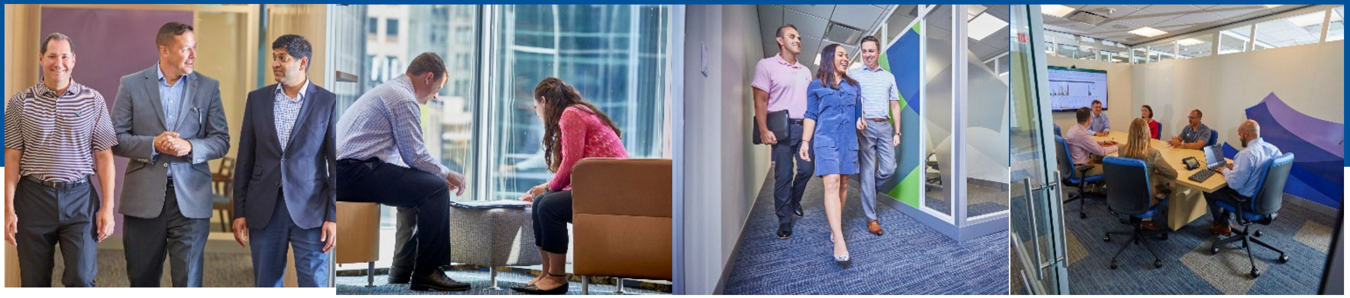
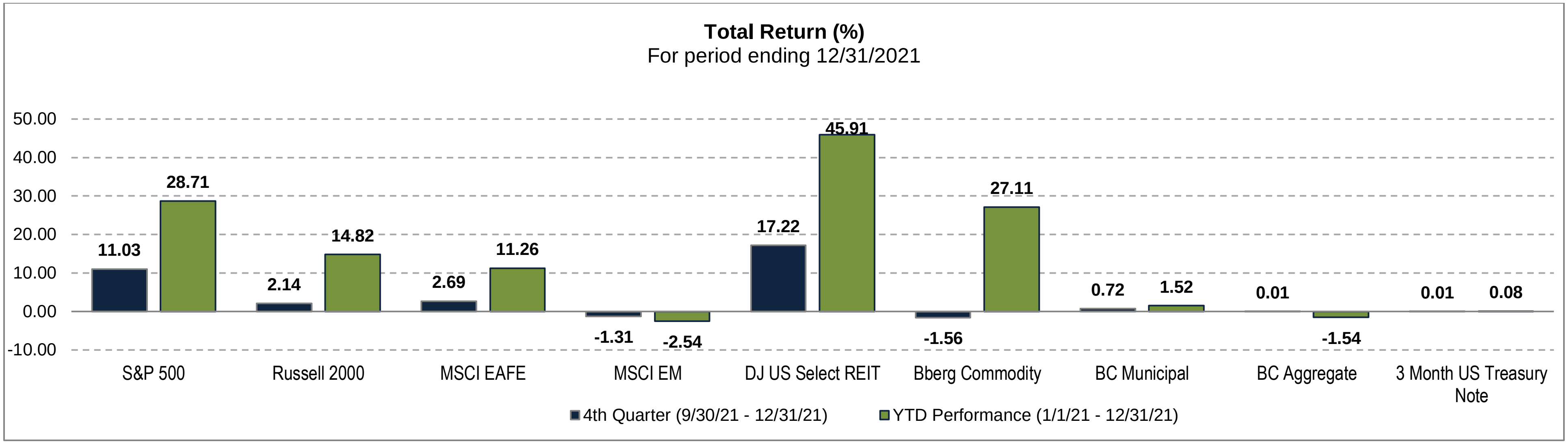
SCHNEIDER DOWNS
Wealth Management

Over in an Instant: 2021
A Year Well Spent Living in the Moment



Schneider Downs Wealth Management Advisors, LP
Q4 2021 Market Commentary

Big Thinking. Personal Focus.



