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MARKET REVIEW
FEBRUARY 2021

WHAT TO EXPECT FROM A DEMOCRAT UNIFIED GOVERNMENT

A president's first 100 days in office are often viewed as an indicator of their governing style and priorities. Some market strategists expect President Biden's first 100 days to largely focus on a new stimulus package and health care reform. Other topics that may be next on the administration's agenda include environmental issues and renewable energy, tax increases, and infrastructure spending.

One major challenge for Biden's agenda is the Democratic Party's narrow majority in Congress. In the House of Representatives, the Democrat's majority shrank to 11 votes, while the Senate is split 50-50 with Vice President Kamala Harris being the tie-breaking vote. The slim majority tempers the prospect of radical policy changes and increases the likelihood of policies leaning toward centrist proposals. The votes of a few centrist Democrat Senators will be more influential since a single defection could stand in the way of passing legislation.

Most major legislation in the Senate needs a 60-vote supermajority which would require support from at least 10 Republicans. If legislation fails to get bipartisan support from 60 Senators then Democrats can use an alternative route to pass some types of legislation with a simple majority through the budget reconciliation process. Using reconciliation requires legislation matters to be related to spending, revenue, and the federal debt limit. Under those criteria, reconciliation could include portions of Biden's agenda such as additional stimulus, raising taxes, health care reform, infrastructure spending, and renewable energy incentives. Since 1980, Congress has passed 20 budget reconciliation bills including the Affordable Care Act in 2010 and Tax Cuts and Jobs Act of 2017. It is possible for Democrats to pass two reconciliation bills in the current calendar year because the previous Congress did not pass a budget resolution for fiscal year 2021, which began on September 1, 2020.

ADDITIONAL STIMULUS

COVID-19 related federal stimulus funding to date totals roughly \$3.5 trillion which represents 16.3% of U.S. GDP. Biden's proposed \$1.9 trillion stimulus package would bring total stimulus to a gargantuan 25.1% of GDP. Some of the key provisions in Biden's proposal include \$465 billion

in direct payments to individuals, \$350 billion for federal unemployment benefits, \$350 billion for state and local government aid, \$170 billion to reopen schools and address other education matters, and an increase of the federal minimum wage to \$15 per hour from \$7.25. Some economists believe the stimulus package could ultimately be around \$1 trillion to \$1.5 trillion in order to ensure support from centrist Democrats. Bloomberg economists estimate another round of stimulus in the vicinity of \$1 trillion would boost U.S. economic growth this year to 5.2% from their current forecast of 3.5%. Their projection also includes the economic lift from this year's stimulus package continuing into next year with growth above 3.0%, compared to a baseline projection of 2.4%. If Biden's full \$1.9 trillion package is passed, Bloomberg's economists project growth could reach 6.0% to 6.5% this year.

HEALTH CARE REFORM

Health care reform is potentially the next major area of focus for Democrats, after the stimulus package. Biden's health care plan includes lowering the Medicare eligibility age to 60 from 65, eliminating the earnings limit for Affordable Care Act tax credits, and creating a government-run health insurance option that would compete with the private health insurance system currently in place.

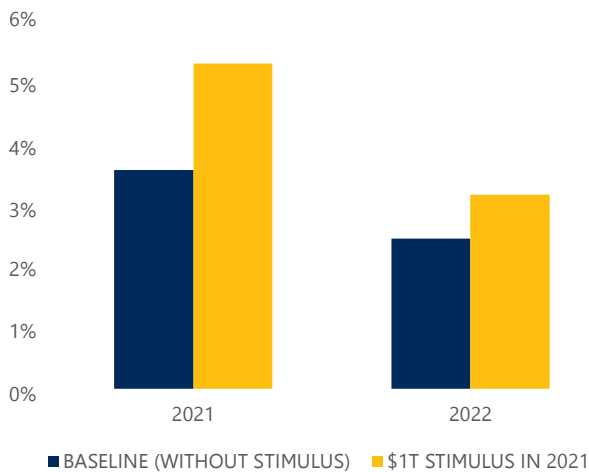
Prescription drug pricing reform is a topic that could receive bipartisan support. Medicare drug prices are currently set freely by pharmaceutical companies. Biden's plan would require negotiating Medicare drug prices, linking drug price increases to inflation, limiting the launch prices of new drugs, allowing drug imports from other countries, and terminating the tax break for drug advertisement spending. The Congressional Budget Office estimates that negotiating Medicare drug prices could reduce government spending on drugs by \$448 billion over 10 years. These policies would likely reduce the earnings of many drug companies and weigh on overall health care sector profits.

