THE NEXT GENERATION WEALTH PERSPECTIVE

Recovery In Motion

Macro Summary

Federal Reserve	▪ At the March Federal Open Market Committee meeting held March 16-17, the Federal Reserve ('the Fed') has once again pledged to keep the federal funds rate very accommodative until labor market conditions improve and inflation reaches a level moderately above 2 percent. ▪ The Fed remains committed to their asset purchase program of at least $120 billion per month.
Economy	▪ Following an extremely strong Q3 Gross Domestic Product (GDP) report, Q4 2020 increased at a 4.3 percent annual rate led by strong demand in exports, business investment, consumer spending, and housing. These increases more than offset decreases by state and local government spending as well as the federal government. ▪ Current GDP estimates for the first quarter range from 6 to 8 percent, with growth accelerating during the year driven by fiscal and monetary stimulus, vaccine rollouts, states reopening and pent-up consumer demand. ▪ Employment continues to strengthen. The March employment report was significantly above expectations with job growth of 916,000, and a positive revision in January and February. The combined job growth in Q1 2021 was 1,528,000 but is still down by 8.4 million from its pre-pandemic peak in February 2020. The unemployment rate fell to 6 percent but is still above its pre-pandemic level of 3.5 percent.
Consumer	▪ The consumer confidence index surged to its highest reading in a year after a modest increase in February. The index now stands at 109.7, up from 90.4 in February 2021. The index is below its pre-pandemic level of 130. ▪ The personal savings rate fell to 13.6 percent in February but remains elevated compared to last year. On the back of stimulus, compensation gains, and high personal savings, consumers will have close to $3.0 trillion in excess cash compared to pre-crisis levels. ▪ Total vehicle sales were at an annual rate of 18.2 million units, up from an annualized rate in February of 16.2 million and above pre-pandemic levels. ▪ Building permits for new residential construction continues to rise, down modestly from the recent January peak, but February's 1,720 number was almost 20 percent higher than the pre-pandemic levels.
Markets	▪ The financial markets started the year on a strong note with the Standard & Poor 500 Index (S&P 500) posting a gain slightly above 6 percent on optimism that the economy is on a path to recovery driven by fiscal and monetary stimulus and vaccine rollouts. ▪ In a reversal of 2020 performance, small company and value stocks led the way. Top performing sectors included energy (+31 percent), financials (+16 percent), and industrials (+11 percent). Laggards included consumer staples (+1 percent) and technology (+2 percent).
Risks	▪ Emerging from one of the quickest and deepest recessions in history the recovery is unlikely to be a smooth path without risks to keep an eye on. ▪ Key potential risks to a full recovery include inflation, COVID-19 spread, higher taxes and systemic risks.

	Q1 RETURN	YTD RETURN
Standard & Poor 500 Index	6.17%	6.17%
Balanced Portfolio - 60 / 40	2.36%	2.36%
Dow Jones US REIT Index	7.70%	7.70%
MSCI EAFE Index	3.48%	3.48%
Barclays Aggregate Bond	-3.37%	-3.37%
Barclays Municipal Bond	-0.35%	-0.35%

