



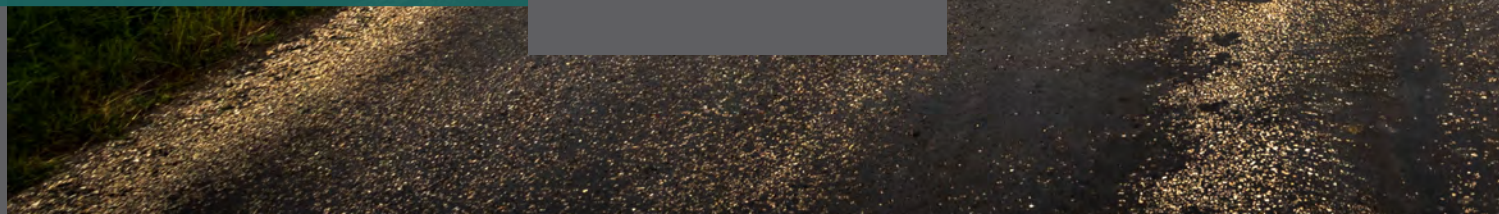
CORBETT ROAD
WEALTH MANAGEMENT

MACRO MUSINGS

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A Rocky Start to the Year

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SUMMARY

- Our models suggest markets will be more volatile in 2022, but declines are unlikely to result in a recessionary bear market.
- The market has started the year with a correction, the first since 2020. An increase in volatility was expected coming into the year, given the large gains and lower volatility last year. When viewed from a historical lens, the recent pullback is unsurprising, but typically, sustained, bear market declines are uncommon absent an economic recession.
- 2021 saw historic gains, with the S&P 500 up over 25%. Gains of that magnitude often followed through the next year, but those returns came with additional volatility and greater market drawdowns.

MARKET UPDATE:

FIRST CORRECTION SINCE SEPTEMBER 2020

Normally, in our January Macro Musings, we conduct an in-depth review of the prior year and assess the current state of the markets with an analysis of **macrocast™**, but given the recent volatility, we will instead focus on what is currently happening in the market. A brief asset class review can still be found towards the end of this note.

As of this writing on Monday, January 24th, the S&P 500 is in the midst of its first double-digit correction since September 2020. Other headline indices, such as the tech-heavy Nasdaq and the small-cap Russell 2000, have seen even greater drawdowns.

There have been several reasons cited for the decline, among them:

1. Inflation reached multi-decade highs last month.
2. The Federal Reserve is set to end quantitative easing (QE) in March and is now expected to raise interest rates four times in 2022.
3. Geopolitical tension between Russia and Ukraine.
4. Continued economic and supply chain disruptions, as a result of the Omicron variant.

While these issues may sound alarming, they are nothing new (outside of the Russia/Ukraine situation). Inflation has been high for the entire second half of 2021. The Fed announced the end of QE in November. Multiple rate hikes were also expected, albeit the base case has shifted from three increases this year to four. COVID cases appear to be declining across most of the globe, and those trends should continue over the next month.

Given the noise in the above headlines, we find it helpful to view the current market through a historical lens, allowing us to put the current correction into perspective and provide insight on what to expect going forward.

First, years with shallow pullbacks like 2021 were almost always followed by larger declines. After a pullback of just 5% last year, 2022 has already doubled that figure and is approaching the average drawdown levels witnessed after similar, shallow drawdown years (table from Truist):

S&P 500 drawdowns and returns in years following shallow pullbacks

Year with shallow drawdown			Following year		
Year	Largest intra-year pullback	Calendar year total return	Year	Largest intra-Year pullback	Calendar year total return
1995	-3%	37%	1996	-8%	23%
2017	-3%	22%	2018	-20%	-4%
1964	-4%	16%	1965	-10%	12%
1958	-4%	43%	1959	-9%	12%
1954	-4%	53%	1955	-11%	32%
1961	-4%	27%	1962	-27%	-9%
1993	-5%	10%	1994	-9%	1%
1972	-5%	19%	1973	-23%	-15%
1991	-6%	31%	1992	-6%	8%
2013	-6%	32%	2014	-7%	14%
2021	-5%	29%		?	?
*Average	-4%	29%		-13%	7%
*Median	-4%	29%		-9%	10%

Second, 2021 was the 15th time the S&P 500 has returned over 25% in a calendar year since 1950. Far from suggesting lower returns ahead, the market was positive a year later in all but two of the prior instances. In the two cases where returns were negative, the losses were less than 10% (table from LPL):

