

# Portfolio Manager Commentary

January 22, 2021



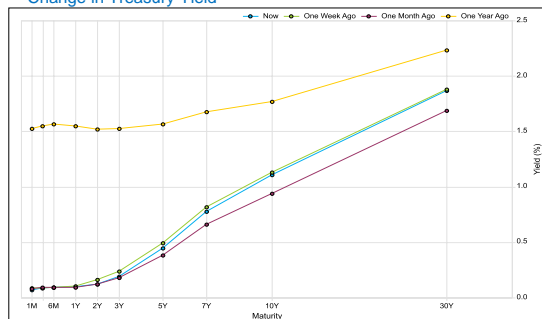
## Economic Outlook

The U.S. National Association of Homebuilders (NAHB) Index was a strong 83 in January, down from 86 in December. Otherwise a slow week for economic releases.

## Fixed Income

In a world flush with cash, long-dated debt is where all the action is for bond traders these days. In Europe, investors looking to escape a sea of negative yields are snapping up some of the longest-maturity debt being offered in an attempt to park their money in assets that still provide some sort of return. In the U.S., the Treasury is selling long bonds amid a looming torrent of government spending, while they bring back up the likelihood of the first-ever Treasury security offered with a maturity over thirty years. On both sides of the Atlantic, the longest maturity debt is the focus of a debate over whether trillions of stimulus will trigger a resurgence in inflation. Those buying long-dated bonds expect central banks will prop up the market for longer with low rates and quantitative easing, investors betting on steeper yield curves expect a pick-up in prices to erode assets maturing further in the future. The pivot into longer-dated bonds is not all voluntary. Over \$17 trillion of investment-grade bonds now come with a negative yield attached, which means an investor holding such an asset until maturity has locked in a losing investment. Europe is the heartland of this phenomenon, with the entirety of Germany's debt market in sub-zero territory, and French securities out to 16 years also negative. While negative yields have not reached the U.S. yet, Federal Reserve policy has pushed the rates on the world's biggest bond market to record lows. Treasury Secretary Janet Yellen has said that she would be "very pleased" to look at issuing long-term debt, when asked about the possibility of a fifty-year Treasury. One of the most recent additions to the Treasury's arsenal was the department's decision a year ago to start selling twenty-year debt again. Last Wednesday, Treasury sold \$24 billion of this maturity. While it yielded more than at the previous auction, the rate of 1.657% remains low for long-term debt by historical standards. Extending the Treasury curve beyond thirty years may still be a way off, but it would give the government an opportunity to lock in low borrowing costs for decades at a time while ramping up debt levels.

## Change in Treasury Yield



## Current Generic Bonds Yields

Treasuries	Agencies	Corporates	Municipals
3 mo. 0.07%	3 mo. 0.00%	3 mo. 0.17%	3 mo. 0.14%
6 mo. 0.08%	6 mo. 0.00%	6 mo. 0.19%	6 mo. 0.15%
1 yr. 0.09%	1 yr. 0.02%	1 yr. 0.21%	1 yr. 0.16%
2 yr. 0.12%	2 yr. 0.15%	2 yr. 0.27%	2 yr. 0.22%
5 yr. 0.43%	5 yr. 0.45%	5 yr. 0.74%	5 yr. 0.36%
10 yr. 1.09%	10 yr. 1.25%	10 yr. 1.63%	10 yr. 0.88%
30 yr. 1.85%	30 yr. 2.72%	30 yr. 1.62%	

## Equity

U.S. Equity finished the week stronger as the S&P 500 Index closed up +1.91%. There was fairly little news on the headline perspectives that was believed to have impacted the market. In other news, the battle between growth and value continues as Energy (-1.59%) and Financials (-1.95%) lag while Communication Services (+5.44%) and Tech (+4.25%) finished strong. Year to date, the real standout has been in the small cap space as the Russell 2000 is up over 9% for the year, while large cap has seen a 2.27% increase so far.

As reported by Reuters, Bank of America's latest "Flow Show" report noted that global equities have seen a record \$255B of inflows over the last three months. Expectations were reiterated for a peak positioning and a correction in Q1. The report also discussed a preference for inflation over deflation assets over the last couple of months, driven by vaccine and fiscal stimulus optimism. The trend continued in the latest weekly reporting period with outsized inflows to U.S. small cap and value, financials, energy, EM equities, TIPS, bank loans and precious metals. However, tech another standout, which is seemingly fitting with the renewed upside leadership this week on the part of growth and momentum factors.

Index Returns	Last Week	YTD
Dow Jones Industrials	0.60%	1.41%
S&P 500 (LCap)	1.94%	2.27%
S&P 400 (MCAp)	1.59%	6.76%
Russell 2000 (SCap)	2.15%	9.82%
NASDAQ Composite	4.19%	5.08%
MSCI EAFE (Int'l)	1.01%	3.00%
iShares Real Estate	1.63%	0.37%

Source: FactSet Research Systems

## Asset Allocation

### Current Sentiment

Cash	Favorable
Short FI	Neutral
Intermediate FI	Neutral
Inflation-Adjusted FI	Neutral
High Yield FI	Unfavorable
International FI	Unfavorable
Equity Income	Neutral
Large Cap Equity	Favorable
Mid Cap Equity	Neutral
Small Cap Equity	Unfavorable
International Equity	Unfavorable
Emerging Markets Equity	Unfavorable
Real Estate	Neutral
Commodities	Unfavorable

### Summary below - Current stance on most asset classes:

**Cash** - Overweighting due to market volatility and uncertainty from Covid-19.

**Short Term Bonds** - Relative to Intermediate Bonds, the reduced duration is preferable given the oversold long-end of the curve.

**Intermediate Term Bonds** - The current trading range of intermediate bonds warrants a neutral position with limited upside potential. Some opportunities still remain in certain sectors.

**Inflation-Adjusted Bonds** - Low inflation expected in near-term providing zero real return.

**High Yield Bonds** - Spreads are rising given the market turbulence and exposure to unnecessary credit risk when compared to Treasuries would not be advised.

**International Bonds** - Foreign bonds offer good diversification qualities and higher yield opportunities, however, risks have been elevated recently and investment should be made cautiously.

**Equity Income** - High quality and higher-dividend-paying companies remain attractive for long-term investors given their favorable risk-adjusted profile and current yield curves.

**Large Cap Stocks** - A favorable weighting is recommended. Growth continues to be a more favorable style and should continue to be overweighted versus Value.

**Mid Cap Stocks** - Mid cap exposure remains neutral - more attractive than small caps but not as attractive as large caps.

**Small Cap Stocks** - In broad market corrections, small cap stocks will suffer most with increased volatility. Underweight until a clearer picture of recovery ensues.

**International Stocks** - Given most foreign investment is in developed markets and European countries, until sovereign debt concerns are alleviated, an underweight is recommended.

**Emerging Market Stocks** - Stronger balance sheets, less debt, and better growth potential make emerging markets more fundamentally attractive than developed countries longer-term. However, trade uncertainty and dollar strength provide a headwind for EM in the near term.

**Real Estate** - Pricing has begun to stabilize and long-term valuations appear attractive. Real Estate should continue to be a strong alternative to other asset classes.

**Commodities** - Global demand should support higher prices if the global recovery remains on track. Volatility will be higher, and commodities will be susceptible to short-term price shocks, however, if used in conjunction with other asset classes, risk can be reduced substantially within a diversified portfolio. Used alone though is not recommended.

Sources of statistical information are Bloomberg and Ned Davis Research.

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