HIGHER TAXES

Biden's agenda includes raising taxes to fund increased spending on the Affordable Care Act, renewable energy, and infrastructure. Biden proposed raising the corporate tax rate to 28% from 21%, and raising the individual tax rate to 39.6% from 37% for the top individual tax bracket.

STIMULUS TO BOOST U.S. GDP

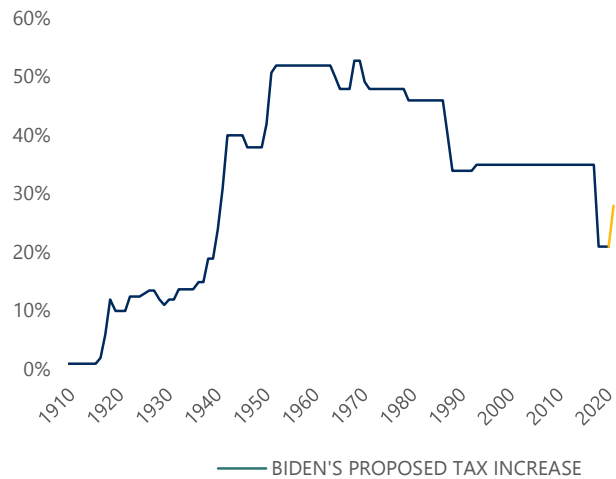
BLOOMBERG ECONOMIST GDP FORECAST



Source: Bloomberg. Past performance does not guarantee future results.

U.S. FEDERAL CORPORATE TAX RATE

BIDEN PROPOSES RAISING TAX RATE TO 28% FROM 21%



Source: Tax Policy Center. Past performance does not guarantee future results.

Investment research provider BCA Research estimates Biden's tax plan would result in an 11.4% reduction in S&P 500 earnings. The real estate, technology, and health care sectors would be most impacted by higher tax rates.

Last September, Biden signaled raising taxes was a priority that he would address on his first day in office, but economic challenges related to the pandemic have likely delayed tax reform until late 2021, at the earliest. However, if Democrats use reconciliation bills for additional stimulus or health care reform, they may be forced to adopt tax reform earlier than planned. Reconciliation requires the federal budget to balance at the end of the ten-year budget window (i.e., 2030), which may necessitate Democrats pulling tax hikes forward.

ENERGY REGULATIONS AND SPENDING

Reducing carbon emissions by shifting the country's energy generation toward renewable energy is foundational to Biden's agenda. Biden plans to support the transition to cleaner energy by spending \$2 trillion on developing renewable and carbon-free energy (e.g., wind, solar, nuclear, hydropower, and batteries), encouraging the use of electric vehicles (EVs), and implementing policies to discourage the use of fossil fuels, such as banning new oil and gas permits on federal land and water (e.g., the Gulf of Mexico). Likely beneficiaries of a transition to cleaner energy include utilities, electric vehicle manufacturers and suppliers, semiconductor makers, renewable energy companies, and certain types of mining companies. Accelerating adoption of electric vehicles is raising demand for mined materials used in batteries, such as lithium, cobalt, nickel, copper, and graphite.