What's Happening

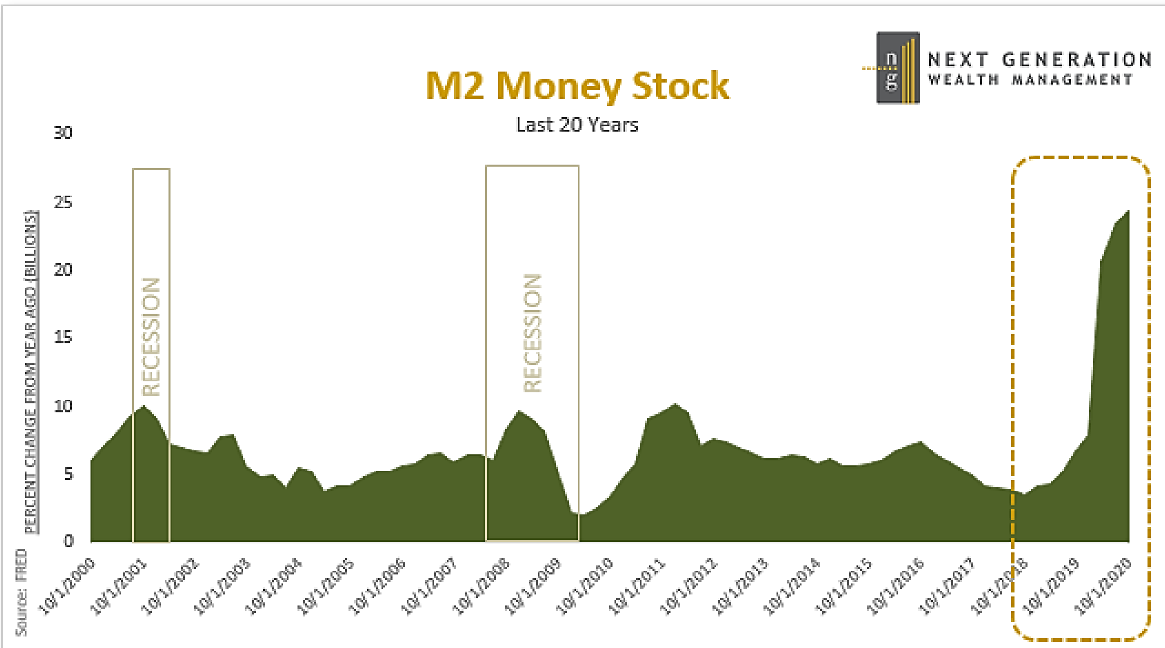
We are beginning to see the economic recovery take shape. Improving job growth, wide-spread vaccine distribution, and further monetary and fiscal stimulus has the economy recovering from one of the quickest and deepest recessions in history. This backdrop has been extremely supportive for the economy and equity markets. The S&P 500 rose 6 percent in the quarter and smaller companies in the Russell 2000, which tend to be more economically sensitive, rose 12.7 percent in the quarter. International and emerging markets were up low single digits for the quarter as well. The bond market was lower as interest rates rose on the expectations of stronger economic growth and the potential for inflation. The yield on the 10-year Treasury note rose from 0.96 percent to 1.74 percent by the end of the quarter.

Monetary & Fiscal Stimulus

The economy avoided a deep and long recession when government entities enacted massive stimulus in 2020. We continue to see more stimulus in 2021 from both the monetary and fiscal authorities. The $1.9 trillion COVID-19 relief bill was passed in March and provided $1,400 checks to many Americans, extended the weekly job benefits, expanded the child tax credit, and more. It also provided money to schools, vaccine distribution efforts, and state and local governments. Following the COVID relief bill, President Biden proposed The American Jobs Plan, a more than $2.0 trillion infrastructure and economic recovery plan. While still being debated, the bill includes spending on clean energy & power, traditional infrastructure such as roads, bridges, rail, public transit, and non-traditional infrastructure including funds allocated to retrofitting affordable housing, upgrade schools, community colleges and modernize VA facilities. According to the plan, most of the funds would be spent over an eight-year period and paid for through higher taxes paid by corporations over the next 15 years.

Monetary policy continues to be extremely accommodative. At the most recent Federal Open Market Committee meeting in March, the Federal Reserve policy makers decided to keep the target range for the federal funds rate at 0 to 0.25 percent. They expect it will be appropriate to maintain this target range until labor market conditions have reached levels consistent with the Committee's assessments of maximum employment and inflation has risen to an average of 2 percent. To get to the average of 2 percent, the committee is willing to let inflation run modestly above 2 percent for some time so that the longer-term inflation expectation remains well anchored at 2 percent. In addition, the Fed will continue its asset purchase program by purchasing at least $80 billion of Treasury securities and $40 million of agency mortgage-backed securities. These purchases help the credit markets function more smoothly and provide accommodative financial conditions, thereby supporting the flow of credit to households and businesses.

