October 2020

INVESTMENT UPDATE

Executive Summary

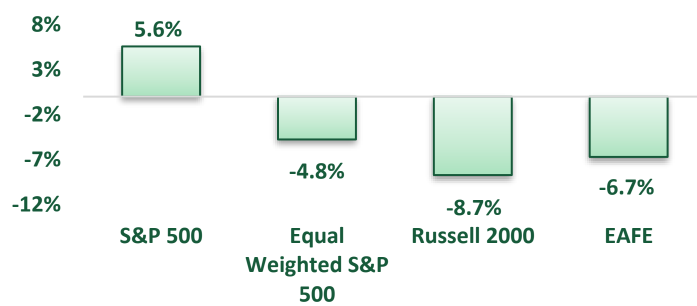
- U.S. markets continue their V-shaped recovery based on the reopening of the economy and stimulus provided by the Federal Government and the Federal Reserve.
- The consumer remains in a strong position with the confidence and the wherewithal to increase spending.
- Support from the Federal Government and Federal Reserve for businesses, consumers, and especially the unemployed to limit the economic fallout from government mandated shutdowns is expected to continue well into 2022.
- Corporate profit estimates are likely to continue to move higher, supporting elevated stock market valuations. Relative to historically low bond yields and with improving economic conditions, stocks remain attractive for long-term investors.

Large Capitalization Technology Stocks Drive Stock Market Recovery with Broader Recovery Still to Come

The ongoing reopening of the U.S. economy and continued support from the Federal Government and Federal Reserve drove the S&P 500 to new highs during the third quarter before giving up some of those gains in September. Large capitalization stocks generated solid returns in the quarter at +8.9% (S&P 500), while small cap (Russell 2000) and foreign stocks (EAFE) also performed well with returns of +4.9% and +4.8%, respectively. Bonds generated a positive return of +0.6% in the quarter. Year-to-date, returns remain mixed with large cap stocks having generated a total return of +5.6%, while small cap and foreign stock returns remained negative, with returns of -8.7% and -6.7%, respectively.

Although overall equity returns were strong in the quarter, there continues to be a large divergence between the S&P 500 (up 5.6%) and the broader market, as measured by the S&P 500 Equal Weight Index, which remained in negative territory down -4.8% year-to-date. This 10.4% return gap is a result of the strong returns among the five largest tech companies (Apple, Microsoft, Amazon, Google, and Facebook) which account for over 22% of the market cap weighted S&P 500. These companies have benefited significantly from consumers accelerating adoption of online commerce and companies implementing new technologies that enable their workforces to work from home. While these companies' stocks have performed well, we expect the broader stock market to begin to catch up as the economy continues to recover and consumers gain the confidence to resume normal activities as the risk of contracting the virus abates.

Graph 1. Broad Market Remains Weak



The Consumer Continues to Spend in Select Areas

The easing of lockdowns and other COVID-19 related restrictions have resulted in a strong initial economic recovery. This is demonstrated by retail sales which are +2.6% higher than they were a year ago. This is a sharp recovery from the lows made in April, when retail sales fell -20%. The recovery has been particularly strong for autos (+4.5%), building materials (+15.4%), and grocery retail (+9.0%). These areas have benefitted from limited consumer spending options as COVID-19 related restrictions and consumer risk aversion have largely prevented consumers from spending on services (down -7.2% in August from the prior year), especially in the areas of travel, leisure and hospitality. This is clearly demonstrated by lower TSA screenings at airports which remain down more than -60% compared to last year.

The strong recovery in retail sales appears to be sustainable as consumers, through a combination of stimulus checks and enhanced unemployment benefits, have significantly increased their savings rates, allowing them to accumulate over $2 trillion in additional savings deposits in the past year (see Graph 2). Additionally, while consumer confidence has declined from the very high levels of the past few years, it remains healthy, near the highs of any other time over the

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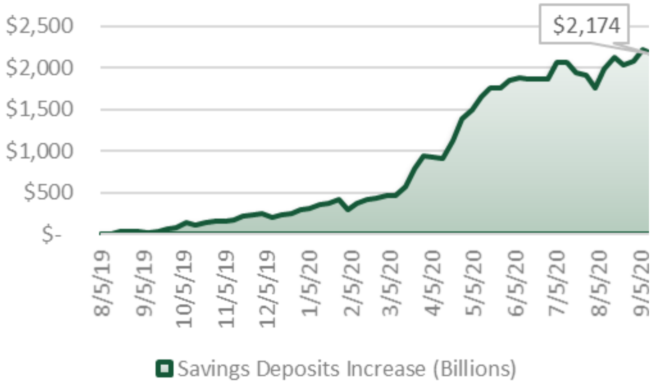
past 20 years (see Graph 3). Therefore, with the wherewithal to continue to spend and still strong confidence, despite ongoing concerns around the virus, the consumer should continue to support a further recovery of the economy.