TECHNOLOGY REGULATION

Democratic control of Congress increases the possibility of new legislation aimed at the technology sector in areas such as data privacy and antitrust. While there is bipartisan support for increased regulation, Congress lacks a consensus

on how to proceed given there are disagreements between and within political parties about which issues should be regulated. Wide-reaching legislation is expected to be constrained by the narrow Democratic majority in Congress, requiring compromises to achieve bipartisan support with Republicans, who are often inclined to favor more business-friendly approaches. Bloomberg's Senior Litigation Analyst, Jennifer Rie, anticipates new legislation will not drastically change the status quo and big technology companies' growth prospects will remain intact. In the meantime, valuations of big technology companies may be occasionally pressured from regulation headline risk as the discussion in Washington slowly progresses.

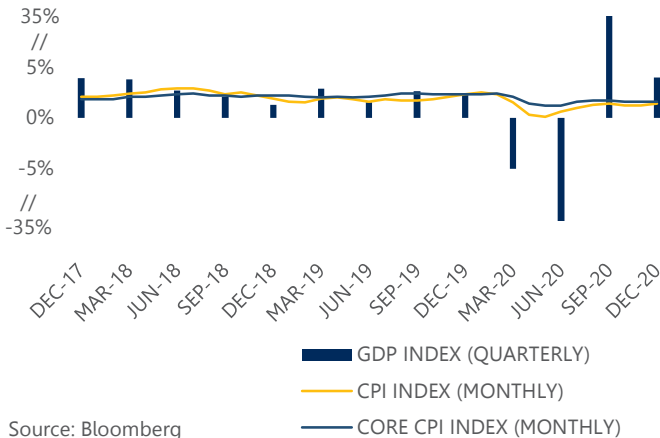
CONCLUSION AND INVESTMENT IMPLICATIONS

Loose fiscal policy and an accommodative Federal Reserve are expected to support above-trend economic growth this year and provide a favorable environment for risk assets. Stronger economic growth in combination with Biden's policies to increase government spending will likely lead to moderately higher inflation and bond yields. The Treasury yield curve may experience further steepening as longer term yields rise while the Fed keeps short-term yields anchored. The central bank's updated and more tolerant inflation policy will likely instill a more patient approach to raising interest rates in response to stronger inflation.

Over the longer term, history suggests that policy changes from a particular president or political party are less impactful for the economy and stock market than many observers believe. Ultimately, economic fundamentals (e.g., GDP growth, interest rates, inflation, and labor growth and productivity) drive the economy and stock market. Political policies can impact these fundamentals, but their effect tends to be gradual and can be outweighed by non-political factors such as the Federal Reserve's monetary policy and demographic shifts.

