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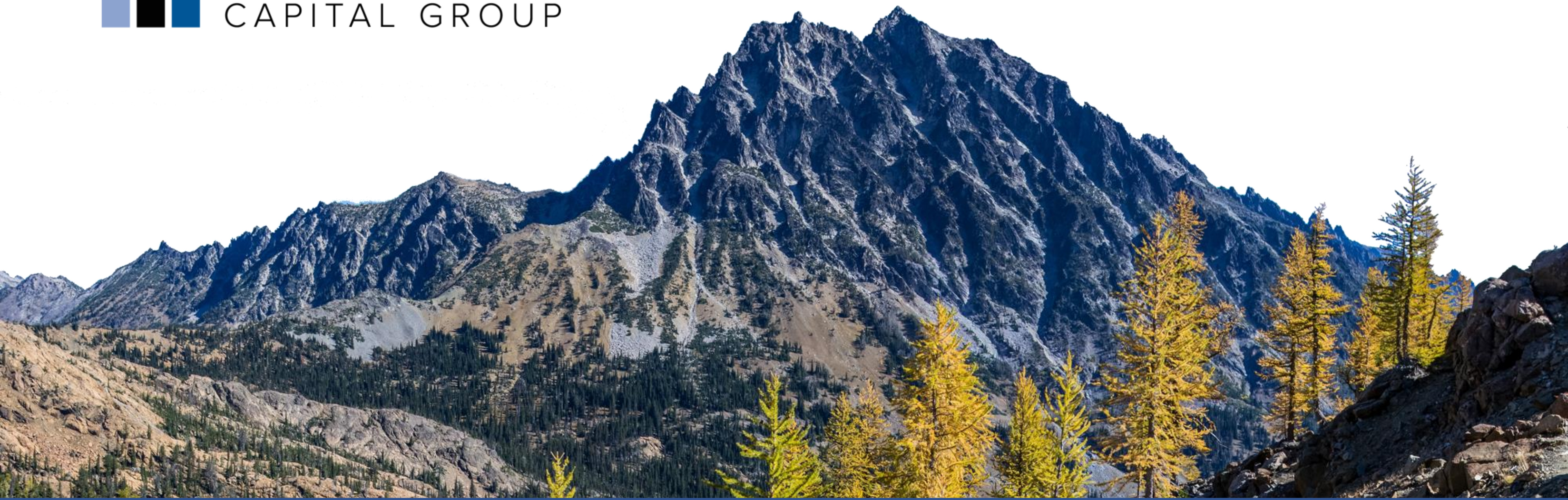

2021 Q4 Outlook
Navigating a Cloudy Horizon

KEY THEMES DRIVING THE FOURTH QUARTER

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Government Policy	➢ Proposals for $4.5T in new spending programs likely to be lowered ➢ Increases in various tax rates likely to be not as steep
Supply Chain	➢ Supply chain disruptions impacting multiple industries' effectiveness ➢ Supply chain disruptions might lead to price increases and inflation
Inflation	➢ Corporations likely to begin passing on costs to consumers ➢ Appears transitory, but how high will it go in the short term?
Bond Yields	➢ Rising bond yields can hurt valuations of growth stocks ➢ Yields unlikely to go too high too fast
China	➢ New regulations hurting stocks but creating buying opportunities ➢ Cracks in economic growth expanding to more sectors of economy

SUMMARY OF VIEWS

		● Current View	■ Previous Quarter
	Favorable	**Neutral**	**Unfavorable**
INVESTMENT GRADE BONDS		● ■	
MORTGAGE SECURITIES		■	●
NON-INVESTMENT GRADE		● ■	
U.S. LARGE CAP EQUITIES		● ■	
U.S. MID & SMALL CAP	●	■	
INTERNATIONAL		● ■	
EMERGING MARKETS		● ■	
INFRASTRUCTURE	● ■		
REAL ESTATE		● ■	
ALTERNATIVES	● ■		

FIXED INCOME ASSET CLASSES

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INVESTMENT GRADE

Neutral

Rationale: Economic growth has been steady, giving the Fed comfort in its view that the time to remove quantitative easing (QE) measures is near. Indeed, the Fed indicated that it might taper security purchases faster than the market originally expected. This would have QE ending around mid-2022 with the focus then shifting to potential rate hikes. We like adding to Municipal exposure as rates backup. Municipals are in good credit health today, and with legislation highly likely to increase personal tax rates, the tax-advantaged nature of Munis makes them especially attractive for investors in the highest tax brackets. While corporate balance sheets are in good shape, credit spreads are tight in Investment Grade credit. We think spreads could remain compressed within this space for a while and have a neutral outlook here.

Risk: Very rarely do things go as planned in the economy and especially in Washington. Gamesmanship over legislation and the debt ceiling could cause rate volatility to pick up. Economic growth could slow into the winter months, causing the Fed to change course or make a monetary mistake if inflation continues to run higher than expected. Credit spreads are priced for perfection, and any misstep could cause spreads to widen.

MORTGAGE SECURITIES

Unfavorable

Rationale: We believe the time to pare back exposure in agency Mortgage-Backed Securities (MBS) has come with the Federal Reserve indicating it is close to tapering purchases of Treasuries and MBS. The Fed owns $2.5 trillion of MBS, roughly 1/3 of the market, and while tapering has been well telegraphed, this excess supply will have to be absorbed elsewhere. It doesn't help that mortgage spreads, while off all-time lows, are still tight by historical standards. We do believe that there are other niche structured credit sectors to invest in that will not be as susceptible to Fed flows.

Risk: The main risk we see to this change in views is that as the economy slows, demand picks up for risk-free assets and the Fed slows or does not taper as expected. Other buyers of MBS could also come into the market and pick up the demand from the Fed, namely banks and foreign buyers and slow the backup in valuations.

