THIRD QUARTER 2021

Matt's Market Update

IN THIS REPORT

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Market Review

Global equities declined broadly in September as Q3 finished with flat to slightly negative gains depending on the index. The S&P 500's streak of five straight quarters of 5+% returns ended with a -4.65% return in September, but a tiny 0.58% gain for the quarter. In the US, the Federal Reserve (the Fed) announced that it will soon (as early as November) begin to slow the pace of its asset purchases (taper), with purchases set to come to an end during the middle of next year. The Fed also released its projections for interest rates over the next few years. The pace of expected future rate increases was faster than the market had been pricing in, resulting in a rise in Treasury yields in the days following the Fed's September meeting, reversing the decline in yields from earlier in the quarter. These projections from the Fed must be taken with a large grain of salt, as they've been frequently wrong in their guesses for timing of future actions. Weakness in the equity markets, legitimate concerns over a slowing domestic economy and ongoing dysfunction in Washington D.C. may cause the Fed to push back their plans for reducing asset purchases and hiking short-term interest rates.

Volatility returned to the forefront in Q3 as market focus shifted from a strong earnings season to concerns over a lingering Covid Delta variant, inflation pressures and the end of certain government stimulus programs. Strong earnings powered stocks higher early in the quarter as U.S. equities gained for a seventh straight month in August, marking the longest winning streak since 2018. Employers added nearly 2 million jobs in June and July, but August nonfarm payrolls widely missed expectations, calling into question the durability of the economic recovery. Global supply chain disruptions came into focus and put upward pressure on prices of goods. The Fed's use of the term "transitory" to describe inflation persistence is looking more and more incorrect.

The negative news from China seemed relentless in the third quarter. First, China's move to turn private tutoring companies into non-profit organizations worried some investors, who started to question whether similar actions would be applied to other sectors. Then, more regulations on the technology sector were announced, which caused a sell-off in popular Chinese large-cap technology stocks. Finally, investors had to contend with fears around the potential default of a large Chinese property developer (Evergrande) and the potential market impact. All this has weighed on Chinese equities. As a result, the average manager in the Morningstar Diversified Emerging Markets peer group declined -6.79% for the quarter. While the long-term growth opportunities in emerging markets remain intact, the near-term outlook remains cautious.

MORNINGSTAR STYLE BOX PERFORMANCE (%)

Q3 2021

	Value	Blend	Growth
Large	-1.26	-0.11	2.35
Mid	-1.49	-0.13	0.20
Small	-2.06	-3.97	-4.50

YTD

	Value	Blend	Growth
Large	12.89	12.83	17.26
Mid	20.30	16.00	9.74
Small	25.35	12.98	-0.35

**Performance is shown in Total Return USD.*
Source: Morningstar Indexes. Data as of September 30, 2021

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Returns & Ranks

As most of our plan sponsor clients are aware, Sentinel has a proprietary quantitative ranking system called the FundScore. This process assigns an overall score between zero and ten to each fund in the Morningstar universe based on returns, risk statistics and other metrics. The scoring system is based on where a fund manager ranks versus other funds in the same Morningstar peer group. The largest contributor to the fund's overall score is its relative return rankings over the trailing one-year, three-year and five-year time periods. As an example, the chart on this page compares three different funds and their returns over the short-term (12 months) and long-term (five years) along with their percentile ranks against the peer group. Percentile ranks are scaled from zero to 100, the lower number signifying a fund that ranks higher in the peer group over that specific time. Each example is a fund we currently recommend (names removed) across many client retirement plans.

