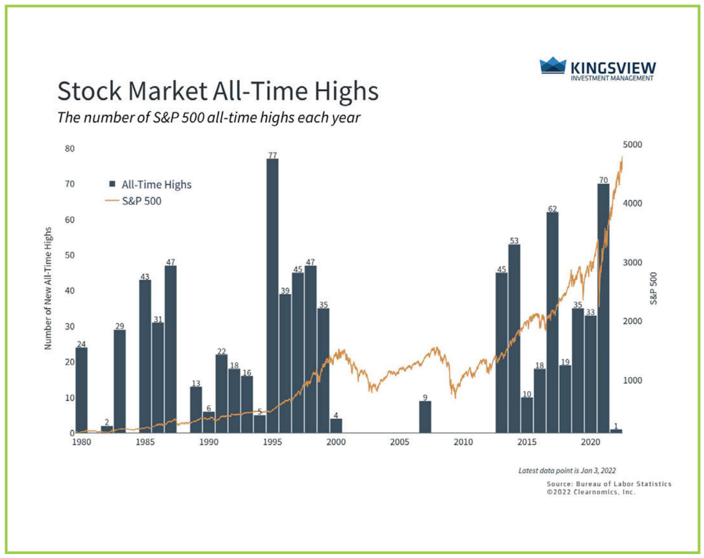
Portfolio Manager Insights

Weekly Investor Commentary | January 5, 2022
Investment Committee

With the ups and downs of the market and the on-going pandemic, the fact that we are approaching the third year of the business cycle may surprise some investors. After the headlines of the past year, one might expect that the market would have struggled. Events during this period include the attack on the U.S. Capitol, the delta and omicron variants, the foreign policy disaster in Afghanistan, Fed tapering, challenges passing new fiscal bills, reddit trades, the rise of cryptocurrencies, China's bursting housing bubble, inflation at multi-decade highs, supply chain disruptions, and many more. As in most years, there was no shortage of reasons to be pessimistic in 2021.

Yet, the S&P 500 gained nearly 29% with dividends over the course of the year and 119% since March 2020, finishing near all-time highs. Even though markets felt choppy, 2021 was objectively one of the least volatile years on record. There were rotations within the market throughout the year, but in the end, growth stocks gained 26% and value stocks 25%. International developed markets rose 12% and although emerging market equities lost -2% in 2021, they are up 70% from the 2020 bottom. This all occurred even though the 10-year Treasury yield jumped to 1.5% and the Fed is set to tighten policy in the coming months.

MARKETS CAN DO WELL WHEN INVESTORS LEAST EXPECT IT



Key Takeaways:

1. **Despite ongoing concerns around a variety of issues, the S&P 500 achieved 70 new record closes in 2021. This is the most since 1995 during the early stages of the dot-com boom.**
2. **This is not unusual - the U.S. stock market has historically risen over long periods of time and, by definition, spends much of each cycle at new all-time highs.**

2020 and 2021 both underscore the importance of staying invested and diversified. The path of markets and the economy are difficult if not impossible to predict, even in the face of a once-in-a-century pandemic or skyrocketing inflation. These lessons will also likely be true of 2022 regardless of what transpires. Already, investors are worried about a possible first Fed rate hike by mid-year, the midterm election in November, and whether inflation will ease or worsen in the second half of the year.

In times like these, it can help to focus on the big picture. Although every market cycle is different, we are still quite early in this expansion. The underlying economic trends are strong with businesses growing, earnings rising and employees finding better jobs and higher wages. Inflation is elevated but much of this is due to year-over-year comparisons and supply chain disruptions. High inflation could become "sticky" and sour the mood among businesses and consumers, but it could also begin to subside later this year.

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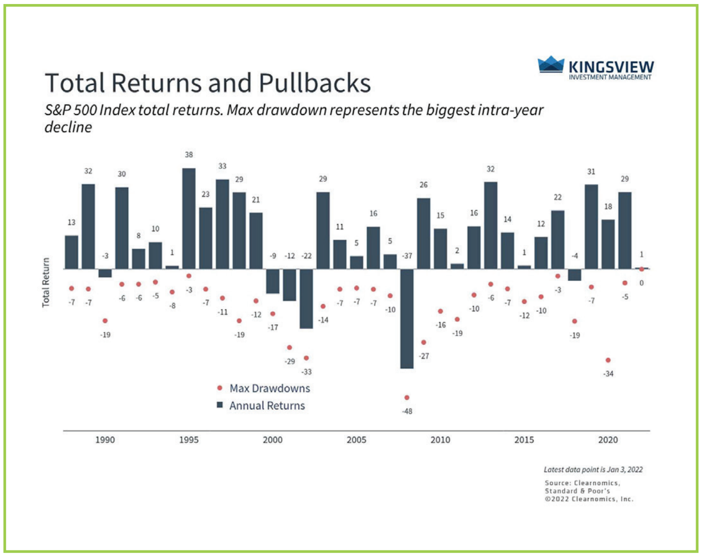
Even without rising inflation, the Fed would reasonably be expected to raise rates at this stage in the cycle. After all, their job is now to make sure the economy doesn't overheat. And although we are still in the middle of another delta/omicron surge, this is having a smaller impact on economic growth and will likely subside as well - until the next variant is discovered.