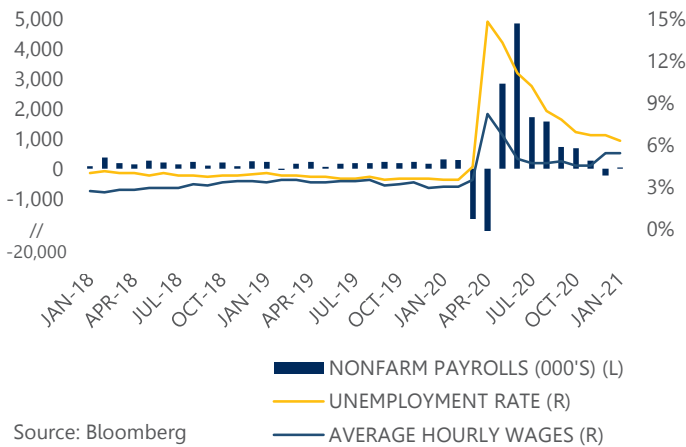
ECONOMY

GDP AND CONSUMER PRICES DECEMBER 2017 THROUGH DECEMBER 2020



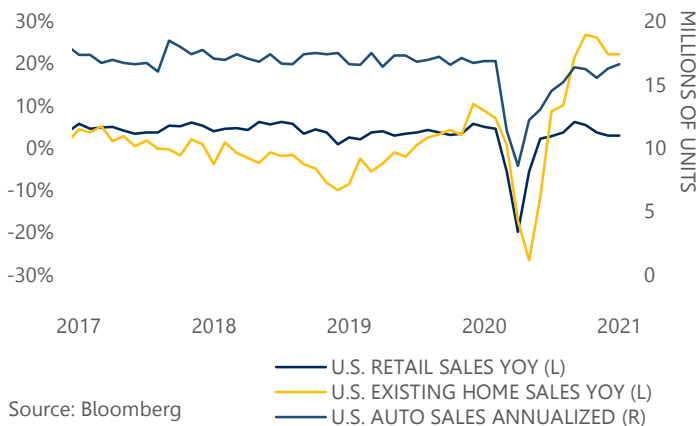
- The U.S. economy expanded at a slightly slower pace than expected in the final quarter of 2020 as the number of new virus cases rose and some areas reinstated lockdown measures. GDP grew 4.0% in the quarter, below the Bloomberg economists' consensus estimate of 4.5%.
- Despite GDP slowing from the third quarter's impressive 33.4% growth rate as expected, the fourth quarter expansion still provided evidence of a continued economic recovery from the sharp declines earlier in the year. GDP contracted 3.5% in 2020, the first annual contraction since 2009.
- The Core Consumer Price Index (CPI) decelerated to 1.62% growth in December from 1.65%. A decrease in prices of used cars and trucks, recreation, and medical care weighed on the index.

LABOR MARKET JANUARY 2018 THROUGH JANUARY 2021



- U.S. job growth returned in January as payrolls increased by 49,000. This was slightly less than the 50,000 jobs expected; however, it was a healthy rebound from the 227,000 jobs lost in December.
- The decline in the unemployment rate to 6.3% from 6.7% was primarily driven by the lower labor force participation rate, as 406,000 workers dropped out of the labor force.
- The leisure and hospitality industries continued to be the hardest hit industries as most hotels, bars and restaurants remained under government-mandated capacity constraints. Employment declined by 61,000 in these industries in January, following a steep decline of 536,000 in December. Leisure and hospitality employment is down 22.9% since last February.

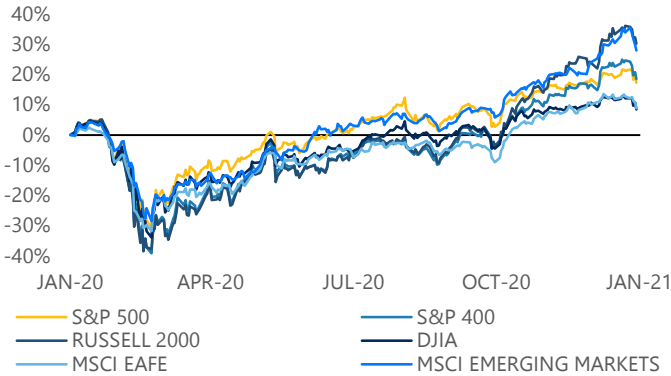
HOUSING, AUTO AND RETAIL SALES JANUARY 2017 THROUGH JANUARY 2021



- Fiscal stimulus and low interest rates have supported auto sales recovery to pre-pandemic levels from their April low. U.S. auto sales reached a seasonally adjusted annual rate of 16.63 million units in January.
- Consumer spending in the U.S. slowed over the last few months amid record COVID-19 infections and slowing labor market recovery. Despite the recent declines, U.S. retail sales were up a healthy 2.9% in January.
- In 2020, U.S. existing home sales reached their highest level since 2006 as Americans took advantage of historically low mortgage rates. Activity in all four major regions recorded double-digit growth in January with total sales increasing 22.2% from a year ago.

