Is the Stimulus Endgame a Phoenix or an Icarus?

Q2 2021 Investment Outlook

Segal Marco Advisors

Overview

In the ancient Greek myth, the Phoenix was a large and brilliantly colored bird whose haunting song enraptured the god Apollo, causing a spark that engulfed the bird and its nest in flames. After three days, however, a new Phoenix would rise from the ashes and live in paradise for 1,000 years. Also in Greek mythology, Daedalus was trapped in the tower of King Minos of Crete with his son Icarus. The craftsman made two sets of wings out of feathers glued together with wax and warned his son not to fly too high or too low. Icarus did not heed this advice and flew high enough that the wax melted and he plunged to the sea and drowned. The question we raise for the global, and particularly the U.S. economy, is: with the spark, the pandemic, moving behind us, will the world rise from the ashes for a long period of prosperity or will the massive amounts of fiscal and monetary stimulus cause us to fly too high, resulting in the eventual meltdown and rapid decline?

The U.S. experience

Let's take the U.S. case on this question: according to Statista, the U.S. provided COVID-19-related stimulus equal to 26.5 percent of GDP as of March 31, 2021. This amounts to approximately $5.7 trillion, given that U.S. GDP in Q4 2019 was $21.7 trillion. If we take that same starting point and calculate GDP since then based upon the pre-pandemic trend (about 1 percent per quarter nominal growth), the value of GDP lost due to the pandemic over the next four quarters (through Q4 2020) relative to what would be suggested by the pre-pandemic trend totaled approximately $5.4T.

Conclusion? The fiscal stimulus almost exactly made up for the reduction in GDP off trend — and when the numbers come in for the first quarter of 2021, we would expect the stimulus will be slightly less than the GDP deficit.

Does an amount of stimulus roughly equal to the magnitude of the reduction in GDP that arose out of the pandemic somehow create a new dynamic that would cause the economy to explode? Doubtful. The number to focus on isn't that the GDP was up 8 percent from the second quarter of 2020 to the third, for example, but rather that it was 6 percent below where it would have been.

This Q2 2021 *Investment Outlook* was written in early May 2021.

Another key question is: how were stimulus payments actually used? In a snapshot survey (mind you this is experimental data), the U.S. Census Bureau determined that of the people who responded that someone in their household received a check during the seven days prior to the survey, 50 percent said they paid off debt; 32 percent said they saved it; and only 18 percent reported actually spending the money. It is also noteworthy that people who spent the money said the largest categories of reported use were for food, household supplies, and utilities and telecommunications (including cable). Not exactly an indication of a spending spree to spark GDP growth.

Rather, to determine whether the U.S. economy is in breakout mode, look at statistics related to critical variables that would indicate things have fundamentally changed. Let's consider a few briefly:

- Productivity — It improved pre-pandemic, then fell back. Where does it head now? Perhaps some elements of managing during the pandemic will change things positively in the future.
- Labor force participation — Pre-pandemic, it was trending down and then dropped off substantially in 2020. Do millennials with growing families return to the workforce and do boomers decide to keep working past expected retirement age?
- Wages — There had been some good news on pre-pandemic gains and then we had very distorted numbers, with much of the gain being the result of a reduction in lower-paying jobs. Does the push to greater income inequality via subsequent fiscal packages change this dynamic?

There are numerous uncertainties, but it does appear that the current mood (and control) in Washington is tilted towards seeking to make substantive changes that may improve all three of these variables.

Stimulus varied in other developed economies

If we look outside the U.S., we see substantial differences in the amount of COVID-19-directed stimulus. According to IMF data, Germany added 38.8 percent of GDP, Japan added 44.2 percent, while the UK was down at 32.3 percent and the entire EU was at 10.6 percent. When combined with the facts that growth rates for the developed non-U.S. world were at trends substantially below the U.S. pre-pandemic and the greater, at least to this point, struggles with lockdowns, surges and vaccines, it is anticipated that the road to trend growth for those economies is likely to be a bit longer than for the U.S. Even upon full recovery, the baseline will be lower due to many of the embedded factors that have created their slow growth in the first place.

Wide range of experience among emerging economies

For emerging economies, as we often remind clients, it is inappropriate to paint them all with the same brush given their unique characteristics. Brazil, for example, has been a disaster in pandemic control. China, a model of state managed control both of the virus and related information, is having challenges with vaccine manufacturing, and India, which seemed to be faring reasonably well, is now struggling with infection surges and vaccine distribution.

Likewise, the economic trends pre-COVID-19 were quite disparate, as were the debt levels and near-term prospects. Many of the emerging economies, dominated by China, were well below developed market levels in terms of stimulus, but the needs varied greatly. In general, however, with China such a substantial part of the emerging world in both GDP and equity markets, we foresee a spotty return to long-term trends, but these may well settle at lower levels in the near term. Recovery of the developed world likely means greater need for commodities that a number of these countries provide, which will support domestic spending and a renewal of the increasing focus on internal economic development.