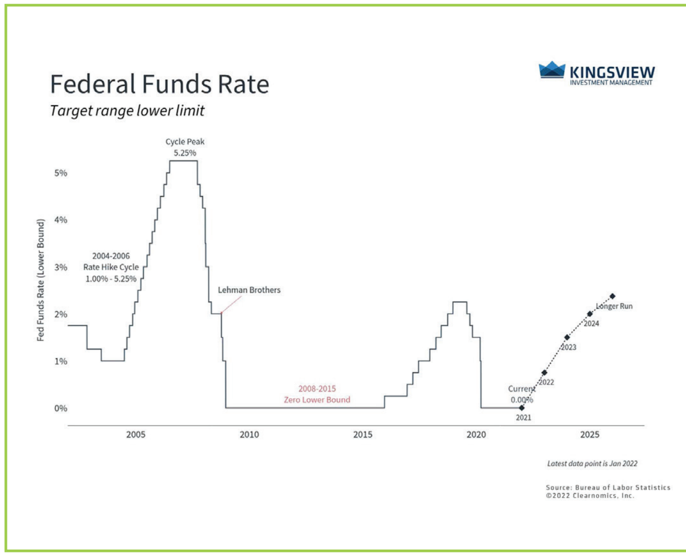
INVESTORS SHOULD EXPECT MORE UNCERTAINTY



Key Takeaways:

1. **Despite the stellar performance of stocks over the past two years, investors were constantly worried on a day-to-day basis. In reality, 2021 was one of the least volatile years on record with only a single 5% pullback that occurred at the end of the third quarter. Thus, there was a wide disconnect between how investors felt and how markets actually performed.**
2. **At the same time, investors should always expect greater uncertainty and volatility in the stock market. After all, the willingness to take appropriate risks is why investors are rewarded in the long run. Last year's volatility fell far short of the average decline experienced by the S&P 500 each year.**

FED RATE HIKES ARE ONLY THE BEGINNING, NOT THE END, OF THE CYCLE



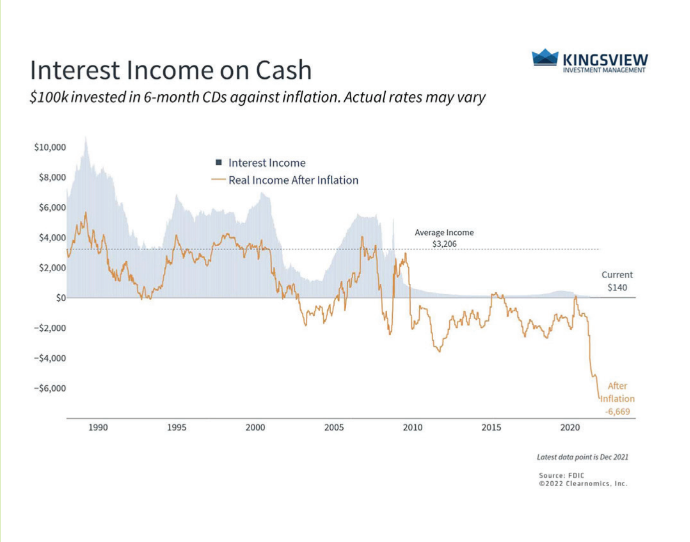
Key Takeaways:

1. **The Fed has accelerated its taper process, which reduces the amount of bonds it purchases each month, and is expected to raise rates by the middle of the year.**
2. **Although this will no doubt continue to drive market volatility, Fed rate hikes are normal and justified if the economy is doing well. Fed officials currently expect three rate hikes in 2022.**

Controversy over these topics is what fuels the day-to-day market debate. Rather than trying to accurately predict every outcome and incur trading costs, the better approach that has worked for decades is to hold an appropriately diversified portfolio that can withstand these uncertainties, while benefiting from the long-term growth of markets and the economy. Doing so in a way that is aligned with broader financial goals, especially with the guidance of a trusted advisor, has stood the test of time.

The commentary highlights five key lessons of the past year that will no doubt carry forward into 2022 and beyond.

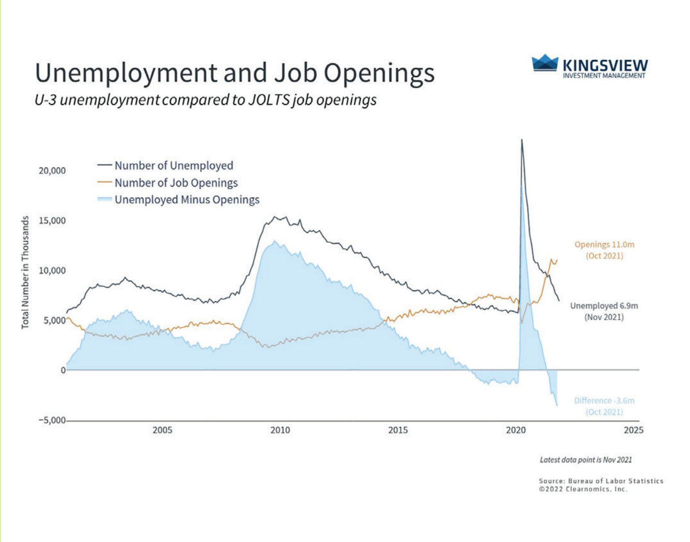
THE VALUE OF CASH IS ERODED BY INFLATION



Key Takeaway:

1. **Rising inflation has a number of implications for the economy and investment portfolios. For many, however, the primary challenge is that inflation erodes the value of hard-earned cash savings. This underscores the need to properly invest this cash to generate a return in order to preserve purchasing power over time.**

MANY PARTS OF THE ECONOMY ARE BOOMING



Key Takeaways:

1. **The economy is doing well. Businesses are hiring at a rapid pace and job openings exceed the number of unemployed individuals.**
2. **Over time, workers who had previously given up may re-join the labor force while others may receive new job training. Ultimately, this is a positive sign for the economy in the years to come.**