

Due to the wide range of risk tolerances of our clients, some topics or asset classes may have more, less, or no importance to your portfolio. For a detailed analysis, give us a call, or request a detailed performance review.

Big Picture

On the Fridge

US Stocks

The US stock market rose 10.1% in the fourth quarter, to wrap up another great year finishing with a 27% annual return.

Tech Sector

The tech sector led all others in the fourth quarter rising 16.7%. That put tech stocks up 34.5% for the year. However, the top 3 mega-cap stocks (AAPL, MSFT, NVDA) make up 48% of the sector and were up 49% in 2021. The rest of the sector was up 22%.

In the Dog House

Communication Services

The Communication Services sector returned 0.0% in the fourth quarter, the only sector to not post a positive return. Like the tech sector, Comm. Services is dominated by just two stocks, FB and GOOGL make up 47% of the sector. In 2021 those two names returned 42% while the rest of the sector was down -5%.

Emerging Markets

Emerging market stocks lost -1.2% in the fourth quarter, good for last place among the asset classes we track. That brings 2021 performance down to -2.2% as emerging

While COVID remains as disruptive as ever, the focus in the fourth quarter shifted to the Federal Reserve. Specifically, to fears that the Fed would significantly tighten monetary policy to combat inflation. The basic idea being that the Federal Reserve will use its tools to raise interest rates slowing the economy down as capital becomes more expensive, thus slowing inflation. This is clearly bad for stock prices for two reasons, the first is obvious, slowing the economy will slow earnings growth. The second, is that rising interest rates increase the discount rate by which future cash flows are brought to present value, bringing company valuations down. It stands to reason then that the companies most affected by these mechanics would be the companies with the most future growth baked into their current valuation. Indeed, that is what we continued to see in the fourth quarter.

The headline print at the index level was buoyed by the largest companies and hid a slaughterhouse of smaller innovative growth stocks underneath. The S&P 500 rose 11% in the quarter, but within the index many companies were crushed, perhaps best illustrated by the continued retreat of all-star fund manager Cathie Wood's ARKK investment funds. From the beginning of 2019 to February 19th, 2021, ARKK rose 319% vs. 62% in the S&P 500. Since then, through the end of 2021, the S&P 500 returned 23.5% while ARKK fell -37.5%. ARKK bills itself as an "innovation" fund, which means many of its holdings are unprofitable disruptive companies whose entire value is based on lofty future expectations, which might explain why they were so harshly punished by the threat of Fed tightening.

Looking Ahead

2022 will be a dance between Inflation, COVID, and the Fed. The pandemic is affecting inflation, and inflation is affecting Fed policy while all three are affecting the stock market. On the COVID-19 front, I believe the first half of 2022 will mark the transition from pandemic to endemic. The recent Omicron surge which sent cases and hospitalizations far beyond previous peaks during the pandemic may end up being the best thing we could have hoped for. Omicron has proven to be a milder infection than previous variants, and while I can personally attest that it is not pleasant at all, it will likely be the final piece towards effective herd immunity. This should, and is, leading to a massive drop in new cases and hospitalizations as the virus has simply reached saturation and is running out of people to infect. A return to full productivity and a shift from goods back into service spending should provide a natural relief for inflation. Whether it is enough to satisfy the Fed before they overreach and harm the economy is the story to watch in 2022. An additional factor to consider this year is China. China has kept COVID-19 cases very low throughout the pandemic, thus they don't have the herd immunity that western countries are now relying upon to reopen. Whether they can meet the world's demands for their goods will have a major impact on whether inflation remains persistent in 2022.

Links and Articles

A Year-End Look Around the World

Joe Zidle of Blackstone reflects on the state of the global economy at the end of 2021.

Endemic Doesn't Mean Harmless

Aris Katzourakis warns the world what "Endemic" really means in the journal Nature.

The Ten Surprises of 2022

Blackstone outlines their annual 10 surprise predictions for the current year.

Revisiting the Beveridge Curve

The Richmond Fed highlights the oddity of the post-pandemic labor market.

