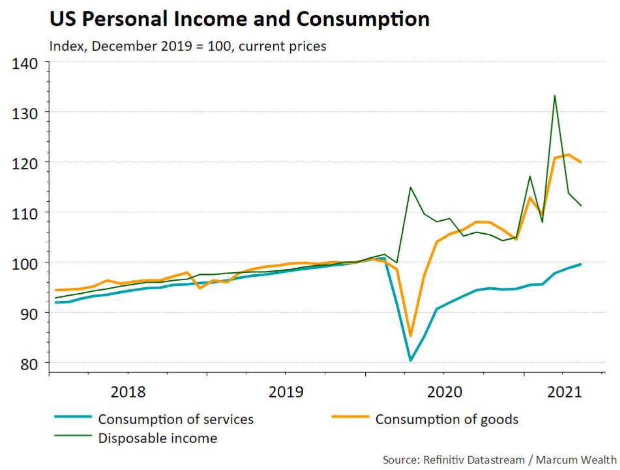
Strategy Newsletter – 3rd Quarter 2021

- The economic recovery continues even with inflation narratives stealing the show.
- Earnings keep delivering for stocks.
- Despite headline inflation, interest rates fell during the quarter.
- REITs were a big winner in the first half of the year.

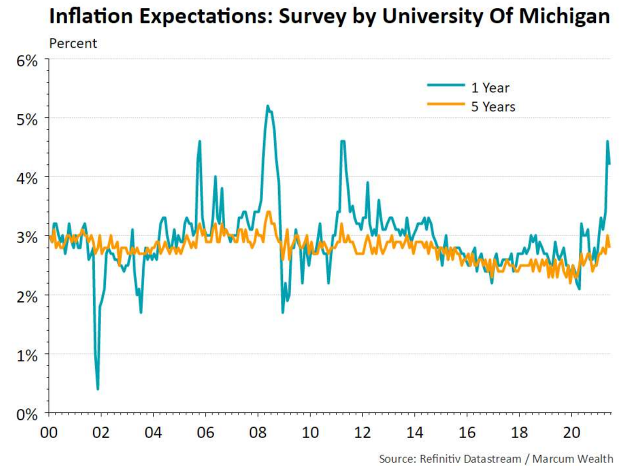
Economy

A unique aspect of this recession was the growth in disposable personal income during the pandemic. Part of this was related to government transfer payments. Another aspect is simply less opportunity to spend.

Consumption is now back to its growth trend. Goods sectors were the big beneficiaries over the last year, especially items sold online. With hospitality sectors closed down during the pandemic, households could not spend in many large service categories such as restaurants.



Inflation is on people's minds as the economy reopens. The latest data are well above the Fed's long-term targets. Yet this was expected because inflation fell so far short of the target in 2020. Supply chain disruptions from semiconductor chips to commodities are affecting prices for consumers. A spike in expectations for inflation over the next year already happened. Expectations are beginning to fall back to a normal range, similar to past periods with rapid increases. The long-term outlook for inflation is in its typical range as shown below.



"The economy only reopens once," is a phrase many commentators have used to describe the current environment. We think it fits. Since many of the stimulus programs are set to expire and are not yet permanent, it makes sense that inflation will not run away from central bankers.

This economic recovery is on fast forward compared to the one following the Great Recession in 2008. It still should have room to run as policy remains accommodative and some industries are just getting back to pre-pandemic levels.

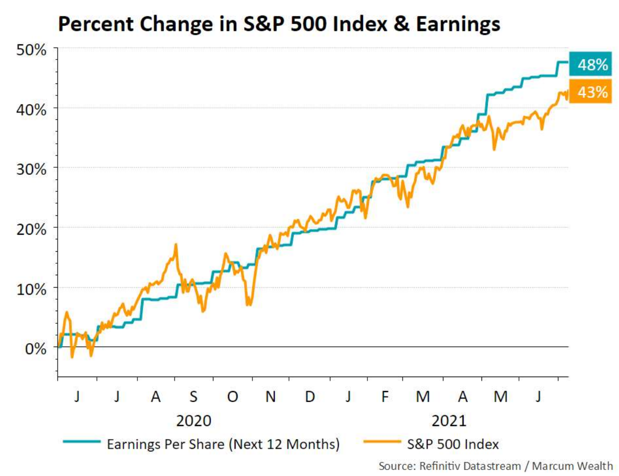
The rest of the world is beginning to catch up to the U.S. in terms of vaccine roll-out. In turn, better economic news should be expected given the low levels of a year ago.