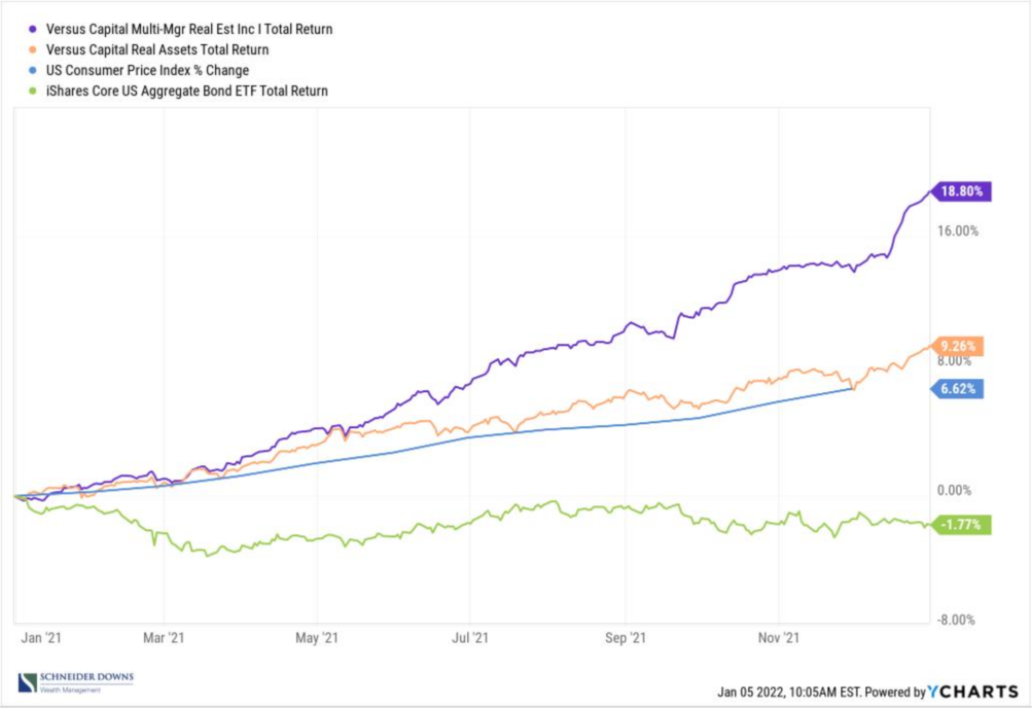
For as long as the year 2020 seemed to last with a toxic cocktail of worsening news about the Coronavirus, rolling lockdowns, and a particularly contentious political season, the following year, 2021, seemed over in an instant. Sporting events had fans in the stands, children returned to school full time in the fall, holidays were spent with our families,[1] and my beloved Cleveland Browns reverted back to crushing my soul.[2] The ability to return to normalcy quickened the pace of 2021 in a fashion that was unexpected, yet wholeheartedly welcomed. For those of you who listen to podcasts, it felt like 2021 was being played at 1.5x speed. Capital markets were strong and correspondingly, portfolios were up, real estate values soared, and wages began growing again – 2021 was as strong of a rebound year as any of us could have hoped for after the long slog that was 2020. People savored every moment spent together, and rightfully so.

In our collective yearning to "live in the moment," there were a litany of items that markets, investors, and central bankers shrugged off that will confront them head on in 2022. The most pressing item that has so far been shrugged off by market participants is what to do about the rising inflation that was observed in 2021. For most of the past 40 years, inflation has mostly been benign, with random occurrences along the way, but nothing sustained enough to warrant attention from central bankers. However, due to the unprecedented amount of monetary and fiscal stimulus poured into the economy by the governments and central banks across the globe, coupled with global supply chain failures that resulted from the unrelenting demand by consumers, everything from used cars to a sack of potatoes costs significantly more than it did only 18 months ago. Jerome Powell, Chairman of the U.S. Federal Reserve, was forced to drop the description of "transitory" as elevated inflation persisted far longer than he and his colleagues at the Fed predicted. In December, Chairman Powell announced that the U.S. Federal Reserve will cease their bond purchasing program by the end of March and signaled that multiple interest rate increases were on the table for 2022[3].

[1] Which depending on your circumstances may have been a negative development… I for one enjoyed the back-and-forth banter and occasional disagreement over football and politics. It felt all so normal.
[2] The Cleveland Browns truly are a Factory of Sadness: https://www.youtube.com/watch?v=tRBDMMVctu8
[3] https://www.pbs.org/wgbh/frontline/article/powell-fed-ending-pandemic-stimulus-early-what-does-it-mean-for-inflation/

In addition to higher observed levels of inflation, the employment picture has improved dramatically from the depths of the COVID crisis. The labor market[4] added over 800,000 jobs in December, further putting pressure on an already tight employment market. Many have opined on the "great resignation," which is a clever framing to explain people leaving their jobs for more money, life/location flexibility, or some combination of the two. Jane McGregor from Forbes does a nice job providing a thorough synopsis of this employment phenomenon, which is footnoted below[5]. The bottom line is that employees are exerting pressure on employers that is causing wages and benefits to increase at their highest clip in several decades. Jerome Powell and the U.S. Federal Reserve have a dual mandate of maximum employment (typically under 5% of the labor force unemployed) and price stability (inflation at 2%). With the former having been largely achieved and the latter becoming increasing untethered to its long-term average, the unprecedented monetary and fiscal measures that have permeated throughout global markets appear poised to change. As the U.S. confronts tight labor markets and higher inflation, the prospect of higher interest rates is no longer an abstract thought but a very real possibility. What remains to be seen is if the U.S. stock market will continue to be resilient with higher inflation and less monetary and fiscal stimulus.

Much like life, which is never as black and white as we might wish it to be, the same can be said for investing. One of the core foundational principles of our investment philosophy at SDWMA is that there should be more to investment portfolios than just stocks and bonds. In previous quarterly commentaries we have discussed our belief that real assets (infrastructure, farmland, timberland, and high-quality commercial real estate) provide differentiated risk/return profiles that are accretive to our client portfolios. The ability to access the highly contracted cash flow nature of these investments (and earn above-average current yields) combined with real assets' ability to have positive convexity to inflation (and combat higher interest rates) provided our client portfolios with another performance lever to pull on. Observing the low interest rate environment, the SDWMA team began allocating to real assets in 2016 and 2017 and ramped up the allocation heading into 2021. Sourcing the real asset exposure from core fixed income (bonds), client portfolios had a way to generate returns that moved beyond bond yields moving ever lower (and pushing bond prices higher) in 2021.



