MONTH IN REVIEW

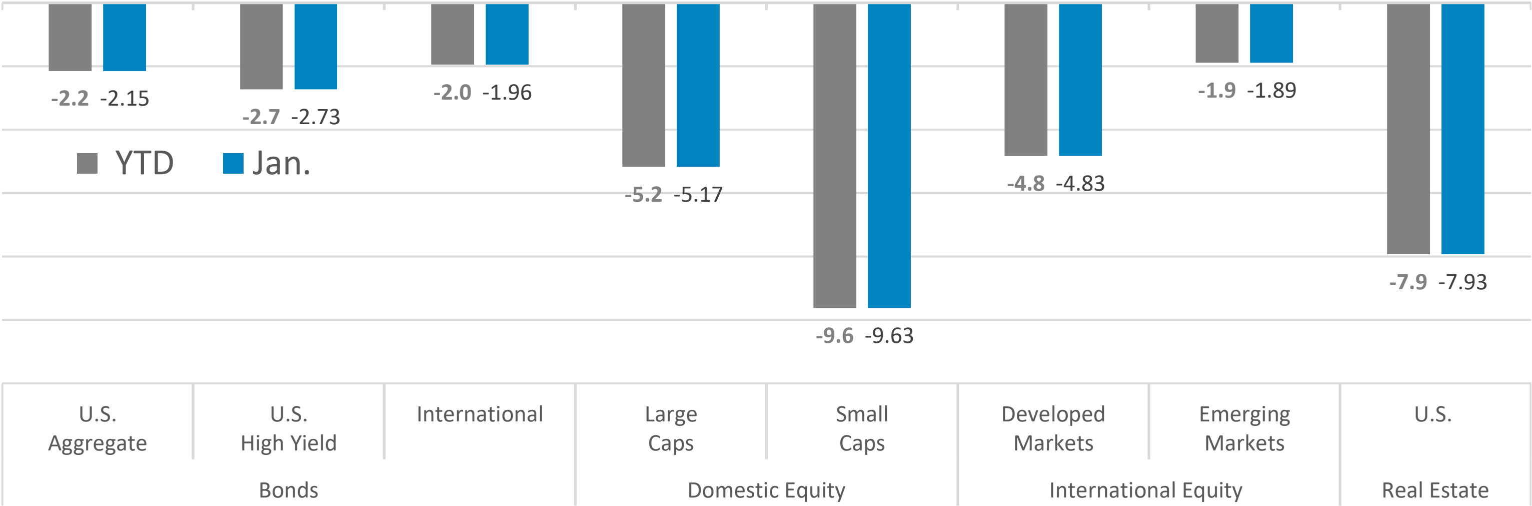
January 2022

Quick Takes

- **Markets Loose Footing as Fed Turns Hawkish.** With the Fed promising to take aggressive action against rising inflation, market participants spent the month of January in risk off mode, sending all asset classes into the red for the first month of 2022.
- **Short-Term Yields and Long-Term Yields Jump.** With the Fed's hawkish stance, yields, both on the 2-Year UST Note and the 10-Year UST Note, skyrocketed as investors priced in a more aggressive monetary tightening process for the year. The first rate hike is now expected to occur in March.
- **Greenback Strengthens in January.** Consistent with a more hawkish Fed, the Dollar strengthened for the first month of the year, but finished the month at 96.54, which was below its high of 97.27.
- **Supply chains, Labor Markets, and Inflation.** Employment spent most of the month softening, this was likely a delayed effect due to the rapid spread of the omicron variant. Inflation, as measured by the Consumer Price Index (CPI) hit its highest level since the 1980s at the January data release and supply chains remained constrained overall. Despite these headwinds, GDP for 2021 posted its strongest advance since the 1980s.

Asset Class Performance

Markets finished the first month of the new year by posting their worst month since March of 2020, or since the start of the global pandemic. Domestic equities led the way down, and while still negative, Bonds, International Equities, and even Emerging Markets were down significantly less than US equities.



Source: Bloomberg, as of December 31, 2021. Asset-class performance is presented by using total returns for an index proxy that best represents the respective broad asset class. U.S. Bonds (Barclays U.S. Aggregate Bond TR), U.S. High Yield (Barclays U.S. HY 2% Issuer-Capped TR), International Bonds (Barclays Global Aggregate ex USD TR), Large Caps (S&P 500 TR), Small Caps (Russell 2000 TR), Developed Markets (MSCI EAFE NR USD), Emerging Markets (MSCI EM NR USD), Real Estate (FTSE NAREIT All Equity REITS TR).

