1.9 trillion stimulus package from President Biden's administration. As we outlined in last quarters Commentary, "the combination of additional fiscal stimulus, a weaker US dollar and the Fed allowing inflation to rise above their 2% target, suggests higher interest rates," and boy did it! The yield on the 10-Year Treasury increased 83 bps to 1.74%, and the 30-Year Treasury bond yield increased 77 bps to finish at 2.41%. For the quarter, the Barclays US Aggregate Index declined -3.11%. From the onset of the quarter our portfolio durations were significantly below their benchmarks and we expect the yield curve to gradually steepen through the end of the year, despite the slight flattening we witnessed during the quarter. Credit spreads narrowed during the quarter fueled by massive central bank liquidity and now only look like fair value versus treasuries. Although we continue to maintain an overweight in credit exposure, our portfolios credit spread duration is slightly less than that of their benchmarks. We have maintained an underweight in MBS versus the index, given the uncertainty over potential defaults due to temporary layoffs and the extension of the CARES act forbearance program until June 30, 2021.

Economically, the U.S. continues to re-open and recover at an accelerated pace as the vaccine availability and rollout has picked up steam in the 1st Quarter. The latest estimate for 1Q growth according to GDPNow is 6.0%. As the re-opening continues and small business and heavily impacted sectors, such as restaurants and travel and leisure rebound from the depths of the pandemic, we expect that growth will continue to expand into the second half of 2021, and possibly beyond. Core inflation (CPI) continues to inch upward though, which has fixed income managers on their toes attempting to look beyond what will potentially be temporary spikes due to the pandemic shutdown last year. March CPI was 0.6% and 2.6% year-over-year (YOY) and 1.6% ex-food and energy, historically volatile sectors. In fact, gasoline prices were up 13.2% over the last year. Under the FED's stated 2% average target (where concern may start to mount), as fixed income mangers, we are cognizant and wary of the potential for the economy to begin "running hot" in coming months (Roaring '20's?) leading to higher interest rates thus stripping portfolios of their principal value. The $1.9 trillion infrastructure package President Biden signed just adds to our concern. On the labor front, total nonfarm payroll employment rose 916,000 in March, and the unemployment rate fell to 6.0%, according to the Bureau of Labor Statistics. The number of unemployed at 9.7 million continues to trend down but is still 4 million higher than the pre-pandemic level in February 2020.

Domestically, despite the positive return for the S&P 500 index for the quarter, the underlying sectors seemed to tell a different story, as only four sectors had positive returns lead by Energy +26.8%, followed by Industrials +5.3%, Finance +5.1% and Consumer Discretionary +4.4%. Technology issues were the big losers for the quarter -16.6%, followed by Healthcare -12.9% and Communication Services -5.0%. For the quarter many of the top performing stocks were in the Energy sector, such as Marathon Oil +61%, Occidental Petroleum +54% and Diamondback Energy + 53%.

In closing, while Spring has sprung, so has everyone's hope and optimism, and for good reason. Vaccines are here and being widely distributed. The Federal Reserve and U.S. Treasury Department have been the ultimate fiduciaries in guiding the U.S. economy through one of the most tragic and volatile times in History! It bears repeating, one could not have predicted the tumultuous year of 2020, but are thankful to see it in the rear-view mirror! However, the concern going forward from an investment standpoint remains the fallout from the pandemic and the unprecedented stimulus and baggage that we are left with? Potential setbacks with the vaccine, the massive debt and FED balance sheet, and of course INFLATION. In the near-term though we continue to look for a "Roaring-Twenties" environment which should help to propel stocks for the foreseeable future or at least until the FED begins to hint of a rate increase. Stay tuned!

As always, we will remain diligent and disciplined in our approach, realizing that it is these principles that steer us to the VALUE capital markets have to offer long-term investors. Stay safe, stay well and when comfortable in doing so, GO OUT AND SPEND! (Remember: consumer spending makes up 2/3 of the U.S. economy)