Considering market sentiment

A last consideration that we would like to highlight briefly is sentiment. While over the long term sentiment seems to ebb and flow and often is not a substantial consideration in actual economic growth, unless sentiment immediately translates to dollars spent, it is often reflected in capital market returns and interest rates. Currently, for example, the steepness of the yield curve — with the U.S. Federal Reserve (Fed) being an anchor telling us there will be no rate increases any time soon — reflects the sentiment among bond market participants that the economy is better than even the Fed believes, and yields will ultimately rise to reflect that.

If we look at the Producer Manufacturing Index (PMI) around the world shown in the chart, we can also see a lot of green indicating that this important segment of the global economy is looking past the red and orange days of the depths of the crisis, and envisioning greater activity going forward. Likewise, in the U.S., sentiment from both consumers and businesses have more than fully recovered from the dark days of last spring.

Global Producer Manufacturing Index

enlarge chart

	May-19	Jun-19	Jul-19	Aug-19	Sep-19	Oct-19	Nov-19	Dec-19	Jan-20	Feb-20	Mar-20	Apr-20	May-20	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21
U.S.	50.5	50.6	50.4	50.3	51.1	51.3	52.6	52.4	51.9	50.7	48.5	36.1	39.8	49.8	50.9	53.1	53.2	53.4	56.7	57.1	59.2	58.6	59.1
Canada	49.1	49.2	50.2	49.1	51.0	51.2	51.4	50.4	50.6	51.8	46.1	33.0	40.6	47.8	52.9	55.1	56.0	55.5	55.8	57.9	54.4	54.8	58.5
UK	49.4	48.0	48.0	47.4	48.3	49.6	48.9	47.5	50.0	51.7	47.8	32.6	40.7	50.1	53.3	55.2	54.1	53.7	55.6	57.5	54.1	55.1	58.9
Eurozone	47.7	47.6	46.5	47.0	45.7	45.9	46.9	46.3	47.9	49.2	44.5	33.4	39.4	47.4	51.8	51.7	53.7	54.8	53.8	55.2	54.8	57.9	62.5
Germany	44.3	45.0	43.2	43.5	41.7	42.1	44.1	43.7	45.3	48.0	45.4	34.5	36.6	45.2	51.0	52.2	56.4	58.2	57.8	58.3	57.1	60.7	66.6
France	50.6	51.9	49.7	51.1	50.1	50.7	51.7	50.4	51.1	49.8	43.2	31.5	40.6	52.3	52.4	49.8	51.2	51.3	49.6	51.1	51.6	56.1	59.3
Italy	49.7	48.4	48.5	48.7	47.8	47.7	47.6	46.2	48.9	48.7	40.3	31.1	45.4	47.5	51.9	53.1	53.2	53.8	51.5	52.8	55.1	56.9	59.8
Spain	50.1	47.9	48.2	48.8	47.7	46.8	47.5	47.4	48.5	50.4	45.7	30.8	38.3	49.0	53.5	49.9	50.8	52.5	49.8	51.0	49.3	52.9	56.9
Greece	54.2	52.4	54.6	54.9	53.6	53.5	54.1	53.9	54.4	56.2	42.5	29.5	41.1	49.4	48.6	49.4	50.0	48.7	42.3	46.9	50.0	49.4	51.8
Ireland	50.4	49.8	48.7	48.6	48.7	50.7	49.7	49.5	51.4	51.2	45.1	36.0	39.2	51.0	57.3	52.3	50.0	50.3	52.2	57.2	51.8	52.0	57.1
Australia	52.7	49.4	51.3	53.1	54.7	51.6	48.1	48.3	45.4	44.3	41.6	35.8	41.6	51.5	53.5	49.3	46.7	56.3	52.1	55.3	55.3	58.8	59.9
Japan	49.8	49.3	49.4	49.3	48.9	48.4	48.9	48.4	48.8	47.8	44.8	41.9	38.4	40.1	45.2	47.2	47.7	48.7	49.0	50.0	49.8	51.4	52.7
China	50.2	49.4	49.9	50.4	51.4	51.7	51.8	51.5	51.1	40.3	50.1	49.4	50.7	51.2	52.8	53.1	53.0	53.6	54.9	53.0	51.5	50.9	50.6
Indonesia	51.6	50.6	49.6	49.0	49.1	47.7	48.2	49.5	49.3	51.9	45.3	27.5	28.6	39.1	46.9	50.8	47.2	47.8	50.6	51.3	52.2	50.9	53.2
Korea	48.4	47.5	47.3	49.0	48.0	48.4	49.4	50.1	49.8	48.7	44.2	41.6	41.3	43.4	46.9	48.5	49.8	51.2	52.9	52.9	53.2	55.3	55.3
Taiwan	48.4	45.5	48.1	47.9	50.0	49.8	49.8	50.8	51.8	49.9	50.4	42.2	41.9	46.2	50.6	52.2	55.2	55.1	56.9	59.4	60.2	60.4	60.8
India	52.7	52.1	52.5	51.4	51.4	50.6	51.2	52.7	55.3	54.5	51.8	27.4	30.8	47.2	46.0	52.0	56.8	58.9	56.3	56.4	57.7	57.5	55.4
Brazil	50.2	51.0	49.9	52.5	53.4	52.2	52.9	50.2	51.0	52.3	48.4	36.0	38.3	51.6	58.2	64.7	64.9	66.7	64.0	61.5	56.5	58.4	52.8
Mexico	50.0	49.2	49.8	49.0	49.1	50.4	48.0	47.1	49.0	50.3	47.9	35.0	38.3	38.6	40.4	41.3	42.1	43.6	43.7	42.4	43.0	44.2	45.6
Russia	49.8	48.6	49.3	49.1	46.3	47.2	45.6	47.5	47.9	48.2	47.5	31.3	36.2	49.4	48.4	51.1	48.9	46.9	46.3	49.7	50.9	51.5	51.1
Emerging Markets	50.5	49.9	50.1	50.4	51.0	51.0	51.1	51.0	51.0	44.6	49.1	42.7	45.4	49.6	51.4	52.5	52.8	53.4	53.9	52.8	52.1	51.6	51.3