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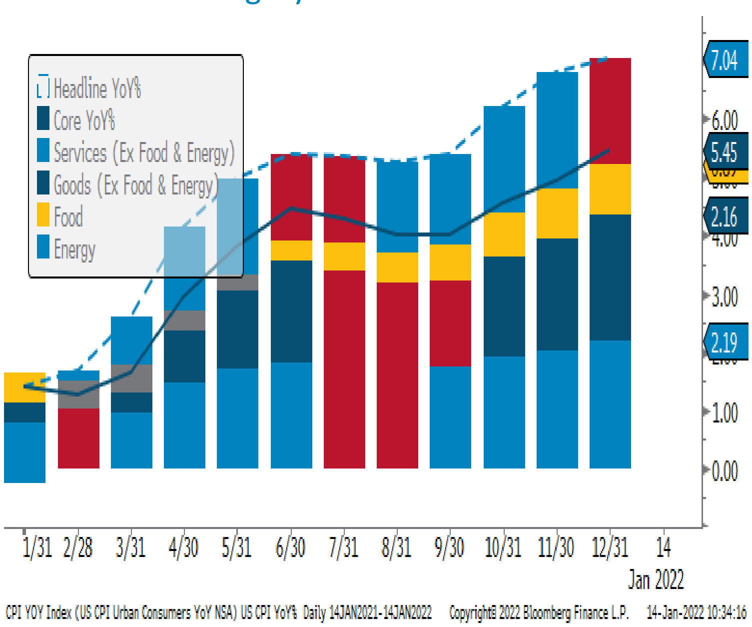
Fed Promises Aggressive Action Against Accelerating Inflation

After Jerome Powell was confirmed for a second term as Chairman of the FOMC and several rotations of regional Presidents becoming voting members, the narrative surrounding the Fed's outlook on future monetary policy actions turned decidedly hawkish. Many members vowed to take aggressive actions in combatting rising inflation. For the January inflation reading, inflation, as measured by the CPI, accelerated at its fastest pace since the 1980s, coming in at +7.0% on an annualized basis. Continued accelerating inflation, combined with robust economic growth, as measured by the change in GDP (right), and tight labor markets, led the FOMC to an acceleration of their tapering process and has opened the door to a sooner than expected liftoff in interest rates. Previously, market participants were expecting the first increase in interest rates to occur in late 2022 or possibly early 2023, after the Fed's shift to a hawkish stance, market participants are now expecting the first increase to occur in March of 2022 and are now expecting multiple rate hikes to occur during this year. Tighter monetary policy typically leads to slowing economic growth, which was the main catalyst for traders shifting into risk off mode for the first month of the year.

Inflation Climbs at Fastest Annual Rate Since 1980s

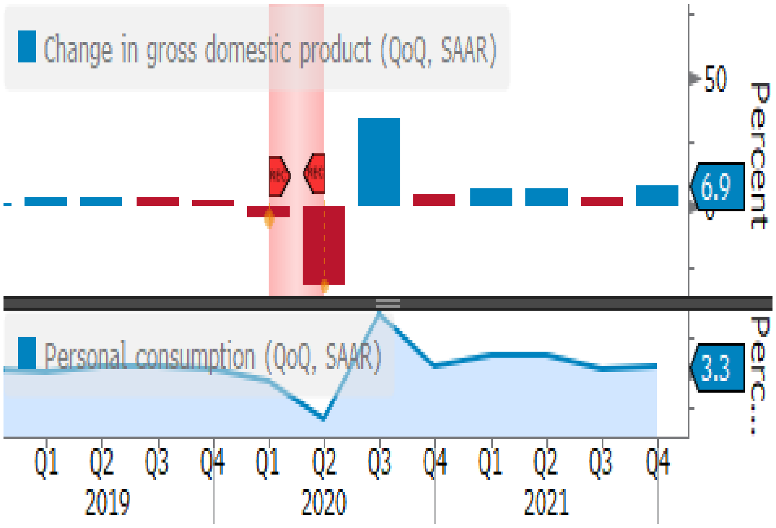
CPI YoY and Category Contribution



Source: Bureau of Labor Statistics, Bloomberg

Economic Growth was Red Hot for 2021

Change in GDP (QoQ), Personal Consumption QoQ (Bottom)



