CIO View
Monthly Strategy Snapshot
March 2021

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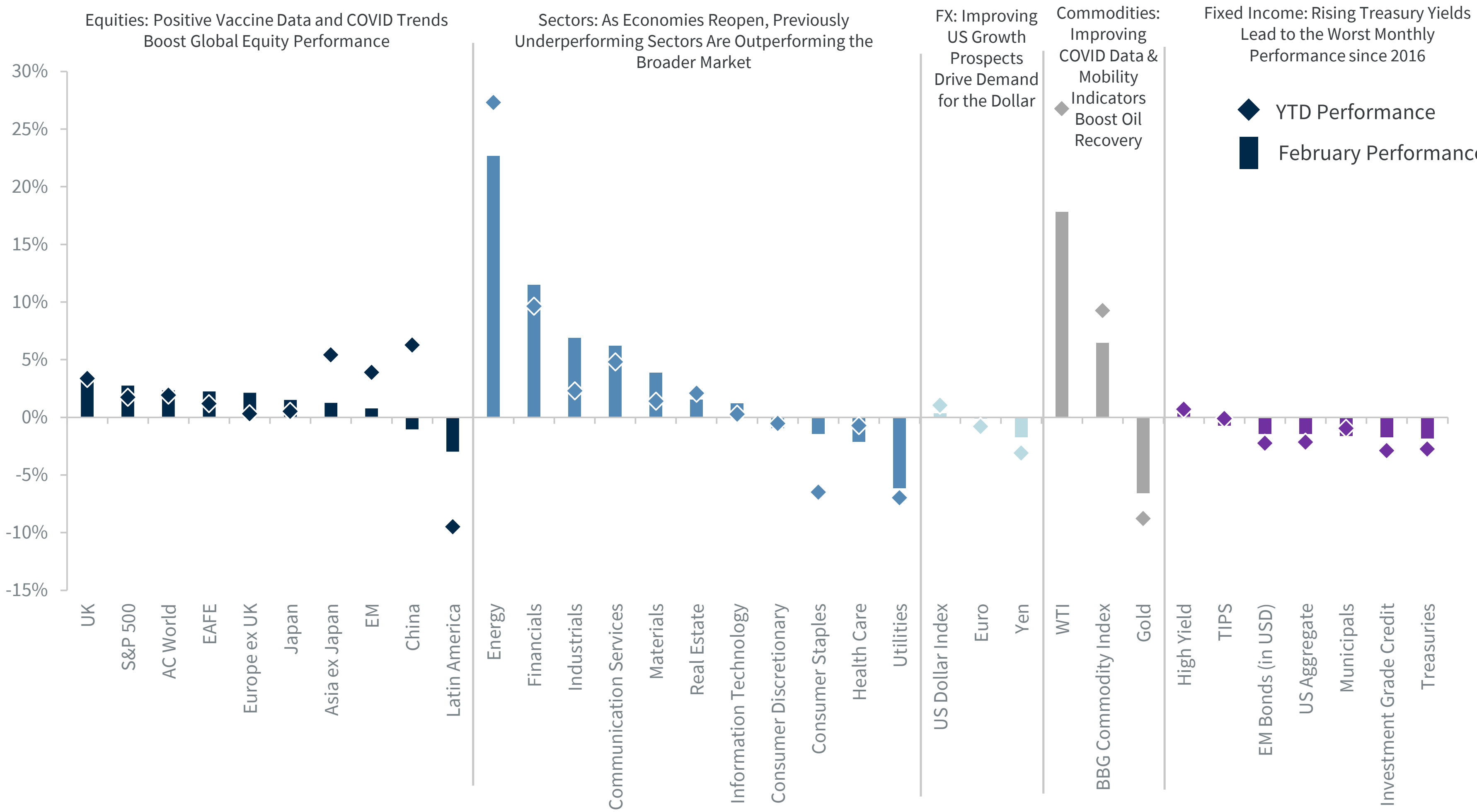
Chief Investment Officer

Returns By Asset Class | Month and Year-to-Date Returns

Returns by Asset Class



Data as of February 28. All international equity indices are MSCI indices and in USD. Diamonds represent the year-to-date total returns and bars represent monthly total returns.