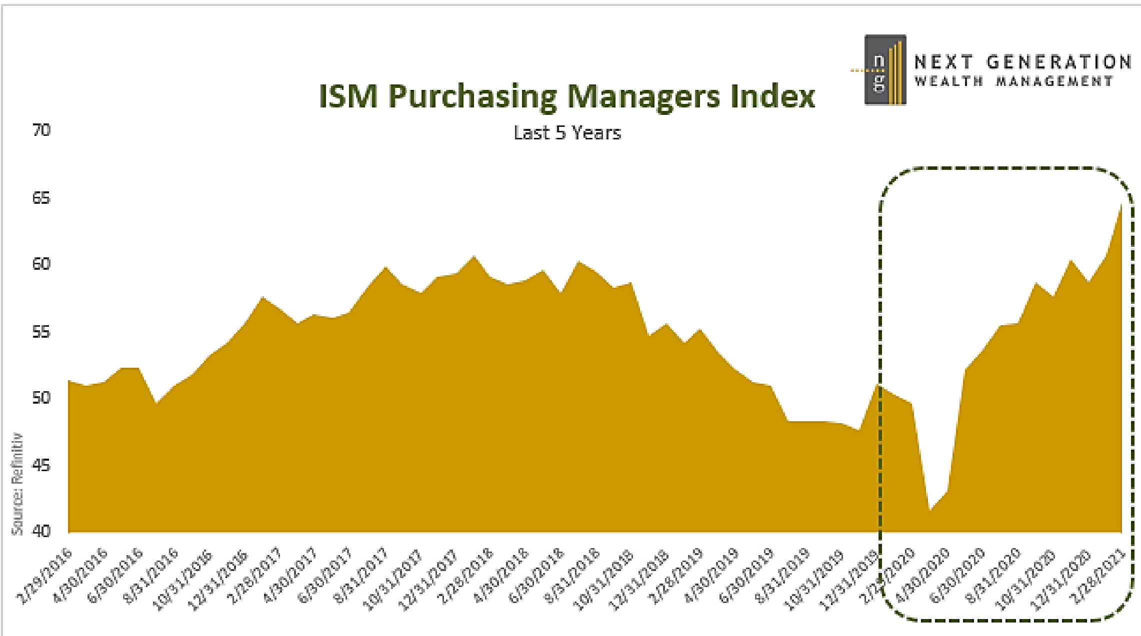
An economy operates similar to an engine, with the smooth flow of credit and money acting as the oil. If you run an engine without oil, it will eventually seize up. An economy will seize up without the smooth flow of credit and money. If the private sector cannot provide the credit and money (oil) to operate the economy (engine), then the public sector will provide it until the private sector can get back to normal. The public sector has provided a lot of oil to keep the engine running, and the M2 Money supply has been growing at a record rate of 27 percent year over year.

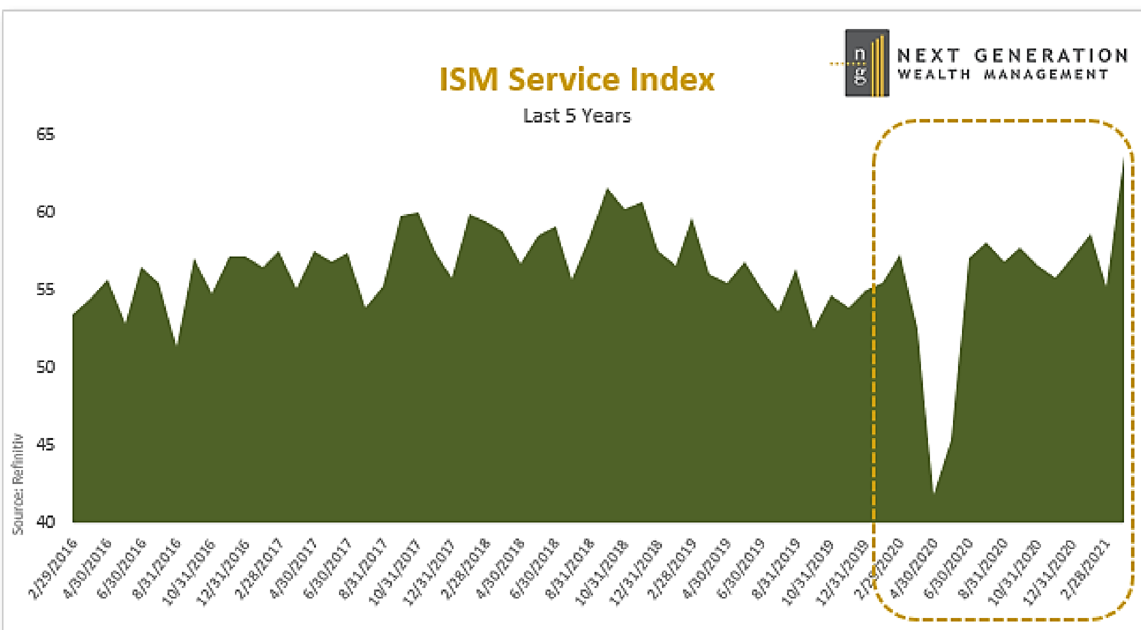


M2 money supply - consists of currency held outside of banks, savings & demand deposits, money market accounts, and time deposits under $100,000.