Source: Bureau of Economic analysis, Bloomberg

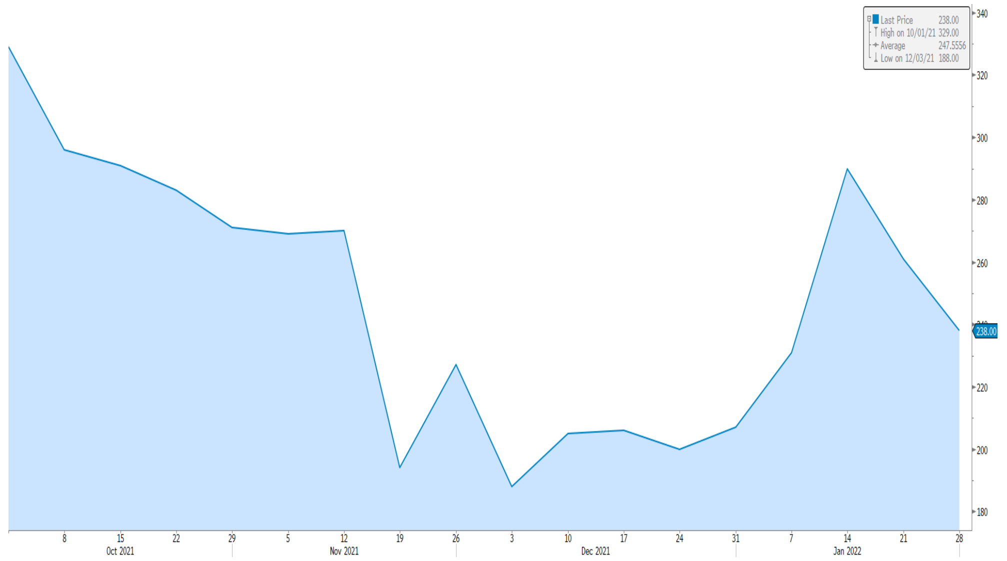
While consumers are still well positioned after the unprecedented amount of stimulus distributed by the government during the global pandemic, the expectation of slowing economic growth seems to be weighing on consumption habits. As seen in the chart above, personal consumption flatlined for the final months of the year, possibly signaling that consumers are delaying current spending due to the expectation of increased costs in the future. Additionally, the rapid spread of the omicron variant may have impacted some spending habits and leisure activities during the holiday season. It's possibly the consumption may swing upwards as omicron cases rollover.

Bottom Line: The Fed's shift to a hawkish stance and promises to aggressively fight inflation led market participants to quickly pivot into risk off mode for the month of January as they priced in a sooner than expected liftoff and frequency in interest rate hikes. This led to all major asset classes posting a negative month for the first month of 2022. This flight to safety and expectation of tighter monetary policy, and thus slowing future economic growth, overshadowed robust economic growth in the final quarter of 2021.

Focused on the Fed

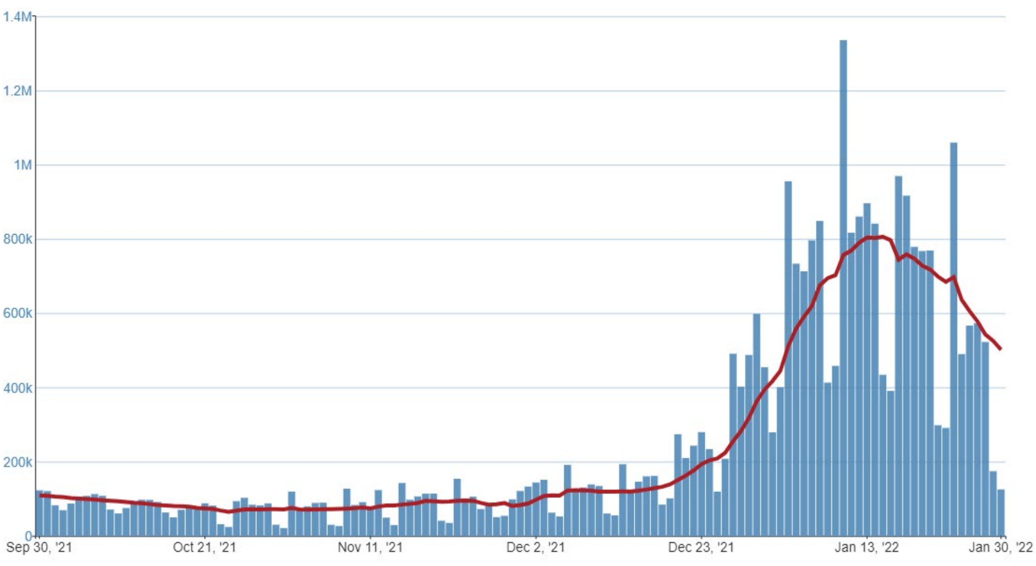
As shown in the chart below, Omicron cases rapidly spiked in the final months of last year but appear to have peaked in the middle of January and continued to rollover as the month went on. While it appears that we will be living with a continued threat from new covid-19 variants, it also appears that their impact may be less severe than previous variants. While any new variant's impact may be less, they are not zero. As shown in the chart on the right, weekly jobless claims spiked in tantum with covid-19 cases. Like the covid-19 cases, the weekly jobless claims quickly rolled over for the month of January but were consistently higher than consensus estimates throughout the month. This may influence the unemployment reading set to be released during the first week of February, but market participants are likely to ignore any missteps in the reading. While traders may shrug off any misses in employment data as short lived, they will likely look deeper at impacts to supply chains caused by the rapid spread in the omicron variant. Constraints relating to global supply chains have placed continued upward pressure on inflation since the start of the global constrained. Over the next several months, market participants will likely look for noticeable improvements in supply chain conditions and their effect on inflation. If supply chain conditions begin to improvement, thus decrease the upward pressure on inflation, this could materially affect the Fed's timeline and magnitude of their tightening process. Ultimately, market participants will continue to place the most emphasis on inflation and the expected actions taken by the Central Bank to combat rising prices.