Global Economy | COVID Improvements Boost Economic Recovery

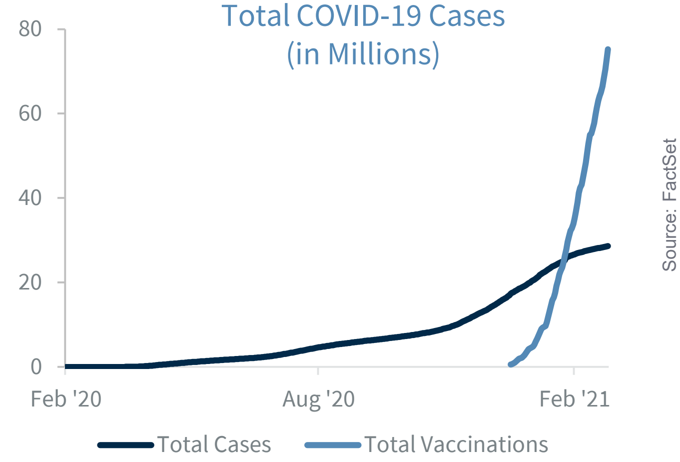
Global Economy | Recent Trends

- The US has likely turned the corner in the battle against the coronavirus pandemic with **average daily deaths down ~50%** from the peak, **hospitalizations down ~70%** from the peak, and the **positivity rate falling below 5%** at the end of February. Globally, average new cases have declined ~63% from their peak in January but still average ~360,000 new cases a day.
- Vaccine rollout has been better than expected as the increased number of doses from Pfizer and Moderna and the J&J single-shot vaccine (received emergency use authorization on 2/27) will allow more doses to be administered quicker than anticipated. **Over 75 million doses were administered by the end of February,** more than double the number of total cumulative cases.
- Consistent with improving virus conditions, **real-time economic activity levels have improved markedly** as mobility indicators (e.g., TSA screenings, hotel bookings) are moving higher.
- An increase in pandemic support, both checks to individuals and extended unemployment support, boosted **personal spending by 10% in January**. We expect this momentum to continue as Biden's **$1.5-1.9 trillion 'Rescue' plan** is likely to be passed by Congress in March.
- Improving economic conditions and record stimulus have sparked investors' fears that inflation will pick up; **however, we believe such concerns are overdone**. This is consistent with the Fed's thinking, as it reiterated that it will look through any transitory near-term increase in inflation.
- **Jobless claims fell 10% in the first weeks of February** (reaching 730,000 for the week ended February 19) reflecting the sharp drop in COVID cases and reopening of the economy.

