FIRST QUARTER,
MARCH 31, 2021

MARKET COMMENTARY

Would you rather receive $100 today or $100 one year from now? This might seem like a silly question, because, all else equal, a rational actor will always prefer a dollar today over a dollar tomorrow. Dollars have utility. They can be exchanged in the present for goods and services, or they can be invested into profitable ventures.

Therefore, in order to be convinced to wait a year to receive $100, you might require compensation, say $5. This changes the choice: $100 today or $105 one year from now. If you don't have much need for $100 today, then $5 might be just enough to convince you to wait. After all, $5 is equal to a 5% rate of return. However, if you really need the $100 today (to pay rent or to buy food, perhaps), then $5 is unlikely to be enough to sway your decision. That's because, to you, the $100 has significant utility in the present. In this scenario, perhaps you would require a future payout of $200, or a return of 100%, in order to forego consumption today.

Notice what we just did. We translated the utility of money into a rate of return, an interest rate. That's all interest rates are, a way to determine the value of money, to equate the value of future dollars with the value of present dollars. If $105 one year from now is enough to convince you to forgo $100 today, then we can conclude the following:

$100 today > $100 one year from now

$100 today = $105 one year from now

Generally speaking, money has more utility and more value when it is scarce. When money is scarce, interest rates tend to be higher. Money has relatively less utility and less value when it is readily available. When there is a lot of money floating around, interest rates tend to be lower.

Using a variety of mechanisms, such as open market operations, the Federal Reserve will increase and decrease the supply of money to influence the direction of interest rates and keep them within a policy range. This policy range relates back to the Fed's goals for inflation and unemployment. For example, during periods of economic stress, the Fed will purchase securities in the open market, which floods the market with cash and puts downward pressure on interest rates. Lower interest rates means lower borrowing costs across the economy, which in turn stimulates consumption, reignites hiring, and reduces unemployment.

> "...because the economy is always in a state of flux, interest rates are always changing."

As you might guess, because the economy is always in a state of flux, interest rates are always changing. Sometimes they change by a lot and sometimes they change by a little. Investors are keenly aware of interest rates – both their magnitude and their direction. When you invest, you forego utility in the present. In exchange, you receive compensation in the future, and this compensation is determined, at least in part, by the level of interest rates in the broad economy.

This brings us to our next point. The value of an investment today can be impacted by the value of its payout in the future. All else equal, an investment that pays out a lot in the future is worth more in the present than an investment that pays out very little. Looked at another way, the same investment will be worth less in the present when interest rates are high and more in the present when interest rates are low. Let's look at an example.

You are considering an investment that will pay you $10,000 five years from now. How much should you pay for this investment? The answer is it depends. Specifically, it depends on the value of money – it depends on interest rates. Let's compare two scenarios, one where a fair market, five-year interest rate is 3% and one where it is 10%. Think of this interest rate as the rate of return you would require over the life of the investment. The math works out as follows:

Paying $8,626 today and receiving $10,000 in five years would be a 3% rate of return

Paying $6,209 today and receiving $10,000 in five years would be a 10% rate of return

Notice how the price today falls as the required rate of return (the interest rate) rises. This is the same premise as our original $100 versus $105 versus $200 discussion above. The only difference is that, in the first example, we fixed today's value at $100 and adjusted the future value to account for the return. In this second example, we fixed the future value at $10,000 and adjusted the value in the present to account for the return.

This helps to explain bonds over the past quarter. Like the stock market, the bond market is forward looking. Participants in the bond market are constantly trying to predict the future level of interest rates across a range of maturities (future dates), and these predictions become manifest in bond prices. As much as the Fed might try to keep interest rates contained within a specific policy range, sometimes trading in the bond market can overcome the Fed's efforts and drive interest rates up or down.

"...the first quarter bond market sell-off surely caught some investors by surprise."

In the first quarter, bond market activity pushed interest rates significantly higher. For example, the interest rate on the five-year Treasury note more than doubled, from 0.377% at the start of the quarter to 0.799% at the end. The interest rate on the ten-year Treasury bond increased from 0.957% to 1.706%. As with our example above, higher interest rates pushed down the value of bonds in the present. The Bloomberg Barclays Aggregate Bond Index, a broad measure of U.S.-based investment-grade bonds with maturities between one and ten years, declined 3.37% on the quarter. Long-term bonds fared even worse, with the Bloomberg Barclays Long-Term U.S. Treasury Index dropping 13.51%.

