



MANAGER COMMENTARY

Third Quarter 2021

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MARKET REVIEW

While investors continue to adjust their collective outlook in response to the evolution of the COVID pandemic and massive government stimulus, the U.S. equity market reflected evolving consensus. The long-awaited value rally this spring was brought to a grinding halt in large part due to delta variant concerns, which resulted in a sharp decline in yields and a significant rotation into growth stocks. While this ruled the day early in the quarter, this effect faded as the worst fears of this variant being both severe and widespread faded. Concerns about a Fed leadership transition, the debt ceiling, and an evolving infrastructure bill did cast a pall over the market as the quarter came to a close.

Russell 3000

The Russell 3000 Index was essentially flat during Q3, despite a 4.5% decline in September. For the year, the Index has posted a 15% advance through quarter-end.

Size/Style

- Q3 returns decline as we go down the cap spectrum. While the S&P 100 Index returned 1% for Q3, the Russell 2000 Index recorded a 4.4% decline.
- Style performance was quite differentiated during Q3, with the Growth advantage substantially larger as we move up in capitalization. While the Russell 2000 Growth posted a 5.7% decline for all of Q3, the Russell Top 200 Growth added 1.6%.

Russell 3000 Sectors

There was pretty good relative performance consistency between Q2 & Q3, as three of the top performers from Q2 led the Russell 3000 during Q3.

- Financial Services, Technology, and Health Care stocks continued their strong relative performance.
 - » Energy performance declined relative to Q2 (despite the group far outperforming all other sectors during September).
- Materials stocks continued their relatively weak performance, declining 5.3% for the quarter.

THIRD QUARTER ATTRIBUTION

The AllCap strategy slipped 1.4% during the quarter, trailing the benchmark Russell 3000 Index's 0.1% decline. The table on the following page breaks down the contributions from sector positioning and stock selection.

In total, sector positioning detracted 0.44% from active return:

- Overweighting the Energy sector detracted 51bps, as the sector underperformed the Russell 3000 Index by about 0.8%.
- Underweighting the Industrials sector added 11bps, as the sector underperformed the Russell 3000 Index by about 4.2%.

Stock selection within the respective sectors detracted 0.90% from active return.

MARKET OUTLOOK

These are unprecedented times – that much is for sure.

Do record high profit margins fueling record high corporate profits justify a pricy stock market? Do incredibly easy financial conditions? So far, they have. Rapid expansion of the Fed's balance sheet, huge fiscal stimulus, and record low real yields are fueling a sharp corporate recovery – but have also fueled inflation. Strong increases in crude oil and many other commodities have led to a 40 year high in PPI; the jury remains out on whether this will continue to fuel consumer price increases.



THIRD QUARTER ATTRIBUTION

SECTOR	GLA WEIGHTING	R3000 WEIGHTING	% ACTIVE	GLA RETURN	R3000 RETURN	% ADDED	SECTOR ALLOCATION	STOCK SELECTION	ACTIVE CONTRIBUTION
Comm. Services	12.62	10.21	2.40	-2.84	-0.33	-2.51	-0.01	-0.33	-0.33
Consumer Disc.	11.49	12.11	-0.62	-3.67	-1.03	-2.64	0.04	-0.30	-0.27
Consumer Staples	7.98	5.30	2.67	9.12	-0.88	10.01	-0.03	0.76	0.74
Energy	4.43	2.51	1.92	6.90	-0.89	7.80	-0.51	0.26	-0.24
Financials	13.71	11.55	2.17	3.93	2.83	1.11	0.07	0.17	0.24
Health Care	9.84	13.73	-3.89	-0.64	0.22	-0.86	-0.07	-0.07	-0.14
Industrials	6.62	9.20	-2.58	-8.94	-4.30	-4.64	0.11	-0.36	-0.25
Technology	23.87	27.13	-3.26	-1.74	0.94	-2.68	-0.03	-0.65	-0.68
Materials	2.54	2.42	0.11	-14.96	-4.65	-10.31	0.00	-0.28	-0.28
Real Estate	3.90	3.41	0.49	0.14	0.71	-0.57	-0.01	-0.03	-0.04
Utilities	2.99	2.41	0.58	-1.37	0.99	-2.36	0.00	-0.07	-0.07
Total	100	100		-1.44	-0.10	-1.34	-0.44	-0.90	-1.34

Source: GLA and Bloomberg. Performance numbers are gross of fees.

The stimulus has certainly also boosted the jobs market, with payrolls – and wages – still growing solidly. The housing market has also been a significant beneficiary of easy conditions and COVID-driven re-prioritization. New home permits, starts, and sales remain solid, existing home sales continue at a robust pace, and the Case-Shiller indices are each up close to 20% year over year. Kind of reminiscent of 2003-2005.

Industrial production has continued its strong recovery, and ISM readings indicate this will continue. Global shipping has awoken from its long slumber, and the Baltic Freight Index is up quite sharply – to 13 year highs.

So yes, stimulus has gotten investors wonderful stock price appreciation up through now, but caution is certainly warranted at these lofty levels.

Positioning:

With the economy still awash in liquidity and the impact of the delta variant showing signs of rolling lower, we see a percolating

reopening trade combined with positioning for inflation, which may not be as transitory as we'd like to imagine. This interplay has led to another pop in Treasury yields since early August, and with this has come a rotation back out of growth and towards value, and especially smaller-cap value. Other **risk factors** which appear favorable include earnings yield, leverage, and momentum.

From a **sector/industry** perspective, the increase in yields is starting to pull the Banks back into favor (Financial Services and Securities & Asset Management are already positive), and the reopening trade is leading to a resurgence of Energy Reserves stocks and retailers. Financials have swung into favor among sectors, but still trail the Consumer Discretionary and Retail sectors. Health Care is most out of favor, driven by the Biotech industry. Software is also unfavorable.

From a **stock selection factor** perspective, we again see the resurgent reopening hopes reflected in building price momentum (WRSI), increased emphasis on valuation (Sales/Price, Cash Flow/Price, Forecasted Earnings/Price), and solid quality (High ROA/ROE).



The data in the attribution table represent the returns for each sector and for the gross returns for a representative composite account for one quarter ending the current calendar quarter. The sector weights are the average weight throughout the calendar quarter. Individual account returns may vary.

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