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Market Comment:

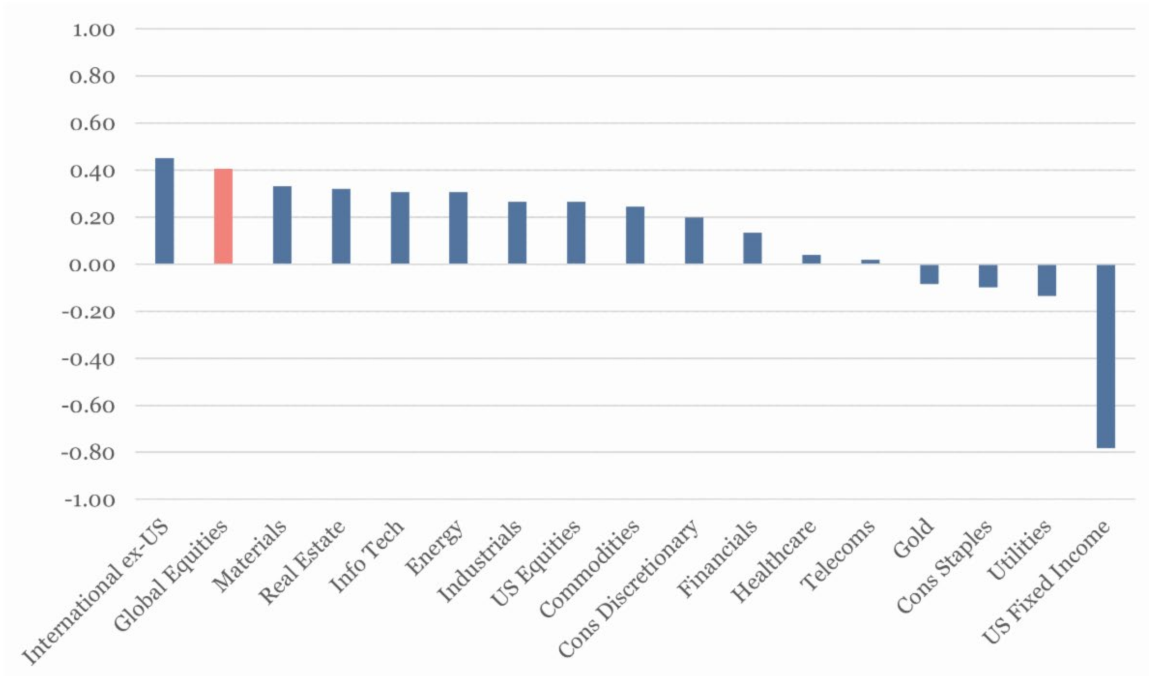
It is likely that inflation will pick up throughout the course of 2021 due to both *base effects* (Inflation was quite low in 2020, so even modest inflation this year will produce 2-4% year-over-year inflation prints.) and economic reopening. The Fed points to market-based measures of inflation expectations, which have been stable around 2%, as evidence that any sharp pick-up in inflation will be transitory. However, we sympathize with many investors that are less certain about the transitory nature of higher inflation.

In January, we published a weekly commentary that concluded global equities have done a better job of protecting portfolios from inflation than gold, commodities, Bitcoin, or Treasury Inflation Protected Securities (TIPS). As a follow up, we received questions asking whether it is worthwhile to over-allocate to specific parts of the equity market as an inflation hedging strategy. The answer is "probably not."

Historically, a globally diversified equity portfolio (U.S. and international equities) has been more effective for combating sharp upticks in inflation than allocating to any specific equity sector, commodities, or gold (Fig. 1). For readers comparing a U.S. versus global approach, global equities generally offer a better inflation hedge than a U.S.-only equity portfolio because higher inflation typically coincides with U.S. dollar weakness.

This analysis reinforces a concern we also raised in January: investors that hold most of their assets in fixed income (or cash) should be very concerned about inflation risk and seek ways to maintain a palatable risk profile while reducing their reliance on fixed income. Sharp upticks in inflation — transitory or not — can quickly lead to negative real returns and the erosion of purchasing power in their portfolios.

Fig. 1: Correlations between various investments and the 12-month change in inflation expectations



Source: Bloomberg, Federal Reserve Bank of Cleveland, Mill Creek. Results cover period from 1990- February 2021.

Updated Benchmark Performance:

Benchmark Performance by Asset Class	Week-to-Date	Month-to-Date	Year-to-Date
U.S. Large Cap Equities	0.42%	0.42%	2.48%
U.S. Small Cap Equities	-0.38%	-0.38%	11.15%
International Developed Equities	-0.49%	-0.49%	0.66%
Emerging Markets Equities	0.05%	0.05%	3.91%
Global Equities	0.11%	0.11%	1.96%
U.S. Bonds	-0.80%	-0.80%	-2.93%
Intermediate Municipal Bonds	0.28%	0.28%	-0.38%
High Yield Bonds	-0.16%	-0.16%	0.54%
Oil	7.67%	7.67%	34.54%
Gold	-1.75%	-1.75%	-10.56%
Key Rates	**3/5/2021**	**12/31/2020**	**3/5/2020**
U.S. 2 Year Treasury Note	0.14	0.13	0.59
U.S. 10 Year Treasury Note	1.56	0.93	0.92

Week in Review:

Equities were choppy and Treasury yields continued rallying last week following positive economic data and a simultaneous increase in inflation expectations. Data from last week included:

- **Jobless claims totaled 745,000**, bringing the four-week moving average to just below 800,000, the lowest level since December. The number, while improving, remains above a pre-pandemic peak of 695,000.

- **The U.S. economy added 379,000 jobs in February versus 200,000 expected by economists.** Restaurants and hospitality businesses began hiring again as the economy continues to re-open.

- **The February unemployment rate ticked down to 6.2%**, slightly better than the 6.3% economists predicted. While the labor market shows signs of improvement, the U.S. still had 9.5 million fewer jobs in February than a year ago.

– **Average 30-year mortgage rates rose above 3% for the first time since July**, weighing on refinancing and home purchases.

– **Five-year inflation expectations exceeded 2.5% for the first time since 2008**. The Institute for Supply Management reported rising prices and manufacturing backlogs due to strong demand. Measures of prices paid jumped to their highest levels since 2008.

Economic Calendar:

– 3/10: Consumer Price Index
– 3/12: Consumer Sentiment
– 3/12: Producer Price Index

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Indices Used: U.S. Large Cap equities: Russell 1000 Index, U.S. Small Cap Equities: Russell 2000 Index, International Developed Equities: MSCI EAFE Index, Emerging Market Equities: MSCI Emerging Markets Index, U.S. Bonds: Barclays Aggregate Bond Index, U.S. 10 Year Treasury Note: Bloomberg 10 Yr. Treasury Note, Municipal Bonds: Barclays Intermediate Municipal Bond Total Return Index, High Yield Bonds: Barclays U.S. High Yield Total Return Index, Oil: Bloomberg WTI Crude Sub-Index Total Return Index, Gold: Bloomberg Gold Sub-Index Total Return Index