The Economy

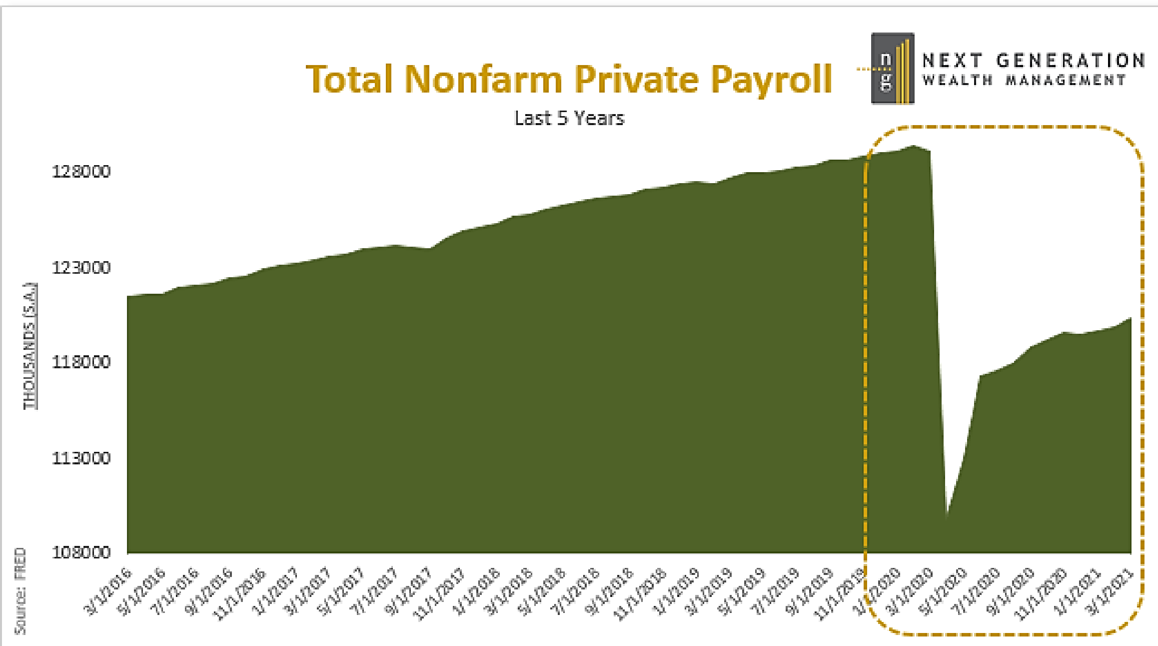
For the most part, the government stimulus programs have been working. GDP forecasts for 2021 are solid with positive revisions. Some forecasts have Gross Domestic Product up as much as 9 percent for the calendar year 2021, the strongest reading since 1959. Monthly progress reports on the economy confirm this strengthening. The March 2021 Manufacturing PMI report from the Institute for Supply Management registered a 12-month high at 64.7 percent. A number above 50 indicates expansion and below 50 indicates contraction. Looking deeper into the report we can see the strength is driven by growth in new orders, rising backlog, and increasing production. The manufacturing PMI report also noted that while the manufacturing economy continues to run hot, companies and suppliers struggle to meet increasing rates of demand due to COVID-19 impacts limiting availability of parts and material, extending lead times and rising commodity prices. Panelists also noted significant difficulties in attracting and retaining labor in their companies' and suppliers' facilities. These types of issues can potentially be inflationary if not kept in check. The March Services PMI report from the Institute for Supply Management confirmed the strength witnessed from the manufacturing economy. The Services PMI registered an all-time high reading of 63.7 percent, a significant increase from February's reading of 55.3 percent. Mirroring the strength for the Manufacturing PMI, the Services PMI was driven by an increase in business activity and new orders. Once again survey respondents noted raw material shortages and challenges in logistics and human resources continue to cause supply chain disruptions.



