

The year everything went right

This is the time of year where we will see a plethora of summaries about the past year along with predictions on what we should expect in the year ahead. SEM has always taken the stance that these exercises serve little purpose and typically do more harm than good. Over the shorter-term stocks go up when more people buy than sell and go down when more people sell than buy. Human behavior takes over during these shorter periods of time and can lead to large moves that seem to defy logic (even though the financial “experts” will attempt to find reasons to justify the moves).

Over the intermediate to longer-term stocks will track the overall trend in economic growth. The short-term fluctuations are often the result of market participants trying to get ahead of the economic trend. At the end of 2020 we put together a list of potential positives and negatives which could impact the market in 2021. We looked back at this in the Traders Blog at the end of December. Pretty much everything that could have gone right in 2021 did, enough so to wipe out the negatives. Looking ahead to 2022 it is not as easy to see very many positive catalysts, but it is clear there are a lot of negatives stocks will have to overcome. This doesn't mean stocks cannot continue to rally. It does mean it will be harder to justify chasing stocks without strong economic growth to support the already high prices.

At SEM we spent most of the year close to maximum investment. This led to a solid year for all of investment models which utilize stocks in their allocations (see ‘What about bonds?’ on the next page for the rest of the story.) We ended the year close to maximum invested across the board. The key difference is we can adjust rather quickly should the negatives lead to more sellers than buyers.

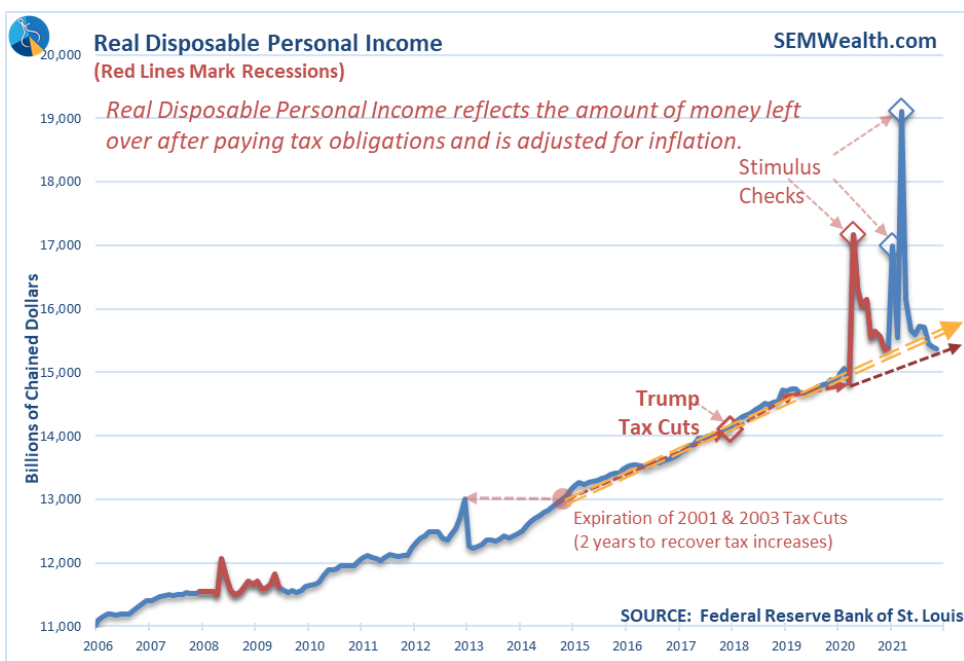
Positives	2021	2022	Negatives	2021	2022
More Stable Government	✓	?	Stocks Overvalued	✓	✓
COVID Vaccine	✓	✗	COVID Worries	✓	?
More Stimulus	✓	✗	Economic Air Pocket	✗	?
Friendly Fed	✓	✗	Short-term Tools	✓	?
Strong Technicals	✓	✗	Sentiment at extremes	✓	✗

[Read the full discussion at Tradersblog.SemWealth.com/mmm2-50](https://tradersblog.semwealth.com/mmm2-50)

Can the economy stand on its own?