Greater Than 25% Years Are A Good Sign For The Next Year

S&P 500 Index Returns After Big Yearly Returns

Year	S&P 500 Return	
	Return	Next Year Return
1954	45.0%	26.4%
1955	26.4%	2.6%
1958	38.1%	8.5%
1975	31.5%	19.1%
1980	25.8%	-9.7%
1985	26.3%	14.6%
1989	27.3%	-6.6%
1991	26.3%	4.5%
1995	34.1%	20.3%
1997	31.0%	26.7%
1998	26.7%	19.5%
2003	26.4%	9.0%
2013	29.6%	11.4%
2019	28.9%	16.3%
2021	26.9%	?
Average		11.6%
Median		13.0%
% Positive		85.7%
Average Year (1950 - 2020)		9.2%
Median		11.8%
% Positive		71.8%

Source: LPL Research, FactSet 01/01/22

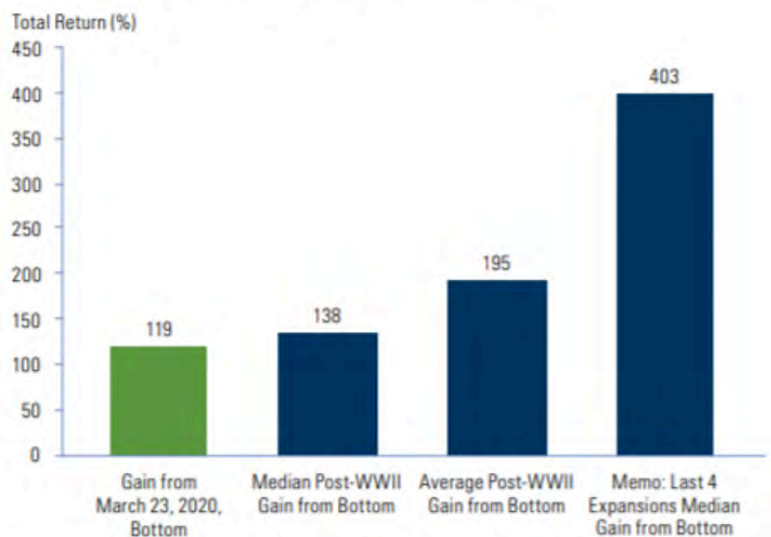
All indexes are unmanaged and cannot be invested into directly. Past performance is no guarantee of future results.

The modern design of the S&P 500 stock index was first launched in 1957. Performance back to 1950 incorporates the performance of predecessor index, the S&P 90.

Third, while the market is up substantially since the March 2020 lows, history suggests we may have more upside before the next recession, especially if we focus on the four most recent economic expansions. The data is as of 12/31, so the gain since the March bottom is lower than the figure shown below (chart from Goldman Sachs):

Exhibit 110: S&P 500 Total Return from Equity Trough to Beginning of Next Recession

Past economic expansions imply further upside for stocks despite the impressive gains seen already.

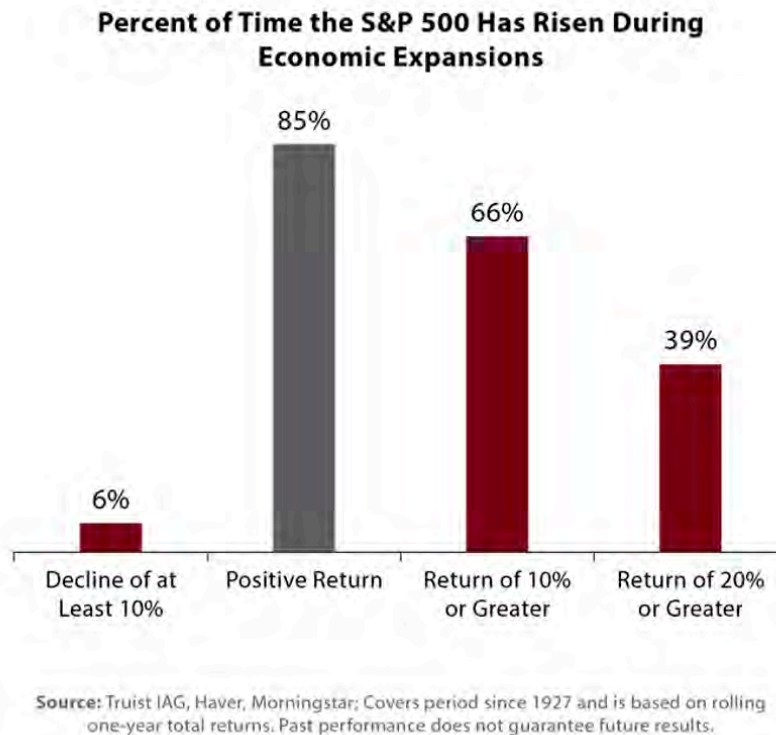


Data as of December 31, 2021.

