Financial Market Outlook and Portfolio Strategy Update

(February 14, 2022)

Given the volatility in the first six weeks of 2021, several clients have been asking about our outlook for the financial markets in 2022.

First let me say, that despite the performance of the stock indexes so far this year, we believe that 2022 can still turn out to be quite good for stocks in general. The key has been, in this frantic environment of rising interest rates and concern about how much the Federal Reserve will hike their Fed Funds Rate, is to limit market risk and seek out investment opportunities for our portfolios that are not dependent on the performance of market indexes. And, to avoid interest rate sensitive bonds and other securities that do not have good prospects in 2022.

Commodities have been stellar performers in 2022. We particularly like energy and base metals, which are overweight in our IRA and non-retirement portfolios. However, commodities across the board have been strong performers and important portfolio diversifiers in this inflationary environment. The three commodity ETFs we hold in our IRA and non-retirement accounts, COM, COMB, and PDBC, were all positive by more than 1% on Friday. That same day the S&P 500 Index was down 1.9% and the Nasdaq Composite was down 2.8%. All three ETFs are delivering strong positive returns year-to-date in 2022.

In our GM, Ford, and other 401(k) portfolios we hold real asset funds in large allocations (where available). These funds hold commodities and other hard assets that tend to perform well in both inflationary and rising interest rate environments. They have also provided diversification for our stock investments, as traditional bonds have not been suitable in this environment. In the Ford 401(k) plan, the SSgA Real Asset Fund is up 4.2% in 2022 through Friday, versus a decline of 4.1% for the BlackRock Bond Index Fund over that same period.

In fact, we have pounded the table about staying away from interest rate sensitive bonds for some time now. The BlackRock Bond Index fund offered in both GM and Ford 401(k) plans is down more than 4% in 2022, after a 1.5% decline in 2021. So much for the safety of bonds! It's also worth noting that we have not held these bond funds in any GM, Ford, and other 401(k) portfolios for nearly a year.

In our IRA and non-retirement portfolio strategies we are also turning to alternative investment strategies. NexPoint Merger Arbitrage Fund is one such fund that is not directly correlated to stocks or bonds. It has a level of volatility lower than most bond funds, but versus the U.S. Aggregate Bond Index that has declined more than 4% in 2022, NexPoint Merger Arbitrage Fund is slightly positive in 2022.

Long/short stock funds are also opportunistic in challenging periods for the stock indexes, such as the environment in early 2022. Long/short funds are long some stock positions in the portfolio and short other positions. Invenomic Fund and AQR Equity Market Neutral Fund are examples of long/short funds we hold and in which we have been increasing allocations in client portfolios. For an example of their benefits, last Thursday when the CPI inflation data was released for January and surpassed the forecast of all major banks and wirehouses, the

S&P 500 Index and Nasdaq Composite fell 1.8% and 2.1%, respectively, that day. Both the Invenomic Fund and AQR Equity Market Neutral Fund were positive for the day. On Friday, the S&P 500 Index and Nasdaq Composite fell another 1.9% and 2.8%, respectively, that day. Invenomic Fund was up 1.9% and AQR Equity Market Neutral was up 1.4% for the day.

Franklin Global Market Neutral Fund is a more conservative long/short fund we own to replace bonds in our portfolios. While more conservative, it is a welcome addition in an era where we must avoid negative returning bond sectors. It also had a positive return on Friday, when the major indexes were deep in the red.

Furthermore, and still at the core of our more aggressive portfolios, we are focusing on funds and ETFs that hold quality companies with strong balance sheets. With the Fed pivoting from an accommodative monetary policy to one of a tightening monetary policy, stock style and sector selection become far more important. Gone are the days of the Fed pumping liquidity into the financial system and the rising tide simply lifting all market indexes. It's back to analyzing fundamentals for companies and stocks to determine those suitable for an investor's portfolio.

This does not mean that many stocks and sectors cannot perform well this year. Indeed, many stock sectors can and will. As 2022 unfolds, there will be several areas within the stock market that will offer immense opportunity. We still look for a positive and very profitable year for our portfolios in 2022.

Our tactical strategy with a bit more diversification and defense early in the year, relative to each portfolio strategies objectives and risk profile, has proved prudent. However, we know that more profitable opportunities will present themselves throughout the year, just as the ones we are currently holding in commodities, alternatives, and other areas. And, we will be working diligently to seek them out and employ them, while avoiding the pitfalls of areas, such as traditional bonds.

It is important to keep your eye on your long-term goals and not get shaken by short-term volatility. Leave the work and worry to us. I hope this report has helped you understand our current strategy a bit better and our outlook for 2022.

Please continue to keep yourself and your loved ones healthy and safe. As always, if you ever have any questions about your portfolio holdings, our investment strategy, the financial markets, your personal financial plan, or anything related to your personal finances, contact us at 810-953-5510 or toll-free at 866-444-6246. We always look forward to talking with you.

Sincerely,

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