WRAPPING UP A SCORCHING YEAR: DECEMBER 2021 MARKETS REPOSITIONING

JANUARY 2022

Omicron: No Match For Markets

Omicron has been spreading quickly, proving to be the most contagious COVID-19 strain yet.[3] Countries worldwide are shattering case records, and the U.S. broke its one-day case record in the final days of December.[4]

Initial concern gave way to relief upon evidence that omicron appears to be milder than its predecessors. A government statement said that while the variant is highly transmissible, it comes with lower hospitalization rates than other waves, along with an insignificant increase in deaths.[5] Fareed Abdullah of the South African Medical Research Council compared omicron in South Africa to a "flash flood" rather than a wave.[6]

That said, healthcare systems are still in danger of being overwhelmed due to the contagiousness of the disease, and unvaccinated people are still getting gravely ill.[7] Schools are also re-evaluating whether to delay re-openings from winter break.[8] However, vaccines and boosters are proving effective against severe disease, and antiviral pill treatments from Pfizer and Merck were FDA approved in December.[9] In short, we have more tools to deal with COVID and are finding ways to manage it without shutting the economy down.

Markets have come to terms with this, and despite over 580,000 reported cases on December 30,[10] both the Dow and S&P 500 saw more intraday record highs.[11] This came on the heels of a six-day and four-day win streak for the indexes, respectively. Most impressively, the S&P 500 had its best December in 11 years.

QUICK TAKE

December 2021 started on shaky ground, with a perfect storm of the Omicron variant, hot inflation readings, and prospects of an accelerating Fed rate hike cycle triggering profit-taking, tax-loss selling, and portfolio repositioning.[1]

However, global equity markets proceeded to power through December. The S&P 500 equity index gained 4.4% in December, ending the year up 27% for a third straight year of double-digit gains.[2]

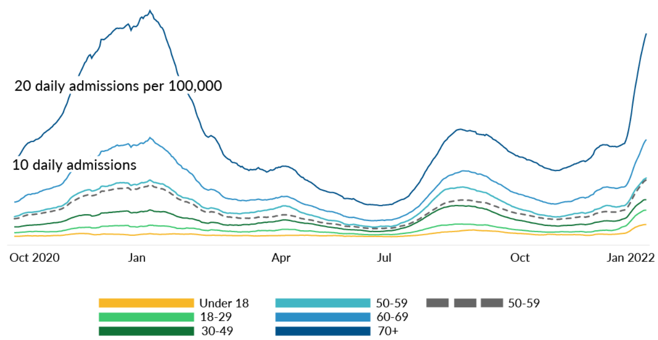
Index Returns
(December 2021 and Year To Date)

Bloomberg Barclays Aggregate Bond Index US investment grade bonds	-0.26% for December*	-1.54% for the year*
S&P 500 Index Large US Equities	4.36% for December*	26.89% for the year*
MSCI World Index Large/mid developed world equities (ex-US, CAN)	4.30% for December*	22.35% for the year*
MSCI Europe Index Large/mid developed european equities	6.61% for December*	16.97% for the year*
MSCI Emerging Markets Index Global emerging market equities	1.92% for December*	-2.22% for the year*

* As of December 31, 2021

Daily New Hospital Admissions by Age

This chart shows for each age group the number of people per 100,000 that were newly admitted to a hospital with Covid-19 each day, according to data reported by hospitals to the U.S. Department of Health and Human Services.



Sources: U.S. Department of Health and Human Services (daily confirmed and suspected Covid-19 hospital admissions); Census Bureau (population data). Data prior to October 2020 was unreliable. Data reported in the most recent seven days may be incomplete.

Tech Underperformance

Perhaps in part due to November outperformance, the tech-heavy Nasdaq underperformed the Dow Jones and S&P 500 indexes in December.[14] As markets became more comfortable with the fight against omicron, "stay-at-home" stocks started to look less fashionable.[15] Some tech weakness can also be attributed to inflation and the prospects of rising rates and tighter Fed policy negatively impacting high-growth stocks.[16]

All that said, in 2021 the Nasdaq underperformed the S&P 500 for the first time since 2016.[17]

Supply Chain Woes, Inflation Keeps Heating

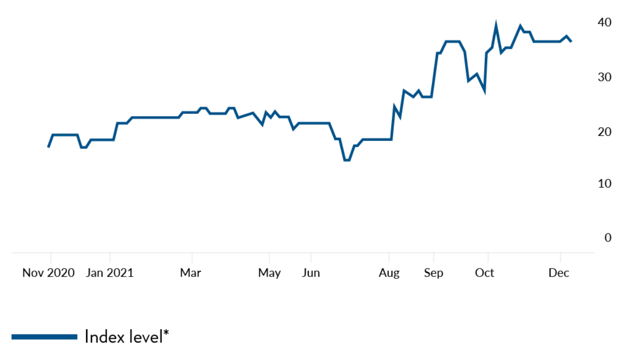
The global supply chain is still in crisis mode. While some analysts believe that pressure on supply chains could ease up by summer 2022, others think this crisis could linger well into 2023.[18] Data from Sea-Intelligence also says that freight bottlenecks may worsen before improving, as North American Cargo Congestion remained relatively stagnant in December.[19]

