2020 Second Quarter Commentary and Outlook

After falling sharply due to the spread of the COVID-19 pandemic during the first quarter of 2020, U.S. equity markets staged their largest quarterly gain since the fourth quarter of 1998. Unprecedented accommodative action from the Federal Reserve and record stimulus packages passed by the U.S. Congress helped start the rally in late March. The rebound in equities during the second quarter was further aided by optimism for the development of a vaccine and effective treatments for the novel coronavirus, the gradual reopening of the economy, better-than-expected economic data and speculation of additional government stimulus. The S&P 500 ended the second quarter up 20.5%, its strongest showing in over two decades. Global equities, as represented by the MSCI All Country World Index, also had a strong recovery, gaining 19.4% for the period.

Index / Market	Q2 2020	1H 2020
Dow Jones Industrial Average	18.51%	-8.43%
S&P 500	20.54%	-3.08%
S&P 400 (Mid Cap)	24.07%	-12.78%
NASDAQ	30.95%	12.67%
Wilshire 5000	21.94%	-3.30%
Russell 2000 (Small Cap)	25.42%	-12.98%
MSCI Europe	15.57%	-12.43%
MSCI EAFE	15.08%	-11.07%
MSCI Emerging Markets	18.18%	-9.67%
MSCI All Country World	19.39%	-5.99%
MSCI All Country World ex USA	16.30%	-10.76%

All S&P 500 equity sectors were positive for the quarter led by consumer discretionary, which was driven by market optimism of an economic recovery to its best quarterly gain on record, climbing by over 32%. The technology sector climbed over 30% for the quarter, as the market continued to demonstrate confidence in this sector's ability to better navigate the new economic realities resulting from the crisis. Rounding out the top three performing sectors, energy stocks rose by over 30%, fueled by rebounding oil prices. The more defensive utilities and consumer staples sectors lagged, gaining only 2.7% and 8.1%, respectively. For the first half of the year, technology remained the leading sector up 15%, while energy was the worst performer down -35.3%, with financials not far behind down -23.6%.

From a style standpoint, growth continued to substantially outperform value during the second quarter – the Russell 1000 Growth Index was up 27.8%, while the Russell 1000 Value Index was up 14.3% – as investors continued to show more confidence in the resilience and future potential for tech companies and others poised for growth. This was further demonstrated by the Nasdaq Composite Index, which returned over 30% during the quarter to bring first half performance to 12.67%, creating multiple record highs in the process. For the year, growth has outpaced value by over 26%. From a market capitalization perspective, mid-cap and small-cap stocks outperformed large-cap, likely due to having suffered steeper declines than large cap during the first quarter. The S&P 400 and Russell 2000 Indices gained 24.1% and 25.4%, respectively vs. a 20.5% return for the S&P 500. Through the first half of 2020, however, the mid and small cap indices have underperformed the S&P 500 by nearly 10%.

The U.S. Treasury market was largely unchanged for the second quarter. The market entered the period on the heels of the Federal Reserve rapidly bringing short-term interest rates to 0%, leaving the yield curve positively sloped and long-term rates near historic lows. The 10 year U.S. Treasury ended the quarter yielding 0.66%. The extent of the Fed's resolve to keep credit flowing was highlighted by its announcement in early April that it would buy exchange traded funds holding high yield bonds. This led to the U.S. high yield market, as reflected by the Barclays U.S. High Yield Index, rising by over 10%, its best quarterly performance in over a decade. Investment grade corporate debt also benefited from the Fed's purchases, with the Barclays U.S. Corporate Bond Index gaining nearly 11.36 % for the quarter. After experiencing a sharp decline and extraordinary volatility during the first quarter amidst larger concerns with state and local governments' ability to meet their obligations in light of the economic slowdown, the municipal bond market rebounded as the Federal Reserve and Congress's aggressive actions to stabilize the overall economy helped allay fears of a total meltdown. The Fed's launch of the Municipal Liquidity Facility (MLF) further boosted investor confidence in the municipal market. Although municipals have bounced back from their lows, we remain cautious going forward, as we expect state and municipal budgets to remain under stress.