Jobless Claims Rollover with Omicron
US Initial Jobless Claims



Source: Department of Labor, Bloomberg

Omicron Cases Rapidly Spike, but Rollover Quickly
Daily Count of Covid-19 Cases Reported to CDC



Source: Centers for Disease Control and Prevention

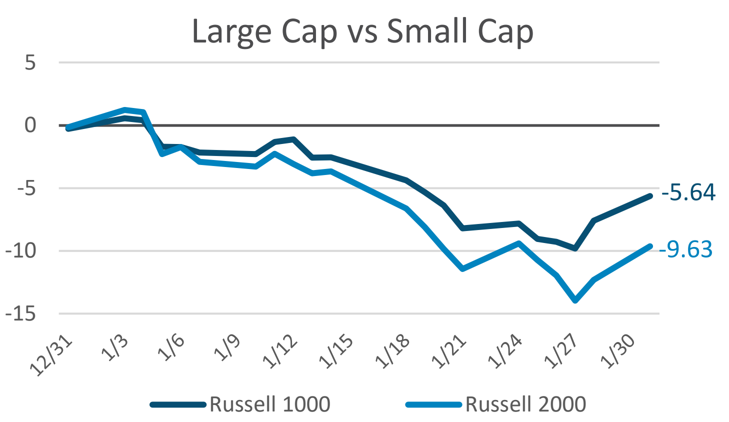
<u>Bottom Line</u>: **Rising costs in the economy will remain top of mind for investors in the coming week as well as the Fed's anticipated actions to combat runaway inflation. With the amount of uncertainty the market is currently facing, market participants can likely expect increased volatility throughout at least the first half of the year. Heightened volatility may continue into the latter half of the year if the Fed isn't able to quickly temper inflation and thus is forced to begin the quantitative tightening process sooner than currently anticipated.**