NON-INVESTMENT GRADE

Neutral

Rationale: Non-Investment grade (Non-IG) credit spreads have been bouncing off their lows for the past few months but have been resilient in the face of increased equity market volatility. While we are neutral on the sector broadly, investors need to be tactical within their Non-IG allocations. We favor loans over fixed rate high yield bonds and prefer private credit for those that can allocate to lock-up structures. We see value within High Yield Munis for taxable portfolios for the same reason we like IG munis. Emerging Market debt is still interesting for its high yield.

Risk: Risks within Non-IG are very similar to their IG brethren, only magnified. Thus far, credit spread movements have been in sync with broader risk assets, just not as severe. This volatility could increase, and spreads could widen at a greater rate with equities. Concerns over Evergrande, and China more broadly, could spill over into broader emerging market and high yield debt markets.

EQUITY ASSET CLASSES

U.S. LARGE CAP

Neutral

Rationale: U.S. large cap equities continue to deliver strong returns and push valuations to higher highs. But in a market where bonds yield less than inflation and non-U.S. stocks have struggled to produce consistent gains, a proper weighting to U.S. stocks remains the prudent course despite the lofty valuations.

Risk: Many risks exist these days: the potential for $4.5 trillion in new spending coupled with major tax hikes, inflation, a potentially tightening Fed, the Delta variant, the debt ceiling, China, or the fact it has been so long since the last correction. The wall of worry for U.S. stocks is very real, tempering enthusiasm for outsized positions.

U.S. MID & SMALL CAP

Favorable

Rationale: Small cap equities have been stagnant since February, but we are increasingly optimistic that the dormant asset class will produce favorable returns over the next 12-18 months. Many of the overhangs in small and medium size businesses, including COVID-19, wage pressure, labor shortages, and supply chain bottlenecks, should start to work themselves out in 2022 as conditions normalize. We do caution that earnings and guidance will be sloppy, but we recommend investors buy into the weakness.

Risks: Especially for small and medium size business, COVID-19 remains a major headwind as it has limited the supply of workers, thereby creating wage pressure and suboptimal work conditions

INTERNATIONAL

Neutral

Rationale: While growth in Europe and Japan cannot match that of the U.S., we are seeing some signs that could point to stronger markets for equities. Currently, European markets are experiencing greater upside earnings revisions for equities vs stalling numbers in the U.S. and declining ones in EM stocks. Additionally, in Japan, more and more companies are beginning to return capital to shareholders via dividends and stock buybacks than previously seen.

Risk: Growth doesn't materialize and investors lose patience with overseas markets after having been told many times over the past decade that these markets were poised to outperform the U.S.

EMERGING MARKETS

Neutral

Rationale: Our rationale is regulatory and headline driven from China. These pressures will continue to weigh on EM investors in the short term, thereby increasing the opportunity cost of maintaining a higher than benchmark weight to EM. The rationale to maintain a market weight is that the asset class has been a relative laggard versus developed markets.

Risk: In addition, any notice or announcement from China that it is either narrowing or ending its regulatory scrutiny may provide investors enough confidence to increase exposure to the asset class. We believe there is low probability of that occurring, but the upside risks are building as China's tech champions continue to suffer from declining share prices.

NON-CORE ASSET CLASSES

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INFRASTRUCTURE

Favorable

Rationale: Exacerbated by recent underinvestment and thriving exports (especially LNG), energy bottlenecks emerged during the third quarter, both in the U.S. and abroad, highlighting the need for additional infrastructure capital. Against this backdrop, we believe the value of existing energy assets will likely continue to rise in the near term. Global travel should also continue to recover through 2022, increasing the demand (revenue) for airports and highways/toll roads – many of which are publicly listed assets in Europe.

Risks: An acceleration in COVID-19 cases from current levels is a material risk to global demand and accordingly the utilization of infrastructure assets. Beyond the pandemic, higher energy prices have always been a precursor to heightened capex, often leading to an oversupplied situation and declining utilization rates.

REAL ESTATE

Neutral

Rationale: Real estate has rebounded well off the 2020 bottom but after a hot start to the year has seen stock price appreciation cool. While concerns persist around softening economic growth, the income generation offered in the sector remains compelling even as bond yields tick higher. Private market funds are the preferred way to gain exposure to the asset class because of the diversification and yield benefits versus publicly traded equities.

Risk: COVID-19 and valuations are big risks to a continued rebound in real estate values. While the Delta variant may have peaked, and vaccination rates are ticking up, many office workers won't return to the office in 2021, and any new variant could further cool business travel and in-person shopping, which are already at depressed levels.

ALTERNATIVES

Favorable

Rationale: Dispersion in valuation and pricing anomalies across capital structures should provide an increased opportunity set for both long/short and relative value managers. In addition, rising interest rates and the volatility that ensues should create further arbitrage opportunities for investors. One recent example is within the convertible bond market. Low government interest rates, a Fed-supported corporate credit market, and high optionality within equity markets have proved to be a healthy backdrop for convertible bonds. Managers are now able to find valuation discrepancies between the convertible bond and equity of the same company, primarily due to a difference in expected volatility going forward. Investors that can pivot across the capital structure and profit from both long and short trades may stand to gain from any future rise in volatility. The outlook for Global Macro managers also remains constructive, as fiscal and monetary policy makers pivot to a post-COVID-19 environment. The market's pricing of inflation expectations is a risk going into 2022. Being able to hedge against this risk may prove valuable to investors.

Risk: Further monetary easing from central banks continues to distort pricing of securities across global markets, hindering price discovery, encouraging excessive risk taking, and further widening pricing anomalies across capital structures. Regulatory uncertainty may also dampen the opportunity set in the near term.

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