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THE ECONOMY AT A GLANCE

ECONOMIC HIGHLIGHTS

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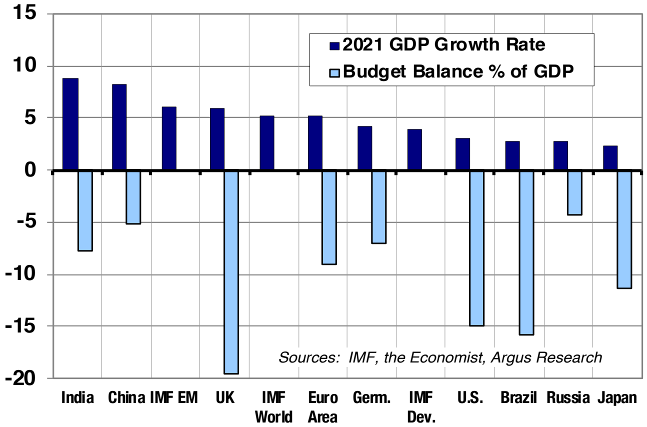
BETTER GLOBAL GROWTH FORECAST FOR 2021

The IMF now projects global growth of 5.5% for 2021 – up from its prior forecast of 5.2% and a rebound from the global GDP decline of 3.5% in 2020. The IMF expects that emerging markets will grow the fastest (at an average rate of 6.3%). Developed economies are expected to grow at an average rate of 4.3%, the Eurozone should grow at a 4.2% clip, and U.S. growth is forecast at 5.1%. We take this with a grain of salt, as catalysts for economic weakness abound in Europe; two of the BRICS, Brazil and Russia, are forecast to grow a relatively modest 3.6% and 3.0%, respectively; and Japan is expected to grow just 3.1%. Much of the global recovery will depend on the distribution of COVID-19 vaccines, and we anticipate that wealthier nations will have more success in this area.

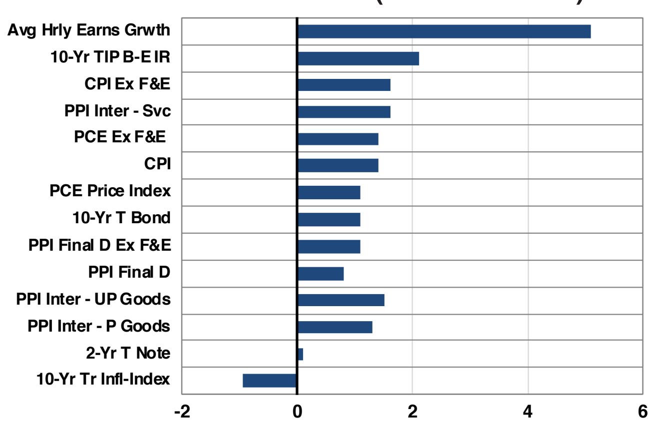
GLOBAL GDP FORECASTS (%)



INFLATION TICKS HIGHER

Most inflation measures remain below the Fed's target of 2.0%, though on average they are up month-over-month. We track 14 inflation measures on a monthly basis. On average, they indicate that prices are rising at a 1.55% rate. Looking at core inflation, our reading is 1.7%. With this backdrop, we expect the Fed to focus on reducing unemployment and backstopping the financial markets, and to keep short-term rates close to zero until at least 2022. This is not to say there aren't threats that inflation may surge at some point. For example, as Western and Asian populations age, there may be a shortage of workers. Further, aging populations and their healthcare needs may encourage politicians to increase deficit spending.

INFLATION MEASURES (% CHANGE Y/Y)



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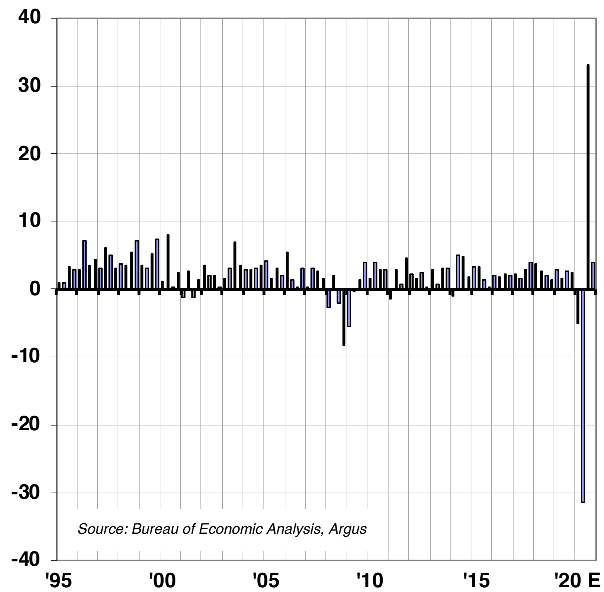
GDP EXPANDS 4% IN 4Q

After two quarters of wild swings, the U.S. GDP growth rate settled down in 4Q20 to an annualized 4.0%. The fourth-quarter increase in real GDP reflected increases in exports (at a 22% rate), business investment (25%), consumer spending (2.5%), housing investment (33.5%), and inventory investment. Those were offset partially by a decrease in government spending (down 1.2%). Imports, a subtraction in the calculation of GDP, increased. For 2020, real GDP decreased 3.5% (from the 2019 annual level to the 2020 annual level), compared to an increase of 2.2% in 2019. On an absolute basis, despite two quarters of recovery, current GDP of $21.5 trillion is about 1% below pre-pandemic levels. Meanwhile, COVID-19 continues to spread, despite the early rollout of vaccines. While we do not expect a double-dip recession in the coming quarters, the country's recovery from the pandemic is likely to remain a challenge, with growth in the low single digits likely.