Typically, investors purchase bonds for their stability, and the first quarter bond market sell-off surely caught some investors by surprise. However, that's how bonds work. When interest rates rise, bond prices fall. The longer the term, the further the fall. Bond markets are complex, and there was more than one reason for the surge in rates. An improving economy coupled with the vaccine rollout and additional stimulus all contributed. An improved economic outlook means the Fed might increase its policy range sooner than expected, and additional stimulus runs the risk of contributing to heightened inflation down the road – a key determinant of interest rates.

For our part, we did a pretty good job anticipating this shift and adjusting client portfolios accordingly. At the end of September, we closed out positions in long-term bonds for most clients. Then, in early-to-mid February, we further reduced duration by about one year, on average. Across all client bond portfolios, the average decline, therefore, was less than 1%.

What happens in the bond market often filters through to the stock market, and vice versa. In the first quarter, the sharp increase in rates led to wild trading and sharp selloffs in high-growth stocks, particularly NASDAQ-listed stocks and stocks that had gone public in the past year via special-purpose acquisition companies (SPACs). From mid-February to the first week of March, the NASDAQ declined 10.45%. Year-to-date, the NASDAQ is positive but still 6.02% off its highs.

The reason for the selloff in growth stocks was the same as in our above example – when an investment's cash flows exist far out in the future and interest rates rise, prices fall in the present. In the case of growth stocks, the lion's share of cash flows are way out in the future, sometimes decades. Therefore, as with long-term bonds, growth stocks get hit particularly hard when interest rates rise.

Value-leaning stocks, on the other hand, had a strong quarter, in part because they tend to pay cash flows in the present (dividends) – making them less susceptible to interest rate increases. In addition, value stocks have benefitted from a months-long rotation out of growth into value and out of "stay at home" into "reopening" plays. The Dow Jones Industrial Average, which has a value tilt (and was left for dead for much of 2020), came back to life in the first quarter with a return of 8.29%. This bested the S&P 500 Index, which also turned in a respectable 6.17%.

"...we expect heightened volatility in the months ahead, both in bonds and stocks."

Looking forward, we expect heightened volatility in the months ahead, both in bonds and stocks. That said, we think stocks will finish the year in positive territory, and, on a relative basis, we view stocks more favorably than bonds over the long term at these prices. Interest rates are still low in a historical context, despite the recent increase, and bonds will struggle to overcome inflation until rates rise further. For now, low rates plus fiscal stimulus and an economic reopening should provide a tailwind for stocks. Of course, certain portions of the stock market continue to look expensive, even after this quarter's pullback in some of the most speculative names. There is always the risk that the bursting of a few mini bubbles here and there could lead to broader market contagion. For this reason, we continue to pay careful attention to valuations. This is also an

SPOTLIGHT ON COMMUNITY

Deighan Wealth Advisors is proud to be a founding donor in the Maine Justice Foundation's work to address interpersonal and systemic racism. This work is urgent, and it is important to the future of Maine. The fund is beginning to bear fruit with a first-ever round of grants in April. These six Maine groups are working with incarcerated BIPOC youth, encouraging civic engagement, improving equity for BIPOC Mainers and immigrants in the workforce, and telling the stories and challenges of BIPOC Mainers.

Learn more about the fund and these great organizations at **www.justicemaine.org**.

Deighan Wealth Advisors believes that vibrant communities are built on the hard work and commitment of dedicated citizens. Deighan Wealth Advisors values its ongoing support of diversity initiatives through state and local multicultural, arts, and educational advocacy. We are dedicated to helping our Maine communities grow and thrive.

argument to remain invested in bonds, despite the challenges of the past quarter. Diversification is as important now as ever, and we plan to continue managing interest rate risk while doing our best to seek yield.

As always, we hope this commentary finds you and yours both happy and healthy. We look forward to any questions you might have and wish you a warm and wonderful spring.

PLANNING CORNER

Revocable Trust Planning

Revocable trusts, also commonly referred to as Living Trusts or Revocable Living Trusts, are popular estate planning vehicles. These trusts come with benefits and drawbacks. Typically utilized to avoid probate and provide for management of assets in the event of incapacity and after death, revocable trusts can be very effective, but can be complicated and involve lots of decisions.

