Second Quarter Report 2021

LUCIEN, STIRLING & GRAY ADVISORY GROUP SM

"Smart Decisions About Serious Money"

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A Message From The President

Thomas G. Twombly

"There are two kinds of forecasters: those who don't know, and those who don't know they don't know."
— John Kenneth Galbraith

I came across this quote in the first couple of years of my career, when I was pretty sure I knew nothing about economic forecasting, so I decided I had no choice but to plant my flag proudly in the first camp. In the 35 years or so that have elapsed since then, I haven't encountered anything new that dissuades me from thinking that initial assessment has changed. I still don't know *anything* for sure.

That doesn't mean I don't try to forecast. I own and lead a business. I have to plan for the future, and forecasting is a necessary evil in that process. It helps to inform me if I can hire someone or not, whether I can confidently award raises or not, and how wise it is to commit a greater portion of our budget to new long-term initiatives. I also advise clients, and I mentor colleagues in the art of providing personal advice concerning long-term financial decisions, and forecasting is a central part of that, too.

What it *does* mean is that I have learned to forecast with humility, to accept my limitations, to embrace ambiguity and uncertainty, to expect the unexpected, and to remind myself constantly of the old saw that "*if you want to make God laugh, tell him your plans.*" (My other favored reminder is a somewhat tougher quip from Mike Tyson: "*everyone has a plan 'till I punch him in the mouth.*")

Planning and forecasting for me is all about preparing for a range of things that might happen, and not about predicting exactly how and when they will play out. It's a way of defining and testing my most important objectives on the one hand, and then on the other hand coming to close grips with all of the things that might go wrong to keep me from achieving those objectives. It's a way of accounting for all my resources, and then screwing up my pugnacious determination *in advance* to improvise, adapt and overcome when things inevitably don't go as I expected. And that's not limited to economics.

Last quarter in my "Uncharted Territory" piece[1] for our Quarterly Report I wrote about the Lewis & Clark expedition, and the 8000 miles of completely unknown and unmapped wilderness they successfully traversed over the course of 1805 and 1806. It was an analogy for where we all find ourselves now.

I lit on that topic because some good friends and I (a group, by the way, that refers to itself appropriately as the "Plan B Paddlers") were planning a 7-day canoe expedition down part of the route that Lewis & Clark took along the Upper Missouri River in present day Montana, and the preparatory reading I had done for that trip struck a chord. A number of our clients subsequently reached out wishing me good luck and encouraging me to keep a journal and share some experiences on our return. Here are a few of the pertinent take-aways.

Foremost, this adventure was a phenomenal investment in my sense of wealth and well-being. Seven days and six nights in such a wild and scenic place without a single email, text message, telephone call, or anxiety-laden newspaper, website, or newscast does wonders for restoring the soul – especially after the last 17 months. To experience that in the close company of a handful of wise, trustworthy, interesting, engaging, well-read

[1] www.lsggroup.com/presidentsmessage-q12021

conversationalists who also treasure the outdoors is truly precious. And nothing beats wide-open spaces, sleeping under the stars, and daily physical exertion to lift the spirit.

But nothing was easy about escaping modernity, and all our plans went awry fast. Just to get there was a (now) comical ordeal of cancelled flights, suddenly decommissioned planes, creative re-routing from Great Falls to Helena, lost baggage, a disappearing baggage agent, a last-minute trip to a sporting goods mega-store to re-equip, and then paying some guy and his grandson for an improvised 3½ hour trek across the state in his dusty pickup truck to overcome the airline's incompetence. Stress.