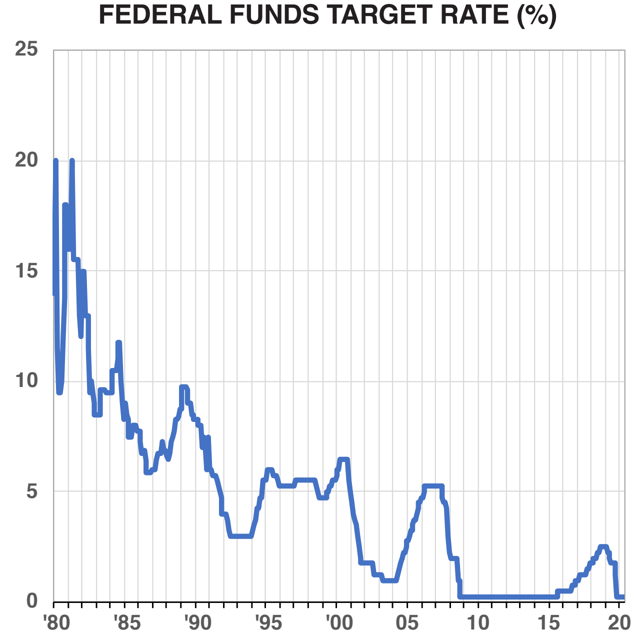
REAL GDP (% GROWTH/QTR)



FED HOLDS STEADY ON RATES

At its recent Open Market Committee meeting, the Federal Reserve decided to maintain the federal funds rate at a rock-bottom 0.00%-0.25%. The action (or non-action) had been widely expected given the current high level of unemployment and little pressure on inflation. The vote was unanimous, and the Fed continues to forecast no changes in rates through at least 2022. In his comments after the meeting, Fed Chairman Jerome Powell noted that he believed the bigger risk to the economy is doing too little, rather than doing too much (remember that the central bank is also purchasing $120 billion in Treasuries and mortgage-backed securities each month). One thing we don't expect the Fed to do is to lower interest rates to below zero. Although that strategy has been used in some countries, it is not clear to Chairman Powell that the tool works; after all, the economies in Europe and Japan that have deployed negative rates continue to struggle. Further, he does not think it is appropriate in the U.S. given the country's dependence on money-market mutual funds.

FEDERAL FUNDS TARGET RATE (%)

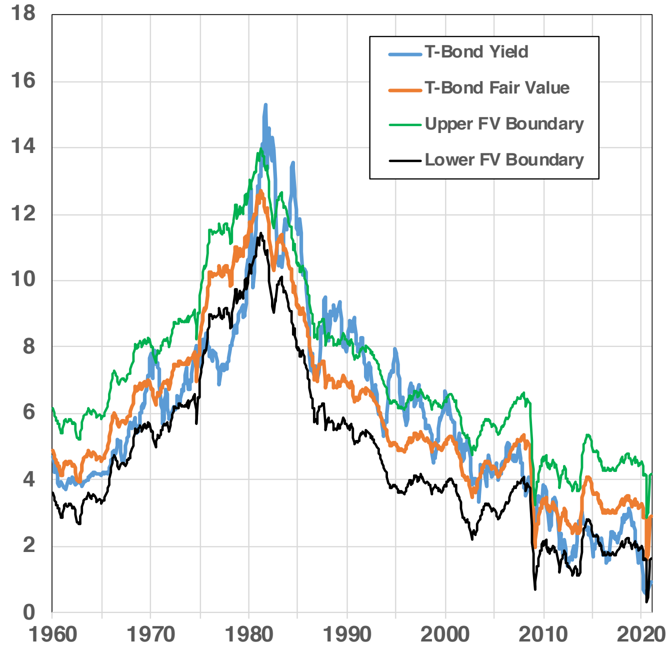


FINANCIAL MARKET HIGHLIGHTS

BONDS YIELDS OUTSIDE OF FAIR VALUE RANGE

Our proprietary Treasury Note Yield Model is signaling that bond yields, which have climbed 50 basis points in recent months, are still too low based on fundamentals. Our model discounts factors such as current yields, GDP growth and long-term inflation, as well as stock prices and earnings. We smooth trends out over a five-year period to avoid short-term momentum swings. Our current 10-year T-bond fair value yield is 2.90%. The normal valuation range has a floor of 1.6% and a ceiling of 4.10%. The current 10-year bond yield is around 1.1%, below the low end of the fundamental range and far from fair value. From an asset-allocation standpoint, we think that bonds remain fully valued compared to stocks and recommend that long-term investors modestly favor equity securities in their diversified portfolios. We typically break the fixed-income component of a portfolio into four areas: Core, such as the industry benchmark ETF AGG or Treasuries; Inflation-Indexed; Opportunistic, such as securitized debt, corporate debt, high-yield, or floating-rate bonds or preferreds; and Cash. We currently favor the Core and Opportunistic segments. On duration, we recommend intermediate-term bonds.

