QUARTERLY REPORT

INVESTMENT PERSPECTIVE

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U.S. equity markets continued to be led by larger capitalization stocks in the fourth quarter with the S&P 500 rising 11.03% and the Russell 2000 Value rising 4.36%. International equity markets also rose modestly with the MSCI EAFE increasing 2.69%. With rising inflationary pressures becoming a political issue, the U.S. Federal Reserve began modestly reducing their Quantitative Easing purchases and provided forward guidance that interest rate increases are on the horizon. Inflationary pressures have peaked in the U.S. and emerging markets but continue to rise in Europe. Although upward pressure on inflation is easing, inflation remains at elevated levels and may limit monetary policy support going forward.

Economic growth continues to slow, and we expect supporting data to become visible as we exit the first quarter and through the second quarter of 2022. As monetary policy becomes incrementally more restrictive, it is important for inflationary pressures to ease faster than economic growth so that real growth can remain supportive of equity markets. Should economic growth slow faster than inflationary pressures, earnings estimates and equity valuations may come under pressure in the first half of 2022.

The Bloomberg Aggregate Index returned a modest 0.01% for the quarter. The yield curve continued to flatten during the quarter with yields in the front and middle parts of the curve increasing in anticipation of the Federal Reserve raising interest rates.

Credit spreads widened seven basis points during the quarter and finished the year at +87 basis points over Treasury yields. Credit spreads traded in a very narrow range (18 bps range) in 2021 buoyed by strong demand for corporate bonds, low volatility, and solid credit quality.

With the Fed accelerating the reduction of its monthly bond purchases and signaling three rate hikes in 2022, we expect volatility in the bond market to increase. This will provide opportunities to generate alpha within spread sectors and through opportunistic duration changes. In preparation for higher rates, we continue to maintain a shorter average duration relative to the benchmark. We trimmed our allocation to corporate bonds in 2021 but anticipate adding to Corporates in 2022 if spreads widen due to changes in economic growth or monetary policy.

The ICE Bank of America AAA-A Municipal Index returned 0.16% in the quarter. Demand for municipal bonds is strong due to the favorable credit outlook and the higher after-tax returns for those investors in elevated tax brackets. This already strong demand is expected to continue, and potentially increase, given the potential for higher tax rates.