The river was a different world. Not once did I ever see a single piece of trash, in the water or on the bank, for the entire 107 miles we paddled. Bald eagles were everywhere, soaring and circling above us in the updrafts, perched in the shade high along the eerily eroded cliffs, or watching like sentinels from the uppermost branches of gnarly old cottonwoods. Contrary to expectations, at least for the first half of the trip, the water was clear. We saw big fish everywhere. I missed it, but a couple of the others were startled as a Shovel-nosed Sturgeon half the length of their canoe swam beneath them. The current was a steady 4-5 miles an hour, reminding me how glad I was to be paddling downstream instead of hauling a fully loaded keelboat upstream, as the grunts in the Corps of Discovery had done over 200 years ago. At times we just drifted, silent and still as the current carried us along, eyeing the distant cliffs and crags above through binoculars for occasional views of elusive Desert Big Horn sheep. It made me sad to know that the lower banks had once been filled with millions of Buffalo.

We had expected warm days and chilly nights, as is normal for northern Montana at that time of year. In preparation, my friend Mark "The Canoe Sherpa", had loaded his special trailer with 100 lbs. of split Texas oak for firewood – along with all our gear and three canoes - and hauled it all the way from Austin. We packed that wood in a dry box in my canoe. But the weather that week turned out to be hotter than it was in Texas, and 100° days gave way to very sultry evenings. We never had a single campfire.

We stayed in four spots along the way that were original Lewis & Clark campsites. The most memorable was a site called McGarry Bar. The stars were bright when we turned in, like every other night, so none of us put a rain fly on our tents – it was too hot not to let the breeze in. Besides, when we'd left civilization 4 days earlier my iPhone had forecast nothing but clear skies. But at 2:15 am we awoke to chilly winds, rolling thunder, and lightning over the hills behind us. We barely had time to adapt before the skies opened up in one of the worst thunderstorms I've experienced. 3 hours of crashing thunder, hair raising lightening, driving rain and wind gusts that threatened to collapse our tents reinforced our ultimate powerlessness. All we could hope to do was hunker down and endure. And the next day we had to call an audible and layover another day just to dry out. We strung paracord between two cottonwoods and hung up our wet clothes and sleeping bags. Mark hung his entire tent from a stout branch and let it billow, kite-like, in the wind.

Our lives and our financial lives are no different. There are times of great wonder and reward, and other times of trial and fearsome challenge. For the unprepared or for the foolishly overconfident, sudden change provokes panic. 20/20 hindsight leads to recriminations and envy in the undisciplined and impatient. But the truth is that *nobody* truly knows what the future holds. So, for all their obvious limitations, a well thought out plan, a purposefully diverse reservoir of resources, and a deliberately resilient attitude are the only ways I know to succeed and prosper in the long run.

Thank you for your confidence and trust.

Thomas G. Twombly
President

Investment Commentary

As we move past the mid-point of 2021, the American economy is continuing its powerful recovery. Spurred by the wide distribution of highly effective vaccines against COVID-19, massive monetary and fiscal stimulus programs, and our own fundamental flexibility, ingenuity, and resilience – which ought never to be underestimated – this country has come back more quickly than virtually anyone expected at this time last year. This growing optimism is being reflected in financial markets.

Coming into 2021, the consensus earnings estimate for the S&P 500 Index was around $165. As this is being written, the consensus estimate for the coming 12 months has now reached $200 and is still being raised as the largest companies in the country demonstrate levels of innovation, efficiency and profitability that continue to surprise. Remote work, plummeting travel budgets, the rapid adoption of new technologies, and a new focus on innovation and adaptation as the way forward is transforming many businesses out there.

Investors have embraced that optimism. The S&P 500 closed the first half of 2021 at 4297, an increase of +15.3% since December 31, 2020, and a massive +92% gain since the shutdown-induced low of 2237 set back on March 23, 2020. Small and mid-sized U.S. companies have also shown remarkable capacity for flexibility and resilience, and the stalwart souls with disciplined allocations in these asset classes have been well rewarded as investment dollars have continued to flow their way. Since the beginning of this year the Russell 2000 Index of small-cap companies is up +17.5% and sports a gain of +134% since the third week of March of last year. The S&P 400 Index of mid-cap companies similarly shows gains of +16.2% for 2021 thus far and has risen almost +120% since those lows of last year. All of our clients have benefitted from holdings in these asset classes.

