Perspectives

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Market Recap

Wow, what a year! Very large equity market returns may lead one to think that it was easy to manage portfolios this year. It was anything but! Though overall market volatility was actually lower than normal, under the surface of the market there was a gigantic tug-of-war between value stocks and growth stocks, reopening stocks and defensive stocks, and technology stocks versus rising interest rates. It was not an easy year at all, and it required eyes on the ball all the time, every day. Before we head into the New Year, let's first take a look back at 2021.

Record fiscal stimulus, and massive increases in money and credit by the Federal Reserve, were able to steady the economy in the early months of the pandemic and paved the way for a swift recovery and a strong economic expansion. Unemployment fell, and wages rose nearly 4.3%.[1] Even so, there are still more job openings than unemployed workers, which paves the way for further above trend job growth.[2]

High double-digit earnings growth and last year's estimated $850 billion in corporate share buybacks[3] ignited a sharp stock market rally that saw the S&P 500[4] gain 27% without as much as a 10% correction and only one 5% pullback. The S&P 500 hit 70 all-time highs during 2021 and just completed its best three-year stretch since 1999, far exceeding expectations. S&P 500 earnings were likely up 45% year-over-year in 2021 according to FactSet. This is an unusually high rate of growth resulting from strong corporate earnings in comparison to weaker, Covid-related earnings in 2020. Last year saw strong corporate profits bolstered by exuberant consumer spending even in the face of higher prices and supply chain delays. U.S. stocks were actually cheaper at the end of the year than they were at the beginning of the year due to contracting price to earnings (P/E) ratios.

It is interesting that just five stocks in the S&P 500 Index (that is, five out of 500 stocks) accounted for 37% of the total return of the S&P 500 in 2021. Just in case you were wondering, they were Apple, Microsoft, Alphabet (formerly Google), Tesla, and Nvidia. The average return of these five stocks was 65%.[5] That's called concentration of returns!

Caught on the other side of the tug-of-war, were emerging market stocks (-2.2%)[6], gold (-4.0%) and other precious metals, and bonds (-1.54%)[7]. This time last year we forecasted a tough year for bond investors due to expectations that interest rates would rise throughout the year. That's exactly the way the year started off. However, with the rise of the Delta variant, interest rates fell back, providing some relief for bonds, only to rise again going into the end of the year. Overall, it was a tough year for bond investors.

In summary, we give thanks for terrific returns in 2021 and we look forward to positive, but more normal returns in 2022 as global economies continue to heal. Happy New Year!

Patrick Powers, CFA®, CPA, CFP®
Partner/Managing Principal

Thomas Steffanci, Ph.D.
Senior Portfolio Manager (Arizona Branch)

Forecast

Welcome to the New Year! Year-to-date market returns are reset to 0%, and the year ahead is still a blank slate. No doubt, 2022 will provide its usual mix of ordinary market behavior and unexpected surprises, and while they can't be forecasted, we can say with near certainty that they will occur. At the same time, markets have patterns that tend to repeat, even if the emphasis is different from year to year.

This year is likely to be more challenging than last. According to Bloomberg, recent periods when there were three consecutive years of double-digit S&P 500 returns were usually followed by modest or negative stock returns the next year. While we don't believe that negative returns will occur this time, as interest rates for this year should barely reach 2.5% on the ten-year treasury bond, and corporate profits are expected to rise 9-10% on average, it is a cautionary sign that equity returns in 2022 could be much more subdued.

Inflation, the pace of the pandemic recovery, the risk of Federal Reserve policy blunders, and the extent the supply chain recovers are major uncertainties that cloud the outlook. With inflation hopefully peaking this quarter, its reversal is likely to be bumpy and importantly determined by the shift of consumers from spending on durable goods (i.e., autos, recreational equipment, home appliances) to services which are dominated by price competitive small-businesses. As important as the rise in labor costs is as an inflation factor, once embedded it is difficult to reduce compared to supply chain and demand determined commodity-linked goods. Without a rise in productivity, rising unit labor costs could persist and and be a headwind against a decline in inflation pressures.

Though underlying economic growth is likely to downshift to 3-4% from the 5-6% pace in 2021, that would still be nearly double the long-term growth rate. With moderating inflation and supply chains healing, that above-trend growth can set the stage for 5-6% overall corporate revenue growth.

Thomas Steffanci, Ph.D.
Senior Portfolio Manager (Arizona Branch)

Portfolio Management

When blockchain technology & cryptocurrencies became popular a few years ago, we were highly skeptical of their durability, security, and value. Regardless of our opinion, blockchain and cryptocurrencies are here to stay and, over time, cryptocurrencies will likely become a legitimate asset class and companies using blockchain may be rewarded by investors for doing so. At this point, investing in cryptocurrencies is highly speculative. However, the underlying blockchain technology holds great promise. This is a new general purpose technology just like mainframe computers (1960's), personal computers (1980's), the internet (1990's), and social media (2000's). Blockchain is likely to become a disruptive technology that may become ubiquitous. Microsoft Word and Excel are examples of products that, like blockchain, became disruptive and ubiquitous.