A trust is essentially a vessel, an empty vase, in the hands of a trustee, who manages and administers the trust, for the benefit of beneficiaries. The Grantor or creator of the trust typically decides what assets will go into the vessel to become a trust asset. When a Grantor transfers an asset to the trust, the Grantor individually no longer owns that asset. The trust owns the asset. The Grantor may serve as trustee of the trust, but title ownership of the asset is in the name of the trust.

Typically, the Grantor serves as trustee and beneficiary of the trust during life, retaining total control over all trust assets. These trusts usually contain language stating that even if the Grantor is not the trustee, the Grantor can demand any distribution from the trust at any time. Upon the incapacity of the Grantor, the Trustee will continue to manage the trust assets for the benefit of the Grantor, and often the Grantor's spouse and family as well. After the death of the Grantor, the trust may terminate, or may divide into continuing trusts for the benefit of the Grantor's spouse and children.

Benefits

Avoid Probate
A primary benefit of a revocable trust is that assets in trust avoid probate. The probate process exists to administer the transfer of title to a decedent's heirs or beneficiaries. In probate court, this is done through a Last Will and Testament, or via the laws of intestacy if a person dies without a will. If a decedent owns property in multiple states, probate will be needed in each state where property is owned. If assets are owned by a revocable trust, the terms of the trust will direct how the property is to be managed or transferred to the intended beneficiary, avoiding the necessity for multiple probate proceedings.

Ease of Management
In the event of incapacity, it is often easier for a trustee to manage trust assets than for an agent under power of attorney to manage a number of accounts. Having centralized management in a trust can create streamlined management for a fiduciary stepping into a Grantor's shoes. It is not unusual for large financial institutions to accept trustee authority much more readily than the authority of an agent under power of attorney.

Continuation Trusts
If a Grantor wishes to have the trust continue on after his or her death, a revocable trust is designed to become irrevocable after the death of the Grantor and can provide for the creation of a number of additional trusts for family members after the death of the Grantor. If there is legacy real estate, such as a camp, that the Grantor wishes to maintain for generations to come, such a trust could be incorporated into a revocable trust. Having all these sub-trusts delineated in a single document creates efficiencies in management and administration.

Drawbacks

Expense
Revocable trusts are typically more expensive to create than simple wills. However, it is often prudent for Grantors to absorb the cost of creating a detailed estate plan, rather than leaving heirs and fiduciaries to litigate over meaning and intention, potentially wasting estate assets that were carefully preserved for their benefit. The cost of a revocable trust may prove much less than the cost of probate administration, particularly if multi-state probate will be needed.

Complexity
A revocable trust can be a complicated document with many moving pieces, particularly after the death of the Grantor. If avoiding probate is a primary purpose of the trust, care must be taken to transfer all probate assets into the trust before the death of the Grantor. One missed account

SOUNDBYTES

Deighan Wealth Advisors is a long-time supporter of the Bangor Symphony Orchestra, and we are thrilled that this year's Symphony Soiree was another resounding success. The evening featured amazing musical performances and a silent auction full of wonderful, donated items. All proceeds from the virtual event will benefit the BSO and its education programs.

We are pleased to support Maine Public's All Books Considered. This Maine Public virtual club features a book from a preeminent Maine author every two months and a virtual meeting attended by the author and hosted by either Jennifer Rooks or Cindy Han from Maine Calling. There is no cost to participate, and several local bookstores provide a discount to anyone purchasing an All Books Considered book club title.

Congratulations to Jean Deighan who will be honored as one the state's most distinguished businesswomen by Junior Achievement of Maine's 2021 Business Hall of Fame North.

Jenifer Butler was elected to serve on the Board of Trustees of Northern Light Eastern Maine Medical Center.

could trigger the need for probate of the Grantor's estate, eliminating the benefit of a trust planned carefully to avoid probate.

No Creditor Protection
Because the Grantor typically retains control over all assets during life, revocable trusts generally do not protect assets from creditor claims. Nor do revocable trusts protect assets for long term care expenses/Medicaid eligibility. Creditor protection can be obtained through irrevocable trusts, which most often requires that Grantors cede control over and access to their assets, an extreme measure recommended only in rare circumstances.

Decisions
Revocable trusts require the Grantor to make many decisions well in advance of implementation. Who will be the trustee if the Grantor cannot serve? Should assets go outright to survivors after the death of the Grantor or remain in trust? For how long? What will the terms for distribution be? The good news is that these trusts can be amended any time during the life of the Grantor as relationships and circumstances change.