International economies, though in most cases slower in getting out of the starting blocks than the US due to tighter lockdowns and delayed vaccine rollouts, are also now experiencing solid recoveries. For the year thus far, developed market international equities have risen by a solid 9.2%, while emerging markets have gained 7.6% - despite heartbreaking numbers of reported COVID-19 deaths in some emerging market countries. But with vaccination rates that are now rising rapidly (see the chart on page 4) and with equity market valuation metrics that are still much lower than those of the US, along with very favorable long-term demographic tailwinds and solid trade surpluses, these economies and the revenues they generate remain important long-range investment components of all well-diversified portfolios, and certainly those of our clients.

As always, there are struggles to overcome, and plenty of reasons to remain sanguine about the challenges ahead. There will surely be surprises none of us can anticipate. The economy continues to contend with supply chain imbalances, as well as with an historic mismatch between the number of job openings available and a continued high (though rapidly declining) level of unemployment. Rising infection rates from new COVID variants continue to disrupt our sense of safety and security, and socio-political unrest continues worldwide. We are also still very much in the middle of an unprecedented experiment in both fiscal and monetary policy; the outcome of which remains impossible to forecast. The possibility that we have overstimulated the economy has been highlighted by a significant resurgence in inflation readings recently, and the financial press has predictably seized on this as the next existential threat and the reason we should all be gripped by fear.

Nevertheless, it's important to remind ourselves that many traditional economic indicators have been, and continue to be, grossly distorted by this convulsion we're still living through, and most of the year-over-year inflation metrics that have been quoted recently are anchored in the very worst months of last year. Those comparative rates of change may eventually smooth out considerably going forward, so we should be careful not to react reflexively right now. Certainly, statements by Fed Chairman Powell indicated a keen awareness of these issues and of these risks, and a promised readiness to act in contravention to them if necessary. Time, as always, will tell. Another area of concern for investors is the administration's proposals this spring with respect to changes in capital gains and estate taxes. The momentum behind these in tiatives seems to have ebbed recently, perhaps due to the looming specter of extremely tight contests in mid-term elections next year, but they bear watching. A resurgence in the probability of their eventual passage could alter substantially both the investment policies and the long-range financial plans of a great many prudent, long-term, buy and hold investors in this country – on both sides of the political spectrum.

Nonetheless, perhaps the most important economic revelation of the last six months came just a few days before the quarter ended. It was that household net worth in this country jumped +3.8% in the first quarter of 2021 – to $136.9 trillion – propelled by broad gains in equity markets and home prices. No doubt this trend will continue to show impressive progress once second quarter results are reported in the next several months. Equally as notable is the fact that the overall ratio of household debt to assets continued to fall steadily and is now down to about where it was 50 years ago.

The consumer powers the global economy, and the consumer has rarely carried more manageable debt levels relative to disposable income – and has simply never held more cash – than he or she does today. In June, the National Retail Foundation raised its outlook yet again; it now expects retail sales to grow 10.5% to 13.5% (that is $4.44 trillion to $4.56 trillion) year over year. Just this past month, with a nod to the anticipated sustainability of this, the retail giant Target raised its dividend by a whopping 32%.

Looking back from here, to the previous market peak on February 19, 2020 – just before the pandemic took hold – the S&P 500 closed at 3,386. It then proceeded to decline 34% in 33 days, amid the worst global health crisis in a century.