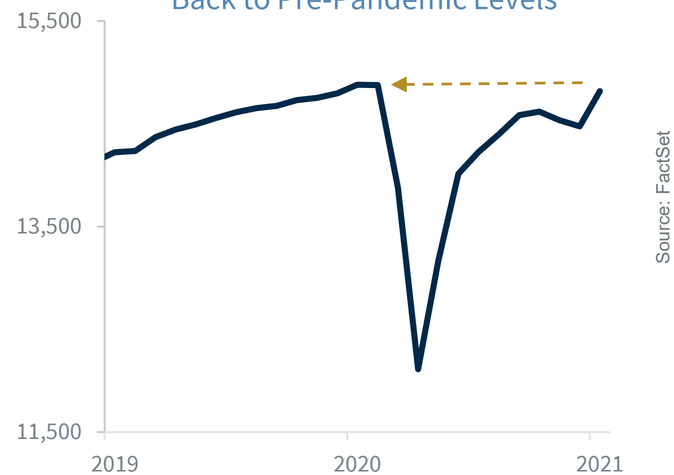
Global Economy | 2021 Outlook

- **Global economic momentum is likely to continue in 2021** as most G20 countries are likely to experience between 3% and 9% GDP growth for the year as social distancing measures wane and economies return to more normal activity. Similarly, **we expect US GDP to grow at ~4.9% in 2021**, despite COVID-19 remaining a key risk for the trajectory of economic growth (evident by the elevated levels of new cases internationally and new mutations). Though wide-sweeping lockdowns as seen in the spring of last year are unlikely to return, several countries around the world continue to impose localized shutdowns in response to the recent case surge.
- Over the medium to longer term, continued **aggressive actions from policymakers (both from a fiscal and monetary perspective) will remain supportive of economic growth**. Globally, central bank balance sheets are increasing while governments continue to pursue additional fiscal stimulus. The Fed alone could reach $10 trillion by the end of 2021 (up from ~$7.6 trillion).
- As vaccines become more widely available, **we expect spending on services to increase after the COVID-related decline in 2020.** As services make up ~66% of total US consumer spending, the increase will be a boost for economic growth going forward.

Total Vaccinations Almost Triple Total COVID-19 Cases (in Millions)



Personal Consumption Nearly Back to Pre-Pandemic Levels



Equities | Interest Rate Surge Stirs Market Volatility

Global Equities | Recent Trends

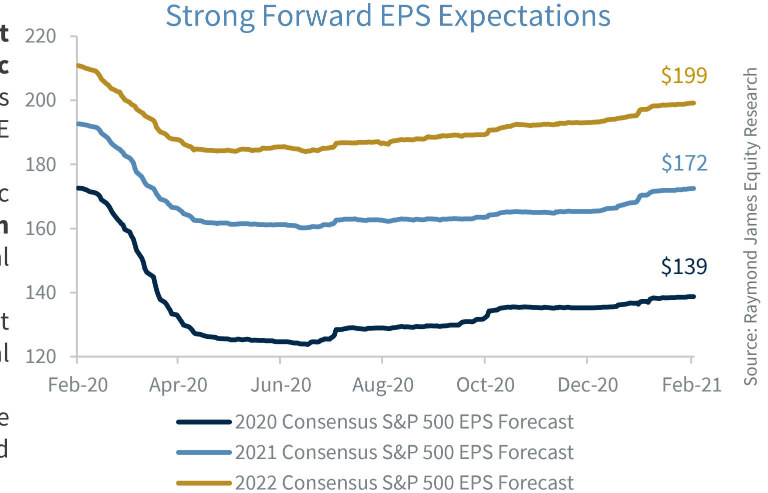
- After getting off to the best start to a February (5.9% through February 12) in the last 30 years, **volatility increased into month end as the surge in interest rates** led to concerns over current elevated equity valuations.
- Despite the pullback at the end of the month, **the S&P 500 was up 2.6% in February, and 7 out of 11 sectors were positive for the month.** As COVID statistics improve and economies continue to reopen, previously underperforming sectors tied to the reopening such as **Energy (22.7%) and Financials (11.5%) were the best performers** in February.
- Small-cap equities continued to outperform in February, as the **Russell 2000 outperformed the S&P 500 for the sixth straight month**—the longest streak since 2003.
- Q4 earnings season came in significantly better than expected as **year-over-year EPS growth ended in positive territory** for the first time in four quarters. **79% of companies beat their earnings estimates by an aggregate of 14.8%** (3x the long-term average of 4.5%). Current consensus estimates reflect **S&P 500 earnings growth of 24% in 2021 (to $172)**, and we see the potential for significant upside to this forecast in the event that the economic reopening and fiscal stimulus leads to better than expected economic growth.
- While still in positive territory, **rising interest rates were a headwind for emerging markets,** as they underperformed developed markets for the first time in three months.

Global Equities | 12-Month Outlook

- While stretched technicals may lead to periods of elevated volatility, **we believe that equities will be higher over the next 12 months on the back of rebounding economic and earnings growth.** However, investors need to dial back their return expectations, as strong EPS growth ($175 2021 S&P 500 earnings forecast) will likely be offset by P/E multiple compression. Our year-end 2021 **S&P 500 price target is 4,025.**
- We remain biased to select cyclical sectors that should benefit from improving economic growth and stronger earnings growth. We favor **Technology, Comm. Services, Health Care, Consumer Discretionary and Industrials—**sectors that can benefit from additional fiscal stimulus, online shopping, the work-from-home trend and rising confidence.
- **We favor large cap relative to small cap in the near term** as large cap has more resilient earnings amidst the slowdown in economic activity. We suggest investors be more tactical within small-cap industries as select industry valuations are elevated within the space.
- **We remain constructive longer term on global equities,** especially EM, due to the expected rebound in global economic growth, but prefer the US over other developed markets due to favorable sector exposure and more resilient economic growth.