Equity

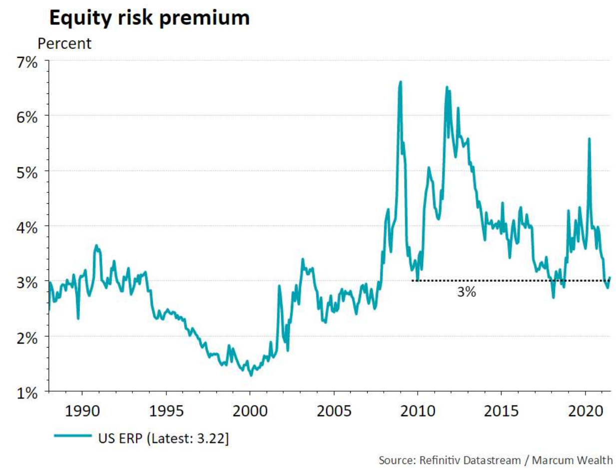
Market leadership changed during the second quarter. Large cap and growth equities took back the mantle as the top performers.

US Equity	2Q 2021
Large Cap Stock	
S&P 500	8.5%
Small & Mid Cap Stock	
S&P 400 Mid Cap	3.6%
S&P 600 Small Cap	4.8%
All Cap Style Indices	
S&P 1500 Value	4.9%
S&P 1500 Growth	11.2%
International Equity	**2Q 2021**
MSCI EAFE	5.4%
MSCI EAFE Value	3.3%
MSCI EAFE Growth	7.6%
MSCI Europe	7.7%
MSCI Japan	-0.2%
MSCI Emerging Markets	5.1%

Many people wonder, “How can stocks be up so much?” Earnings are the simple answer. Companies continue to outperform expectations. Higher equity prices followed the strong results and outlook from the corporate sector.

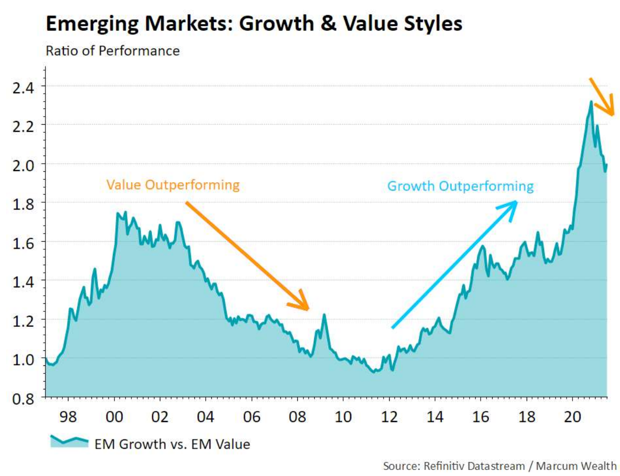


The excellent price performance brought on higher multiples and valuations. The forward price-to-earnings ratio for U.S. equity is currently just under 23 times. The equity risk premium, or the expected real return of stocks over bonds, fell to 3% during the quarter. This level has been the low end of its range since 2010.



For the premium to fall further, stock prices would have to continue rising or bond yields would need to fall further. This leaves the market dependent on earnings outperformance.

While growth staged a comeback in developed markets, emerging markets are a different story. Value outperformed for the third straight quarter.



Emerging markets value stocks were the winner in the 2000s while growth took the lead in the 2010s. Chinese tech firms struggled recently, and it could be a sign of a trend change.