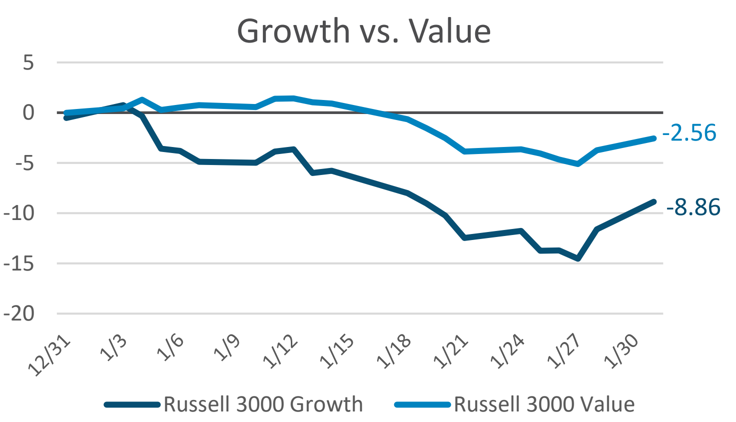
January 2022

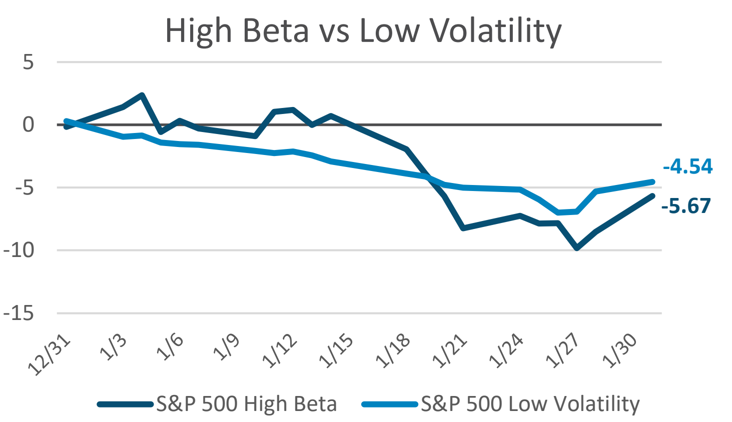
Equity Themes

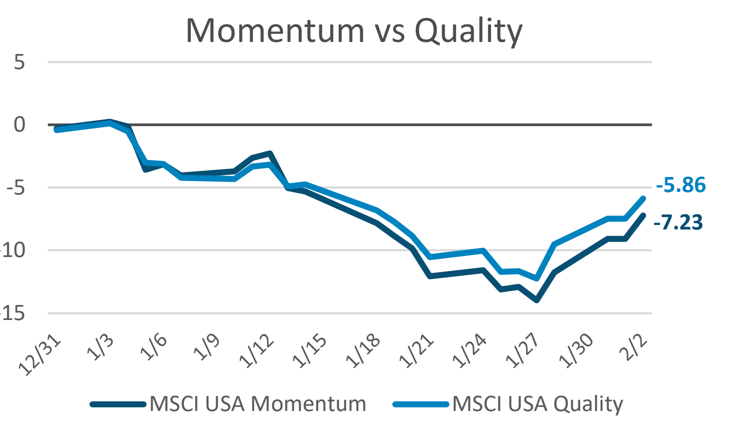
What Worked, What Didn't

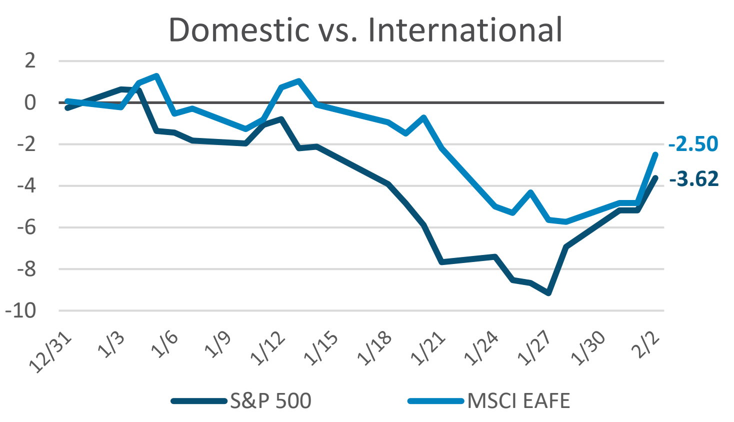
- **Large over Small, Value over Growth.** Small Cap equities tumbled during the first month of the year as market participants switched to risk off mode. Large Cap equities outperformed relative to Small Caps but were still deeply in the red for the month of January. Value candidly outperformed Growth, consistent with the risk off theme.
- **Quality and Low Volatility Outperform.** Continuing where December ended, Quality and Low Volatility outperformed their respective Momentum and High Beta peers for the month of January, but all were still negative for the first month of the year.
- **International Markets Offer Downside Protection.** After struggling all last year to keep pace with Domestic Equities, International Markets, especially Emerging Markets, offered some downside protection for the month.