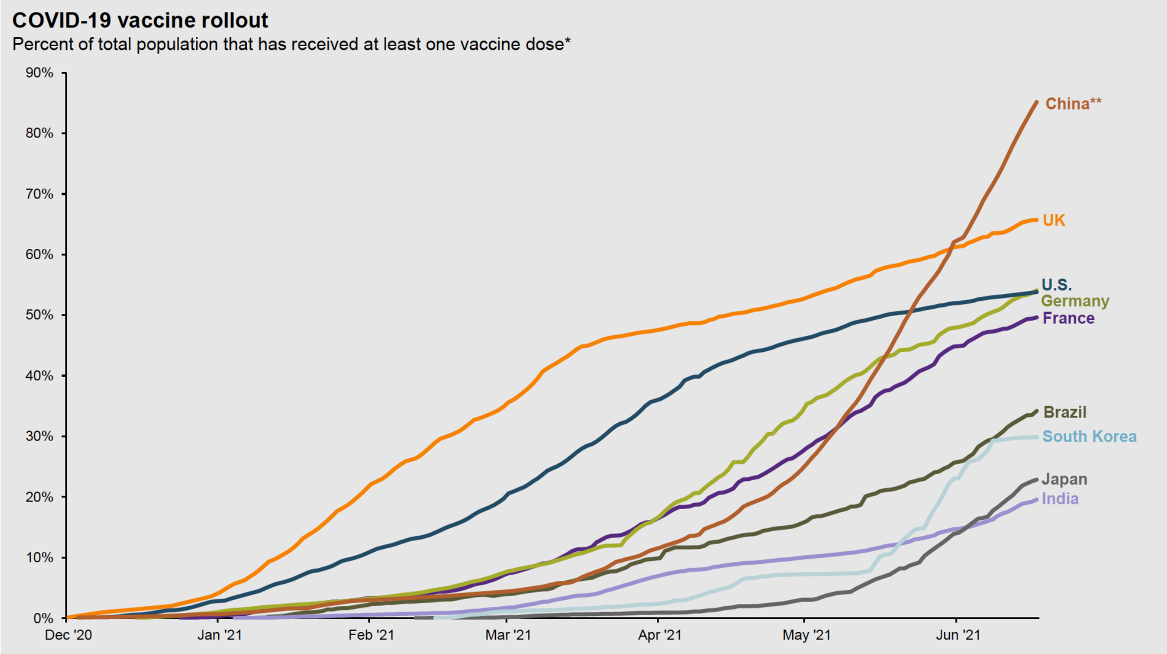
But if you had bought the Index at that epic top and were still holding it on June 30th of this year, your total return with reinvested dividends would have been almost 30%. For domestic mid cap and small cap indices those results would have been +31% and +38.8% respectively. We have never seen – and don't expect ever to see again – a more vivid demonstration of Peter Lynch's dictum that: "The real key to making money in stocks is not to get scared out of them."

Please give us a call if you would like to explore our perspective further, or if you have specific concerns about your personal situation. We're here to help.

International

Global COVID-19 vaccinations

GTM – U.S. | 57



Source: Our World in Data, J.P. Morgan Asset Management.
*This metric represents the share of the total population that has received at least one vaccine dose. If a person receives the second dose of a 2-dose vaccine, the metric stays the same. Share of total population may not equal the share that is fully vaccinated if the vaccine requires two doses.
**Data for China represents cumulative doses administered per 100 people, as China does not report the breakdown of doses administered by first and second doses.
Guide to the Markets – U.S. Data are as of June 30, 2021.

J.P.Morgan Asset Management

General Market Results

	2nd Quarter	YTD	One Year	Three Year	Five Year	Ten Year
Barclays Agg Bond	1.83	-1.60	-0.33	5.34	3.03	3.39
S&P 500	8.55	15.25	40.79	18.67	17.65	14.84
DJI	5.08	13.79	36.34	15.02	16.66	13.50
S&P 400	3.64	17.59	53.24	13.17	14.29	12.40
Russell 2000	4.29	17.54	62.03	13.52	16.47	12.34
NASDAQ	9.68	12.92	45.23	25.72	25.80	19.32
MSCI EAFE	5.17	8.83	32.35	8.27	10.28	5.89
MSCI EM	5.05	7.45	40.90	11.27	13.03	4.28

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