EQUITY

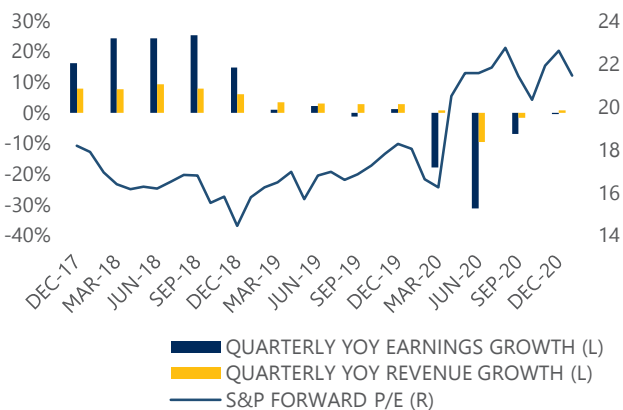
TRAILING 12-MONTH EQUITY RETURNS PRICE APPRECIATION, JANUARY 2020 THROUGH JANUARY 2021



Source: Bloomberg. Past performance is no guarantee of future results.

- After a strong start to the month, stocks retreated from record highs and posted their first monthly loss since October. The initial stages of the vaccine rollout and prospects for further fiscal stimulus helped the economic recovery outlook. Stimulus expectations rose after Democrats won both Georgia Senate runoff elections.
- The S&P 500 index fell over 3% in the last week of the month amid concerns about vaccine supply delays in Europe and increased market volatility partly due to retail investor activity concentrated in a few small and heavily shorted stocks. Retail flows into stocks such as GameStop (GME) and AMC Entertainment (AMC) forced some hedge funds to abandon their short positions.

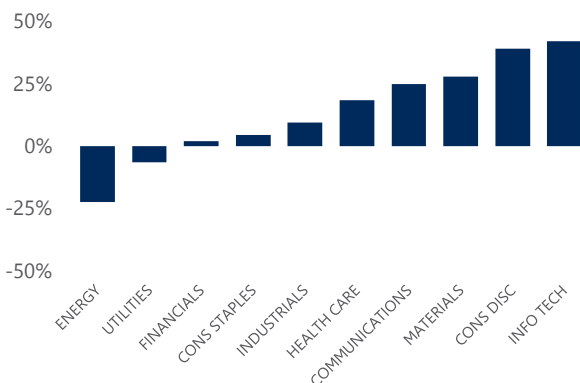
S&P 500 YOY EARNINGS & REVENUE GROWTH BY QUARTER, DECEMBER 2017 THROUGH JANUARY 2021



Source: Bloomberg

- Around half of S&P 500 companies reported fourth quarter earnings in January. S&P 500 earnings are recovering quicker than analysts projected. Earnings are on track for positive growth compared to analysts' initial estimate for an 8.78% decline.
- Cyclical sectors are posting the best results as financials and materials are on pace for double-digit earnings growth. Technology is the only other sector with double-digit earnings growth.
- Analysts continue to revise their earnings expectations upward for the coming quarters. Earnings are projected to rise 20.52% and 48.44% in the first and second quarters, respectively. Analysts expect 22.82% earnings growth this year after contracting 12.69% in 2020.