Large and Small-Cap Valuations Remain Elevated

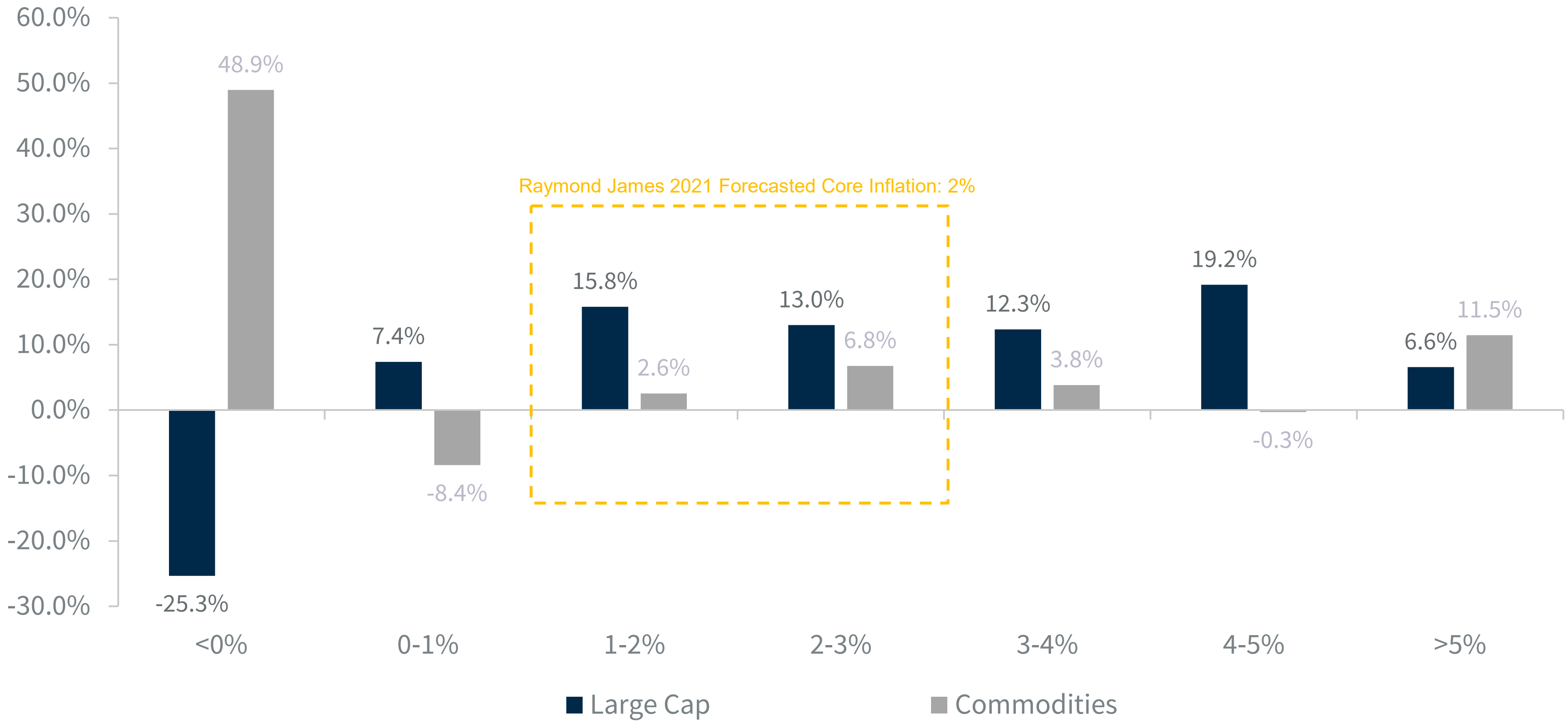
Strong Forward EPS Expectations



Inflation | Where to Turn if Inflation Picks Up

WHILE NOT OUR BASE CASE, IF INFLATION DOES SUSTAINABLY INCREASE, EQUITIES ARE THE BEST PLACE TO INVEST

- When inflation (Core PCE) is between 1-5% year-over year, equities have experienced robust positive returns and have outperformed other asset classes.
- However, in periods of deflation and hyperinflation (>5%), commodities typically outperform.