Source: FactSet as of 3/31/2021, most recent data available

Looking ahead

Turning to our expectations for market returns over the next 12–18 months, we repeat our previously stated notion that the stimulus has basically eliminated the downturn that was largely created by the pandemic — literally wiped it off the graph and returned us, with specific sectors faring differently of course, to where we were in January 2020. At that time, we were in the 128th month of the longest economic expansion in history with a stock market that simply went up and interest rates that only went down. So, now here we are fundamentally in our 144th month of that post-Global Financial Crisis cycle. During that extra 16 months, the U.S. equity market, as measured by the S&P 500©, has risen 32 percent (from January 1, 2020 to April 30, 2021) — well above long-term trends.

It would be easy to look at the somewhat elevated valuations that are the result of this appreciation and conclude that there is a reckoning in our near-term future. In our view, the combination of very favorable sentiment and a U.S. government that appears poised to solve some of the problems that have held back gains in productivity and wages will enable stocks to continue to provide attractive returns to investors. Generally low interest rates and a sense that there are few alternatives to stock ownership further support this thesis. An accommodative Fed, at least for now, combined with the expectation of even more fiscal support, causes us to be somewhat bullish on U.S. stocks.

Outside the U.S., we believe that developed-market returns will face greater headwinds, at least versus the U.S., in the near future as the unevenness of the response to the pandemic as well as the lack of a coordinated response to some of the more fundamental reform needs will offset what seem to be more attractive valuations. Overall, compared to developed economies outside the U.S., emerging markets may be a bit of a favorable exception as the U.S. recovers, but may continue to reflect the “haves versus the have nots” depending upon region and individual country. (Some industry forecasts suggest higher 2021 earnings growth for EM, Japan and Europe based on the idea that a greater proportion of cyclical sectors in these countries will be positively impacted by a gradual global rebound consistent with pandemic-control progress).

For fixed income, with a forecast of a mostly benign economic backdrop, short rates are likely to be rangebound at a low level under central bank control. Corporate bonds, even with what appear to be narrow spreads, will provide their modest return advantage to investors. Generally, this should reflect itself through modest absolute returns, which may actually be negative after inflation, for the broad indexes and some realized premium for higher-yielding alternatives.