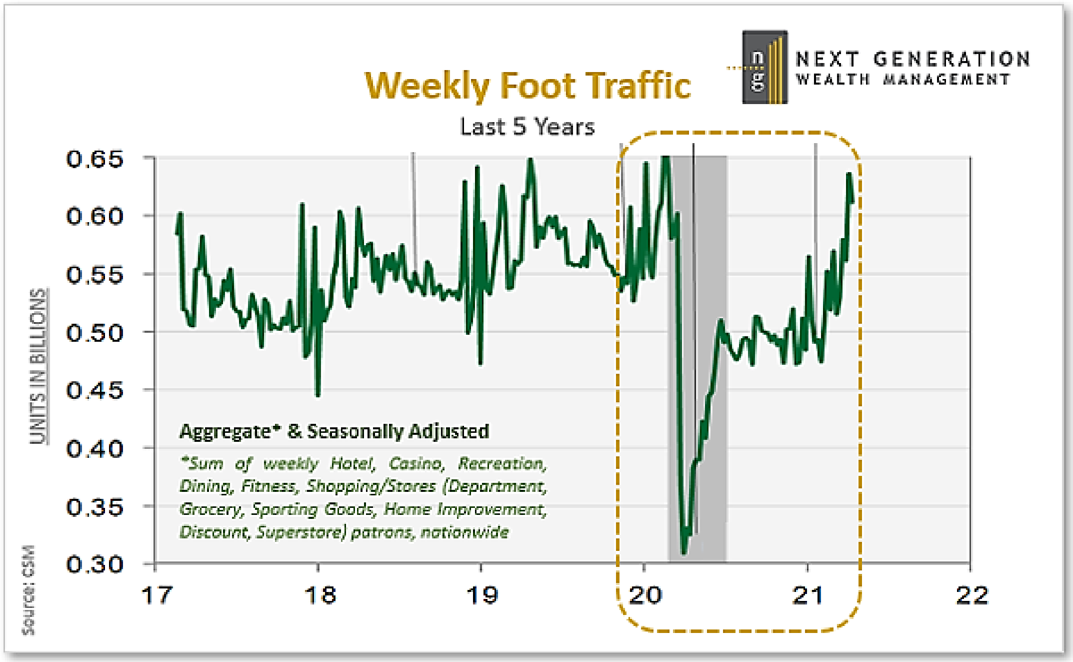


Employment & Consumer

The employment picture is improving. The March nonfarm payroll report confirmed this strength as employment rose 916,000 in March and the unemployment rate fell to 6 percent from 6.2 percent. The report also includes a positive revision in January and February of 156,000 jobs. Job growth was widespread in March led by gains in leisure and hospitality (one of the hardest hit sectors last year), public and private education, and construction. From its low, payrolls are up 13 million, but still 8 million below pre-COVID levels. Forecasters are predicting continued strong gains in employment.



As stimulus money is received and the employment picture improves, the consumer is positioned to take the handoff from the government entities and drive the economy forward. Economists are forecasting, as we move past COVID-19 with further vaccine distribution, that job gains and increased compensation added to the elevated amount of personal savings, could drive consumer spending given the pent-up demand. We may already be witnessing such an environment with the increase in foot traffic and recovery in auto sales.