S&P 500 SECTORS 12-MONTH PRICE RETURNS JANUARY 2020 THROUGH JANUARY 2021



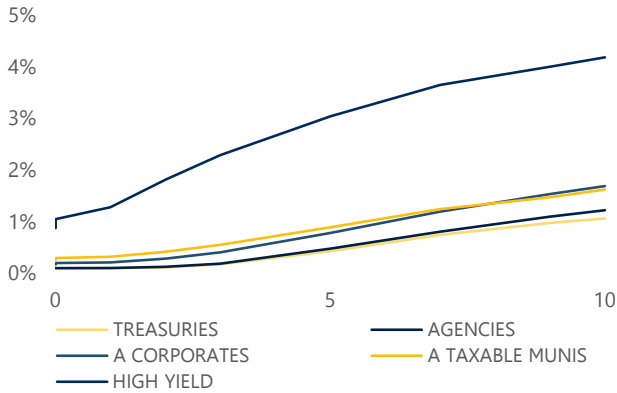
Source: Bloomberg

- The energy sector's fourth quarter momentum carried over to January with a 3.79% monthly gain, the best among the S&P 500 sectors. The price of West Texas Intermediate (WTI) crude oil rose above \$50 per barrel for the first time since the start of the pandemic. Oil's rally was driven by shrinking inventory and Saudi Arabia's decision to unilaterally increase its oil production cuts by 1 million barrels per day.
- Industrials' 4.30% monthly loss made it the second worst performing sector in January behind consumer staples. Industrials are the only sector on track for a double-digit earnings decline in the fourth quarter as airlines and railroad companies remain weak.

FIXED INCOME

CURRENT YIELD CURVES

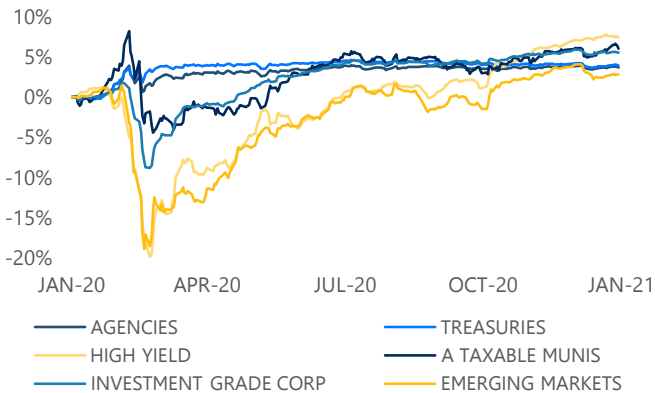
YIELD CURVES AS OF JANUARY 2021



Source: Bloomberg

- The U.S. Treasury yield curve steepened in January as yields remained relatively unchanged on the short end, but increased on the long end. The two-year yield declined 0.05% in the month to 0.11%, the five-year increased 0.06% to 0.43%, and the 10-year rose 0.15% to 1.07%.
- Shorter dated U.S. Treasury yields remained anchored at historically low levels driven by indications from Federal Reserve officials that the central bank's policy rate will stay at the zero bound for the foreseeable future.
- Agencies began to see some pick-up in yield over their government counterpart Treasuries in January beginning at around five years on the maturity spectrum.

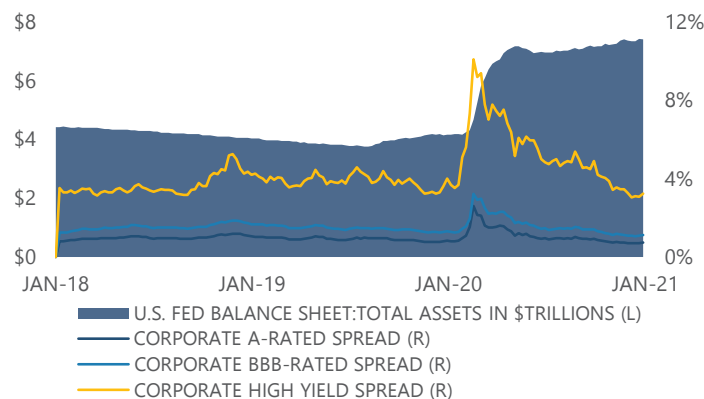
12-MONTH RETURNS, TAXABLE BOND SEGMENTS JANUARY 2020 THROUGH JANUARY 2021



Source: Bloomberg. Past performance is no guarantee of future results.

- High yield and emerging market bonds experienced the sharpest recoveries in performance from the March lows amid building expectations for a robust global economic recovery in 2021. Emerging markets bonds have benefitted in recent months from a bout of significant U.S. dollar weakness.
- All the bond segments in the accompanying chart have experienced positive returns since the beginning of the pandemic as well as over the last 12 months.
- Moving forward, the size and scope of a prospective wide-ranging stimulus package will likely determine the path of relative performance for U.S. corporate and municipal bonds.