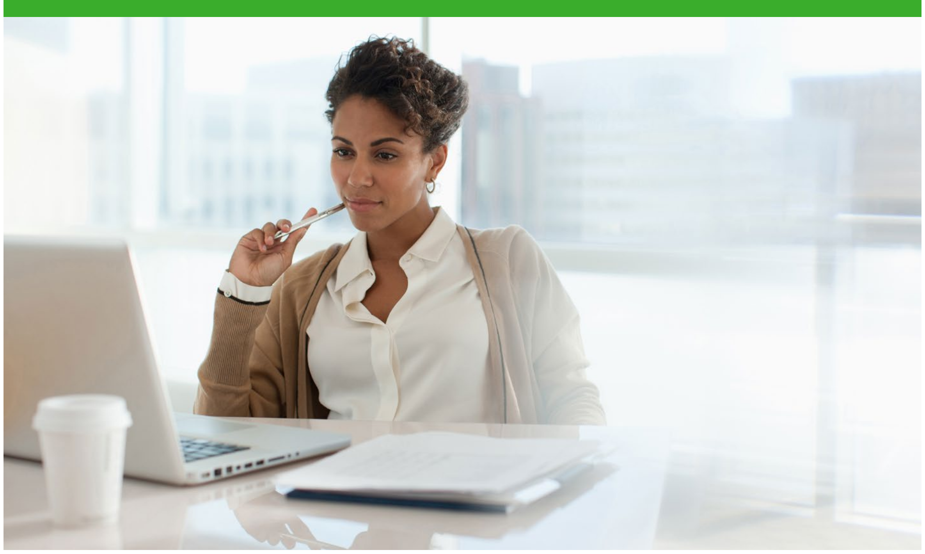
Broadly speaking, private market alternatives signals remain unchanged from last quarter and are anticipated to approximate our longer-term market assumptions, as these asset classes continue to maintain a solid recovery pace from the heights of the pandemic. The next 12–18 months should be a favorable time to deploy private equity dry powder as transaction volume remains strong. Robust valuations and increased distributions from anticipated deal flow will buoy returns. Real estate and infrastructure prospects are, as always, strategy- and regional-specific, but mostly will benefit from a renewal of economic growth and demand along with advantageous pricing and an improved outlook from certain COVID-19-impacted sectors, such as lodging, student housing, transportation and leisure. Across hard assets, value add and flexible strategies that can take advantage of evolving market conditions are favored.

Gratitude, some concerns and an opportunity

As we look back on the crisis period and contemplate our future, we have much to be thankful for. We can be grateful for the tireless efforts of our front-line healthcare workers, the rapid response from government to support the millions of those who lost their jobs and the thousands of shuttered businesses, and the ingenuity of our pharmaceutical industry to create vaccines that were game changers.

We also have much to be concerned about as the value of science has been continuously contested, medical advice somehow became politicized and many questioned the undeniable reality of the loss of nearly 600,000 fellow Americans and several times that around the world. In the midst of the pandemic posing a severe test for our vision and values as a nation we encountered an almost surreal increase in public awareness of the number of people of color who lost their lives to violence from mass shootings and police action with cell phone and body camera images putting all of us in the middle of these tragedies.

The “Phoenix” in the U.S. may be the now widespread recognition that the vision of America as the beacon of freedom and equality demands a response from its government, its citizens and its corporations. If we can use this opportunity and this commitment to those principles to lift the standards for all Americans, then we can break out of the ho-hum economic trend of the last decade. It is said that a rising tide lifts all boats, but if many can barely float, that will not happen.



Overview
Global Macro Signals and Outlook
Asset Class Signals and Outlook
Questions? Contact Us.

Outlook for Canada

The Canadian economy grew at an annual rate of 6.5 percent through the first quarter of the year, nearly reaching pre-pandemic output levels. The preliminary estimate beats the slowdown estimated months ago. However, it falls short of the 9.6 percent annualized growth rate from Q4 2020.

In March alone, prices rose in five of the eight major components year over year, with transportation (+7.1 percent) and shelter (+2.4 percent) prices contributing the most to CPI growth. Compared with March 2020, consumers paid less for clothing and footwear (-5.4 percent) and for household operations, furnishings and equipment (-0.2 percent). Service industries that suffered at the beginning of the COVID-19 pandemic showed a small gain in February, while goods-producing industries dropped marginally for the first time since April 2020.

During the first quarter, easing of public health restrictions for pandemic-related health issues were reversed to combat a third wave of cases. Despite continued COVID-19 challenges, employment gains improved notably from the end of 2020, reflecting a decrease in unemployment from 8.8 percent to 7.5 percent as of the end of March.

WTI Oil continued to appreciate in the quarter. At the end of the quarter it was up approximately 25 percent to $60.50 USD per barrel.

The Canadian dollar (vs. USD) appreciated through the end of March from 79 to 80 cents, a level not seen since 2018.

Canada's S&P/TSX Composite total return climbed to record highs, returning 7.3 percent for the quarter. Strong returns were fueled by continued rollout of COVID-19 vaccines, global fiscal stimulus and relatively strong earnings. Healthcare and energy, last year's worst-performing sectors, were leaders. Returns were supported by the strong performance of large financials. Materials, utilities, information technology and consumer staples underperformed as consumer confidence, yields and threats of inflation rose.

Bond prices fell as yields pushed higher around the globe, reflecting rising expectations of inflationary pressures because of economic recovery. The Canadian bond market (FTSE Universe Bond Index) dropped 5 percent for the quarter, as yields rose from 1.21 percent to 1.72 percent. Early in Q1, the Bank of Canada (BoC) indicated its desire to reduce bond purchases and began doing so in February. This move points to the hope that the Canadian economy will recover more quickly than other global economies. Stronger economic growth may be accompanied by the prospect of raising interest rates. However, the BoC also stated its desire to attain 2 percent inflation. Accordingly, with that target yet to be achieved, the BoC kept its overnight rate unchanged in Q1 at 0.25 percent.