Source: FactSet. Data dates back to 1971.

Fixed Income | Treasury Yields Move Higher

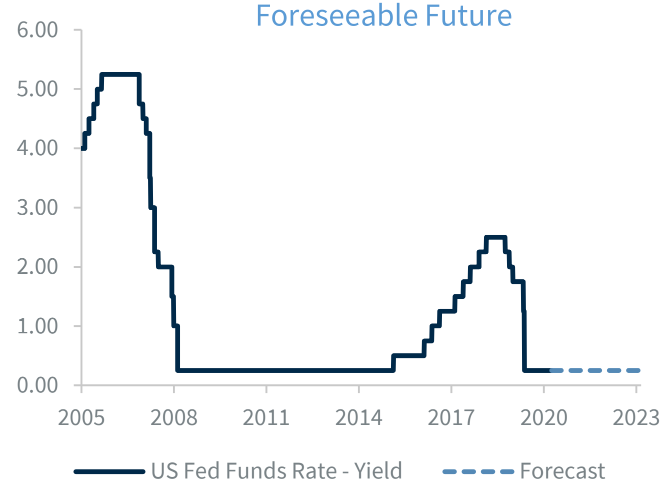
Global Bonds | Recent Trends

- **Longer-duration yields continued their recent surge higher**, as the 10-year Treasury yield has risen ~100 bps off of the August 2020 lows and is at the highest level (1.46%) in a year. However, the **sharp rise in yields may be overdone in the near term**, as technical indicators (e.g., 14-day RSI) suggest that the rise in yields is stretched at current levels.
- Treasury yields have moved higher on **rising expectations for future economic activity**, driven by rising vaccine distribution, a sharp improvement in COVID cases and continued fiscal stimulus (an additional $1.5-$1.9 trillion likely in March). The rise in yields has also been driven by rising inflation expectations, as the 10-yr breakeven rate rose to an eight-year high.
- **Spreads between short and long-term Treasurys widened in February to the highest level since July 2017** as the market priced in the Fed remaining lower for longer (through 2023) while investors priced in a stronger than expected economic recovery.
- Credit spreads (yield over Treasurys) moved lower during the month, **as both investment-grade and high-yield bond spreads** declined to pre-COVID lows.
- Following the recent rally, **municipal bond valuations are now significantly more expensive**, as the AAA municipal bond yield is ~70% of the 10-yr Treasury yield (avg: 0.9%)

Global Bonds | 12-Month Outlook

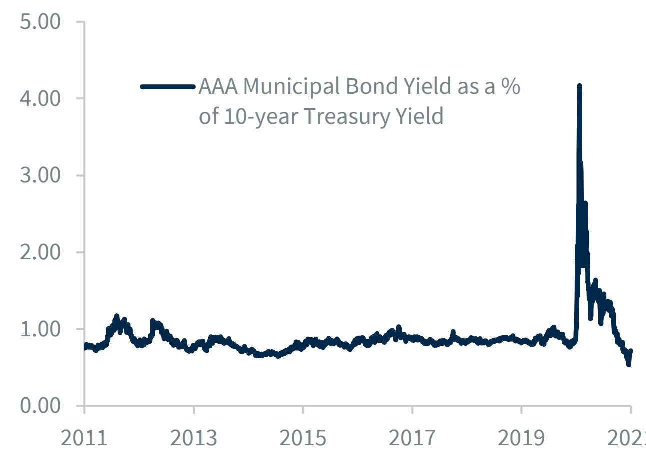
- As the market is pricing in continued economic recovery through 2021 and the potential for more stimulus following Democrats taking the Senate, **we forecast the 10-year Treasury yield to end 2021 at 1.5%**. However, **we anticipate the rise in yields to be limited** due to temporary inflation, continued buying from global central banks, increased demand from foreign investors and aging demographics.
- While our forecasted rise in yields will likely lead to **limited, if any, capital appreciation for bonds in 2021**, **fixed income remains an important piece within investors' portfolios** as it limits/hedges equity market risk and provides increased diversification.
- Given our expectation for a modest rise in longer-duration interest rates while the Fed is set to leave policy rates unchanged for the foreseeable future (keeping shorter-term rates low), **we recommend a shorter than benchmark duration for bond portfolios.**
- From a credit perspective, while spreads have narrowed dramatically from their post-crisis highs, **we expect them to remain tight around pre-COVID levels** in 2021. We would favor holding higher-quality bonds and therefore **favor investment grade over high-yield bonds**. In general, we would **prefer to add additional risk in the equity market over high yield** as we believe investors are better compensated for taking on risk in the equity market.

