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Capital Markets Review and Outlook

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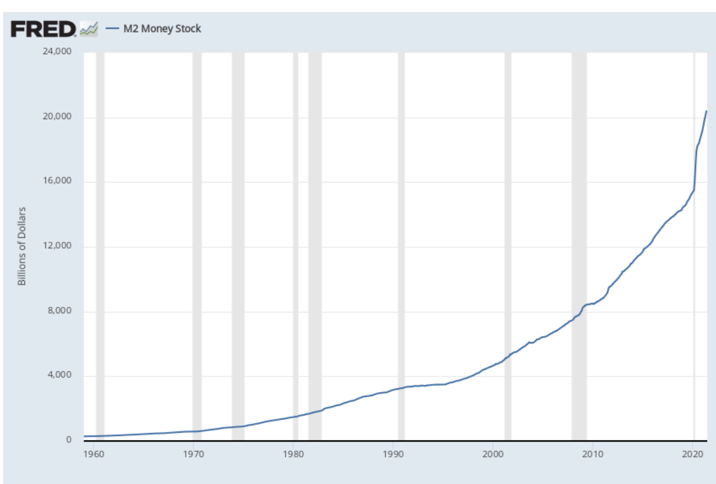
Economy and Outlook

The fast-spreading delta variant has cast a cloud on an otherwise improving backdrop for the global coronavirus pandemic. After falling sharply in the 1st half of the year, the number of new daily infections has increased significantly with the 7-day average now above the level seen last summer. While vaccine hesitancy is an issue, much progress has been made in defeating COVID-19. The percentage of adults in the United States who have received at least one vaccine dose has reached 70%, a major milestone. Additionally, the pace of vaccinations, after dropping sharply, has also begun increasing. Globally, while the 4.2 million deaths from the virus is a sobering figure, almost 4 billion vaccine doses have now been administered reflecting significant progress in combating the virus. Despite challenges from the coronavirus variants, economies continue to rebound strongly. In the United States, real GDP grew at an annualized rate of +6.5% in the 2nd quarter of this year enabling the economy to surpass its pre-pandemic size. The eurozone economy expanded by 8.3% for the same period and is expected to exceed its pre-pandemic level by year-end. The International Monetary Fund (IMF) is projecting that the world economy will expand by 6% this year following the -3.2% contraction in 2020. There is, however, a differentiation based on vaccination rates with the IMF raising growth forecasts for advanced economies and lowering its growth expectations for emerging and low-income countries where vaccination rates are low. The upbeat outlook for economic growth is underpinned by the continued expansive fiscal and monetary policies in place across much of the globe. The July employment report for the United States showed an increase of 943,000 jobs, the fastest pace in almost a year, with the unemployment rate dropping to 5.4%. While the Federal Reserve remains sanguine about inflationary pressures, with Chairman Powell continuing to maintain that the recent sharp increases in inflation are transitory, the chart on the left shows the explosive growth of money supply (M2) over the past year. Since March 2020, M2's annualized growth rate has averaged 24%, the fastest growth in over 70 years. As the late renowned economics Nobel Laureate, Milton Friedman, repeatedly emphasized, inflation is a monetary phenomenon. The 4% year-over-year increase



in hourly wages, and the 5.3% increase in the consumer price index suggest that the Fed may be behind in tapping the brakes on its unprecedented accommodation of monetary policy. This may, in turn, have adverse consequences for the high-flying risk markets.

Equity Markets

The broad equity markets continued to make record highs in July buoyed by the enormous amounts of liquidity courtesy of governments and central banks. July marked the sixth consecutive month of gains for the market with the Russell 3000 index rising +1.7% which brought the total return for the first seven months of the year to +17.1%. For the 5-year and 10-year periods ending 7/31/21, the annualized returns for the Russell 3000 index are a remarkable +17.4% and +15.2% respectively. In terms of capitalization, Large Cap (+2.1%) decisively outperformed both Mid Cap (+0.8%) and Small Cap (-3.6%) for the month. From a Style perspective, Growth outperformed Value across all capitalizations by a significant margin for the second consecutive month. Year-to-date, however, Value continues to lead Growth especially in the Small Cap and Mid Cap space. While sector performance in July was characterized by a move to Defensives with Healthcare (+4.9%) the best performing sector, Cyclicals such as Technology (+3.9%) and Materials (+2%) were also good performers. The interest rate sensitive sectors, Utilities (+4.3%) and Real Estate (+4.6%) benefitted from the decline in interest rates. Energy (-8.3%) was hit hard by the volatility and sharp decline in oil prices intra-month. The international equity market index was negatively impacted by the sharp decline in China (-13.8%) as regulators in China stepped up their market oversight in several leading sectors causing skittish investors to flee the markets. The MSCI Emerging Markets index lost -6.7% in July dragged down by China, Korea (-5.7%) and Brazil (-6.1%). The Developed Markets index, MSCI EAFE, gained +0.8% for the month. Underlying performance was mixed with outperformers in France (+1.7%) and Italy (+0.7%). Japan lost -1.3% despite the +1.6% rise in the yen versus the dollar. Conversely, Australia declined -1.3% on the heels of the decline in the Australian dollar. For the first seven months of the year, the previous gains in Emerging Markets have mostly evaporated with the index up just +0.2%. The Developed Markets index, on the other hand, has gained +9.6% year-to-date.