Summary of Outlook Views

The tables on the following pages provide a snapshot of our forward-looking observations on the key macroeconomic factors driving markets and the direction of specific asset classes.

Overview
Global Macro Signals and Outlook
Asset Class Signals and Outlook
Questions? Contact Us.

Global Macro Signals and Outlook

Our global macro signals are represented by arrows that reflect select economic indicators' directional movement. Gray-shaded boxes indicate a change in our view of a particular economic indicator from the previous quarter. Arrows reflect impact on growth except for policy rates where they reflect directional movement.

Key:

↓	↘	→	↗	↑
Negative	Neutral, Trending Lower	Neutral	Neutral, Trending Higher	Positive

Developed Markets

<table>
<tr><th>Market</th><th>GDP Growth</th><th>Inflation</th><th>Policy Rate</th><th>Currency</th><th>Equity Valuations</th></tr>
<tr><td>U.S.</td><td>↗</td><td>↗</td><td>→</td><td>↗</td><td>↓</td></tr>
<tr><td colspan="6">GDP growth rose 6.4 percent in Q1. Unemployment fell in the quarter, as reopenings accelerated with a nationwide vaccination effort. The Fed kept short-term interest rates at zero and indicated that it was likely to hold rates low for the relatively near future. Inflation increased with evidence of a strengthening U.S. economy and a stronger U.S. dollar. Valuations are above the historic median.</td></tr>
<tr><td>Canada</td><td>↗</td><td>↗</td><td>→</td><td>→</td><td>→</td></tr>
<tr><td colspan="6">GDP growth in Canada increased 2.3 percent in Q1. The Bank of Canada left the policy rate unchanged. Inflation rose, but the Canadian dollar stayed relatively flat against the USD. Valuations of Canadian stocks are still more moderate than those of U.S. stocks.</td></tr>
<tr><td>Eurozone</td><td>↘</td><td>↑</td><td>→</td><td>↘</td><td>↘</td></tr>
<tr><td colspan="6">GDP shrank 0.6 percent in the quarter. COVID-19-related lockdowns and an uneven vaccination effort hampered the eurozone's economy. The euro weakened against the USD, and inflation increased. Equity valuations are above their long-term median and are cheaper than U.S. stocks.</td></tr>
<tr><td>UK</td><td>↗</td><td>→</td><td>→</td><td>→</td><td>→</td></tr>
<tr><td colspan="6">GDP growth rose 1.3 percent quarter over quarter in Q1. The pound was relatively flat against the USD, inflation also did not move much in the quarter, and the Bank of England kept rates steady. Equity valuations are near their long-term median and cheaper than U.S. stocks.</td></tr>
<tr><td>Japan</td><td>↗</td><td>↘</td><td>→</td><td>→</td><td>→</td></tr>
<tr><td colspan="6">Growth rose 2.8 percent in Q1. The yen was flat against the USD, and the Bank of Japan held the policy rate steady. Inflation fell in the quarter. Equity valuations are close to their long-term median.</td></tr>
</table>

Key:

↓	↘	→	↗	↑
Negative	Neutral, Trending Lower	Neutral	Neutral, Trending Higher	Positive

Emerging Markets

Market	GDP Growth	Inflation	Policy Rate	Currency	Equity Valuations
China	↗	↘	→	→	↘
GDP grew 0.6 percent quarter over quarter in Q1. The Bank of China held rates stable in the quarter. The yuan was flat against the dollar, and inflation declined a bit. Equity valuations were higher than the long-term median.					
Rest of EM	↗	↗	→	→	↘
Economic growth among EM countries varied as the pandemic continued, with India and Brazil still very much struggling with the virus. A stronger USD was a negative in the quarter. Central banks across the EM spectrum largely remain dovish, though a few have lifted rates in response to inflation fears. EM stocks rose in Q1 and valuations sit above their historic median.					

Asset Class Signals and Outlook

There is a set of five signals for each asset class, represented by shaded circles ranging from an above-normal return outlook (dark green) to a below-normal return outlook (dark red), with the middle circle indicating a neutral outlook (gray). The views represented our 12–18 month perspective for each of the asset classes are relative to our longer-term expectations (10+-year capital market assumptions).

If our views on an asset class change from quarter to quarter, that change is represented by an arrow that stretches from the previous quarter's signal to that of the current quarter.