	Return 9/30/20 - 9/30/21	Percentile Rank 1 Yr.	Percentile Rank 5 Yr.
Large Cap Growth Fund	22.41%	82	26
Mid Cap Growth Fund	24.11%	88	27
Small Cap Growth Fund	36.53%	59	7

**Past performance does not indicate future results. The funds selected have had their names excluded. The above chart is for illustrative purposes only. Morningstar Rating for Funds can be found here.*

Equity returns over the trailing twelve-month period have been extremely strong as the economy has started to recover from the Covid crisis combined with extraordinary stimulus provided by the government and central banks. Looking at the chart, you'll note the actual returns are greater than 20% with returns increasing as you move down the list. What's interesting though are the ranks over the past year for these funds (middle column). As you can see, none of the funds rank in the top half of the peer group despite the strong positive returns. Two of the funds (Large Cap and Mid Cap) are actually in the bottom quartile (not top 75% of the peer group). We've actually had a few clients ask what is wrong with the funds that are displaying the weaker ranks over the past year. In almost every case, the simple answer is that nothing is wrong. Despite posting strong returns, these funds have simply failed to gain as much as some of their competitors. We highlighted growth funds in this example, but this same story is evident across all sectors of the market. The main conclusion here is that anything can happen over a short time period. We hope that our managers are making portfolio decisions that will benefit returns over the long-term and not simply the next 12 months. This is why our FundScore system assigns greater importance to the long-term ranks a manager displays. Look at the last column that shows the ranking for each manager over the trailing five-year period. Here, we see rankings that are well above average. A 26 rank for the Large Cap Growth fund means this fund ranks in the top 26th percentile of the peer group for example. While we monitor and report on performance for short time periods, the long-term performance ranks have much more influence over our decisions to add or remove a fund manager.

Wealth Management Corner

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Each year, our team of financial planners and financial wellness educators meet with thousands of individuals whom look to us for financial guidance and advice. Although the pandemic created some obvious concerns back in March of 2020 regarding our ability to continuously deliver on these needs, we have actually seen an increase in client engagement as well as an improvement in how effectively we're able to quickly connect with our clients.

Throughout the year, we chat amongst our team about some of the themes that are keeping folks up at night, or simply seem to be at the forefront of every discussion. Each year, we find one constant that seems to take up real estate in the minds of individuals as it relates to their financial lives. Simply put, folks spend a majority of their financial planning conversations either second guessing their historical financial decisions or analyzing things that may simply be out of their control. Spending too much time focusing on questions such as " what if I did this" or "what if I was positioned a little differently" will wear you down, reduce the amount of time you can focus on future decisions and take away the abilities to confidently implement changes in the future.

For this article, we want to transition to 10 areas that you can focus on in the fourth quarter as we wrap up 2021. Although this tends to be the time of year where we all begin to think about our New Year's resolutions, there is still plenty of time to take action to create positive impacts within our financial plans. While understanding that this list isn't conducive to everyone's financial picture, it can serve as a solid framework that can be successfully evaluated prior to year-end.

1. **Evaluate additional savings capabilities within your retirement plan.**
2. **Consider rebalancing your investment portfolios.**
3. **Check your balances within Flexible Spending Accounts.**
4. **Satisfy any required minimum distributions from qualified accounts including that of inherited accounts.**
5. **Begin to think about Open Enrollment if your company's benefits are aligned with the calendar year.**
6. **Year End Tax Planning for non-retirement Accounts with possible tax loss harvesting.**
7. **Analyze whether or not you and your loved ones are adequately insured.**
8. **Explore possible Roth IRA conversions depending on your tax and financial situation.**
9. **Review Estate Plan and Beneficiary Information.**
10. **Schedule a review with your Property and Casualty insurance agent to review coverages.**

Financial planning brings a lot of stress and concerns for all of us. Consistently making decisions while trying to absorb new information can create complexities and eliminate our ability to make confident choices. Remain focused on your overall plan and follow a process. If you don't have a plan, consider taking this whole "financial planning thing" a bit more seriously before it's too late. Remember to focus on the areas that you can control and hopefully with some strategic planning and a regular review, much of the items outside of your control will fall into place over time. More often than not, people find themselves better prepared by having a plan that is well-aligned with their overall goals.