Fed Likely to Remain on Hold for Foreseeable Future



Source: FactSet

Muni Valuations More Expensive



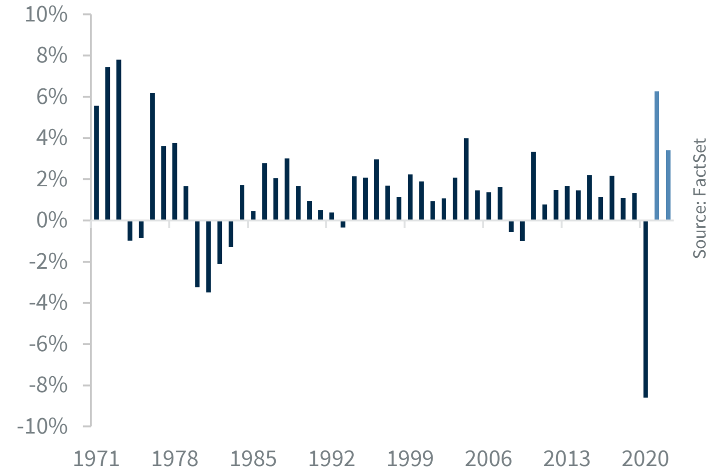
Source: FactSet

Commodities & Currencies | Commodity Rally Continues

Commodities & Currencies | Recent Trends

- Broad commodities continued to rally in February as **the Bloomberg Commodity Index rallied for the fifth consecutive month and rose to the highest level since October 2018.** While crude oil demand remains well off of its pre-COVID peak, **crude oil rallied to the highest level since April 2019 ($63.5/bbl)** as improving COVID conditions (both new daily cases and hospitalizations), faster vaccine inoculations, rising mobility indicators and severe weather conditions (particularly in the Midwest) boosted demand.
- Similar to crude oil, **industrial metals rallied for the 10th time in the last 11 months and rose to the highest level since February 2013.** Copper was a standout within the sector, as the industrial metal rose to its highest level since 2011 and is now up ~100% off of the lows in March. This suggests that **investors are pricing in an ongoing improvement in global economic activity in 2021**, particularly in China and the emerging markets.
- While the continued risk-asset rally on the vaccine roll-out and improving economic growth pushed the dollar to the lowest level intra-month since April 2018, **increased volatility in the final days of the month caused the dollar to strengthen.**
- On the back of rising real interest rates, **Gold declined for the second consecutive month and fell to an eight month low.** Gold is now down 17% off of recent highs.

Crude Oil Demand Set to Increase



Annual Change in Global Oil Demand

Commodities & Currencies | 12-Month Outlook

- As US economic activity recovers following the continued roll out of vaccines and reopening of the economy, **crude oil prices will remain strong over the next 12 months (year-end 2021 WTI target: $60/barrel) due to improving global demand.**
- However longer term, as the price of crude oil is above current breakeven levels for US producers (thereby incentivizing more capital investment), **rising US crude oil production as well as increasing OPEC production will likely limit a substantial further rise in prices.**
- The US dollar typically moves in long-dated cycles. After a nine-year run, **the recent dollar bull market has likely come to an end**. Pressuring the dollar lower will be fundamental factors, as improving global economic activity and falling global economic policy uncertainty (due to the counter-cyclical nature of the USD) will likely reduce demand for the dollar. Additionally, **aggressive US fiscal and Fed monetary policy easing**, leading to rapid money supply growth and widening fiscal deficits will also likely lead to a weaker dollar.
- While gold has been a solid hedge for investors throughout the COVID-crisis, **the demand for gold will likely wane** as US economic activity improves as we move through 2021 and on the expectation that real interest rates move modestly higher from current levels.

