JAG CAPITAL MANAGEMENT LLC

Quarterly Comments

Celebration(ish) Economy

Important and welcome progress in the global war versus COVID-19 continues apace. As of early July, over 182 million people — almost 55% of the total American population — have received at least one dose of the vaccine (source: ourworldindata.org). The Centers for Disease Control (CDC)'s May relaxation of mask guidance opened the path to normalized work and social activities in the US for those who are fully vaccinated. This is due largely to widespread adoption of vaccinations and the high probability that the US population is crossing the threshold into herd immunity.

Economic Activity Ramps Up

Not coincidentally, economic activity has ramped up significantly as consumers and businesses have re-oriented to some version of a post-COVID reality. Although many growth statistics are obviously skewed by the fact that the year-over-year data is now lapping the dismal statistics from early/mid-2020, we are now seeing some of the most robust economic growth data ever seen or likely to witness again in the near future.

US GDP (Gross Domestic Product) increased at an annual rate of 6.4%[1] in the first quarter and is on pace for an annual rate of +7.9%[2] for the second quarter. After peaking at almost 15% in April 2020, the civilian unemployment rate collapsed to less than 6%[3] by June 2021. Indeed, there is now arguably a labor shortage. Despite wage growth of 4.6% — the highest year-over-year growth in wages since the early 1980's — many businesses are finding it difficult to fill open positions. The National Federation of Independent Business (NFIB) May survey showed that 48% of small businesses had at least one job they were unable to fill. This is the highest such survey result for this datapoint since 1975.

Disconnect Between Labor Supply & Demand

Like most phenomena in the markets and economy, the drivers behind the disconnect between labor supply and demand is a complex topic which resists simple explanations. For investors, the current imbalance in the labor force raises a myriad of questions that will be addressed by corporations and businesses over the coming months and years. For example, in parts of the service and manufacturing industries, a persistent shortage of workers will likely spur companies to increase the scale and pace of investments in automation and technology. A faster and more widespread move to automate jobs and tasks will, in turn, create longer-term challenges for policymakers as they seek to craft unemployment benefits and labor policies that address the changing landscape of the job market. This inevitable tension between human capital and technological innovation has been occurring for more than a century, but rarely, if ever, with the current intensity.

Source: Cartoonistgroup.com

Firm Highlights

- **Five interns are working for JAG this summer** on various projects. They hail from Washington University, Southern Methodist University, Saint Louis University, Southern Illinois University Edwardsville, and Miami University/Ohio.
- **JAG's Chicago office has expanded and moved to Chicago's iconic and beloved Wrigley Building at 400 North Michigan Avenue.** We welcome visitors!

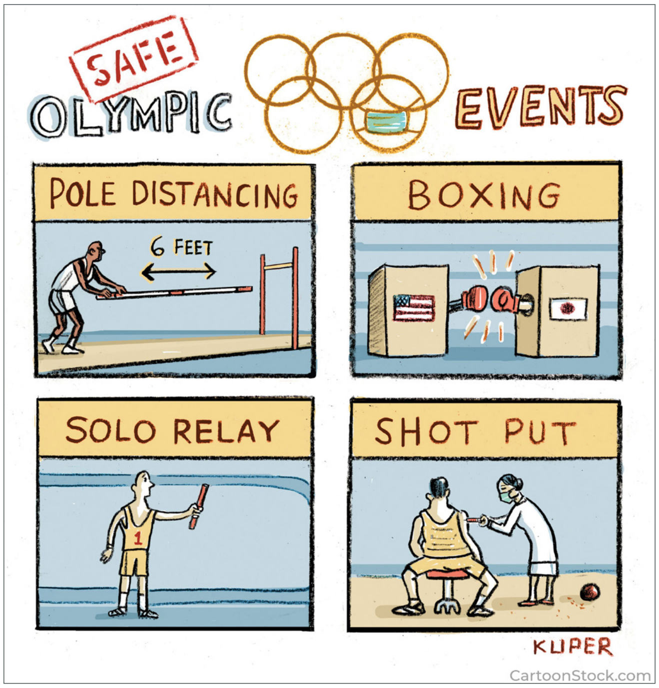
Our JAG Investment Framework

Thanks in large part to the Internet and endless volumes of data, over-confident predictions on all manner of economic and

1. Source: Bureau of Economic Analysis (BEA) Q1-21 GDP Report.
2. Source: Atlanta Fed's GDPNow estimates.
3. Source: Bureau of Labor Statistics (BLS) Employment Report.

Our JAG Investment Framework (Continued)

investment topics have never been as abundant, while solid and thoughtful insights are rarer than ever. For many investors, this turbulent mosaic of facts, opinions, and prognostications can be disorienting. At JAG, we navigate the incessant noise of the markets by relying on the tools, processes, and investment approaches that we have built over the years and seek to continuously improve. Per Warren Buffett, "Forecasts may tell you a great deal about the forecaster; they tell you nothing about the future." Our investment framework does not rely upon specific or granular forecasts of the near- or intermediate-term future states of the markets, economy, or even individual companies. Rather, we utilize a disciplined and repeatable process to identify specific investments to build focused but diversified portfolios that we believe offer high odds of favorable long-term returns. Our approach may not be as provocative as the over-confident daily forecasts offered up by some of our more bombastic brethren in the media. But we long ago made the choice to favor success over bluster — and we have no plans to change.



