Monthly Commentary Report

January 5, 2022

Index/ETF	1-Mo	1-Y
Equities		
US Large-Caps (SPY)	4.63%	28.75%
US Growth (QQQ)	1.15%	27.42%
US Small-Caps (SPSM)	4.55%	26.69%
US Mid-Caps (SPMD)	5.11%	24.77%
US Value (IVE)	7.02%	24.72%
International Developed Equities (IEFA)	4.22%	11.65%
Broad-based Emerging Markets (EEM)	1.53%	-3.62%
China (MCHI)	-3.03%	-21.73%
US Bonds		
Treasury Inflation Protected Notes (TIP)	0.40%	5.67%
High Yield Credit (HYG)	2.28%	3.75%
Municipal Bonds (MUB)	-0.01%	1.02%
US Aggregate Bond Index (AGG)	-0.36%	-1.77%
Investment Grade Corporate Bonds (LQD)	-0.03%	-1.84%
US Treasury 7-10 Year (IEF)	-0.52%	-3.33%
Commodities		
Crude Oil (USO)	13.46%	64.68%
Broad-based Commodities (BCI)	3.26%	25.85%
Gold (GLD)	3.30%	-4.15%
Silver (SLV)	2.14%	-12.45%

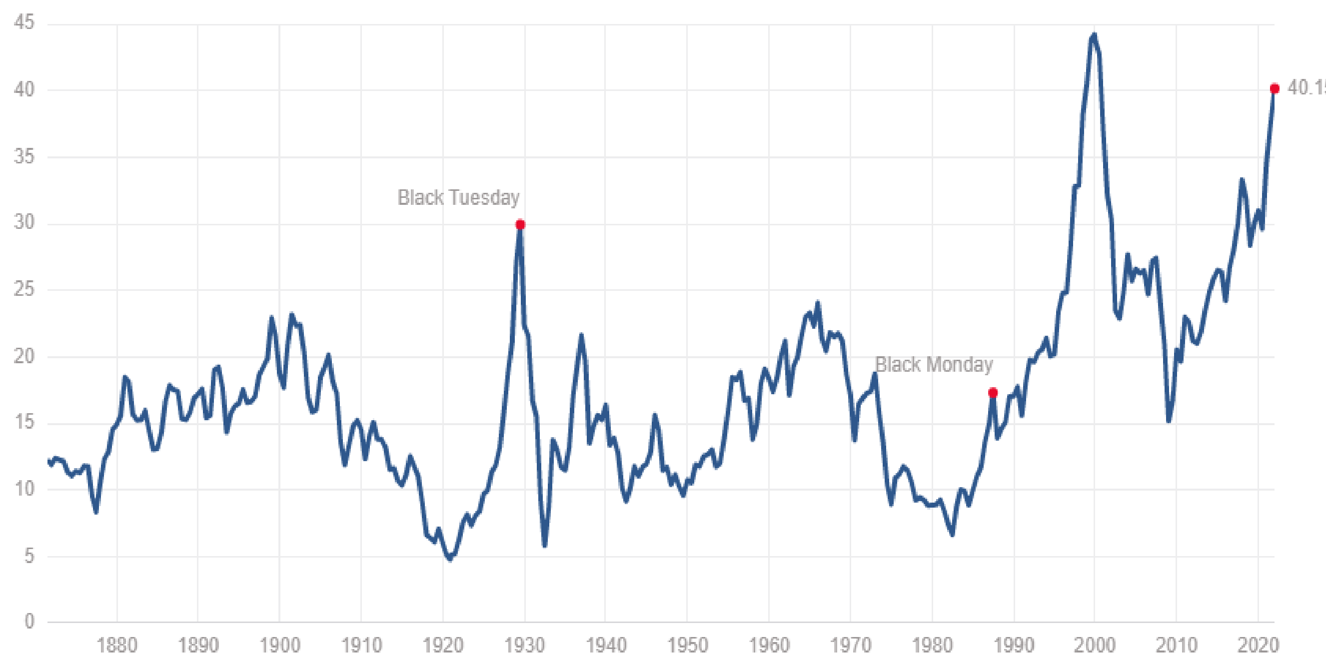
Inflation will continue to be a big theme in 2022. The number one question coming from clients is how to prepare portfolios for higher inflation. As communicated in our previous commentaries, we indicated that inflation would not be transitory. As a refresher, cyclically oriented sectors such as energy, materials, industrials, and financials have historically shown higher sensitivity to rising inflation. Energy stocks were the best performing sector in the US last year (refer to the second page). Additionally, commodities serve to provide additional protection as they tend to move at a different stage of the inflation cycle.