Weekly Foot Traffic
Last 5 Years
NEXT GENERATION
WEALTH MANAGEMENT
0.65
0.60
0.55
0.50
0.45
0.40
0.35
0.30
UNITS IN BILLIONS
Aggregate* & Seasonally Adjusted
*Sum of weekly Hotel, Casino, Recreation, Dining, Fitness, Shopping/Stores (Department, Grocery, Sporting Goods, Home Improvement, Discount, Superstore) patrons, nationwide
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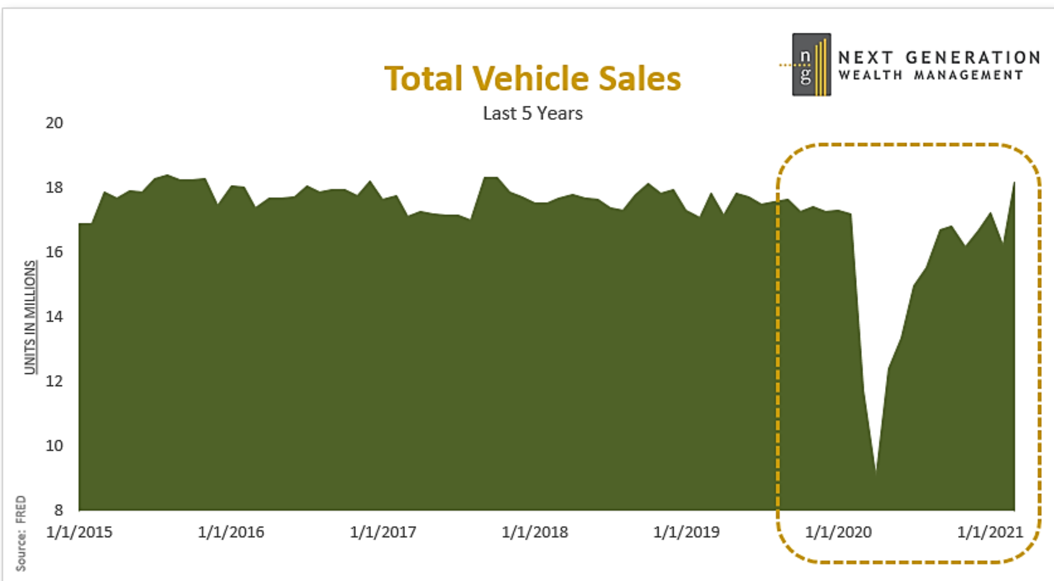
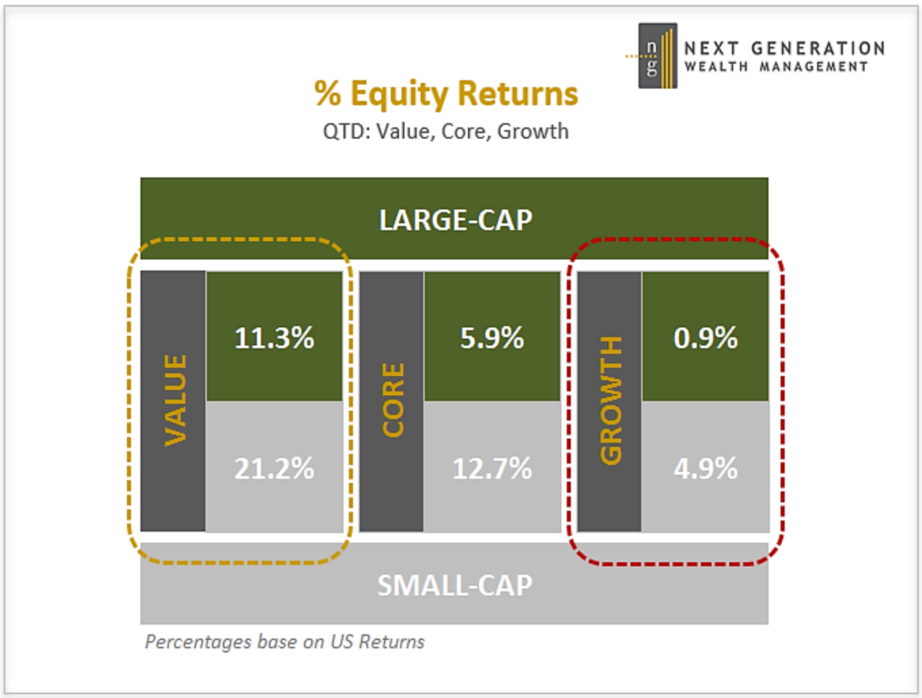
Source: CSM


Total Vehicle Sales
Last 5 Years
NEXT GENERATION
WEALTH MANAGEMENT
20
18
16
14
12
10
8
UNITS IN MILLIONS
1/1/2015
1/1/2016
1/1/2017
1/1/2018
1/1/2019
1/1/2020
1/1/2021
Source: FRED

The Financial Markets

The monetary and fiscal stimulus combined with rising payrolls and widespread vaccine distribution has been an extremely positive backdrop for the broad stock market. The 76 percent return from the March low is the third best going back 100 years. A statistic that conveys investors' euphoria is that 96 percent of the companies in the S&P 500 are currently trading above their 200-day moving average. This is the highest percentage level looking back at least 20 years. The first quarter of 2021 witnessed a continuation of trends we started to see unfold in the fourth quarter of 2020. At that time, market performance began to broaden out and cyclical and value stocks started to outperform. The trend continues into 2021—and to a greater extent. The Russell 1000 Value outperformed the Russell 1000 Growth by over 10 percent in the first quarter. We continue to believe that there is significant opportunity for mean reversion potential for value relative to growth and the ownership of good, high quality companies that have a balance of reasonable valuation, growth potential, and attractive dividend yield is a sound investment strategy in this environment.