With supply chain constraints, consumer demand, and easy monetary policy, U.S. inflation data released on December 17 was predictably high. In November, the consumer price index, which measures the changing prices of a basket of consumer goods, climbed to a 39-year high and jumped 6.8% from a year earlier.[20]

Gasoline prices, fuel, other energy sources, and cars continued to contribute the most to this historic inflation reading.[21]

North American Cargo Congestion

Sea-Intelligence says freight bottlenecks may worsen before improving



*Reflects container terminal and intermodal congestion data from the carrier HMM

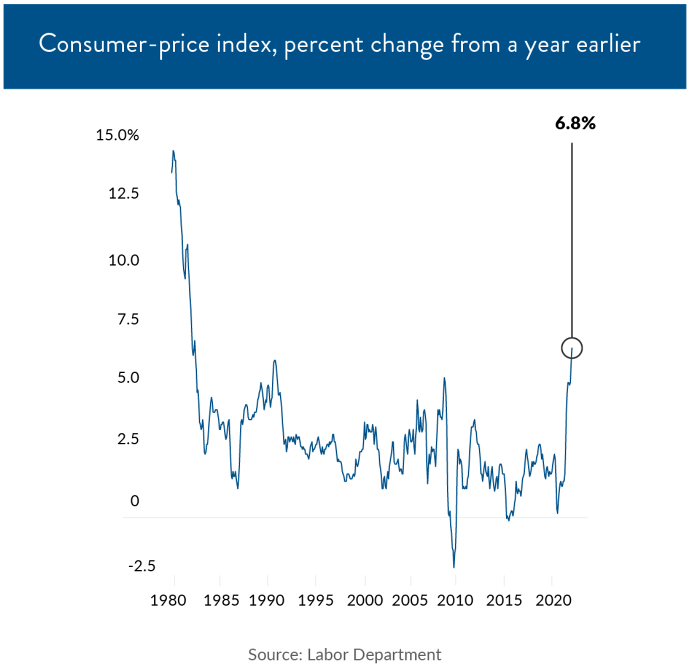
Source: Sea-Intelligence

Government and Central Bank Stimulus Fading

To combat inflation, the Federal Reserve officially turned more hawkish during its mid-December meeting. After early signaling that we discussed in November, the Fed announced that it would end its bond purchasing program by March, and officials expect as many as four potential interest rate hikes in 2022.[22]

Two days later, the Biden administration's $1.7 trillion "Build Back Better" social spending bill did not survive pass after losing key support from Senator Joe Manchin.[23] Afterwards, Goldman Sachs cut its economic growth forecast for the first quarter from a 3% to 2% annualized rate, also lowering Q2 and Q3 forecasts.[24] They blamed the cuts on the expiration of the child tax credit and the lack of new anticipated spending.

The Build Back Better bill remains up for discussion in 2022 and is a top Democratic priority.[25] Ahead of the 2022 midterms, Congress will also be tackling an agenda including government funding and confirmation of Federal Reserve board leaders like Chair Jerome Powell.[26]



Charging into the New Year

December 2021 began with some pessimism and fear but ended on quite the opposite note.

Overall, despite rising prices and fading policy support, US consumers are optimistic about their financial prospects, with most expecting their personal finances to keep improving over the next three years.[27] Consumer spending underpins economic growth, and on December 22, the consumer confidence index rose to 115.8. This was the highest reading since July, despite a surge in prices on both necessities and holiday gift purchases.[28]

Markets could have more surprises for us in 2022, and we'll be watching the strong consumer and labor market to see if inflation continues to increase. We're entering 2022 with a healthy dose of realism, but also a dash of optimism.

Those mixed emotions underscore the importance of taking a disciplined, calm, and strategic investment approach. After all, the world can always surprise us, and while we can't know what kind of surprise to expect, exactly, we do believe that prudence can help us plan for the unexpected.

As always, if there is anything we can do to answer your concerns, please don't hesitate. We are here as your partner to help you navigate these uncertain times. Please call us if you would like to schedule a meeting or call in the beginning of the year.

We hope you've had a wonderful holiday season and a healthy and happy start to 2022!

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Asset Allocation and Diversification do not guarantee a profit or protect against a loss.

The Bloomberg Barclays U.S. Aggregate Bond Index measures the investment-grade U.S. dollar-denominated, fixed-rate taxable bond market and includes Treasury securities, government-related and corporate securities, mortgage-backed securities, asset-backed securities and commercial mortgage-backed securities.

The S&P 500 Index is an unmanaged, market value-weighted index of 500 stocks generally representative of the broad stock market.

The MSCI World Index is a broad global equity index that represents large and mid-cap equity performance across 23 developed markets countries and covers approximately 85% of the free float-adjusted market capitalization in each country.

The MSCI Europe Index captures large and mid-cap representation across 15 developed markets countries in Europe and covers approximately 85% of the free float-adjusted market capitalization across the European Developed Markets equity universe.

The MSCI Emerging Markets Index captures large and mid-cap representation across 26 emerging markets countries and covers approximately 85% of the free float-adjusted market capitalization in each country.

The Nasdaq Composite is a market-capitalization-weighted index consisting of all Nasdaq Stock Exchange listed stocks that are not derivatives, preferred shares, funds, exchange-traded funds or debenture securities.

Gross domestic product (GDP) is a monetary measure of the market value of all the final goods and services produced in a specific time period. GDP is the most commonly used measure of economic activity.

SOURCES

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