

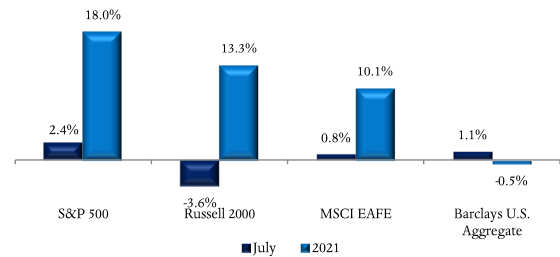


MARKETS

The global economic recovery continued in July, with the coronavirus vaccine rollout making steady progress. While pandemic restrictions on activity were on an easing path, sentiment was dented by the spread of the more contagious Delta variant of Covid-19, raising concerns that the road to normalcy may be bumpier than previously expected.

US equities led financial markets higher, with the S&P 500 breaching record highs and returning +2.4% for the month (+18.0% ytd). With over half of the bellwether index's companies having reported earnings by the end of July, close to 90% exceeded analysts' earnings expectations. Growth stocks (+2.9%) benefited from a decline in interest rates, outperforming value equities (+0.7%). However, smaller capitalization stocks, as measured by the Russell 2000 index, suffered from negative sentiment surrounding the potential for a deceleration in economic growth (-3.6% in July; +13.3% ytd). Overseas equities produced mixed performance. The Stoxx Europe 600 index advanced +2.1% last month (+18.2% ytd), while the MSCI EAFE benchmark added +0.8% (+10.1% ytd). Conversely, emerging market equities lagged, returning -6.7% (+0.3% ytd), dragged down by weak performance from China (-4.6% in July; -0.3% ytd), where announcements of tighter regulation for several sectors triggered a sharp decline in stock prices.

Bond market trading activity in July was quite notable. The US 10-year Treasury yield continued its descent, falling below 1.20% during the month (from a peak of 1.75% at the beginning of the second quarter). Perhaps most intriguing, real (inflation-adjusted) yields on US corporate junk bonds turned negative on the back of sharply rising inflation. This environment led the Barclays US Aggregate Bond index higher by +1.1% in July (-0.5% ytd).



Commodities rose for a fourth consecutive month, leading the S&P GSCI index higher by +1.6% in July (+32.2% ytd). Many individual commodities, constrained by production and distribution issues, continued to be in deficit around the world, while reopening and reflationary demand persisted. The US Energy Information Administration reported that natural gas now makes up a record 40% of annual US electrical generation, with renewables having entered second place at 21%. The green transition continues to be one of the key themes affecting commodity price action.

GEOPOLITICS

Covid-19 vaccines have thus far proven highly effective at preventing severe disease, hospitalization, and death from the infectious disease. However, with the advent of the Delta variant, a share of fully vaccinated individuals are becoming infected. These infrequent occurrences are known as "breakthrough cases" which are to be expected, and have historically occurred with other vaccines, none of which are 100% effective. We sought to quantify the matter and have gathered the following data points from official US State sources (of which 25 report such information). Importantly, not all hospitalizations and deaths of those fully vaccinated and diagnosed with Covid-19 are due to the virus. For example, Washington D.C. reported that 50% of recent hospitalized breakthrough cases were due to Covid-19, 19% were not, and 31% were of unknown reason. The rate of breakthrough cases reported among those fully vac-

cinated, in all reporting states, ranges from 0.01% in Connecticut to 0.29% in Alaska. The hospitalization rate among fully vaccinated people with Covid-19 ranged from effectively zero (0.00%) in California, Delaware, D.C., Indiana, New Jersey, New Mexico, Vermont, and Virginia to 0.06% in Arkansas. The rates of death among fully vaccinated people with Covid-19 were even lower, near-zero (0.00%) in all but two reporting states, Arkansas and Michigan where they were 0.01%. Conversely, more than 9 out of 10 recent Covid-19 cases, hospitalizations, and deaths have occurred among people who are unvaccinated or not yet fully vaccinated. These, albeit limited, findings echo the abundance of data demonstrating the effectiveness of currently authorized Covid-19 vaccines.

US President Biden's infrastructure spending ambitions continue to be challenged. Following news that the outline of a bipartisan infrastructure bill had been agreed at the end of June, subsequent details have been scarce. Passing a bill that requires only Democrat support via the "budget reconciliation" process remains an option, although this would likely require compromises on the size of spending.

UNITED STATES

The US economy continued to rise, at a 6.5% annualized pace in the second quarter, surpassing its pre-pandemic level. The overall increase came thanks to increasing personal expenditures, which rose 11.8%, with consumers accounting for 69% of all activity. Inflation again surprised to the upside for the fourth consecutive month, with the increase in the headline consumer price index (CPI) reaching 5.4% year over year in June. The contribution from sectors that are clearly benefitting from the reopening of the economy, such as travel and tourism, remained strong, but there were also signs that inflationary pressures are broadening across the spectrum.

At the July FOMC meeting, the Federal Reserve acknowledged that the economy has made progress toward its goals, but this advance was not yet viewed

July 2021 Economic Statistics

	Jul-21	Dec-19	Dec-18
Federal Funds Target Rate	0 - 0.25%	1.50-1.75%	2.25-2.50%
Consumer Confidence Index	129.1	126.5	128.1
Manufacturing PMI Index	59.5%	47.2%	54.1%
Unemployment Rate	5.7% (est.)	3.5%	3.9%
JPY / USD	109.70	108.61	109.56
USD / EUR	1.1870	1.1210	1.1469
Gold / oz.	\$1,813.58	\$1,517.01	\$1,282.73
Oil (WTI) / bbl	\$73.95	\$61.06	\$45.41

as "substantial." Fed Chairman Powell made very dovish comments at the post-FOMC press conference, quashing speculation that the Fed will pull back on its \$40 billion per month mortgage bond buying. He also stated that the Fed's objective with regard to employment had not been achieved. Lastly, when asked, his definition of "transitory" inflation was that it would not go on indefinitely, a very loose interpretation.