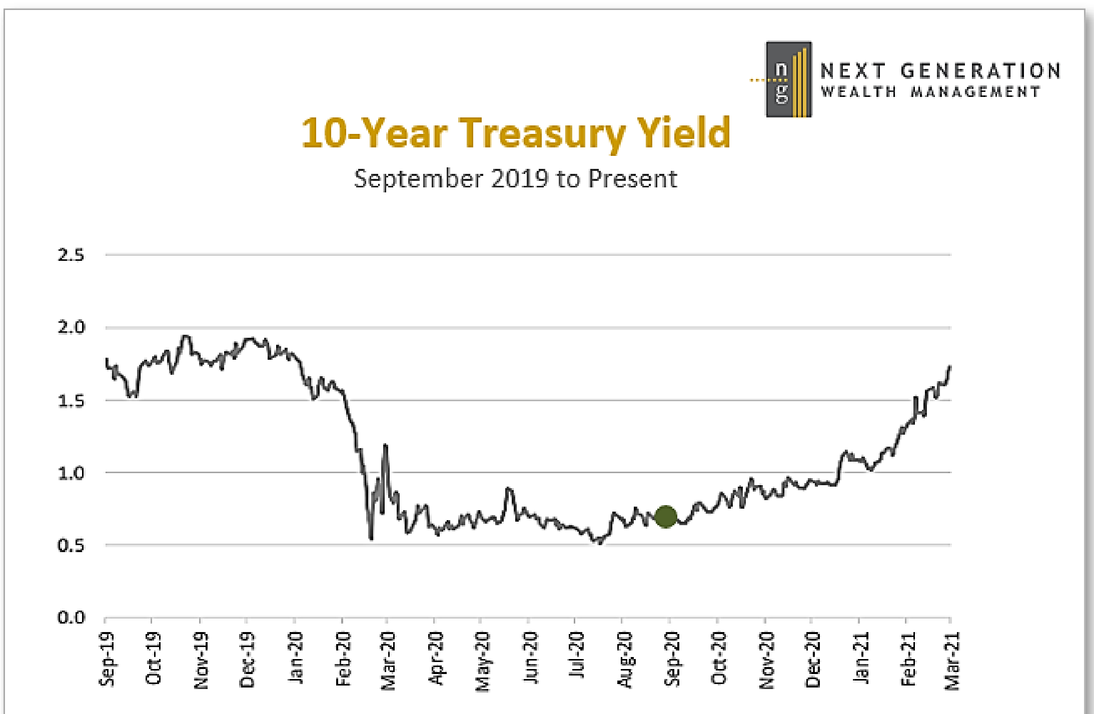
The trend in small company outperformance continued as well. The Russell 2000 outperformed the Russell 1000 by 6.8 percent. For the most part, smaller companies are more sensitive to the business cycle and their earnings should recover to a greater extent than large companies. Our investment team continues to favor an increased allocation to small and midsize companies where appropriate to benefit from a re-opening of the economy.

The international markets are experiencing an uneven recovery from the pandemic. However, as in the United States, international policy makers have been extremely accommodative supporting their economies until the private sector can take over the lead. Equity markets generally performed well in the first quarter with developed markets up 5 percent and emerging markets up 3 percent. As an investment committee, we believe the international markets provide US investors a tremendous opportunity to benefit from diversification.

The Bond Market

The first quarter was a challenging period for long-term bonds. Long-term treasuries experienced their worst quarter in years as long-term rates rose on the anticipation of a dramatically brighter economy than one could have imagined in the second half of 2020. The rapidly improving economic environment has the bond market worried about potential inflation. While only back to its pre-pandemic level, the yield on the 10-year Treasury note rose from 0.96 percent to 1.74 percent. While long-term rates are based on market conditions, the Federal Reserve controls the short end of the curve through adjusting the federal funds rate. Historically the Fed has used its economic models to predict inflation and tap the brakes before the economy starts experiencing real inflation. However, they feel the economy has changed and inflation never really moved up in previous cycles as unemployment declined. Globalization of the economy and technology have enabled manufacturing to take place all around the world so it is very hard for companies to raise prices. The Fed expects any inflation we experience in 2021 will be transitory. They believe based on past cycles that they can wait to see actual inflation at 2 percent or slightly higher on a sustainable basis before they must raise interest rates. While no one at the Federal Reserve currently anticipates raising the short term rates in 2021, stronger growth than the expected current 6 to 6.5 percent and continued robust payroll expansion may set the stage for monetary authorities to slow bond buying and begin tapering in the second half of 2021 or early 2022.