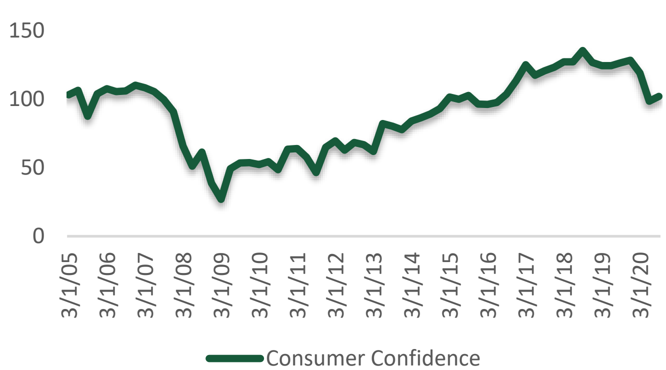
Graph 2. U.S. Savings Rate and Deposit Growth Over the Last 12-Months



Source: Federal Reserve Board

Over the next several months, we anticipate continued improvements in COVID-19 treatments and, potentially, a vaccine. This would allow for the further removal of COVID-19 related restrictions and reduce the consumers' aversion to activities such as travel, going to restaurants, and attending crowded events. While we believe the economy is on pace to fully recover in the next 1-2 years, any positive developments regarding treatments or vaccines for COVID-19 have the potential to provide an additional boost to economic growth and allow the economy to fully recover much sooner.

Graph 3. Despite the Virus, The Consumer Remains Confident



Source: The Confidence Board

Monetary and Fiscal Policy Remain Accommodative

Along with the strong underlying fundamentals of consumers' incomes and balance sheets, the unprecedented support provided by both the Federal Reserve and Federal Government remains a primary contributor to the sustained recovery of the economy. The Federal Government's COVID-19 relief bills more than covered the lost wages resulting from safer-at-home related job losses and provided corporations much needed liquidity through business loans and grant programs. Meanwhile, the Federal Reserve reduced the Federal Funds rate to zero and is purchasing Treasuries, mortgage backed securities, corporate bonds, and even high yield corporate bonds providing additional liquidity to the markets. This exceptional level of support is likely to continue throughout the next couple years as the Federal Reserve remains committed to holding interest rates near zero until the labor market fully recovers, even if that means inflation runs above its 2% target. Furthermore, the Federal Government continues to negotiate additional aid bills. These extraordinary levels of support should provide more than enough stimulus and liquidity to support continued economic growth for the next several years even with ongoing headwinds from the COVID-19 pandemic.

Stock Market Valuations Remain Attractive for Long-Term Investors

Although the S&P 500 price-to-earnings (P/E) multiple is currently elevated at 21x the next 12 months expected EPS versus a 25-year historical average of 16.5x, we believe long-term investors should be cautiously optimistic that a multi-year, broad-based recovery in economic activity and corporate profits is underway and will drive the stock market higher longer term. Considering extremely low interest rates, the extraordinary stimulus being provided to consumers and businesses by both the Federal Government and the Federal Reserve, improving economic activity, and the strong rebound in corporate profitability, we continue to believe the stock market should be valued at above average levels.

Moreover, stock valuations are likely much closer to their historical average valuations than they appear as current forward P/E multiples do not fully reflect the strong above average growth we expect in corporate earnings in 2021, 2022, and potentially 2023. This is because early estimates tend to be slow to adjust upward at the beginning of a recovery as near-term earnings, particularly for cyclical companies, accelerate rapidly from trough earnings. Lastly, when you remove the top 5 stocks (Apple, Microsoft, Amazon, Google, and Facebook) from the S&P 500, the P/E multiple for the broader market drops to a much more reasonable 18x forward earnings estimates. Therefore, we continue to believe stocks are attractive for long-term investors and recommend adding to stocks should equity allocations fall below the middle of one's targeted range. While there remains much uncertainty around the ongoing impact of COVID-19 and the upcoming Presidential Election, we do not believe either one has the potential to derail the economic momentum and we continue to take comfort in our philosophy of investing primarily in high quality, consistent growth companies that have proven their ability to grow their earnings in both good and bad times.