QUARTERLY MARKET REVIEW

SECOND QUARTER 2021

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JULY 30, 2021

Dear Investors,

The equity markets rallied again in the second quarter, posting a fifth straight quarterly gain since the dramatic sell-off of Q1 2020.[1] Compared to the last year and a half, the second quarter was relatively calm and devoid of extreme market reactions to headlines of potential economic uncertainties. The second quarter felt almost like a mid-cycle lull, and was a welcomed change of pace. After the dramatic reversion from growth to value, we experienced in the first quarter as the "re-opening" trade was on and interest rates moved higher, we saw a more balanced equity reaction in the second quarter as rates leveled out. Large cap growth again outperformed, with the Russell 1000 Growth appreciating 11.93% and the Russell 1000 Value gaining 5.21%. Interestingly, we saw much more balanced performance in the small and mid-cap sectors, with the Russell 2000 Growth up 3.92% and the Russell 2000 Value up 4.56%. The S&P 500 posted an approximate 8.5% gain for the three months ending in June, another indication of large caps again outperforming small and mid-caps.[2]

Continued central bank liquidity, fiscal stimulus, vaccine progress, GDP & earnings growth, equity inflows & corporate buy-backs, and re-opening momentum provided for an environment where the path of least resistance remained to the upside. That said, those expansive policies also continue to fuel concerns on how long they can last, and, perhaps more importantly, what may happen when they need to be changed. The Fed's balance sheet surpassed $8 trillion late last quarter, up from approximately $4 trillion at beginning of 2020, and is on track to reach $9 trillion before 2023. This would represent approximately 40% of GDP, a level not seen since World War II[3] Implicitly, policy makers' willingness to continue on this path reflects an expectation that the U.S. is able to follow these polices because the US dollar is the world's reserve currency. While this may be true for now, the markets may at some point challenge this view.

The key metric we, as well as the markets, will continue to monitor closely is inflation. Fed chair Powell believes the current rise in inflation is transitory and, so far, the markets seem to agree. However, if the main drivers of this recent inflation are coming from the aggressive monetary and fiscal stimulus, then we may be in for more persistent inflation starting now. The argument for transitory inflation is predicated on the fact that prices are rising primarily due to supply chain disruptions, higher raw-materials costs, shipping constraints, pent-up demand being unleashed, and a tightening labor market, all factors which should, in theory, be temporary as we make our way back to a "normal" economy. Although inflation itself is not troublesome for growth assets, in fact, it should be beneficial for earnings as revenues rise while companies raise prices reflecting higher costs. It is the Fed's potential action to control inflation that could eventually provide a headwind for the markets.

As long as the Fed remains patient, global monetary and fiscal stimulus remains accommodative and corporate earnings remain robust, we are inclined to believe the path of least resistance will remain to the upside. That said, markets rarely offer a smooth ride, and we don't anticipate they will going forward. Despite the solid overall performance year to date, through June we had 124 trading days, 55 of which were negative. Said another way, the market has been down approximately 44% of the time so far this year.[4] We recently heard someone say that in order

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to be a winner over time, an investor has to be a good loser during shorter periods. This is a good reminder for us all to try and remain unemotional during periods of volatility, which we expect more of going forward. Since 1979, the S&P has gained 10% or more 14 times during the first half of the year and has gone on to average a 6.3% gain over the second half of the year.[5] We anticipate this may be a year in which history repeats itself.

As always, we deeply appreciate the confidence and trust you place in us.

Regards,

Chris

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Important Considerations:
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[1] *FactSetAccount Summary. "US Quarterly (Q2 2021) Recap: Dow +4.61%, S&P +8.17%, Nasdaq +9.49%, Russell 2000 +4.05%". July 1, 2021.*
[2] *Source: Orion Advisor Solutions.*
[3] *Federal Open Market Committee by the Markets Group of the Federal Reserve Bank of New York. "Open Market Operations During 2020", P. 47, 48. https://www.newyorkfed.org/medialibrary/media/markets/omo/omo2020-pdf.pdf.*[4] *Source: Factset.*
[4] *Source: Factset.*
[5] *Sonenshine, Jacob. "The S&P 500 Notches Its Second-Best First Half Since the Dot-Com Bubble. What Comes Next". https://www.barrons.com/articles/stock-market-futures-crash-gains-51625071996?mod=hp_LEAD_1.*

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