Note: Recession start date is defined as the first date of the NBER business cycle peak month.

Source: Investment Strategy Group, Bloomberg, NBER.

Finally, whenever the market declines, instinct leads one to assume the next big bear market is right around the corner. While every market correction is frustrating, it's important to remember that major market declines rarely occur outside of economic recessions:



In fact, big gains were much more common than losses. During economic expansions, the market was almost seven times more likely to see gains of 20%+ than declines of at least 10%.

While we expect to see some slowdown in global growth this year, there is no evidence to suggest the US economy is entering a recession. **macrocast™** remains positive, job growth is strong, and household balance sheets are in the best shape in decades.

In summary, while market corrections can be difficult to stomach, most corrections do not turn into a bear market. Bear market declines are even less common during periods of economic growth, which we are currently in. **macrocast™** remains positive, while **microcast™** is neutral. This combination suggests a scenario less benign than we experienced last year, but one that is not a major concern yet.

ASSET CLASS REVIEW

The following table highlights major asset class returns over the past fifteen years (from Novel Investor):

Asset Class Returns

2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Total
EM 39.8%	HG Bnd 5.2%	EM 79.0%	REIT 28.0%	REIT 8.3%	REIT 19.7%	Sm Cap 38.8%	REIT 28.0%	REIT 2.8%	Sm Cap 21.3%	EM 37.8%	Cash 1.8%	Lg Cap 31.5%	Sm Cap 20.0%	REIT 41.3%	Lg Cap 356.8%
Int'l Stk 11.6%	Cash 1.7%	HY Bnd 57.5%	Sm Cap 26.9%	HG Bnd 7.8%	EM 18.6%	Lg Cap 32.4%	Lg Cap 13.7%	Lg Cap 1.4%	HY Bnd 17.5%	Int'l 25.6%	HG Bnd 0.0%	REIT 28.7%	EM 18.7%	Lg Cap 28.7%	Sm Cap 249.1%
AA 7.6%	AA -22.4%	Int'l Stk 32.5%	EM 19.2%	HY Bnd 4.4%	Int'l Stk 17.9%	Int'l Stk 23.3%	AA 6.9%	HG Bnd -0.6%	Lg Cap 12.0%	Lg Cap 21.8%	HY Bnd -2.3%	Sm Cap 25.5%	Lg Cap 18.4%	Sm Cap 14.8%	REIT 194.8%
HG Bnd 7.0%	HY Bnd -26.4%	REIT 28.0%	HY Bnd 15.2%	Lg Cap 2.1%	Sm Cap 16.4%	AA 11.5%	HG Bnd 6.0%	Cash 0.0%	EM 11.6%	Sm Cap 14.7%	REIT -4.0%	Int'l Stk 22.7%	AA 9.8%	Int'l Stk 11.8%	HY Bnd 173.1%
Lg Cap 5.5%	Sm Cap -33.8%	Sm Cap 27.2%	Lg Cap 15.1%	AA 0.3%	Lg Cap 16.0%	HY Bnd 7.4%	Sm Cap 4.9%	Int'l Stk -0.4%	REIT 8.6%	AA 14.6%	Lg Cap -4.4%	AA 18.9%	Int'l Stk 8.3%	AA 10.9%	AA 153.4%
Cash 4.4%	Lg Cap -37.0%	Lg Cap 26.5%	AA 13.5%	Cash 0.1%	HY Bnd 15.6%	REIT 2.9%	HY Bnd 2.5%	AA -1.3%	AA 7.2%	REIT 8.7%	AA -5.6%	EM 18.9%	HY Bnd 7.5%	HY Bnd 5.4%	EM 102.1%
HY Bnd 2.2%	REIT -37.7%	AA 24.6%	Int'l Stk 8.2%	Sm Cap -4.2%	AA 12.2%	Cash 0.1%	Cash 0.0%	Sm Cap -4.4%	HG Bnd 2.7%	HY Bnd 7.5%	Sm Cap -11.0%	HY Bnd 14.4%	HG Bnd 6.1%	Cash 0.0%	Int'l Stk 82.4%
Sm Cap -1.6%	Int'l Stk -43.1%	HG Bnd 5.9%	HG Bnd 6.5%	Int'l Stk -11.7%	HG Bnd 4.2%	HG Bnd -2.0%	EM -1.8%	HY Bnd -4.6%	Int'l Stk 1.5%	HG Bnd 3.5%	Int'l Stk -13.4%	HG Bnd 8.7%	Cash 0.6%	HG Bnd -1.5%	HG Bnd 82.4%
REIT -15.7%	EM -53.2%	Cash 0.1%	Cash 0.1%	EM -18.2%	Cash 0.1%	EM -2.3%	Int'l Stk -4.5%	EM -14.6%	Cash 0.3%	Cash 0.8%	EM -14.3%	Cash 2.2%	REIT -5.1%	EM -2.2%	Cash 12.9%