Gold Moves Lower With Rising Real Yields

Summary | Views and Key 2021 Year-End Targets

1 ECONOMY

2021 US GDP: ~4.9%

The US economy experienced its deepest and shortest recession ever due to the COVID-19 pandemic, but is quickly beginning to rebound. The rebound is likely to continue during 2021 especially if policymakers continue to exhibit a “by any means necessary” approach to defeat this virus.

2 BOND MARKET

2021 10-Year Treasury: 1.50%

We forecast that the 10-year Treasury yield will be 1.50% by year-end 2021, supported by improving economic activity and continued fiscal stimulus. As we prefer higher-quality bonds, we prefer investment grade over high yield.

3 EQUITIES

2021 S&P 500: 4,025

Our expectation for a rebound in 2021 economic activity and stimulus from the Fed and Congress should support equities. In contrast to recent years, we expect positive returns to be driven by EPS growth rather than P/E expansion. Use pullbacks as buying opportunities within our favorite sectors (Info Tech, Health Care, Communication Services, Industrials and Consumer Discretionary).

4 DOLLAR DIRECTION

2021 EUR/USD: 1.25

Our expectation is that aggressive fiscal and monetary policy and a burgeoning budget deficit may cause the dollar to modestly weaken throughout 2021. Separately, the easing of trade restrictions from the Biden presidential administration may weaken the dollar relative to other currencies. However, the potential for near-term volatility in riskier assets is likely to support the dollar.

5 OIL

2021 WTI: $60/bbl

Over the next 12 months, crude oil will be supported by the reduction in social distancing measures, increasing economic activity in 2021 and thereby improving demand. However, as prices rise above breakeven levels here in the US and OPEC raises production levels, the rise in oil prices will likely be limited.

6 ELEVATED VOLATILITY

Volatility: ↓

After a year of unpredictable events (e.g., COVID crisis, 2020 election) we expect the overall level of volatility to decrease in 2021 due to the continued roll out of vaccines, a more stable political environment in the US, improving global economic activity, still accommodative global central banks, and easing trade rhetoric (particularly between the US and Europe).

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Diversification does not ensure a profit or guarantee against a loss. A credit rating of a security is not a recommendation to buy, sell or hold the security and may be subject to review, revision, suspension, reduction or withdrawal at any time by the assigning Rating Agency. Ratings and Insurance do not remove market risk since they do not guarantee the market value of the bond.

INTERNATIONAL INVESTING | International investing involves additional risks such as currency fluctuations, differing financial accounting standards, and possible political and economic instability. These risks are greater in emerging markets.

SECTORS | Sector investments are companies engaged in business related to a specific economic sector and are presented herein for illustrative purposes only and should not be considered as the sole basis for an investment decision. Sectors are subject to fierce competition and their products and services may be subject to rapid obsolescence. There are additional risks associated with investing in an individual sector, including limited diversification.

OIL | Investing in oil involves special risks, including the potential adverse effects of state and federal regulation and may not be suitable for all investors.

CURRENCIES | Currencies investing are generally considered speculative because of the significant potential for investment loss. Their markets are likely to be volatile and there may be sharp price fluctuations even during periods when prices overall are rising.

GOLD | Gold is subject to the special risks associated with investing in precious metals, including but not limited to: price may be subject to wide fluctuation; the market is relatively limited; the sources are concentrated in countries that have the potential for instability; and the market is unregulated.

FIXED INCOME | Fixed-income securities (or “bonds”) are exposed to various risks including but not limited to credit (risk of default of principal and interest payments), market and liquidity, interest rate, reinvestment, legislative (changes to the tax code), and call risks. There is an inverse relationship between interest rate movements and fixed income prices. Generally, when interest rates rise, fixed income prices fall and when interest rates fall, fixed income prices generally rise.