Return Outlook

Key:					
	● (dark red)	● (light red)	● (gray)	● (light green)	● (dark green)
	Below Normal		Neutral		Above Normal

Equities

Opportunity Set	Below Normal		Neutral		Above Normal
U.S. large cap	○	○	●	○	○
Significant government stimulus and low short-term interest rates should be a recipe for improving growth in 2021. Continuing COVID-19 vaccinations should help the overall economy reopen more and more as the year goes on. Valuations remain well above median, though they could keep going higher as positive economic and earnings news rolls in. News-based volatility may decline somewhat, though won't disappear completely.					
U.S. small cap	○	○	●	○	○
A still improving post-pandemic economy, along with low rates and strong stimulus, will be good for small caps. Corporate tax increases could be a headwind here, but small caps will still benefit from overall economic and earnings trends.					
Int'l dev. large cap (unhedged)	○	○	●	○	○
COVID-19 vaccination rates in Europe have lagged those of the U.S., which may hold back growth in the near term. However, Europe's export-driven economies are set to benefit in a global recovery. Valuations are more appealing than for U.S. stocks.					
Int'l dev. small cap (unhedged)	○	○	●	○	○
Similar story to that of large cap. Ongoing COVID-19 vaccination delays cause growth problems in the near term for developed markets.					
Emerging markets (unhedged)	○	○	●	○	○
Must continue to distinguish between China and the rest of emerging markets — while China's economy has largely recovered from a pandemic-related downturn, other EM countries (particularly India) face huge struggles. As developed markets' economies recover, however, EMs stand to benefit through exports.					

Overview
Global Macro Signals and Outlook
Asset Class Signals and Outlook
Questions? Contact Us.

Return Outlook

Key: Below Normal — Neutral — Above Normal

Fixed Income

Opportunity Set	Below Normal		Neutral		Above Normal
U.S. core	●	○	○	○	○
The Fed's stated desire to keep interest rates low for the foreseeable future means U.S. core bonds are more likely to perform below our long-term expectations. Long-term rates are likely to remain rangebound.					
Non-U.S. core (hedged)	●	○	○	○	○
Safety of international sovereign debt is somewhat appealing, though yields remain low to negative in many countries. Returns from the asset class for U.S. investors will be highly influenced by any changes in performance of the U.S. dollar.					
Emerging market debt (hedged)	○	○	●	○	○
Similar to EM equity, expectations for EM debt are somewhat muted due to continuing pandemic-related woes in many countries. Yields in EM debt are relatively attractive to developed market debt.					
High yield	○	○	●	○	○
Spreads are quite tight at the moment, though if defaults remain low there is justification for it. High yield still offers solid opportunities for bonds of financially sound companies. We favor the higher-quality end with a focus on selectivity and active management.					
Bank loans	○	○	●	○	○
Bank loan yields are fairly attractive relative to other fixed income sectors. We favor the higher-quality end with emphasis on active management.					
TIPS	○	○	●	○	○
Inflation has arrived in an anecdotal way in some sectors, but the official government inflation data overall has yet to show a concerted uptick.					

Continued on the next page

Return Outlook

Key: Below Normal | Neutral | Above Normal

Fixed Income

Opportunity Set	Below Normal		Neutral		Above Normal
Structured credit	○	○	●	○	○
Arbitrage spreads in collateralized loan obligation formation look particularly attractive as increasing risk appetite and demand for collateralized loan obligations has driven financing costs down while asset spreads remain high. This dynamic is particularly attractive for equity and subordinated tranche investing, and we would expect to continue to see robust issuance in the market, which should keep the CLO and bank loan engine humming.					
Private credit	○	○	●	○	○
Elevated levels of dry powder, the return of competition, and elevated valuations and pricing limit the upside and overall attractiveness of credit markets. However, nimble and flexible managers and strategies serving as “solutions providers” offer access to uniquely structured deals, emphasizing downside protection with greater upside. The “beta” in private credit markets looks more like late 2019 than summer 2020, emphasizing the importance of manager selection.					
Long bonds	○	○ →	●	○	○
As the Fed is set to hold short rates down for the near future, attention for investors will focus on the long end of the yield curve, where we saw a meaningful rise in long yields in Q1. With U.S. yields still more appealing than other developed, the hedge to unexpected stress that longer bonds can offer is still relevant as well. The caveat is an unforeseen rise in inflation could negatively impact nominal bonds.					
Municipals	○	○ →	●	○	○
Government stimulus will be a tailwind as evidenced by the recent actions taken by the rating agencies — Moody’s and S&P — revising their outlooks on state and local governments from negative to stable on expectations of stronger tax collections. Additionally, there is a favorable supply/demand dynamic.					

