W A I N W R I G H T   I N V E S T M E N T   C O U N S E L , L L C

FINANCIAL MARKETS HIGHLIGHTS

Third Quarter 2021

The summer months brought more than just warmer weather across the country. There was also a notable uptick in Covid-19 cases, a troubling reversal in declining case numbers and deaths, brought upon by stagnating vaccination rates and the virus's new Delta variant. Unsurprisingly, this weakening virus outlook, combined with deadlock in Washington and rising interest rates, led to some capital market volatility during the quarter.

Washington continues to fight over the highly contested infrastructure and spending bills. A bipartisan physical infrastructure bill (~$550 billion) for bridges, roads, airports, ports, broadband, etc. passed in the Senate with 17 Republican votes. However, the bill has been held up in the House as Democrats struggle to unite over the passing of a $3.5 trillion bill with a sizable "social" infrastructure component (*i.e.*, funds for child-care, Medicare, climate change, tax reform, etc.).

Further complicating matters is the seat breakdown in the Senate: 50 Republican, 48 Democrat, and 2 Independent. If the House were to agree on the parameters for the $3.5 trillion social infrastructure bill, it would require Senate approval. Typically, 60 votes are required to pass any bill in the Senate, however through a process called Reconciliation a bill can pass by simple majority (51 votes). The Reconciliation process may only be used once per year and in this instance 50 votes + the vote of Vice President Harris would be enough to pass the legislation, meaning the Democrats can't lose a single vote among their own party and need both independent Senators to vote with them. Because of the razor thin margin for error, and reservations among several key senators (including Manchin, WV and Sinema, AZ), there will likely be a modified bill proposed. The next few days, and weeks, will have major implications for the American people and for both political parties.

In a longer-term context, the stock market, as defined by the S&P 500 index, continues to climb to new highs amidst all the noise, but there have been setbacks of late, disrupting quiet markets since last winter. The S&P 500 eked out a quarterly gain of +0.6%, but this index, dominated by mega-sized and tech-oriented stocks, was the outlier. The Russell 2000 index of small-cap stocks returned -4.4% during the quarter, the broad Russell 3000 index -0.1%, the S&P 400 index of mid-sized stocks -1.8%, and the international stock markets, which are covered below, were also down.

On a sector basis, within the S&P 500 index, returns were led by Financials (+2.7%), Utilities (+1.8%), and Communication Services (+1.6%), while Industrials (-4.2%), Materials (-3.5%), Energy (-1.7%), and the Consumer Staples (-0.3%) sectors were down.

The NASDAQ 100 was not immune to increasing volatility, having declined -5.7% during September alone, but closed September with a +1.1% quarterly return. The *FAANG* tech giants that dominate the NASDAQ and the S&P 500 were a mixed bag during the quarter. Positive performance from Apple (+3.5%), Google (+6.3%), and Netflix (+15.6%), was weighed down by losses from Amazon (-4.5%) and Facebook (-2.4%).

Growth-oriented stocks continued to outperform their value counterparts during the quarter (Russell 3000 Growth index +0.7% vs. Russell 3000 Value index -0.9%), and performance by market capitalization stayed on trend with large company stocks outpacing mid and small company stocks.

The MSCI EAFE Index of international, developed country stocks returned -0.5% during the quarter, outperforming the MSCI Emerging Market Index, which declined -8.1%. The performance disparity was primarily attributable to two primary factors: Covid-19 and new Chinese regulatory policies. Regarding the former, lagging vaccination rates in emerging economies have delayed their reopening relative to more developed economies, in general. The latter, and potentially more impactful development, was the recent regulatory crackdown in China (which represents more than a third of the emerging market index). The MSCI China index was down -18.2% during the quarter, on the back of

Selected Index Returns (%) as of September 30, 2021 (Source: Morningstar Direct). 3, 5, 10 year returns are annualized.

	Jul.	Aug.	Sep.	QTR	YTD	1 Year	3 Year	5 Year	10 Year
S&P 500	2.38	3.04	-4.65	0.58	15.92	30.00	15.99	16.90	16.63
S&P 400	0.35	1.95	-3.97	-1.76	15.52	43.68	11.08	12.97	14.72
Russell 2000	-3.61	2.24	-2.95	-4.36	12.41	47.68	10.54	13.45	14.63
Wilshire U.S. REIT Index	5.10	1.91	-5.11%	1.64	24.97	38.04	10.39	6.97	11.30
MSCI EAFE	0.75	1.76	-2.90	-0.45	8.35	25.73	7.62	8.81	8.10
MSCI Emerging Markets	-6.73	2.62	-3.97	-8.09	-1.25	18.20	8.58	9.23	6.08
Barclays Aggregate Bond	1.12	-0.19	-0.87	0.05	-1.55	-0.90	5.35	2.94	3.01
Barclays High Yield	0.38	0.51	-0.01	0.89	4.53	11.28	6.91	6.52	7.42

President Xi's reemphasis on China pursuing "Common Prosperity" for all, with wide ranging business, regulatory and social implications. This will be a story to watch closely moving forward as the policies seem to have no immediate end in sight.

The Federal Reserve's Open Market Committee ("FOMC") met in September and, for the 18th consecutive month, left the short-term Fed Funds rate at a range of 0.00 – 0.25%. The FOMC "Dot Plot" indicated nine members (up from eight in June, four in March and one in December) expected a 2022 rate hike, and all but one member believed that 2023 rate hikes would be called for. The Committee's median economic growth forecast for 2021 fell over 100 bps (from 7% in June to 5.9% in September) as the forecast now falls below those from the March meeting. However, projections for 2022 and 2023 improved slightly to 3.8% and 2.6%, respectively. The Committee's 2021 unemployment rate forecast ticked up slightly between June and September (from 4.5% to 4.8%) but was unchanged for 2022 and 2023. Once again, the Fed raised expectations for 2021 inflation. The Personal Consumption Expenditures price index increased to 3.7% in September from 3.4% in June and 2.4% in March. Chairman Powell commented on inflation by saying, "we appear to have achieved more than significant progress, substantial further progress. That part of the test is achieved in my view and the view of many others."

The 10 Year U.S. Treasury Bond yield ranged from 1.45% at the end of June, to a low of 1.19% in August, before settling the quarter at 1.52%. The Bloomberg Barclays Aggregate Bond index returned only +0.1% during quarter and has generated a negative total return for the year-to-date and trailing 12-month periods, a byproduct of the rising rate environment. The Bloomberg Barclays High Yield Index, which holds below investment grade credit, continued to outperform the Aggregate index with a +0.9% and +4.5% quarterly and year-to-date returns, respectively.

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