Performance

US Stocks rose 10.1% in the fourth quarter to bring 2021 to a whopping 27%. Developed market stocks rose 3.2% for a 13.2% annual gain, while emerging market stocks fell -1.2% for a -2.2% annual return. Bonds were largely flat in the quarter, with the exception of TIPS which returned 2.4% to reflect increasing inflation expectations. That brings the annual return on TIPS to 6%, interestingly, TIPS have returned 8.4% annually over the last three years, while inflation expectations really only took off in 2021. Even longer term, TIPS have performed well, returning 3.1% annualized over the last 10 years, while treasuries returned just 2.1% over the

	Benchmark Index	2021 Q4	YTD	LTM	3yr	5yr	10yr
Cash	Bloomberg US Treasury Bill 1-3 M TR USD	0.0%	0.0%	0.0%	0.0%	1.1%	0.6%
Fixed Income	Bloomberg Global Aggregate TR USD	-0.7%	-4.7%	-4.7%	3.6%	3.4%	1.8%
Fixed Income Blend	Bloomberg Global Aggregate TR USD	-0.7%	-4.7%	-4.7%	3.6%	3.4%	1.8%
Government	Bloomberg US Government TR USD	0.2%	-2.3%	-2.3%	4.1%	3.1%	2.1%
Inflation Protected	Bloomberg US Treasury US TIPS TR USD	2.4%	6.0%	6.0%	8.4%	5.3%	3.1%
Municipal	Bloomberg Municipal TR USD	0.7%	1.5%	1.5%	4.7%	4.2%	3.7%
Floating Rate	Bloomberg US Trsy Floating Rate TR USD	0.0%	0.1%	0.1%	1.0%	1.2%	0.0%
Corporate	Bloomberg US Corp Bond TR USD	0.2%	-1.0%	-1.0%	7.6%	5.3%	4.7%
High Yield	Bloomberg US Corporate High Yield TR USD	0.7%	5.3%	5.3%	8.8%	6.3%	6.8%
International Bond	Bloomberg Gbl Agg Ex USD TR USD	-1.2%	-7.0%	-7.1%	2.5%	3.1%	0.8%
Equity	MSCI ACWI GR USD	6.8%	19.0%	19.1%	21.0%	15.0%	12.4%
Equity Blend	MSCI ACWI GR USD	6.8%	19.0%	19.1%	21.0%	15.0%	12.4%
US Equity	MSCI USA GR USD	10.1%	27.0%	27.0%	26.6%	18.8%	16.6%
Developed Markets	MSCI World ex USA GR USD	3.2%	13.2%	13.2%	14.6%	10.2%	8.4%
Emerging/Frontier	MSCI EM GR USD	-1.2%	-2.2%	-2.2%	11.3%	10.3%	5.9%
Alternatives	Wilshire Liquid Alternative TR USD	0.6%	4.7%	4.7%	4.9%	3.0%	2.4%
Alternatives Blend	Wilshire Liquid Alternative TR USD	0.6%	4.7%	4.7%	4.9%	3.0%	2.4%

Sector	2021 Q4	6mo	YTD	1yr	3yr	5yr	10yr
Information Technology	16.7%	18.3%	34.5%	34.6%	42.7%	32.1%	24.0%
Financials	4.6%	7.4%	35.0%	35.1%	20.6%	13.3%	16.3%
Health Care	11.2%	12.8%	26.1%	26.2%	20.0%	17.6%	17.2%
Consumer Discretionary	12.8%	12.8%	24.4%	24.5%	28.5%	21.4%	19.6%
Consumer Staples	13.3%	13.0%	18.6%	18.6%	18.8%	11.8%	12.2%
Industrials	8.6%	4.1%	21.1%	21.1%	20.3%	12.8%	14.2%
Energy	8.0%	6.2%	54.6%	54.7%	4.7%	-1.4%	1.2%
Utilities	12.9%	14.9%	17.7%	17.7%	14.3%	11.8%	11.1%
Materials	15.2%	11.2%	27.3%	27.3%	24.2%	15.1%	12.8%
Communication Services	0.0%	1.6%	21.6%	21.6%	25.9%	11.5%	11.6%
Real Estate	17.5%	18.6%	46.2%	46.2%	22.6%	14.9%	13.1%

Source: Morningstar; The 1,3,5, and 10 year performance is annualized.

same period. Alternatives returned just 0.6% in the quarter, but finished the year up 4.7%, inline with their 3yr annualized return of 4.9%.

