"Sooner and Faster"

Performance for Week Ending 1.7.2022

The Dow Jones Industrial Average (Dow) finished off 0.29%, the Wilshire 5000 Total Market Index^{SM} (Wilshire 5000^{SM}) lost 2.35%, the Standard & Poor's 500 Index (S&P 500) slumped 1.87% and the Nasdaq Composite Index (NASDAQ) dipped 4.53%. Sector performance had a cyclical bias with Energy (+10.6%), Financials (+5.4%) and Industrials (+0.65%) posting the biggest gains. On the flip side, the interest rate sensitive Real Estate sector (-4.9%) was the biggest loser.

Index*	Closing Price 1/7/2022	Percentage Change for Week Ending 1/7/2022	Year-to-Date Percentage Change Through 1/7/2022
Dow	36231.66	-0.29%	-0.29%
Wilshire 5000	47321.15	-2.35%	-2.35%
S&P 500	4677.03	-1.87%	-1.87%
Nasdaq	14935.90	-4.53%	-4.53%

Market Observations: 1/3/22– 1/17/22

The major market indices finished the first week of the new year on a negative note reflecting the ongoing surge in Covid cases, mixed payroll data, and the more hawkish than expected December Federal Open Market Committee (FOMC) meeting minutes. On the latter, Fed members said they "generally" believe the central bank may need to raise interest rates "sooner or at a faster pace than participants had earlier anticipated." Treasury yields moved higher with the benchmark 10-year yield climbing to 1.76% - the highest level since January 2020.

Payroll Data: While the December payroll report was mixed, overall it appears strong enough to keep the Fed on track to raise rates in the coming months. According to the Labor Department, nonfarm payrolls advanced by 199K, well short of the 450K expected by economists. However, the Labor Department upwardly revised the prior two months' worth of data, showing an additional 141K jobs created. The unemployment rate dropped to 3.9%, the lowest since February 2020, and below the 4.1% forecast by economists. In addition to the drop in the unemployment rate, average hourly earnings rose at a 4.7% year-over-year pace, exceeding the 4.2% forecast. The payroll report followed the much better than expected ADP report on private payrolls earlier in the week. According to the ADP Research Institute the US added 807K jobs during December, nearly double economist expectations. Jobless claims, a barometer for layoffs, continued to hover near the lowest level in 5 decades as companies maintain staffing levels amid widespread worker shortages.

FOMC Meeting Minutes: The release of the December FOMC meeting minutes sent the markets into a tailspin mid-week as they were viewed as more hawkish than expected. According to the minutes, Fed officials signaled greater discomfort with high inflation at their meeting last month, where they eyed a faster timetable for raising interest rates this year. Most central bank officials, in projections released at the conclusion of their Dec. 14-15 meeting, penciled in at least three quarter-percentage-point rate increases this year. In September, around half of those officials thought rate increases could wait until 2023. The minutes also showed rising concern that higher inflation could persist and force a more aggressive response from the Fed, particularly if businesses and consumers begin to expect prices to keep rising rapidly.

What really seemed to spook the market was the discussion of reducing the size of the balance sheet. According to the minutes "some participants also noted that it could be appropriate to begin to reduce the size of the Federal Reserve's balance sheet relatively soon after beginning to raise the federal funds rate." However, no firm plans appear to have been formed at the December meeting. "Participants generally noted that, given their individual outlooks for the economy, the labor market, and inflation, it may become warranted to increase the federal funds rate sooner or at a faster pace than participants had earlier anticipated," the minutes said.

According to Bloomberg's World Interest Rate Probability tool, investors are fully pricing in the first 25 basis point (bps) rate hike at the May FOMC meeting followed by a second at the July meeting and a third at the December meeting. The coming week's CPI report, which is expected to show headline inflation running at a 7.0 percent year-over-year pace, coupled with drop in the unemployment rate could force the Fed's hand to lift rates sooner than May, with a grow odds of a March lift off – stay tuned.

Bullish Narrative Intact: As we look forward, our positive view on the equity market remains intact. While volatility is likely to remain elevated and the pace of gains are likely to slow in the year ahead, we feel the macro environment will remain supportive and should continue to provide a sturdy backbone for additional upside. The US economy remains in good health and growth in the quarters ahead is expected to remain above trend. The US consumer is in good shape and savings rates remain above pre-pandemic levels, suggesting that as consumers become more comfortable with the economic recovery, pent up demand will be unleashed. Earnings expectations also suggest solid forward growth. Based on consensus expectations from Bloomberg, earnings are forecast to grow by nearly 9 percent this year followed by over 10 percent growth in both 2023 and 2024. While a near-term period of consolidation cannot be ruled out, we would view weakness as an opportunity to selectively increase equity exposure.

The Week Ahead: Inflation and Federal Reserve leadership will be the focal points for the week ahead with the release of the December Consumer Price Index (CPI) and the nomination hearings for Fed Chair Powell's second term and Governor Brainard's nomination as Vice Chair. In addition to the CPI data, reports of interest on the data calendar include; retail sales for December, the December producer price index, jobless claims for the week ended January 8, the December import and export prices indexes, December industrial production and the January consumer sentiment report from the University of Michigan. The Fed speaking calendar will be busy with seven speeches on the docket. On Wednesday, the Fed is also scheduled to release the Beige Book report – which will be used as the playbook for this month's FOMC meeting on

January 24 and 25. Fourth quarter earnings season will kick off in earnest with seven members of the S&P 500 scheduled to release results.

Definitions

The Dow Jones Industrial Average is a price-weighted average of 30 blue-chip stocks that are generally defined as the leaders in their industry. It has been a widely followed indicator of the stock market since October 1, 1928.

Wilshire 5000 Total Market IndexSM represents the broadest index for the U.S. equity market, measuring the performance of all U.S. equity securities with readily available price data. The index is comprised of virtually every stock that: the firm's headquarters are based in the U.S.; the stock is actively traded on a U.S. exchange; the stock has widely available pricing information (this disqualifies bulletin board or over-the-counter stocks). The index is market cap weighted, meaning that the firms with the highest market value account for a larger portion of the index.

Standard and Poor's 500 Index is a capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The Nasdaq Composite Index is a broad-based capitalization-weighted index of stocks in all three NASDAQ tiers: Global Select, Global Market and Capital Market. The index was developed with a base level of 100 as of February 5, 1971.