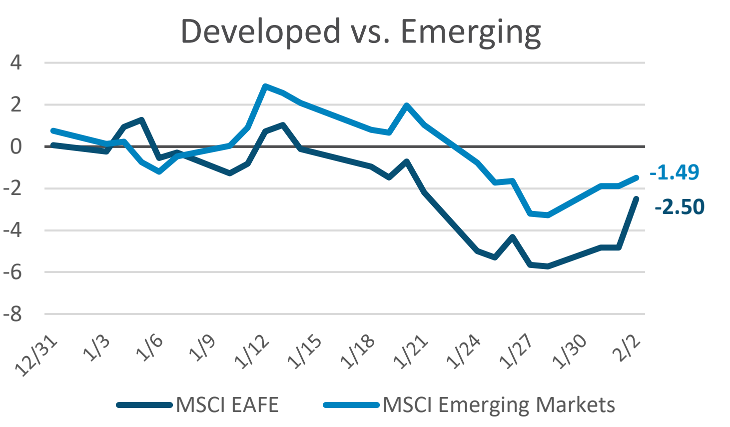








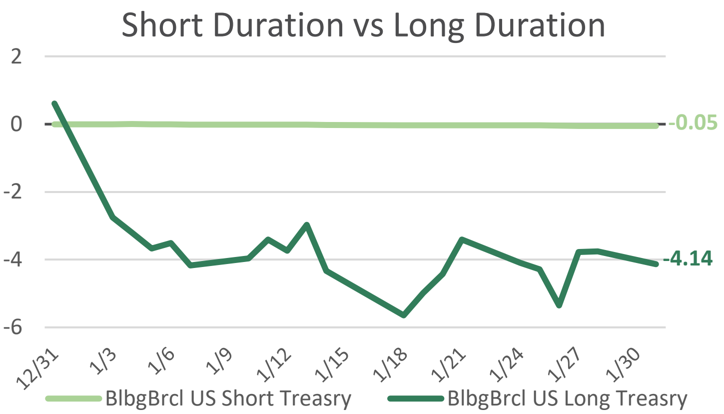


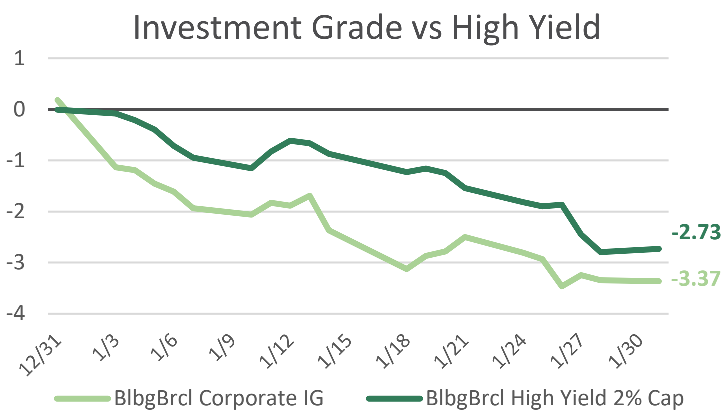


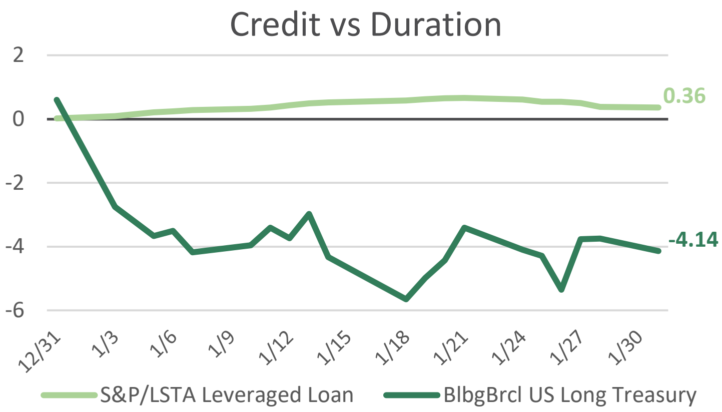
Source: Bloomberg.

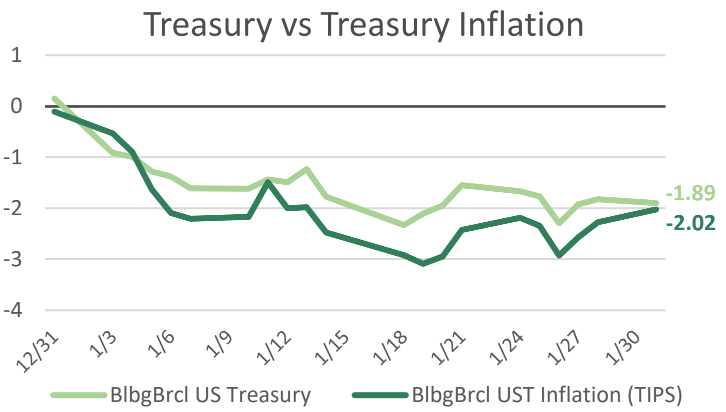
What Worked, What Didn't

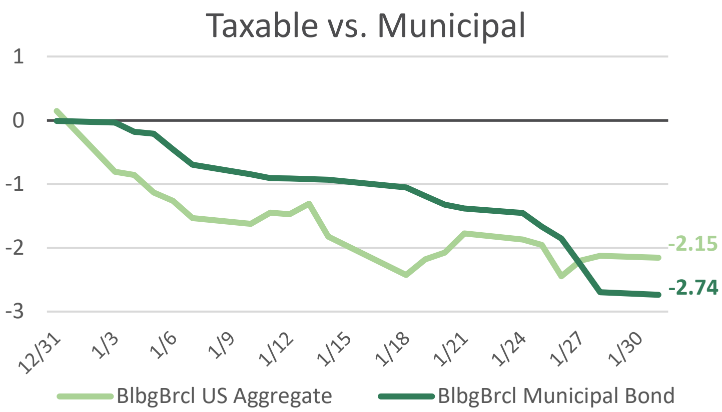
- **Short Duration and Risky Bonds Outperform.** Continuing right where last year ended, the yield curve steepening yet again, leading to Short Duration bonds outperforming their longer dated peers. While still negative for the month, High Yield offered some downside protection versus Investment Grade.
- **Flight To Safety.** Reversing the previous trend, Treasuries outperformed their Inflation Protected peers, albeit by a small margin, and Taxables offered more downside protection compared to Munis for the month of January.
- **Go Abroad.** International bonds offered limited downside protection relative to their domestic peers but were still in the red for the month of January.