[4] https://www.cnbc.com/2022/01/05/adp-december-2021.html

[5] https://www.forbes.com/sites/jenamcgregor/2021/12/14/2021-brought-us-the-great-resignation-no-one-can-agree-what-to-call-it/?sh=7609a314509c

At the beginning of 2021 few people were talking about inflation, yet by the end of the year it dominated the media landscape and was one of the most highly discussed topics during our client meetings in the second half of 2021. As the chart[6] above demonstrates, allocating to real assets (purple and orange lines) provided differentiated and attractive returns relative to traditional fixed income (green line) and higher inflation readings (blue line). Looking forward into 2022, the SDWMA team will continue to lean into what we call strategic income (real assets) to generate differentiated risk/return streams for client portfolios.

For those of us who came of age during the NBA Jam arcade/video game craze of the early 1990s (and for those of you who as parents had to deal with the constant nagging to get the game and then deal with us playing it non-stop), you will be familiar with the term "he's on fire." For those that may be unaware, NBA Jam was a popular video/arcade game featuring NBA players playing two-on-two full-court basketball games. A player was deemed to be "on fire" after he made several shots in a row. Once a player was "on fire," he had the ability to make shots from virtually anywhere on the court for a finite amount of time. Looking back on the sheer resilience of the S&P 500 in 2021, it harkened me back to my youth playing the NBA Jam game with my twin brother, Brandon; simply put, the S&P 500 was on fire. No matter what was thrown at it, be it: persistently higher inflation, significantly elevated price to earnings ratios, the COVID delta variant, the COVID omicron variant, the failure of the Build Back Better spending bill, or the U.S. Federal reserve signaling a quicker end to its bond buying program and openness to increase interest rates multiple times in 2022 – no matter what was thrown at it, the S&P 500 shrugged it off and moved higher than anyone imagined in 2021. However, just like in the video game, where a player could only stay "on fire" for so long, it is likely that after a decade of outperformance capped off by a resounding and captivatingly strong performance in 2021, the S&P 500 is likely to take a breather in 2022.

Higher than expected inflation and an increase in interest rates are likely to converge onto U.S. large cap stocks that are trading well above their long-term averages. This isn't to say we are predicting a crash of some kind in the equity market, but what we are saying is that other parts of the equity market are more attractive. Domestically, "value" as a style across market capitalization looks attractive versus their high growth peers. Internationally, emerging markets went from the top performer of the broad market indices in 2020 to the low person on the totem pole in 2021. Emerging market equities finished 2021 in the red after a year where saber rattling and policy shifts in China reverberated across the EM landscape. The volatility we saw in 2021 presents an opportunity in 2022, as accommodative fiscal and monetary tools and attractive valuations create a tailwind for the asset class. We are also quite sanguine about the opportunity set in international developed markets, where we maintain a bias to high-quality growth companies.

There was so much to be grateful for in 2021; after plodding through 2020, we began to get our lives back. We hope you and your families were able to "live in the moment" and reacquaint yourselves with the little things in life that make living so special. Capital market performance to start off this new decade has been strong, with 2020 and 2021 delivering above-expectation results. We expect 2022 to be a more formidable opponent as the trends of deglobalization and the desynchronization of global monetary policies continue. As our CEO, Nancy Skeans, indicated in our December/Holiday newsletter, our team is back in the office having implemented a hybrid work schedule that gets us back together several days each

[6] Chart shows the performance of high quality commercial real estate manager Versus MM Real Estate Income (purple line +18.8%), our real asset (infrastructure, farmland and timberland) manager Versus Capital Real Asset (orange line +9.26%), high quality bonds as measured by the iShares US Core Aggregate Bond ETF (green line -1.77%), and US Consumer Price Index % annualized change (blue line, reading through November, +6.62%). The above referenced strategies were generated from yCharts and represent the total return if held from 1/1/2021 through 12/31/2021. These returns <u>are not</u> net of SDWMA advisory fees; past performance does not guarantee future returns.

week. In addition, we added two new teammates, Gregg Daily and Demetrius Kokales, serving roles as a Senior Investment Relationship Manager and Associate Investment Advisor/Financial Planner, respectively. The SDWMA team enters 2022 excited and reinvigorated after over a year of working remotely. If we can safely meet you in person (in our offices, at your homes, or sharing a meal at your favorite restaurant) we welcome the opportunity! If we cannot meet in person, we have mostly mastered meetings on Zoom or Microsoft Teams (no promises that we have 100% mastered the "mute" functionality 😊). For those of you who did not see our December newsletter, I end this letter with the same quote from Anne Frank, "What a wonderful thought it is that some of the best days of our lives haven't happened yet." We look forward to hearing from you about some of these "best days" in the days, weeks, and months ahead!