Abbr.	Asset Class - Index	Annual	Best	Worst
Lg Cap	Large Cap Stocks - S&P 500 Index	10.66%	32.4%	-37.0%
Sm Cap	Small Cap Stocks - Russell 2000 Index	8.69%	38.8%	-33.8%
Int'l Stk	International Developed Stocks - MSCI EAFE Index	4.09%	32.5%	-43.1%
EM	EM Stocks - MSCI Emerging Markets Index	4.80%	79.0%	-53.2%
REIT	REITs - FTSE NAREIT All Equity Index	7.47%	41.3%	-37.7%
HG Bnd	High Grade Bonds - Bloomberg Barclays U.S. Agg Index	3.99%	8.7%	-2.0%
HY Bnd	High Yield Bonds - ICE BofA US High Yield Index	7.02%	57.5%	-26.4%
Cash	Cash - S&P U.S. Treasury Bill 0-3 Mth Index	0.81%	4.4%	0.0%
AA	Asset Allocation Portfolio*	6.66%	24.6%	-22.4%

Past performance does not guarantee future returns. The historical performance shows changes in market trends across several asset classes over the past fifteen years. Returns represent total annual returns (reinvestment of all distributions) and does not include fees and expenses. The investments you choose should reflect your financial goals and risk tolerance. For assistance, talk to a financial professional. All data are as of 12/31/21.

*Asset Allocation Portfolio is 15% large cap stocks, 15% international stocks, 10% small cap stocks, 10% emerging market stocks, 10% REITs, 40% high-grade bonds, and annual rebalancing.

Some additional insights:

- 1. US stocks led the way.** US-based stocks (both large and small) finished higher than international indices thanks to a combination of fiscal stimulus and a highly supportive Fed.
- 2. Emerging Markets (EM) stood out as a negative.** With significant exposure to Chinese stocks, EM finished the year negative, despite double-digit returns for most other equity markets. Emerging markets have finished dead last in performance about half the time over the last decade.
- 3. Real Estate Investment Trusts (REITs) went from worst to first.** REITs struggled in 2020 because so much of that market is tied to areas of the economy that suffered due to the pandemic. Although the pandemic did not go away, REITs nevertheless rebounded and saw the best performance of all major asset classes for the first time since 2015.
- 4. The S&P 500 outperformed Novel's Asset Allocation strategy for the thirteenth consecutive year.** Novel Investor outlines a basic asset allocation portfolio, which they include in the above table as indicated by the gray box with the "AA" heading. From 2000-2008, the AA model consistently beat the S&P 500 despite the portfolio's large allocation to bonds. We first highlighted the recent weakness of the Asset Allocation portfolio in 2015. In 2021, the S&P again outperformed the AA portfolio. This remarkable streak over the past decade highlights both the strength of US Large Cap stocks vs. Small Cap stocks, as well as the relative weakness in emerging markets and Europe. We will ask the same question we did last year: will 2022 finally be the year asset allocation beats the market?

IN THE WEEKS AHEAD

The next episode of the Corbett Road Podcast will be published in the coming weeks. We will recap our 2022 outlook and discuss the volatile start to the year.

The Corbett Road Podcast is available on all major podcasting platforms, including Apple, Google, and Spotify. Search “Corbett Road Podcast” and be sure to hit Subscribe to get the latest episode as soon as it’s released. You can also listen on our website at <https://www.corbettroad.com/podcasts>.



ALREADY FORGOT YOUR NEW YEAR'S RESOLUTION?

Whether your 2022 goals are relative to your financial picture or you need your financial picture to help fund other goals, contact your Wealth Manager today to put together a plan that will help bridge the gap between your “to do” list and your “done” list.

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