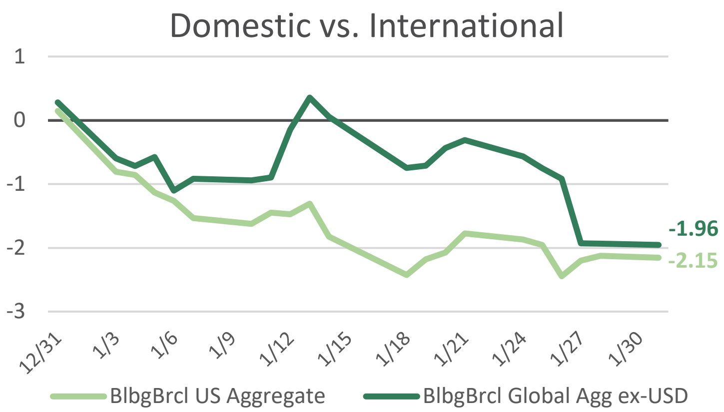












Source: Bloomberg.

January 2022
Asset Class Performance

MONTH IN REVIEW

The Importance of Diversification. From period to period there is no certainty what investment will be the best, or worst, performer. Diversification mitigates the risk of relying on any single investment and offers a host of long-term benefits, such as less portfolio volatility, improved risk-adjusted returns, and more effective compounding.

	Jan-03	Jan-04	Jan-05	Jan-06	Jan-07	Jan-10	Jan-11	Jan-12	Jan-13	Jan-14	Jan-18	Jan-19	Jan-20	Jan-21	Jan-24	Jan-25	Jan-26	Jan-27	Jan-28	Jan-31	Jan	YTD	
High	SCG 1.24	MCV 1.02	IBD 0.18	SCV 0.84	EM 0.91	HYB 0.08	EM 2.31	EM 1.66	USB 0.18	SCV 0.61	HYB -0.49	IBD 0.49	EM 0.59	IBD 0.46	SCG 3.17	USB -0.10	LCG 0.05	USB 0.33	LCG 3.52	SCG 2.86	RE 11.17	EM -0.02	High
	SCV 1.22	LCV 0.88	USB -0.31	EM 0.46	IBD 0.50	EM 0.00	MCG 1.60	IEQ 0.98	IBD 0.09	LCG 0.25	USB -0.61	EM 0.43	USB 0.05	USB 0.39	MCG 1.98	EM -0.19	HYB -0.34	LCV -0.29	RE 3.11	SCV 2.69	MCV 7.78	USB -2.00	
	LCG 0.72	SCV 0.68	HYB -0.77	MCV 0.44	IEQ 0.29	LCG -0.06	SCG 1.43	IBD 0.96	SCV -0.20	EM -0.04	RE -0.90	USB 0.22	HYB -0.19	HYB 0.01	SCV 1.79	HYB -0.29	IEQ -0.39	HYB -0.44	MCG 3.01	MCG 1.31	LCV 7.35	LCV -2.37	
	EM 0.72	IEQ 0.57	LCV -0.88	MCG 0.20	LCV 0.25	MCG -0.07	LCG 1.14	60/40 0.35	MCV -0.26	HYB -0.09	IBD -1.25	IEQ -0.09	IBD -0.22	RE -0.24	LCG 0.80	IBD -0.35	IBD -0.55	60/40 -0.47	SCG 2.51	MCV 1.28	SCV 6.15	HYB -2.65	
	IEQ 0.65	60/40 0.01	IEQ -0.88	LCV 0.20	MCV -0.04	USB -0.09	IEQ 1.09	LCG 0.33	RE -0.32	IEQ -0.10	60/40 -1.36	HYB -0.09	IEQ -0.49	60/40 -0.84	MCV 0.68	LCV -0.40	USB -0.56	IEQ -0.47	MCV 1.61	EM 1.24	IEQ 5.01	IBD -2.98	
	LCV 0.35	USB -0.01	60/40 -1.24	SCG 0.13	60/40 -0.18	LCV -0.15	MCV 1.02	HYB 0.16	HYB -0.36	LCV -0.16	LCV -1.46	60/40 -0.28	60/40 -0.49	IEQ -1.36	LCV 0.17	RE -0.45	60/40 -0.61	IBD -0.75	LCV 1.47	LCG 0.98	LCG 3.96	IEQ -3.63	
	60/40 0.00	IBD -0.15	MCV -1.55	HYB 0.01	HYB -0.26	60/40 -0.29	LCV 0.81	RE 0.10	LCV -0.41	SCG -0.21	IEQ -1.47	MCG -0.75	LCV -0.95	LCV -1.40	RE 0.16	SCV -0.57	LCV -0.68	MCV -0.78	SCV 1.39	RE 0.97	MCG 3.55	60/40 -3.97	
	MCV -0.03	RE -0.19	EM -1.63	RE -0.02	USB -0.29	SCG -0.38	60/40 0.80	LCV 0.08	60/40 -0.65	60/40 -0.28	MCV -1.72	LCV -0.88	MCG -1.24	EM -1.45	60/40 -0.03	IEQ -0.61	MCV -0.72	LCG -0.86	60/40 0.97	IEQ 0.91	SCG 3.16	MCV -4.40	
	HYB -0.05	HYB -0.25	SCV -2.21	60/40 -0.07	SCV -0.45	SCV -0.42	SCV 0.73	MCV 0.08	IEQ -0.73	MCV -0.29	EM -1.78	LCG -1.08	LCG -1.24	SCV -1.45	HYB -0.11	60/40 -0.68	MCG -1.14	EM -1.16	EM 0.49	LCV 0.86	60/40 3.10	SCV -5.85	
	USB -0.68	EM -0.35	RE -2.96	USB -0.11	RE -0.67	IBD -0.49	HYB 0.47	USB 0.00	EM -1.42	USB -0.56	LCG -2.31	MCV -1.20	RE -1.24	MCV -1.46	USB -0.12	MCV -0.78	SCV -1.26	MCG -1.43	IEQ 0.34	60/40 0.80	HYB 2.27	RE -8.23	
	RE -0.76	SCG -0.99	LCG -3.19	IBD -0.23	LCG -1.10	RE -0.51	RE 0.25	SCV -0.41	SCG -1.77	MCG -0.64	SCV -2.44	RE -1.26	MCV -1.49	SCG -2.28	IBD -0.32	LCG -2.24	EM -1.27	RE -1.50	HYB 0.28	IBD 0.44	EM 1.16	LCG -8.68	
	IBD -0.95	LCG -1.04	MCG -3.87	LCG -0.28	MCG -1.63	MCV -0.58	USB 0.19	MCG -0.43	LCG -2.49	IBD -0.66	MCG -2.59	SCG -1.54	SCG -1.77	MCG -2.37	IEQ -1.00	SCG -2.53	SCG -1.61	SCV -2.02	USB 0.07	USB 0.28	IBD 0.31	MCG -12.93	
Low	MCG -1.03	MCG -1.43	SCG -4.36	IEQ -0.51	SCG -1.85	IEQ -0.93	IBD 0.18	SCG -1.04	MCG -2.67	RE -0.95	SCG -3.67	SCV -1.61	SCV -1.99	LCG -2.61	EM -1.41	MCG -3.10	RE -1.62	SCG -2.58	IBD -0.30	HYB 0.27	USB -0.38	SCG -13.42	Low