Mean reversion in 2022? Expect US large-cap index returns will be relatively lower in the years to come. US large cap equity valuations are reaching bubble-like territory. The chart below shows the Shiller CAPE PE ratio which is currently at 40. The last time it was around these levels was in 1999/2000 when the internet bubble burst. International diversification continues to make sense.

Dividends should be a focus in 2022. Total returns have two components: 1) Price return and 2) Dividends. Over the past decade, investors were enamored with growth and focused mostly on capital appreciation. We think investors should now focus on total return of which dividends play a crucial role. Consistent high-yielding, low-cost dividend ETFs have a place in strategic portfolios.

Exhibit 1

Shiller PE Ratio



Source: Multpl.com. Data as of January 5, 2022.

2021 Recap

Despite new Covid-19 variants and soaring inflation, US equities performed well in 2021. The S&P 500 climbed 29% and reached 70 closing highs. Mega-cap stocks outperformed as the S&P 500 Top 50 was up 31%. International equities also rose given the S&P Developed Ex-US BMI index was up 11%. Although the S&P China BMI fell largely, emerging markets were able to post a gain as the S&P Emerging BMI was up 1%. Amongst factors, high beta (+41%) was unsurprisingly the best performer given the risk-on sentiment, followed by enhanced value (+36%) and dividend strategies (+32%). Momentum and low volatility were the laggards (up 23% and 24%, respectively). US fixed income produced mixed returns as both TIPS and high yield posted gains while Treasuries declined. Both broad-based commodities and crude oil performance were positive.

How did Sectors Perform Last Year?

In 2021, all sectors posted gains. Energy, which was up a remarkable 53%, was the best performer, followed by Real Estate and Financials (up 46% and 35%, respectively).

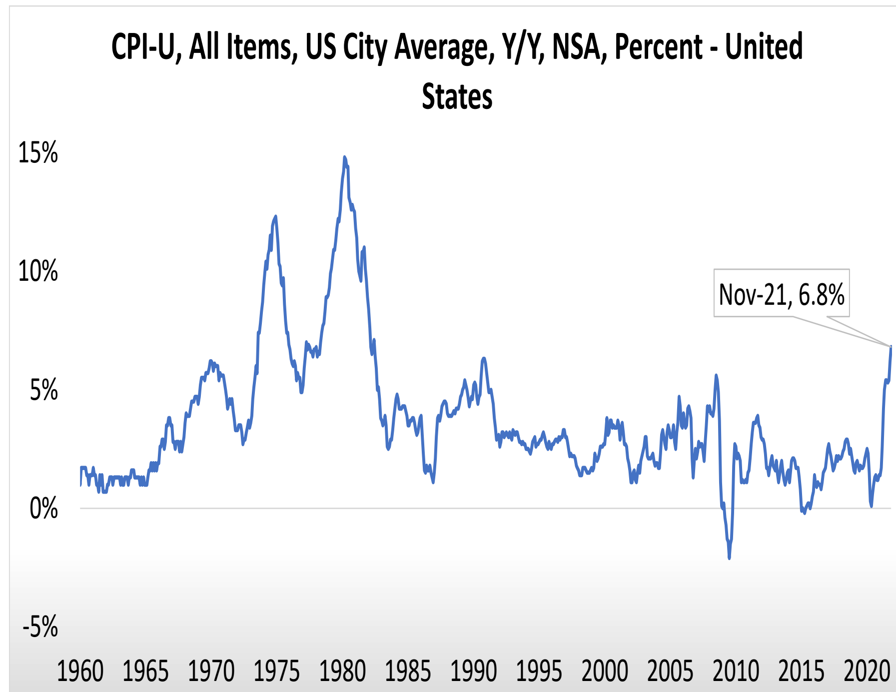
- Energy: +53%
- Real Estate: +46%
- Financials: +35%
- Technology: +35%
- Consumer Discretionary: +28%
- Materials: +27%
- Health Care: +26%
- Industrials: +21%
- Utilities: +18%
- Consumer Staples: +17%
- Communication Services: +16%

Largest Inflation Print in 40 Years

The current level of the Consumer Price Index (CPI), a widely followed economic indicator for inflation, is at a 40-year high. It has been a perfect storm for higher inflation. Supply chains broken plus tons of liquidity being pumped into the system by governments and central banks translated to higher-than-expected inflation. Remember, inflation was largely ignored over the past decade, and we think we are still in the early stages of the inflation cycle. Moreover, inflation-linked assets still offer an attractive margin of safety.

Exhibit 2

United States CPI



Source: FactSet, US Department of Labor. Data as of December 10, 2021.