It is easy to forget the unprecedented steps Congress and the Federal Reserve took to boost the economy during the pandemic. Going into 2022 not only are we not likely going to see any more stimulus, the Federal Reserve has said they plan on pulling back theirs.

The question will then be whether or not the economy can stand on its own. One indicator we are watching closely is Disposable Income. The orange line on the chart at the left shows it is now running BELOW the trend going all the way back to 2015. If Disposable Income growth slows, consumer spending and thus economic growth will likely follow.



For the latest updates and analysis, go to tradersblog.semwealth.com

What about bonds?

Following a third consecutive above average year for stocks, many investors may be asking themselves, “why even bother with bonds?” The Barclay’s Aggregate Bond Index ended the year with negative returns. While SEM’s actively managed fixed income based models finished ahead of the overall bond market we understand years like 2021 lead to questions about the role these models play in a portfolio.

First, we must understand most investors cannot stomach a 35-50% drop in their investment portfolios which will occur at times if you only invest in stocks. Therefore, other assets need to be used to lower the risk in the overall portfolio. Secondly, bond returns often move in opposite directions of stocks. This provides a nice buffer when stocks decline. Finally, as shown in the table to the right, it is quite rare for bonds to decline for two consecutive years.

When investing it is important to not let the recent past influence our decisions. The recent weakness in bonds could be an opportunity to readjust portfolios that may be significantly overweight stocks.

Stay tuned to TradersBlog.SEMWealth.com for more details on economic developments in the months ahead and how we are positioning our portfolios.

BOND MARKET RETURNS

SOURCE: Blackrock Student of the Market, December 2021

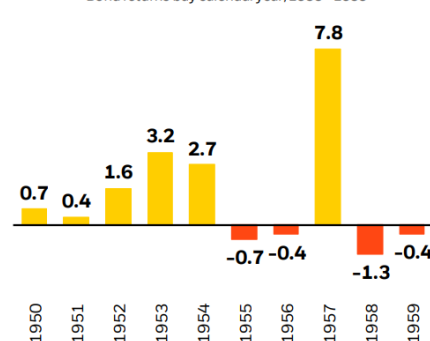
Consecutive years with negative bond returns are rare

Bonds are on pace for a negative calendar year in 2021

Bonds have not lost money in back to back years since the 1950s (1/1/1926 – 11/30/21)

	Return	Return the following year
1994	-2.9	18.5
1931	-2.3	8.8
2013	-2.0	6.0
2021	-1.3	?
1958	-1.3	-0.4
1999	-0.8	11.6
1969	-0.7	16.9
1955	-0.7	-0.4
1956	-0.4	7.8
1959	-0.4	11.8

The 1950s had two periods with back to back years where bonds lost money
Bond returns buy calendar year, 1950 - 1959



Data Source: Morningstar Direct | Past performance is not a guarantee of future results | Informational purposes only; Not Investment advice | You cannot invest directly in the index without additional fees.

News & Notes:

2021 Year-End Tax Statements—what to watch for early 2022:

For taxable accounts, federal law requires your custodian to mail your **IRS Form 1099** to you by January 31. Due to the increasing amount of reclassified mutual fund distributions, Axos Advisor Services has had this **extended to February 15, 2022**.



SEM strongly recommends you do not make your tax appointment until after February 15.

The 2021 Consolidated 1099 mailings to you includes cost basis and sales proceeds for investments sold during 2021. This provides **essential information** needed to complete your **Federal Tax Filing Form 1040 Schedule D and Form 8949**. Please wait until you receive Axos’s 2021 Consolidated 1099 prior to completing your taxes.

For those clients that consolidated taxable accounts from another custodian to Axos, you will receive forms from both custodians.

SEM will be posting additional information on the tax reports on our website:

SEMWealth.com/tax-information

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