Return Outlook

Key: ● Below Normal ● ● Neutral ● ● Above Normal

Alternatives

<table>
<tr><th>Opportunity Set</th><th>Below Normal</th><th></th><th>Neutral</th><th></th><th>Above Normal</th></tr>
<tr><td>Hedge funds</td><td>○</td><td>○</td><td>●</td><td>○</td><td>○</td></tr>
<tr><td colspan="6">The first quarter of 2021 opened with an unprecedented rally in heavily shorted “meme” stocks, leading to outsized negative performance results for select long-short equity mandates. It remains to be seen what level of influence social media and other online messaging forums will have on equity market performance going forward; thus, for the time being, we are taking a more cautious stance towards long-short equity strategies with fundamental biases. Importantly, however, the vast majority of hedge fund strategies proved largely insulated from these unusual market dynamics and behaviors. Price dispersion and volatility have remained relatively elevated, which are generally supportive of hedge funds. Select event-driven/special situations strategies that are focused on specific catalysts, along with relative value strategies that look to isolate alpha through more net neutral positioning are well-positioned to capitalize on the prevailing market environment. Unique investment opportunities within credit remain rather robust as well.</td></tr>
<tr><td>Multi-asset class strategies (MACS)</td><td>○</td><td>○</td><td>●</td><td>○</td><td>○</td></tr>
<tr><td colspan="6">Global equity markets surged during the first quarter, as forecasts showed robust economic expansion in 2021 on the back of positive momentum in vaccine distribution across many developed economies, combined with highly accommodative, “do-whatever-is-necessary” stimulus in the U.S. Simultaneously, interest rates have been pushed higher and, due to rising inflation expectations, oil prices saw strong gains during the quarter as well. Overall, market participants have generally embraced positive economic news while dismissing negative news; thus, strategies that are more reliant upon “beta” as a means to generating returns (e.g., risk parity) are likely to generate positive performance results in the nearer term. Those strategies that place a greater emphasis on “alpha” through effective shorting, tactical asset allocation decision-making, security selection and/or market expression, remain well-positioned to achieve their respective return targets as well, but may face greater headwinds if the prevailing market euphoria persists.</td></tr>
<tr><td>Private equity</td><td>○</td><td>○</td><td>●</td><td>○</td><td>○</td></tr>
<tr><td colspan="6">The near term represents an attractive time to put capital to work, given momentum driving secular growth in technology, healthcare, business and consumer services, as well as other segments, along with favorable financing conditions in the public and private lending markets. Despite elevated prices and valuations driven by record levels of dry powder and deal competition, transaction volume is anticipated to remain on pace as willing buyers and sellers find ways to navigate bid-ask spreads. Higher purchase prices present a risk factor, but can be mitigated by strong business growth and value creation across strategies. There will be also be a diverse opportunity set to continue to capture alpha through unique special situations involving distressed credit, operational turnaround and restructurings.</td></tr>
</table>

Continued on the next page

Return Outlook

Key: ● Below Normal ● ● Neutral ● ● Above Normal

Alternatives

<table>
<tr><th>Opportunity Set</th><th>Below Normal</th><th></th><th>Neutral</th><th></th><th>Above Normal</th></tr>
<tr><td>Real estate</td><td>○</td><td>○</td><td>●</td><td>○</td><td>○</td></tr>
<tr><td colspan="6">There are continued signs of improvement from the dislocation experienced in 2020. Office valuations have held firm, with longer leases supporting valuations while transactions remain limited. While the supply and demand dynamic of the office sector prospectively remains uncertain, fundamentals within growth-oriented, non-gateway markets appear to be well positioned for a quicker recovery. The multi-family segment will continue to show resilience, notably in growth-oriented markets in the Southeast. High-rise apartments in urban areas are expected to struggle due to migration trends. The outlook for industrial remains favorable, although high levels of industrial construction activity over the past year may put pressure on leases in certain markets. The retail and hotel sectors have started to see improvements in net operating income, which should continue with increased vaccinations, however e-commerce and reduced business travel will remain as headwinds. Dry powder remains elevated and any uptick in interest rates will be additional headwind.</td></tr>
<tr><td>Infrastructure</td><td>○</td><td>○</td><td>○</td><td>●</td><td>○</td></tr>
<tr><td colspan="6">Overall outlook is relatively favorable. Although valuations remain depressed for passenger transportation-related assets, recovery is anticipated in line with increased COVID-19 vaccination rates. Freight transportation has rebounded strongly and that trend is expected to continue. The U.S. federal government’s $2 trillion infrastructure plan will be a tailwind for investment that will include opportunities for private sector participation. The renewables sector will receive additional boost from the administration’s heightened focus on climate change, as the pace of the shift from oil, natural gas and coal to alternative energy sources is projected to accelerate. Demand for digital infrastructure will continue to surge after the COVID-19 pandemic ends, and strong investor interest will maintain upward pressure on valuations. Overall, the asset class remains attractive, fueled by the increasing opportunity set and strong and resilient income.</td></tr>
<tr><td>Commodities</td><td>○</td><td>○</td><td>●</td><td>○</td><td>○</td></tr>
<tr><td colspan="6">The outlook for the near term is neutral, as supply starts to catch up to increased demand, but is likely to be balanced by secular tailwinds of decarbonization, a weak U.S. dollar and low to negative interest rates globally that support higher commodity prices. Energy prices in the near term are expected to rise reflecting rising growing demand, which has resulted in OPEC production increases. Long-term headwinds for crude include global economies’ focus on clean energy and renewable technologies. Agricultural prices have been surging above pre-pandemic levels, and are forecasted to maintain pace. Near-term grain price increases have been driven by supply disruption from lower-than-projected plantings partially driven by poor weather in the Midwest. Stock levels for corn, wheat and soybeans are all down from last year’s levels, further supporting pricing in the near term. Metals will continue to benefit from the longer-term transition towards clean energy, particularly for high-conductivity silver metal and platinum as a low-cost catalyst for hydrogen fuel cells. In the short run, copper prices have gone up and producers are hedging by buying commercial short contracts. Demand for gold will be further supported by low interest rates and rising global debt-to-GDP levels.</td></tr>
</table>