Legend

- 60/40 Allocation (60/40)
- Large Growth (LCG)
- Large Value (LCV)
- Mid Growth (MCG)
- Mid Value (MCV)
- Small Growth (SCG)
- Small Value (SCV)
- Intl Equity (IEQ)
- Emg Markets (EM)
- U.S. Bonds (USB)
- High Yield Bond (HYB)
- Intl Bonds (IBD)
- Real Estate (RE)

Source: Bloomberg. Asset-class performance is presented by using market returns from an exchange-traded fund (ETF) proxy that best represents its respective broad asset class. Returns shown are net of fund fees for and do not necessarily represent performance of specific mutual funds and/or exchange-traded funds recommended by the Prime Capital Investment Advisors. The performance of those funds may be substantially different than the performance of the broad asset classes and to proxy ETFs represented here. U.S. Bonds (iShares Core U.S. Aggregate Bond ETF); High-Yield Bond (iShares iBoxx $ High Yield Corporate Bond ETF); Intl Bonds (SPDR® Bloomberg Barclays International Corporate Bond ETF); Large Growth (iShares Russell 1000 Growth ETF); Large Value (iShares Russell 1000 Value ETF); Mid Growth (iShares Russell Mid-Cap Growth ETF); Mid Value (iShares Russell Mid-Cap Value ETF); Small Growth (iShares Russell 2000 Growth ETF); Small Value (iShares Russell 2000 Value ETF); Intl Equity (iShares MSCI EAFE ETF); Emg Markets (iShares MSCI Emerging Markets ETF); and Real Estate (iShares U.S. Real Estate ETF). The return displayed as "Allocation" is a weighted average of the ETF proxies shown as represented by: 30% U.S. Bonds, 5% International Bonds, 5% High Yield Bonds, 10% Large Growth, 10% Large Value, 4% Mid Growth, 4% Mid Value, 2% Small Growth, 2% Small Value, 18% International Stock, 7% Emerging Markets, 3% Real Estate.

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