FED BALANCE SHEET EXPANSION AND CREDIT SPREADS JANUARY 2018 THROUGH JANUARY 2021

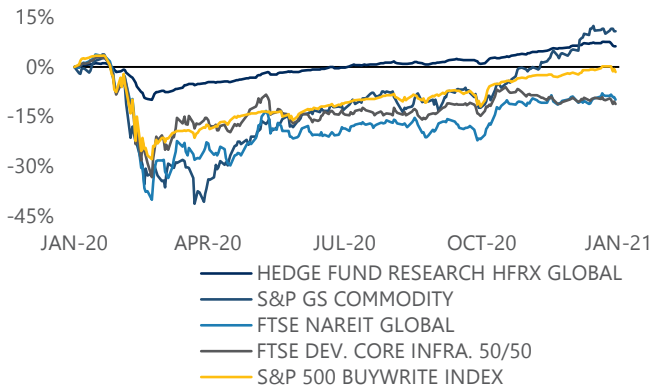


Source: Bloomberg

- The U.S. Federal Reserve's balance sheet has swelled since the beginning of the pandemic as policymakers have implemented and maintained several large bond purchasing programs in an effort to help support the economy.
- As seen in the accompanying chart, credit spreads across the maturity spectrum increased drastically at the onset of the COVID-19 pandemic. Fed policy support helped spreads steadily decrease throughout most of 2020. Spreads widened moderately in January as economic data weakened.
- In the January FOMC statement, Fed officials indicated they will continue purchasing \$80 billion in Treasury securities per month and \$40 billion in agency mortgage-backed securities until further notice.

ALTERNATIVES

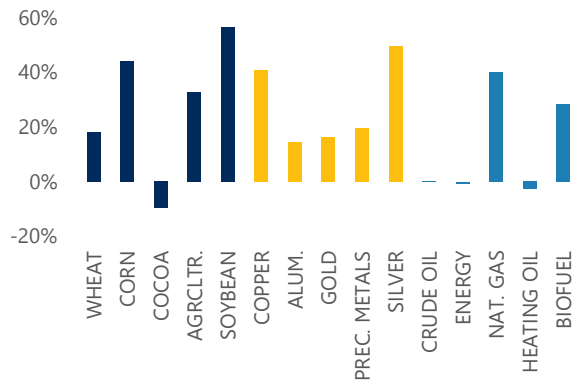
ALTERNATIVES, 12-MONTH RETURNS JANUARY 2020 THROUGH JANUARY 2021



Source: Bloomberg. Past performance is no guarantee of future results.

- Of the five alternative asset class segments shown in the accompanying chart, a basket of trade-weighted commodities generated the best returns in January by a wide margin. This was driven by a nearly 8% increase in U.S. crude oil prices amid Saudi-led production cuts and expectations for above-trend economic growth in 2021.
- Across the hedge fund world, merger arbitrage, convertible arbitrage and equity market neutral strategies generated the best returns in January.
- The real estate and infrastructure indexes shown in the accompanying chart mostly tracked the global equity market's moderate losses in January. Both could face moderate headwinds from a continuation of rising government bond yields in coming months.

COMMODITIES, 12-MONTH SPOT RETURNS JANUARY 2020 THROUGH JANUARY 2021



Source: Bloomberg. Past performance is no guarantee of future results.

- Driven by strength in energy and industrial metals, the broad commodities asset class has outpaced the S&P 500 and MSCI ACWI indexes over the five-month period spanning September to January by 13.5% and 9.6%, respectively.
- The petroleum complex, copper and iron ore have benefitted from building expectations for a vaccine-driven revival in demand for travel, leisure, transportation to near pre-pandemic levels in 2021.
- The S&P GSCI Corn index advanced 13.0% in January, spurred by a spike in U.S. export demand. In the last four days of the month, the USDA confirmed that China purchased 5.85 million metric tons of U.S. corn, which is more than the U.S. has ever shipped to China in an entire marketing year (September through August).



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