Index / Market	**Q2 2020**	**1H 2020**
Barclays U.S. Aggregate Index	2.90%	6.14%
Barclays U.S. Corporate Bond Index	11.36%	6.34%
Barclays U.S. High Yield Index	10.38%	-2.19%
Barclays U.S. Treasury Index	0.48%	8.71%
Barclays U.S. Municipal Bond Index	2.72%	2.08%

While strong second quarter equity market performance reflected optimism for a return to better days, the economic data released through the past three months have painted a more mixed picture. The unemployment rate peaked at 14.7% in April and fell to 11.1% in June after 7.5 million jobs were recovered in May and June. However, new unemployment claims exceeded 1.3 million in each week of the quarter. Consumer spending, the largest and most consistent driving force for U.S. economic growth, fell by 12.6% in April as lockdowns were forced, but rose 8.2% in May as all parts of the country entered reopening phases and the spread of coronavirus in the Sunbelt states had not yet begun in force. Second quarter GDP declined 32.9% although GDP expectations for the full year are expected to rebound to a decline of 5-7% annualized.

Outlook

We will continue to closely monitor and analyze several key themes through the third quarter that can help provide more clarity regarding the direction of the economy and financial markets.

Resurgence of COVID-19 and Status of Therapeutic and Vaccine Development

After a period of declining infection rates and coronavirus-related deaths, several states began reopening businesses and public services, only to see a resurgence of COVID-19 cases. In response, many governors decelerated the restart of their economies and mandated stricter safety measures, which in turn slowed second quarter market gains. Infectious disease officials and leading scientists remain optimistic that the development of a vaccine is inevitable, and markets have reacted positively with any positive news from pharmaceutical companies. However,

experience has shown that developing effective and safe vaccines can be elusive, and the timing very unpredictable. It also remains uncertain how quickly a vaccine can be delivered to the public and whether enough Americans will be willing to take a vaccine to achieve "herd immunity." The optimism of the equity markets undoubtedly is linked to the success of a vaccine, and disappointing developments on this front could lead to increased volatility.

Labor Markets

Unemployment remains at near-historic levels despite significant job recoveries in May and June. As many households limit their spending due to lost income and others remain more conservative, businesses will continue to be impacted, potentially leading to additional layoffs in the coming months. Additionally, with jobs in food services, entertainment, and travel and leisure being particularly hard-hit, and with no certainty that there will be a return to normalcy in the near-term, finding employment in other industries will likely present a challenge for these workers. State and local governments also are under financial pressure to reduce spending in the face of declining sales tax and income tax revenue, which may lead to public sector layoffs. Uncertainty regarding the opening of schools also impacts whether some parents will be able to work even if jobs are available. It took nearly seven years for the U.S. economy to recover the 8.7 million jobs lost during the Great Recession of 2007-2009, so expectations are for a long, drawn-out recovery from the current level of unemployment. Ultimately any sustained recovery of the job market will require effective containment of coronavirus.

Consumer Spending

Despite rebounding in the second quarter, the U.S. consumer faces potential challenges going forward. As noted above, any slowdown or reversal in business activity will impact employment. To date income has been supported by $1,200 stimulus checks and the $600-per-week Federal support to unemployment benefits, which are set to expire at the end of this month. Congress is poised to pass a bill authorizing a second round of stimulus checks and to extend unemployment subsidies, although perhaps at a lower level. A return to U.S. GDP growth ultimately will require consumer sentiment and spending to rise.

Corporate Earnings

Wall Street consensus estimates that second quarter corporate earnings will fall by approximately 44% year-over-year, in what is expected to be the nadir of the earnings recession. However, a substantial number of companies in the S&P 500 have suspended forward guidance, underscoring the challenge for analysts and investors to value equity markets today. The potential slowdown of the economic recovery and any setback to consumer confidence and spending would further increase the uncertainty surrounding future corporate earnings. This could prove to be a significant headwind to equities, as many stocks are trading on optimistic earnings outlooks for the second half of 2020 and for 2021.

Monetary & Fiscal Policy

At every turn throughout the pandemic, the Federal Reserve has demonstrated with both words and actions that it will do whatever is necessary to maintain the liquidity and stability of the financial markets. Federal stimulus packages also have contributed heavily to the stabilization of

the economy and relief to businesses and consumers, and more Federal spending is highly anticipated. However, businesses in sectors heavily affected by coronavirus may struggle to survive even with government support. States have been vocal about the need for further Federal support, but there is reticence in Washington to support pre-pandemic fiscal problems. Individuals undoubtedly will face grim choices if Federal subsidies are reduced. The markets have rallied on the back of monetary and fiscal stimulus but questions remain about how far this can go.

