Portfolio Manager Commentary
November 12, 2021

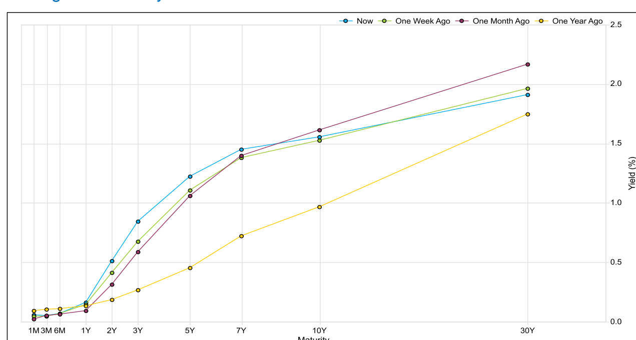
Economic Outlook

U.S. Producer Prices were up 0.6% in October versus up 0.5% for September. Consumer Prices were up 0.9% in October versus up 0.4% in September. The Preliminary University of Michigan Consumer Sentiment Survey came in at 66.8 for November, down from 71.7 for October.

Fixed Income

Warning signs are starting to emerge inside the $22 trillion U.S. Treasury market, which is being whipsawed by volatility just as the Federal Reserve begins pulling back from its bond-buying program that has helped prop up the market since the end of March 2020. Sparked by a report of surging inflation that led traders to move up the timetable for the Fed's first rate increase, the yield on two-year Treasury notes rose around ten basis points last week. The recent volatility also led to a messy thirty-year bond auction last week which drove a gauge of market liquidity to its most troubled level since the meltdown soon after the pandemic began. The fissures are appearing just as market regulators are set to convene this Wednesday for an annual event that's been held since 2015, a year after a 12-minute "flash rally" when yields crashed and rebounded with no apparent trigger. That's not supposed to happen in the world's biggest debt market. The agenda is to consider "proposals to improve overall market functioning and resilience." The Fed, which has been buying $80 billion of Treasury securities since the beginning of the pandemic, is implementing plans to start scaling back its buying by $10 billion a month. Also while regulators are meeting, the Treasury Department will hold its monthly auction of twenty-year bonds, providing a test of whether last week's thirty-year sale was an anomaly or a sign that the market's ability to function smoothly may be imperiled as the central bank withdraws its support. The recent swings in the Treasury market reflect the broad uncertainty about the direction of the economy and monetary policy amid surging prices, labor shortages and yields that are trading well below the rate of inflation.

Change in Treasury Yield



Current Generic Bonds Yields

Treasuries		Agencies		Corporates		Municipals	
3 mo.	0.04%	3 mo	-0.04%	3 mo	0.29%	3 mo	0.21%
6 mo	0.06%	6 mo	0.00%	6 mo	0.32%	6 mo	0.22%
1 yr	0.16%	1 yr	0.15%	1 yr	0.40%	1 yr	0.24%
2 yr	0.51%	2 yr	0.54%	2 yr	0.65%	2 yr	0.32%
5 yr	1.22%	5 yr	1.08%	5 yr	1.46%	5 yr	0.76%
10 yr	1.56%	10 yr	1.64%	10 yr	2.14%	10 yr	1.27%
30 yr	1.93%	30 yr		30 yr	2.77%	30 yr	1.75%

Equity

U.S. Equity finished snapped a five-week winning streak as the S&P 500 finished the week negative with a -0.27% return. As stated by FactSet Research Systems, the biggest overhang seems to be inflation concerns following the biggest annual increase in consumer prices in over 30 years, though the bullish narrative continues to remain intact, and the negative return could be due to a natural pullback from extreme overbought conditions.

FactSet's "Earnings Insight" model showed that with 92% of S&P 500 companies having reported third quarter earnings, 39.1% blended earnings growth rate is ahead of the 27.5% expected rate at the end of the quarter and is on pace for the third-highest year-over-year earnings growth rate since the second quarter of 2010. This, of course, plays into the theme of inflation as 285 S&P 500 companies used the term "inflation" during their third quarter earnings calls.

Sectors were a mixed bag for the week as Materials (+2.60%) was the clear leading sector. Other positive sectors included Health Care (+0.72%), Industrials (+0.48%), Financials (+0.32%), and Technology (+0.14%). Consumer Discretionary (-3.54%) and Energy (-1.22%) were the biggest losers.

Index Returns	Last Week	YTD
Dow Jones Industrials	-0.56%	19.58%
S&P 500 (LCap)	-0.27%	26.07%
S&P 400 (MCap)	-0.10%	25.82%
Russell 2000 (SCap)	-1.04%	22.12%
NASDAQ Composite	-0.69%	23.06%
MSCI EAFE (Int'l)	-0.55%	13.05%
iShares Real Estate	-0.18%	29.95%

Source: FactSet Research Systems

Asset Allocation

Current Sentiment

Asset Class	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 overweighed 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

Sources of statistical information are Bloomberg and Ned Davis Research.

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