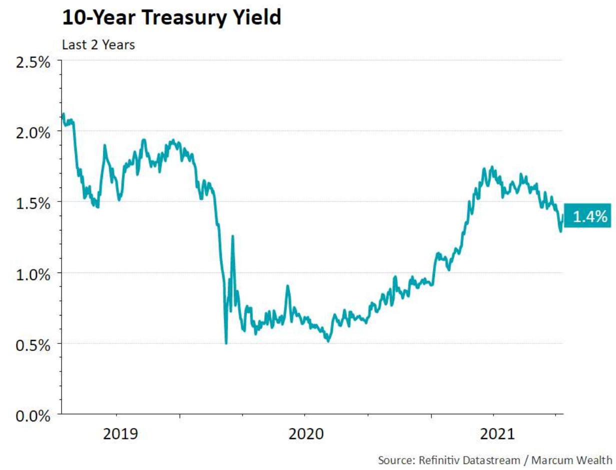
Equities remain at the strategic target weight within the Marcum Wealth Asset Allocation Frameworks.

Fixed Income

Bonds performed well during the second quarter. Falling interest rates and tighter credit spreads provided a nice backdrop for investors.

Fixed Income	2Q 2021
Barclays U.S. Aggregate Bond	1.9%
Barclays Corporate Inv. Grade	3.7%
Barclays High Yield Bond	3.1%
Barclays Global ex. U.S. Treas.	1.1%
Barclays Municipal Bond	1.5%
Barclays TIPS	4.6%

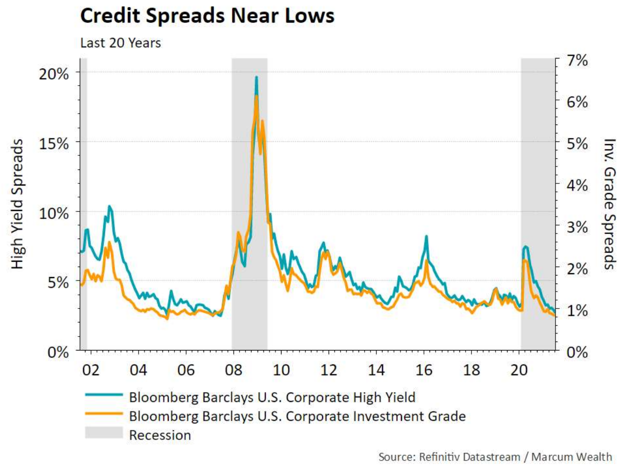
Interest rates had quite a ride over the last two years. With emergency interest rate cuts and panic across capital markets, interest rates dove during March 2020. As the recovery gained steam into the first part of 2021, interest rates hit nearly 1.8%. Today, the 10-year Treasury sits at 1.4%.



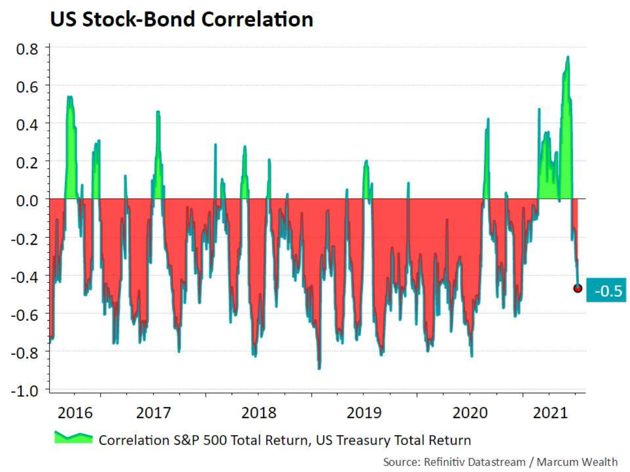
Even with the high inflation data of late, bonds shrugged it off.

This has left investors looking for yield across other areas of fixed income. From mortgages to corporate bonds, the search is on to provide any return on capital.

Because of all of the flows in the U.S. and from abroad, corporate credit spreads sit near 20-year lows. Investment grade spreads are less than 1%. High yield spreads were only lower in 2007 and have a pick up over Treasuries of just 2.7%. This compares to the 20-year average of 5.3%.



To start the year, Treasuries and equities flipped to a positive correlation. This means the diversification benefits of holding high quality bonds were much less attractive than in the last five years. The relationship flipped back towards the end of the quarter to being negative.