Bonds continue to play an important part of a well-diversified investment strategy. We continue to keep the average duration of the fixed income portfolio short. If longer-term rates were to continue to rise, we may use it as an opportunity to gradually add longer duration bonds for more income.



What We're Monitoring

Inflation

In a sense, inflation is more of a risk now because it has been so immaterial for most of the past 20 years. This has led policy makers, consumers, business, and investors to become complacent (at least up until very recently), as reflected in low interest rates and bond yields, and high stock market valuations. The primary catalyst for the recent sharp uptick in inflation is the combination of the positive macroeconomic factors: (1) expected reopening of the economy as the pandemic is brought under control, (2) ongoing highly accommodative monetary policy, and (3) unprecedented fiscal stimulus and the prospect for more to come from the new administration and Congress.

In the next few months, we expect the headline inflation rate will spike higher (likely in the 3 percent plus range). This will be due to a combination of the flow-through from recent commodity price inflation, temporary supply-chain bottlenecks, and, most significantly, so-called base effects—meaning the year-over-year inflation calculation based off the temporarily depressed price levels during the early months of the pandemic. As the months roll on, the base effects from a year earlier will roll off. Expert opinions diverge as to whether this is likely the beginning of a sharp and sustained rise in inflation, or just a temporary blip before it settles back to around 2 percent.

While remaining vigilant and flexible, our investment committee continues to think the weight of the evidence leans toward a low likelihood of a major sustained rise in the inflation rate, at least for the next few years. The two key reasons behind our leaning are: (1) the economy still has tremendous slack – in terms of the gap between current and potential GDP and to reach maximum employment; and (2) the pandemic-related fiscal stimulus is temporary. Structural disinflationary forces also remain, such as demographic trends and technology, automation, and digitalization adoption, with the latter accelerating during the pandemic. Remember, inflation is rate of change in prices. To have a sustained inflationary period requires an ongoing increase or acceleration in that rate of change, not a one-time or short-term increase in the price level.

COVID-19 Spread & Severity

Over the past two months, the United States has seen very sharp declines in daily new cases, current hospitalizations, and daily new deaths from COVID-19. Meanwhile, the rate of COVID-19 vaccinations has soared to 2.8 million per day; more than 93 million Americans (nearly 30 percent of the population) have now received at least one dose, including 51 million who have been fully vaccinated. From an economic perspective, getting the pandemic under control will enable increased activity, employment, household income, consumer spending, economic growth, and corporate earnings. There is a risk from the spread of new, more infectious variants, as is happening in several European countries; however, overall, we are seeing some positive developments on the pandemic front.

Higher Taxes

President Biden has proposed significant tax increases for corporations to help pay for his American Jobs Plan. In addition, the President will soon lay out his proposal for what he calls the American Family Plan. This proposal represents the second part of his agenda and will increase spending on childcare and education paid for through raising the top marginal income tax and the tax on capital gains. Higher taxes run the risk of offsetting the positive impacts of the economy opening and previously passed stimulus.

Systemic Risks

Excess liquidity creates bubbles and the potential for systemic breakdown if bubbles burst. Recently, a large hedge fund (Archegos) borrowed billions of US dollars from multiple banks to speculate in stocks. When the stock prices declined significantly, the hedge fund suffered material losses, and consequently banks liquidated positions also taking large losses. and the banks had to liquidate the positions and ended up taking large losses. As rates rise, this can put stress on borrowers. Like a weak link in a chain, it has the potential to break the borrower. It becomes systemic when the failure of the borrower causes other firms to fail and the potential for a cascading effect of failures across an industry.

Concluding Thoughts

As we begin the second quarter of 2021, the economy continues to be on a clear path to recovery. Vaccines have been developed and are available for widespread distribution. At this time, approximately 25 percent of adults are fully vaccinated. The economy is re-opening around the country and the unemployment rate is falling. Consumers are in relatively good shape thanks to the ongoing rounds of fiscal and monetary stimulus. The global financial markets are reacting positively as companies report improved earnings and expect further growth to continue.

The path to full recovery will not be an even one as potential risks lurk around every corner; however, please know we continue to be extremely vigilant in managing your wealth and are here to answer your questions if and when they arise.

Stay safe. Stay healthy. Be well.

All the best,

Ed

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