U.S. Election Season and Geopolitical Concerns

In the second half of the year, the U.S. faces what will almost certainly be a polarizing and contentious 2020 election cycle. The outcome of Presidential and Congressional elections could dramatically impact the economy and financial markets, as material changes to tax policy, healthcare, the minimum wage, infrastructure and environmental policy are at issue. The possibility of further social unrest throughout the country and the government's response looms large. Additionally, tensions between the U.S. and China are growing and Brexit remains unresolved. We believe the environment is ripe for continued market volatility throughout the remainder of the year.

Housing

Not surprisingly, the overall housing market has been negatively impacted by the pandemic. Housing starts fell drastically, falling over 26% from March to April, representing the slowest pace of new home construction since the first quarter of 2015. Existing home sales also fell by over 20% during this time period. After the initial decline early in the second quarter, the housing market saw a jump in home sales, driven by a decline in supply and an increase of buyers in the suburbs due to fears of coronavirus spread in densely populated cities and the desire for more space in which to shelter at home. Homebuilder confidence has rebounded nicely, and the ability of the real estate industry to operate effectively under social distancing restrictions is also a positive sign. Mortgage rates have remained quite low, supporting mobility. However, a meaningful recovery in housing will likely only begin once the job market starts to recover in earnest.

Portfolio Construction

Within the equity portfolio we continue to favor larger companies as we think that companies with larger balance sheets are better positioned than smaller firms to survive any potential extended economic decline. We also have tilted the portfolio towards growth-oriented companies, particularly technology firms that can adapt to and prosper from the new economic reality resulting from the pandemic

During the quarter we made two shifts within the fixed income portfolio to better position client portfolios in light of the low interest rate environment. First, we added exposure to two ultra-short term bond ETFs. The funds hold investment grade securities with a duration of under one year and seek to deliver a higher yield than cash. Given the credit quality and the support being provided by the Federal Reserve to the bond market, we felt that this was a prudent decision for clients. We also shifted our short term Treasury bill investment to a new ETF, ticker SGOV, as a means to reduce fees and maximize yield.

We believe the portfolio is positioned to successfully navigate the uncertain times ahead, while preserving the ability to participate in the upside should equity markets continue to rally. The KLS Investment Committee continues to be vigilant in assessing the ever-changing market environment and we will modify client portfolios as appropriate. As always, we encourage you to reach out to your KLS Advisor with any questions that you may have on the economic landscape, the capital markets, or regarding your specific circumstances.

We continue to wish you and your families the very best during this challenging time.

July 30, 2020

The above commentary represents the economic and market views of our firm. We remind you, however, that each client's portfolio is managed individually. Please speak with your KLS advisor with respect to your personal circumstances and individual portfolio performance.

The opinions expressed and information contained in this publication are given in good faith, may be subject to change without notice, and are as of the date issued. This publication discusses general market activity, industry or sector trends, or other broad-based economic, market or political conditions and should not be construed as research or investment advice and does not represent a complete analysis of every material fact with respect to the economy, financial markets, interest rates, and any industry or sector mentioned in the publication. The graphs and charts presented were created for informational purpose only and may use data sourced from third parties. The accuracy and completeness of sourced data is believed to be reliable, but has not been independently verified.

About KLS, A Division of Boston Private

KLS, A Division of Boston Private is a division of Boston Private Wealth. Boston Private Wealth offers investment management & consulting, wealth advisory and planning, and family office services as well as private banking and trust services in partnership with its parent company, Boston Private Bank & Trust Company.

Investments are not insured by the FDIC or any other government agency, are not guaranteed by Boston Private Bank & Trust Company or its subsidiaries, affiliates or parent company, may lose value, and are not a bank deposit.

The information contained in this material is not intended for distribution to, or use by, any person or entity in any jurisdiction or country where such distribution would be contrary to law or regulation or which would subject Boston Private Bank & Trust Company or its subsidiaries or affiliates to any registration requirement within such jurisdiction or country. The information in this material is not intended as an offer or solicitation for the purchase of stock, any other security or any financial instrument of Boston Private Bank & Trust Company or any other issuer or company.

© 2020 All Rights Reserved.

Investments are not insured by the FDIC or any other government agency, are not guaranteed by Boston Private Bank & Trust Company or its subsidiaries, affiliates or parent company, may lose value, and are not a Bank deposit.