Fixed Income Markets

Treasury yields tumbled lower in July despite indications that the Federal Reserve was having more discussions about tapering its quantitative easing program. Fixed income investors seemed more focused on the rising number of coronavirus cases from the more contagious delta variant, and the potential for a further slowdown in the economy as a result. The continued rally in the equity markets is, of course, at odds with this view. Unlike the prior month, yields declined across the entire yield curve with 2-year Treasury yields down 6 bp to 0.19%, while 5-year yields dropped 18 bp to 0.69%. Longer maturity Treasury yields continued their sharp drop from June with the 10-year and 30-year declining by 21 bp and 17 bp respectively. At the end of July, the 30-year Treasury's yield broke back below 2% to end the month at 1.89%, while the 10-year yield closed at 1.24%. The Treasury yield curve continued to flatten with the 2-year/30-year spread narrowing by an additional 11 bp to end the month at +170 bp. Unlike the equity markets, the investment grade credit sector gave up gains with the credit index option-adjusted spread (OAS) widening by 4 bp to +81 bp resulting in -38 bp of underperformance versus duration-matched Treasuries. Following two consecutive months of flattening, the corporate quality and credit curves both steepened in July as is typically seen when the credit sector underperforms. The Single-A sector outperformed the BBB-rated sector by 4 bp in excess return, while the short and intermediate sectors outperformed the long maturity credit sector by an average of +53 bp. The best performing sectors include REITs (+16 bp) and Financial Companies (+6 bp), while Oil Field Services (-90 bp) and Wirelines (-71 bp) lagged. Despite the spread widening in the investment grade sector, the index posted a positive total return of +1.3 % for the month due to the sharp drop in Treasury yields. Year-to-date, the index's total return is now flat (0%). Performance in the high yield sector mirrored its investment grade counterpart. The Bloomberg Barclays High Yield index OAS widened sharply by 26 bp in July to end the month at +294 bp leading to excess return of -34 bp. Like the investment grade sector, higher quality high yield bonds outperformed – on a total return basis, the Ba-sector outperformed the single-B and Caa-sector by +65 bp and +101 bp respectively. The best performing sectors include Metals and Mining (+114 bp) and Electric Utilities (+101 bp), while Oil Field Services (-229 bp) and Leisure (-101 bp) were among the underperformers. For the month, the high yield index posted a total return of +0.4% aided by the sharp drop in Treasury yields. For the first seven months of the year, the index has gained a total return of +4%. International developed market government yields also had significant declines like U.S. Treasury yields in July as investors worried about the economic effects from the rising number of coronavirus cases. Government bond yields in the eurozone have dropped further into negative territory. Additionally, the U.S. dollar lost some ground with the dollar weighted index (DXY) declining -0.3% for the month. As a result, the FTSE non-US World Government Bond Index (WGBI) rose +1.8% in July outperforming the U.S. government bond index by +50 bp. However, year-to-date, the international government bond index (-4.3%) continues to trail the U.S. government bond market's return of -1.2%.

			Returns as of 7/31/21 (In %)			
		Month	YTD	1 Year	3 Years	5 Years
Russell 3000®	US AllCap Equity	1.7	17.1	38.7	18.1	17.4
Russell 1000®	US Large Cap Equity	2.1	17.3	38.0	18.6	17.6
Russell 1000® Growth	US Large Cap Growth	3.3	16.7	36.7	25.3	23.3
Russell 1000® Value	US Large Cap Value	0.8	18.0	39.3	11.3	11.4
Russell Midcap®	US Mid Cap Equity	0.8	17.1	42.6	15.8	14.8
Russell Midcap® Growth	US Mid Cap Growth	1.0	11.6	34.5	21.9	19.6
Russell Midcap® Value	US Mid Cap Value	0.6	20.2	47.1	11.1	11.0
Russell 2000®	US Small Cap Equity	-3.6	13.3	52.0	11.5	14.3
Russell 2000® Growth	US Small Cap Growth	-3.6	5.0	41.0	13.9	16.4
Russell 2000® Value	US Small Cap Value	-3.6	22.2	63.7	8.3	11.6
MSCI ACWI ex-US	Global Equity ex-US	-1.6	7.4	27.8	7.9	9.6
MSCI EAFE	Global Developed Mkts Equity	0.8	9.6	30.3	7.7	9.4
MSCI EM	Emerging Mkts Equity	-6.7	0.2	20.6	7.9	10.4
Bloomberg/Barclays US Agg	US Core Fixed Income	1.1	-0.5	-0.7	5.7	3.1
Bloomberg/Barclays US Interm. Agg	US Intermediate Fixed Income	0.7	-0.1	0.2	4.7	2.6
Bloomberg/Barclays US Credit	US Corporate Bonds	1.3	0.0	1.2	7.6	4.6
Bloomberg/Barclays US MBS	US Mortgage Backed Securities	0.6	-0.1	0.0	4.0	2.4
Bloomberg/Barclays US Corp HY	US High Yield	0.4	4.0	10.6	7.2	7.0
FTSE Non-US WGBI	Global Fixed Income ex-US	1.8	-4.3	-0.2	3.6	1.5

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