Our Portfolio Strategy & Allocation Outlook

It was a very quiet Q3 in our managed portfolios. While we made some minor manager changes within our retirement plan CIT portfolios (please see the separate commentary for details), there were no changes made within our individual wealth portfolios. As we mentioned in our last commentary, patience is a valuable trait for all investors right now. Equity valuations are very high while interest rates remain locked in a very low range (which we foresee being the case for some time), which limits the return potential across the fixed-income landscape. We remain fully diversified across all portfolios strategies and have the flexibility to take advantage of opportunities as they present themselves. In no particular order, here are the top five concerns we observe for investors entering Q4.

1. Equity valuations today across virtually every metric rival or surpass those valuations last seen during the technology bubble of '99-00. Remember, high valuations aren't a great timing tool (as excessive valuations can become more extreme), but they do tend to limit forward-looking returns for the marginal dollar invested today at these elevated prices.

2. Current estimates for Q3 & Q4 GDP growth in the U.S. have been coming down dramatically. The widely followed Atlanta Fed model estimate for real GDP growth (seasonally adjusted annual rate) in the third quarter of 2021 is 0.5% as of mid-October, down from nearly 4% growth estimated in August. This seriously calls into question the strength of the U.S. economy.

3. The twin issues of the ongoing supply chain crisis along with soaring energy prices are likely to stay in the headlines for the foreseeable future. How long can the stock market perform well in the face of these problems? Rising energy costs are a tax on consumers and will certainly have an impact on corporate earnings.

4. Equity markets had an immediate negative reaction to the September Federal Reserve meeting. These losses have since recovered, but how will markets react to the official start of the Fed's expected tapering of asset purchases in Q4? As we've documented frequently in the past, any event that suggests less stimulus for the market is typically met with declining prices.

5. The dysfunction in Washington D.C. How much worse can it get? Remember, the debt ceiling and potential government shutdown issues are only delayed until December. In addition, there has been no movement on the infrastructure bill at this moment as the partisan bickering continues.

Please let us know if you'd like to discuss your personal investing and financial planning needs.

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Market Scoreboard

Index Returns (%)	Q3 2021	YTD	1 Year	3 Year	5 Year	10 Year
S&P 500	0.58	15.92	30.00	15.99	16.90	16.63
DJIA	-1.46	12.12	24.15	11.00	15.69	14.72
NASDAQ	-0.38	12.11	29.38	21.54	22.16	19.58
Russell 2000	-4.36	12.41	47.68	10.54	13.45	14.63
MSCI ACWI Ex USA	-2.99	5.90	23.92	8.03	8.94	7.48
Barclays Aggregate Bond	0.05	-1.55	-0.90	5.35	2.94	3.01

Source: Morningstar

S&P 500 TR: A market capitalization-weighted index of 500 widely held stocks often used as a proxy for the large-cap segment of stock market.

Russell 2000 TR: Consists of the smallest 2000 companies in the Russell 3000 Index, representing approximately 7% of the Russell 3000 total market capitalization often used as a proxy for the small-cap segment of the stock market.

Barcap Aggregate Bond TR: The Barclays Capital Aggregate Bond Index is a market capitalization-weighted index, meaning the securities in the index are weighted according to the market size of each bond type. Most U.S. traded investment grade bonds are represented. The index includes Treasury securities, Government agency bonds, Mortgage-backed bonds, Corporate bonds, and a small amount of foreign bonds traded in U.S.

MSCI EAFE NR USD: Widely accepted as a benchmark for international stock performance, the EAFE Index is an aggregate of 21 individual country indexes that collectively represent many of the major markets of the world.

DJ US Industrials TR USD: Computed by summing the prices of the stocks of 30 U.S. companies and then dividing that total by an adjusted value--one which has been adjusted over the years to account for the effects of stock splits on the prices of the 30 companies.

NASDAQ: Measures the performance of all issues listed in the Nasdaq Stock Market and is often used as a proxy for the large-cap technology segment of the U.S. stock market.

DJ/UBS Commodity: The DJ-UBSCI is composed of futures contracts on physical commodities and is often used as a proxy for broad-based exposure to the commodity markets.

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