EUROPE

The European Central Bank's strategic review, completed last month, led to a more symmetric 2% inflation target (versus the previous target of "below, but close to 2%"). Going forward, housing costs will be incorporated into the calculation of inflation. In addition, the ECB's Governing Council added stronger forward guidance to its statement, reinforcing that interest rates will remain low for a very long time. Policymakers now hope that the launch of the European Union's Recovery Fund will aid the region to break out of its low-growth, low-inflation environment. Presently over half the member states have received approval of their recovery plans. Meanwhile, business activity grew at its fastest rate in 21 years, with a robust improvement in service sector activity more than offsetting a modest decline in the manufacturing PMI that was linked to supply chain disruptions.

The European Union launched its "Fit for 55" package of proposals (referring to the EU's 55% emission reduction target by 2030). They include a large number of initiatives designed to set the union on a course to achieve its climate change goals. A carbon border ad-

justment mechanism (CBAM) would apply a levy linked to carbon prices on a range of imported goods in an effort to preserve the competitiveness of domestic corporations. There will be a gradual phase-in of CBAM fees between 2023 and 2035, which will mirror the phase-out in free emissions credits to European industry. The taxes to be levied on EU importers will apply after 2025 to cement, iron/steel, aluminum, power, and fertilizers. In 2026 there will be a review to consider extending CBAM to other sectors and an attempt to capture indirect emissions.

UK economic data painted a slightly more mixed picture in July, with flash PMIs showing clear signs that supply bottlenecks are putting a ceiling on activity levels. The growth outlook remains strong, but with businesses struggling to fill job vacancies and shortages of raw materials starting to affect end products, business costs rose at the fastest pace on record in July, while the more broad-based CPI advanced 2.5% year-over-year in June.

ASIA

China's economy has largely recovered from disruptions caused by the pandemic, with GDP growing by 7.9% in the second quarter, compared to the same period last year. Manufacturers continue to grapple with supply chain issues as well as new challenges from higher raw material prices. Chinese reforms, recently aimed at local technology champions, migrated to the private tutoring sector as well as the housing market (via a crack down on debt). The changes appear to reflect a renewed focus from policymakers on their long-term structural goals, with particular efforts to curb inequality and ensure healthy competition. China also launched a national carbon trading program focused initially on utility power generation. The government also stated its intention to expand into heavy polluting industries. We note this is the same playbook the EU used to expand its carbon taxes.

OUTLOOK

Most equity markets have delivered strong returns thus far in 2021. However, there are budding concerns that inflation, supply chain bottlenecks, as well as the Delta

Covid-19 variant, may result in a decelerating, potentially stagflationary, economy in the coming quarters. Consumers continue to drive strong growth, spending the savings they amassed from pandemic-induced austerity, but this is sure to wane. Additional drivers of equities, and support for valuations, appear to be faith that policymakers worldwide will continue their significant fiscal spending, while central banks maintain massive bond buying programs based on the belief that the current inflationary trends are transitory. Given the above, and currently low interest rates, there remains scope for risk assets to move higher over time, albeit with the potential for elevated volatility. Should interest rates begin to rise once again, it may lead to a momentum shift towards reflation themed stocks and value oriented equities, whose valuations remain relatively cheap.

Overall, we do not believe that the recent decline in US bond yields is sending a negative signal about the health of the economy. Rather, it is partially due to a technical consolidation of the significant advance in rates during the first four months of the year. Given the ongoing strength of the economic recovery in the US, coupled with robust inflation data (CPI +5.4%; PPI +7.3%) we expect yields to eventually move higher. As such, our analysis continues to point towards the avoidance of long-dated bonds, and in favor of inflation adjusted securities.

Given the ongoing economic recovery, rebounding corporate profits and the potential for higher corporate taxation in the US, it is likely that actively managed investments will add significant value, versus their benchmarks, going forward. Should interest rates begin to rise once again, the environment would also bode well for select alternative strategies. We hold a positive view of hedged credit, as well as inflation protected investments such as real estate, energy exploration, and water infrastructure. In addition, as long-term investors with the belief that technology will advance secularly, we continue to highlight our recently-launched proprietary Nordic Technology and Innovation Fund.

Important Disclosure and Terms of Use: Property of Papamarkou Wellner Asset Management, Inc. For targeted distribution only and not a solicitation. This report may not be displayed, reproduced, distributed, transmitted, or used to create derivative works in any form, in whole or portion, by any means without express written consent by Papamarkou Wellner Asset Management, Inc. or its operating subsidiary, Papamarkou Wellner & Co., Inc. MEMBER: FINRA/SIPC. All opinions expressed within unless otherwise stated are those of Papamarkou Wellner Asset Management, Inc. based on the most recent market, security, and economic data available.

Sources: Barclays, Bloomberg, Bureau of Labor Statistics, Conference Board, Department of Agriculture, Federal Reserve, Financial Times, IMF, Institute for Supply Management, MSCI, Reuters, Russell, Standard & Poor's, and the Wall Street Journal.