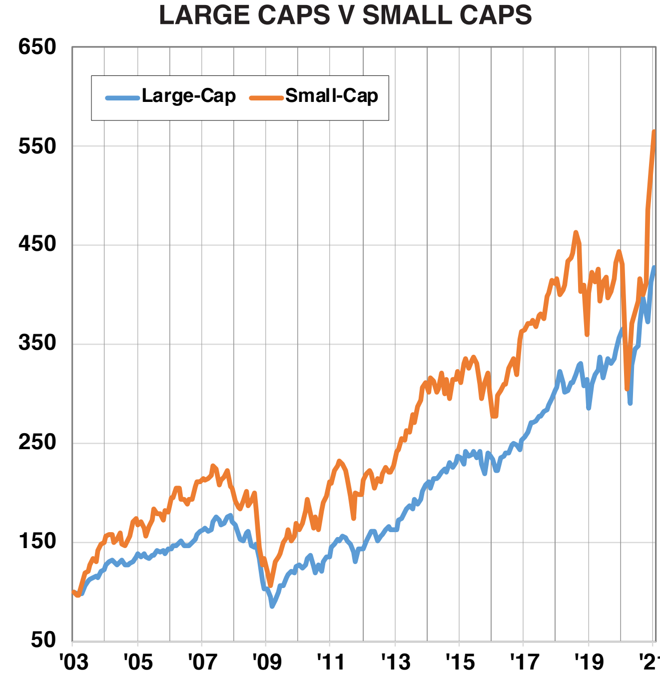
TREASURY NOTE YIELD MODEL (%)



SMALL- AND MID-CAP OPPORTUNITIES

Small- and mid-cap stocks (SMID stocks) have surged over the past quarter and outperformed large-caps over the past 12 months. They may also be in a better position to generate market-beating returns going forward. For one thing, most SMID companies focus on domestic markets and their businesses appear poised to rebound quickly once COVID-19 vaccines are widely distributed. For another, SMID stocks generally trade at lower multiples than large-caps; the P/E ratio on the Russell 2000 Small Cap Index is 20.3, compared to 28.3 for the S&P 500. The long-term record also favors SMID stocks over large-caps. From 2003 to 2020, the Russell 2000 climbed 465% compared to an advance of 327% for the S&P 500. Yet SMID stocks can be risky. Large-caps outperformed SMID stocks in 10 of the 18 years of our test period. Annual returns were negative four times for both, but the average decline for SMID stocks was 16% in down years versus 12% for large-caps. Despite the risks, diversified investors will have exposure to small- and mid-caps based on their long-term performance record. We estimate that 20%-25% of the U.S. stock market's capitalization is comprised of small- and mid-cap stocks.

LARGE CAPS V SMALL CAPS



ECONOMIC CALENDAR

Previous Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
1-Feb	ISM Manufacturing	January	60.7	60.0	59.8	NA
	Construction Spending	December	0.9%	1.0%	0.8%	NA
3-Feb	ISM Non-Manufacturing	January	57.2	57.0	56.9	NA
4-Feb	Factory Orders	December	1.0%	1.8%	1.8%	NA
	Non-farm Productivity	4Q	4.6%	1.0%	-2.7%	NA
	Unit Labor Costs	4Q	-6.6%	4.0%	4.0%	NA
5-Feb	Trade Balance	December	-$68.1 Bln.	-$68.0 Bln.	-$66.4 Bln.	NA
	Non-farm Payrolls	January	-140 K	75 K	100 K	NA
	Average Weekly Hours	January	34.7	34.7	34.7	NA
	Average Hourly Earnings	January	0.8%	0.5%	0.3%	NA
	Unemployment Rate	January	6.7%	6.7%	6.7%	NA

Next Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
17-Feb	Retail Sales	January	-0.7%	NA	NA	NA
	Retail Sales; ex-autos	January	-1.4%	NA	NA	NA
	Business Inventories	December	0.5%	NA	NA	NA
	Industrial Production	January	1.6%	NA	NA	NA
	Capacity Utilization	January	74.5%	NA	NA	NA
	PPI Final Demand	January	0.3%	NA	NA	NA
	PPI ex-Food & Energy	January	0.1%	NA	NA	NA
18-Feb	Import Price Index	January	0.9%	NA	NA	NA
	Housing Starts	January	1669 K	NA	NA	NA
19-Feb	Existing Home Sales	January	$6.76 Mil.	NA	NA	NA