Source: Cartooncollections.com

Inflation Risks

Not surprisingly, the colliding forces of economic re-opening, supply chain disruptions, tight labor market conditions, rising wages, commodity price spikes, and more government stimulus has raised the specter of "higher for longer" inflation. Capital markets spent much of the spring trying to reckon with inflation risks in real time, which is inherently a messy process given the Federal Reserve's ongoing attempts to shape inflation expectations amid economic re-opening. According to Bloomberg, within the context of fluctuating inflation expectations, 10-year Treasury yields began 2021 at 0.92%, ramped to 1.74% by the end of March, before ending the 2nd quarter at 1.45%. Within the context of ultra-low global interest rates, this level of volatility in Treasury yields is quite rare and reflects a fair amount of disagreement within the markets. Fed Chairman Powell and most of his colleagues on the Federal Open Market Committee believe that recent inflationary pressures are "transitory," but the truth is that no one can be sure about the precise future path or trajectory of prices for goods and services.

Stocks & Inflation

For most of the year thus far, many stocks of long-moribund companies have risen in part from the perception that they will benefit from higher commodity prices. Also, interest rate sensitive companies have outperformed secular growth companies in the Information Technology and Communication Services sectors. The inflation narrative reached a fever pitch in May. Although prices for many commodities were ramping early this year, lumber prices got special attention from the financial media. The importance of lumber as a key input to residential housing construction, combined with a widespread shortage of single-family homes in many geographies, caused many observers to flag skyrocketing lumber futures as the apparent harbinger of persistent price pressures in the broader economy. According to FactSet, reality eventually prevailed over far-fetched expectations and near-term lumber futures prices peaked on May 7, before slumping by 47.6% through June 23.

Lumber Price Peak vs. Inflation

Interestingly — and ironically — the peak in lumber prices coincided nearly perfectly with Barron's magazine May 14th cover story, which blared **The I** [Inflation] **Word**, with the sub-title "Inflation is heating up fast — and it could last longer than many think. How to protect your portfolio." These sorts of loud media headlines may produce anxiety or calm, depending upon the reader's point of view. In reality, they are intentionally crafted to sell newspapers and attract clicks online. In hindsight, Barron's cover story appears to have marked an inflection point in fears of accelerating inflation expectations. It is important to note that inflation expectations and absolute price levels are not the same. Even as short-term inflationary pricing pressures subside, absolute price levels may remain elevated for prolonged periods of time. It continues to be critically important to differentiate investment opportunities and risks within this context. This cannot easily be done through passive investments in index funds, which is why we believe our disciplined and active approach to investment management is particularly well suited to this environment.

Risks & Opportunities

Inflation is one of the many risks and opportunities that JAG monitors for our clients. When it comes to managing portfolios in the context of an ambiguous future, we often think of John Maynard Keynes' admonition that "it is better to be roughly right than precisely wrong." Our quest to maintain and grow the long-term purchasing power of our clients' capital does not require us to make precise forecasts on the future of interest rates, inflation, or commodity prices. Our mandate compels us to carefully apprise the always-changing investment landscape and evaluate and invest in individual companies that can successfully grow their revenue and earnings over time regardless of short- or intermediate-term fluctuations in the macroeconomic trends. Broadly speaking, from a qualitative perspective we strongly favor companies who have earned the right to maintain strong pricing power for their goods and services.

These types of companies can be broadly referred to as "price **makers**," in that their market position and standing with their customers allows them to increase the prices charged for their products (within reason) without compelling their customers to flee to a competitor. On the other hand, we try to avoid investing in "price **taker**" enterprises, which have little to no pricing power in their served markets. These types of companies typically sell commodities or services, in which all producers are forced to accept the prevailing market prices for their goods or services.

We are also keeping abreast of the various legislative and policy agendas that are being proposed by the Administration and Congress. Corporate and personal taxes are likely to be a focus in the second half of 2021, with potential changes coming to income tax rates and potentially dramatic adjustments to estate taxes. Although it is too soon to discern the contours of the new tax landscape, it is possible that investors and advisors will need to revisit and optimize their strategies to adapt to significantly different tax policies beginning late this year or early in 2022. We will be watching closely.

Market Outlook

There is an array of investment opportunities and challenges that we expect to present themselves in the coming months, including the prospects for greater infrastructure spending, the growing importance of corporate cybersecurity, the digitization of healthcare, and the global drive towards renewable energy. As always, markets are being buffeted by short-term crosswinds, headwinds, and tailwinds. Long-term, we continue to find attractive opportunities and we see a favorable path ahead for prudently constructed active investment portfolios.

We at JAG remain hard at work to position clients' portfolios for long-term success. Our responsibility is to successfully navigate these markets and develop the strongest investment ideas that can survive and thrive in the future.

Enjoy the Summer!

Warm regards,

Norm Conley
CEO, Chief Investment Officer &
Portfolio Manager

Mike Kimbarovsky
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Disclosures

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