Often choosing successor fiduciaries is a difficult decision for Grantors. It is common for other responsible family members to serve as successor trustee after the death or incapacity of the Grantor. But where there are no immediate family members with a sophisticated understanding of the assets, or where putting a family member in the position of trustee would create family tensions, a third party trustee may be the best solution. Third party trustees will typically charge a fee for trust administration. Banks, accountants, attorneys, and investment advisors often offer such fiduciary services. A third party trustee should be someone the Grantor trusts, and often is a trusted professional who understands the family dynamics and needs of the beneficiaries.

Revocable trusts can be a great vehicle for continuing a family legacy and provide the Grantor with an opportunity to create a roadmap for the care and maintenance of family members after death. These are not simple trusts, however, and involve not only a host of thoughtful decisions in creation, but attention to funding and management to achieve the goals of the Grantor. As a fiduciary, Deighan Wealth Advisors can serve as a third party trustee if desired. We are always available to review your estate plan to ensure that your plan will meet your intent.

PORTFOLIO CHANGES

Throughout 2020, we had a growth tilt in our international equity portfolios, and this worked in our favor. However, in early 2021, we decided to shift a bit more toward value, consistent with the rotation we were seeing out of growth. To that end, we added a small position in the Causeway International Value Fund (CIVVX). As a firm, Causeway has a value focus. The fund itself is managed by a long-tenured team, and its performance has historically been in the top quartile among peers.

On the domestic side of equity portfolios, things were a bit reversed. We had a slight value bias throughout 2020 into 2021. We therefore viewed the pullback in growth stocks mid-quarter as an opportunity to move toward a more neutral mixture of growth versus value. We eliminated positions in the ProShares S&P 500 Dividend Aristocrats ETF (NOBL) where appropriate and replaced the allocation with investments in the Schwab U.S. Large-Cap ETF (SCHX) and the Schwab U.S. Large-Cap Growth ETF (SCHG). Both of the Schwab ETFs provide exposure to their respective indices at an extremely low cost.

In addition to the above, we also initiated a position in Alibaba Group Holding, Ltd. (BABA), the world's largest online and mobile commerce company. Alibaba operates China's most-visited online marketplaces, including Taobao and Tmall. Shares are trading at a significant discount to our estimate of fair value and represent a buying opportunity, in our opinion.

Regeneron Pharmaceuticals, Inc. (REGN) was another addition in the quarter. Regeneron has capitalized on its monoclonal antibody research to drive profitability and generate cash flow. Medicines and pipeline products target macular degeneration, allergic and inflammatory diseases, cancer, cardiovascular and metabolic diseases, infectious diseases (including a COVID cocktail), pain and rare diseases.

Lastly, as touched upon in our Market Commentary, we took steps to reduce duration in client portfolios. As part of this strategy, we added the Water Island Credit Opportunities Fund (ARCFX), a short-duration fund that has low correlation with traditional bonds. ARCFX focuses on a broad range of catalysts and events, such as mergers, refinancings, deep value credit, and regulatory changes via investments in bonds, bank loans, convertibles, and preferred stocks.

DEIGHAN
WEALTH ADVISORS

TELEPHONE 207-990-1117
www.deighan.com
DEIGHAN WEALTH ADVISORS
455 HARLOW STREET
BANGOR, ME 04401

LUCIE E. ESTABROOK, CTFA
CHIEF EXECUTIVE OFFICER
PRINCIPAL
lucieestabrook@deighan.com

JENNIFER L. EASTMAN, JD
CHIEF OPERATIONS OFFICER
PRINCIPAL
jennifereastman@deighan.com

MATTHEW T. SKAVES, CFA
CHIEF INVESTMENT OFFICER
matthewskaves@deighan.com

JENIFER L. BUTLER, CFA, CFP®
SENIOR ADVISOR
PRINCIPAL
jeniferbutler@deighan.com

TYLER D. HOXIE, CFA
INVESTMENT ANALYST
tylerhoxie@deighan.com

ALISON L. BERUBE
OPERATIONS ASSOCIATE
alisonberube@deighan.com

DONNA A. BUSHEY
CLIENT RELATIONS SPECIALIST
donnabushey@deighan.com