Right now, investing in blockchain and cryptocurrencies is full of risks - from which platform to use, securing your cryptos, government regulation, and which cryptos to invest in. Although we are not advocating investing in cryptocurrencies for our clients at this time, we understand that some of our clients may want to do so on their own. Over the past two years, we have been boning up on this emerging field and we feel confident that if you seek advice, you can come to us and we can point out the pros and cons of such a speculative investment. Also, keep a look out for our first blockchain and cryptocurrency symposium in February.

Steven Yamshon, Ph.D.
Partner/Managing Principal

Talk With Us!

At one point in my professional career, I sold insurance policies. I always joked that though I was raised a gentleman, I had to ask women the two things you are never supposed to ask, "How old are you?" and "What is your weight?" Luckily, we do not sell insurance at BFSG, which has saved me from having more of these awkward conversations.

When insurance makes sense:

Our clients' insurance needs can vary from life, disability, long-term care, umbrella liability, medical, or even to business insurance. Insurance at its core tries to make you “whole” when a catastrophic event occurs. Simply put, when something major in life happens, insurance is supposed to provide enough benefit for the victim to maintain the same standard of living they enjoyed before the unfotunate event occurred.

When to avoid insurance:

Insurance products are not designed to be investment products. They are designed to sove a problem. Unfortunately, unscrupulous salesman pitch insurance as an excellent investment vehicle for retirement. If anyone pitches insurance as an investment, you should see nothing but red flags.

What to consider when looking at insurance:

Every insurance discussion is best held in the context of one’s comprehensive financial plan. Any discussion should be framed around two very simple questions:

If something happens, can you afford to pay the bill?

As we already stated, the idea of insurance is to make you “whole” if a catastrophe occurs. A very common example is, if a spouse dies prematurely, can the surviving spouse and kids maintain the same standard of living? If you do not have enough assets to handle the circumstances on your own, then insurance is needed.

If you do have sufficient assets, then I like to ask a second question:

If something happens, do you want to pay the bill or do you want someone else to pay the bill?

There are times where people may have enough assets but may still want to have insurance. A common example of this would be long-term care. If a spouse gets sick they may have enough assets to cover the costs for a while, but what happens if the need is longer than anticipated? In these situations, it can be beneficial to have insurance in case it is ever needed, and to provide our clients peace of mind and more assets for their heirs.

If you have an insurance-related question, please do not hesitate to ask for our opinion to see how we may be able to help!

Paul Horn, CFP®, CPWA®
Senior Financial Planner/Wealth Manager

BFSG – In The News

November 12, 2021 – Tina Schackman, Principal and Senior Retirement Plan Consultant at BFSG, joined the WE Inspire Promote Network (WIPN), previously known as Women in Pension Network, to drive membership and promote the advancement of Diversity, Equity and Inclusion (DEI) for women in the retirement industry. She joined the Board in January 2021 and is proud to be serving a 2nd year with this incredible group of women.

The Score Board

	12/31/2021	YTD Change
Dow Jones Industrial Average	36,338.30	20.95%
S&P 500*	4,766.18	26.89%
NASDAQ Composite*	15,644.97	21.39%
MSCI EAFE (USD)*	2,336.07	8.78%
Bloomberg Commodity Index	99.16	27.05%
Barclays Aggregate Bond Index	2,355.14	-1.54%
10 Yr U.S. Treasury Bond Yield	1.51%	59 bps
30 Yr Fixed Mortgage Rate	3.05%	38 bps
Prime Rate	3.25%	UNCH
Crude Oil ($ / Barrel)	$75.21	55.00%
Gold ($ / Oz.)	$1,829.20	-4.00%
U.S. $ / Euro €	$1.14	-8.50%
Core Inflation (excluding food / energy)		4.93%**
Inflation (including food / energy)		6.81%**

**Without Dividends; **Unadjusted 12-Months ended November 2021; bps (1 Basis Point = 1/100%); UNCH (Unchanged)*
Sources for Score Board and quoted statistics: WSJ, US Dept. of Labor, Federal Reserve

Sources:

1. Source: Federal Reserve Bank of Atlanta, Wage Growth Tracker, November 2021.
2. Source: Bureau of Labor Statistics, Job Openings and Labor Turnover, November 2021.
3. Source: S&P Dow Jones Indices
4. The S&P 500 is designed to be a leading indicator of U.S. equities and is commonly used as a proxy for the U.S. stock market. Price return quoted.
5. Source: Kostin, David. *US Weekly Kickstart*. Goldman Sachs, January 2022.
6. The MSCI Emerging Markets Index captures large and mid-cap segments in 26 emerging markets. Price return quoted (USD).
7. The Barclays Aggregate Bond Index is a broad-based index used as a proxy for the U.S. bond market.