Looking for assets that zig while others zag is a hallmark of portfolio construction. Even adding assets with a zero correlation, or no relationship to one another, provides diversification benefits. Bonds play an important role in diversified portfolios over time.

The Asset Allocation Frameworks continue to maintain exposure within fixed income. We decreased exposure to credit and increased allocations to high quality bonds during the quarter.

Real Estate

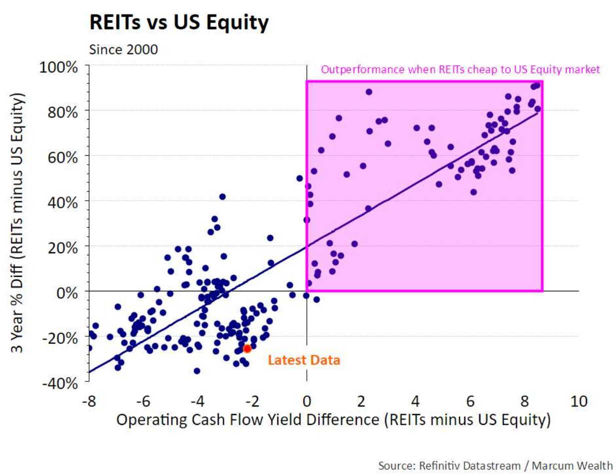
REITs were the top performing sector in the second quarter. This comes on the heels of strong outperformance of market averages.

Real Estate	2Q 2021
Wilshire U.S. REIT	12.8%
Wilshire Int'l REIT	7.9%

With more travel coming back, the hotel sector rallied during the quarter. In addition, falling interest rates provided a tailwind.

Investors are looking for yield. The lack of high quality assets providing yield continue to push up prices. Over the long-term, real estate provides an inflation hedge for investors concerned about this risk.

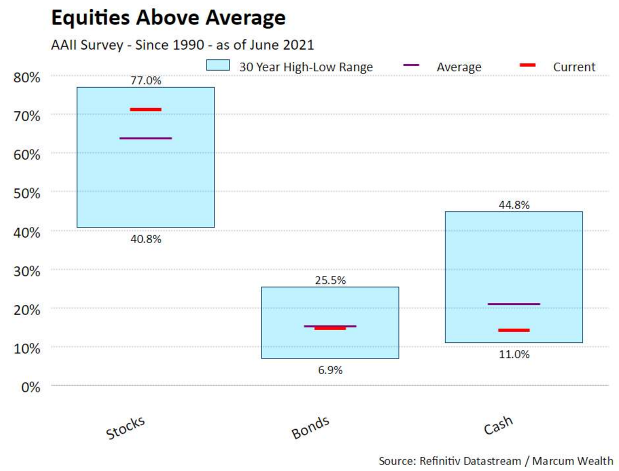
REITs came into the year with a discount to the broader market. After strong outperformance, the discount is now a premium. Further outperformance in the near term may be more challenging.



The Asset Allocation Frameworks continue to maintain equal weight exposure to REITs.

Summary

With cash yielding nothing, investors increased stock holdings in portfolios to above the long-term average. This is partly due to the strong bull market over the past year. It has been the fastest recovery in prices following a recession in the last 60 years. Thinking about the strategic asset allocation targets is important, as this is based on long-term financial plans. Even with the positive economic data of late, moving back towards the targets makes sense to manage risk.



Marcum Wealth Asset Allocation Frameworks

	Income	Conservative	Balanced	Moderate	Growth
Asset Class	Strategic	Strategic	Strategic	Strategic	Strategic
Equity	**20%**	**35%**	**50%**	**65%**	**80%**
U.S. Equity	12%	21%	30%	39%	48%
International Equity	6%	11%	15%	20%	24%
Emerging Markets Equity	2%	4%	5%	7%	8%
Fixed Income	**77%**	**62%**	**47%**	**32%**	**17%**
US Fixed Income	69%	56%	42%	29%	15%
Global Bonds	8%	6%	5%	3%	2%
Real Estate / REITs	**3%**	**3%**	**3%**	**3%**	**3%**

The risk designations are relative only to the five Strategic Allocation targets and do not represent comparisons with any other investment or risk of the overall strategies.

Important Disclosure Information