US TREASURIES | US Treasury securities are guaranteed by the US government and, if held to maturity, generally offer a fixed rate of return and guaranteed principal value.

US DOLLAR | The US Dollar Index is an index (or measure) of the value of the United States dollar relative to a basket of foreign currencies,[1] often referred to as a basket of U.S. trade partners' currencies.[2] The Index goes up when the US dollar gains "strength" (value) when compared to other currencies.

DEFINITIONS

AGGREGATE BOND | **Bloomberg Barclays US Agg Bond Total Return Index:** The index is a measure of the investment grade, fixed-rate, taxable bond market of roughly 6,000 SEC-registered securities with intermediate maturities averaging approximately 10 years. The index includes bonds from the Treasury, Government-Related, Corporate, MBS, ABS, and CMBS sectors.

HIGH YIELD | **Bloomberg Barclays US Corporate High Yield Total Return Index:** The index measures the USD-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody’s, Fitch and S&P is Ba1/BB+/BB+ or below.

CREDIT | **Bloomberg Barclays US Credit Total Return Index:** The index measures the investment grade, US dollar-denominated, fixed-rate, taxable corporate and government related bond markets. It is composed of the US Corporate Index and a non-corporate component that includes foreign agencies, sovereigns, supranationals and local authorities.

MUNICIPAL | **Bloomberg Barclays Municipal Total Return Index:** The index is a measure of the long-term tax-exempt bond market with securities of investment grade (rated at least Baa by Moody’s Investors Service and BBB by Standard and Poor’s). This index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds, and prerefunded bonds.

BBG COMMODITY INDEX | Bloomberg Commodity Index is calculated on an excess return basis and reflects commodity futures price movements.

S&P 500 | The **S&P 500 Total Return Index:** The index is widely regarded as the best single gauge of large-cap U.S. equities. There is over USD 7.8 trillion benchmarked to the index, with index assets comprising approximately USD 2.2 trillion of this total. The index includes 500 leading companies and captures approximately 80% coverage of available market capitalization.

EMERGING MARKETS EASTERN EUROPE | **MSCI EM Eastern Europe Net Return Index:** The index captures large- and mid-cap representation across four Emerging Markets (EM) countries in Eastern Europe. With 50 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.

ASIA EX JAPAN INDEX | **The MSCI AC Asia ex Japan** Index captures large and mid cap representation across 2 of 3 Developed Markets (DM) countries* (excluding Japan) and 9 Emerging Markets (EM) countries in Asia. With 983 constituents, the index covers approximately 85% of the free float adjusted market capitalization in each country.

AC WORLD INDEX | **The MSCI AC World** Index is a market capitalization weighted index designed to provide a broad measure of equity-market performance throughout the world. The MSCI ACWI is maintained by Morgan Stanley Capital International (MSCI) and is comprised of stocks from 23 developed countries and 24 emerging markets.

EMERGING MARKETS LATIN AMERICA | **MSCI EM Latin America Net Return Index:** The index captures large- and mid-cap representation across five Emerging Markets (EM) countries in Latin America. With 116 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.

EMERGING MARKETS | **MSCI Emerging Markets Net Return Index:** This index consists of 23 countries representing 10% of world market capitalization. The index is available for a number of regions, market segments/sizes and covers approximately 85% of the free float-adjusted market capitalization in each of the 23 countries.

JAPAN | **MSCI Japan Net Return Index:** The index is designed to measure the performance of the large and mid cap segments of the Japanese market. With 319 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in Japan.

EUROPE EX UK | **MSCI Europe Ex UK Net Return Index:** The index captures large and mid cap representation across 14 Developed Markets (DM) countries in Europe. With 337 constituents, the index covers approximately 85% of the free float-adjusted market capitalization across European Developed Markets excluding the UK.

MSCI EAFE | The **MSCI EAFE** (Europe, Australasia, and Far East) is a free float-adjusted market capitalization index that is designed to measure developed market equity performance, excluding the United States & Canada. The EAFE consists of the country indices of 22 developed nations.

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DATA SOURCES

FactSet as of 2/28/2021.

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