The tech sector was the top performer in the fourth quarter, although taking a headline number on the tech sector can be very misleading. The sector was up 35% as a whole, but the top 3 stocks (AAPL, MSFT, NVDA) represent a full 50% of the sector index. Without the three mega-caps, the rest of the sector was up 22%, which would have made it the 7th best sector in the year rather than a tie for second. The emergence of trillion-dollar mega-cap companies is forcing investors to rethink how they view index level data.

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Asset Class	Benchmark	Description
Cash	Bloomberg US Treasury Bill 1-3 M TR USD	Measures US dollar-denominated, fixed-rate, nominal debt issued by the US Treasury.
Fixed Income	Bloomberg Global Aggregate TR USD	The Bloomberg Global Aggregate Index is a flagship measure of global investment grade debt from twenty-four local currency markets. This multi-currency benchmark includes treasury, government-related, corporate and securitized fixed-rate bonds from both developed and emerging market issuers.
Government Bonds	Bloomberg US Government TR USD	The Bloomberg US Government Bond Index comprises the US Treasury and US Agency indices. The index includes US Dollar-denominated, fixed-rate, nominal US Treasuries and US agency debentures (securities issued by US government owned or government sponsored entities, and debt explicitly guaranteed by the US government).
Inflation Protected	Bloomberg US Treasury US TIPS TR USD	The Bloomberg US Treasury Inflation-Linked Bond Index (Series-L) measures the performance of the US Treasury Inflation Protected Securities (TIPS) market.
Municipal	Bloomberg Municipal TR USD	The Bloomberg U.S. Municipal Index covers the USD-denominated long-term tax exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds and prerefunded bonds.
Floating Rate	Bloomberg US Trsy Floating Rate TR USD	The Bloomberg US Treasury Floating Rate Index measures the performance of floating rate bonds issued by the US Treasury.
Corporate Bonds	Bloomberg US Corp Bond TR USD	The Bloomberg US Corporate Bond index measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD-denominated securities publicly issued by US and non-US industrial, utility and financial issuers.
High Yield Bonds	Bloomberg US Corporate High Yield TR USD	The Bloomberg US Corporate High Yield Bond Index measures the USD-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below.
International Bonds	Bloomberg Gbl Agg Ex USD TR USD	The Bloomberg Global Aggregate Index is a flagship measure of global investment grade debt from twenty-four local currency markets. This multi-currency benchmark includes treasury, government-related, corporate and securitized fixed-rate bonds from both developed and emerging market issuers. This version excludes USD-denominated debt.
Equity	MSCI ACWI GR USD	The MSCI ACWI captures large and mid cap representation across 23 Developed Markets and 23 Emerging Markets countries. With 2,477 constituents, the index covers approximately 85% of the global investable equity opportunity set.
US Equity	MSCI USA GR USD	Captures broad US equity coverage. The index includes 3,108 constituents across large, mid, small, and micro capitalizations, representing about 99% of the US equity universe.
Developed Market Equity	MSCI World ex USA GR USD	Captures large and mid cap representation across 22 of 23 Developed Market countries, excluding the United States. With 1,023 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.
Emerging Market Equity	MSCI EM GR USD	The MSCI Emerging Markets Index captures large and mid cap representation across 23 Emerging Markets (EM) countries. With 829 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.
Alternatives	Wilshire Liquid Alternatives TR USD	Measures the collective performance of the five Wilshire Liquid Alternative strategies that make up the Wilshire Liquid Alternative Universe, including the Wilshire Liquid Alternative Equity Hedge, Global Macro, Relative Value, Multi-Strategy, and Event Driven indices. This index is meant to provide a representative baseline for how the liquid alternative investment category performed as a whole. Constituents comprised of '40 Act mutual funds.
US Large Cap Equity	S&P 500	Widely regarded as the best gauge of large-cap US Equities. The S&P 500 is a market-weighted index that includes 500 leading companies and captures approximately 80% coverage of available market capitalization.