Continued on the next page

Return Outlook

Key:

Below Normal		Neutral		Above Normal
● (orange)	● (pink)	● (grey)	● (light green)	● (green)

Alternatives

Opportunity Set	Below Normal		Neutral		Above Normal
Energy	○	○	●	○	○
The midstream sector is well positioned for attractive cash-flow generation, given rising demand from a rebounding global economy and infrastructure cost reductions. Renewable sources, especially wind and solar, remain favorable due to capacity expansion, positive investment trends, heightened public policy initiatives, continued decrease in generation costs and improving distribution capabilities. In the near-to-intermediate term, oil and gas prices are anticipated to stay above pandemic period levels, but likely to remain within in the U.S. $60+/- per barrel range, due to forecasted market supply-demand balance. Uncertainty remains with regard to the strength and sustainability of the global economic recovery and future OPEC production policy decisions.					
Timber	○	●	○	○	○
The near-term outlook for timber remains mixed. Low interest rates, elevated levels of single-family housing starts, continued recovery in multifamily housing starts, demand-pull price increases and an apparent societal shift toward suburbs are all domestic tailwinds. However, uncertainty remains over the medium term with respect to the duration of low rates and other potential challenges, such as increasing unaffordability of new single-family homes, oversupply in certain key timber markets and increased severity of adverse weather events and natural disasters. Recent finished lumber spot shortages and price spikes related to pandemic-induced mill production slowdowns have not yet linked to boosting timber values. Internationally, continued recovery in global trade is a positive for the asset class, although natural disasters and currency fluctuations remain a concern.					
Farmland	○	○	●	○	○
The short-to-intermediate-term outlook remains unchanged as recovery from the COVID-19 pandemic continues, accompanied by improving conditions related to labor, supply chain disruptions and uncertain consumption patterns. Increasing farm income and land values are anticipated to maintain pace from federal subsidies and rising commodity prices, as eighty percent of agricultural products are now trading above pre-pandemic levels. Farmland values will experience tailwinds from increased demand for land, elevated concerns regarding food security and an emphasis on sustainability. The asset class will remain in demand from investors due to favorable income component and potential to appreciate at a faster rate than inflation.					

Overview
Global Macro Signals and Outlook
Asset Class Signals and Outlook
Questions? Contact Us.

Questions? Contact Us.

To learn more about how our forward-looking views can help enhance your investment strategy, contact your Segal Marco Advisors consultant or Chief Investment Officer Tim Barron.

In Canada, contact your Segal Marco Advisors Canada consultant or Joe Cerullo, Senior Consultant.

Stay informed

Sign up to receive our latest reports, articles, webinars and videos featuring timely commentary on economic, political and market developments as well as critical analysis of new investment products and marketplace trends.

Who we are

Investors rely on Segal Marco Advisors to achieve their long-term goals and create better financial outcomes. We are an employee-owned, independent global investment consulting firm serving more than 600 clients with combined advisory assets exceeding $500 billion.

Multiemployer plans, state and local governments, private companies, nonprofit organizations, endowments, foundations and financial intermediaries all rely on us for help managing their investment programs. Our expertise, research and technology enable us to build customized strategies that achieve the unique objectives of defined benefit, defined contribution, VEBA, operating, training and health and welfare plan sponsors and other investors.

Segal Marco Advisors is the investment consulting affiliate of Segal, a benefits and strategic human resources consulting firm founded in 1939 and headquartered in New York. Clients gain a global advantage in their investment decision-making from the regional expertise we provide as a founding member of the Global Investment Research Alliance.

Follow us:

Segal Marco Advisors