MARKET
INSIGHT
MONTHLY

OUR THOUGHTS

UNITED BANK
Wealth Management

After a resounding December stock market flourish, the calendar had barely turned to 2022 when investors were reminded of how quickly short-term perception can change. The S&P 500 Index fell nearly 10% from January 3 through January 27 amid fears that the Federal Reserve (Fed), by its own accord, may become more aggressive in its fight against inflation. Though the market has staged an impressive rally since then, volatility has been reintroduced after months of relative stability. The transition from extremely low interest rates to more normalized, market-driven rates will take some adjustment. In addition, the recent military activity concerning Russia and Ukraine has compounded market anxiety.

Sophisticated equity market investors, however, often adjust quickly. They have been able to see-through the noise and concentrate on material economic figures that provide true direction. Though anxiety levels may rise from time to time, here are some facts that provide reassurance:

- On average, and even in positive years for the S&P 500, the index experiences a maximum peak-to-trough decline of around 11%. Volatility in some shape or form is perfectly normal.
- In general, after a correction of 10-15%, the index has experienced an average one-year gain of 22% off the lows and has risen in 12 of the 13 one-year periods.
- The average stock market gain one year after the first Fed rate hike of an economic cycle has been 11%, with positive gains the past eight cycles dating back to 1983.
- When investor sentiment is most negative, as it was during the past two weeks based on the American Association of Individual Investors (AAII) investor sentiment survey, stocks have risen an average of 11% in the next year.

This data suggests long-term equity investors should not fall prey to periodic or episodic volatility. Markets are susceptible to all information no matter its origin or veracity. Even reliable and factual information which can be interpreted as negative at first glance, can quickly be re-interpreted as not nearly as negative or impactful. But, as the economy transitions from unprecedented federal support to a self-sustaining environment, it would be prudent to anticipate added uncertainty and volatility as we move forward.

The good news is that an inflation peak may be near as COVID-19 loosens its grip on global trade. Slower, but still solid, economic growth this year will help cool inflation as Fed rate hikes take hold. We're already seeing backlogs and bottlenecks start to abate. We expect more people will re-enter the labor force later this year, easing wage pressures.

The U.S. consumer and small businesses are also in excellent shape. The U.S. economy may grow 4% this year, well above the pace of the last decade. Corporate America is affirming once again that fourth quarter activity was excellent. S&P 500 earnings are poised to, once again, set quarterly and annual records establishing a positive track well into 2022.

As always, we remain focused on your welfare and continually evaluate both the risks and opportunities that lie ahead. Thank you for the trust you have placed in your team at United Wealth Management.

Sincerely,
Your United Wealth Management Team

MARKET INSIGHT MONTHLY

February Update

MONTHLY COMMENTARY

UNITED BANK Wealth Management

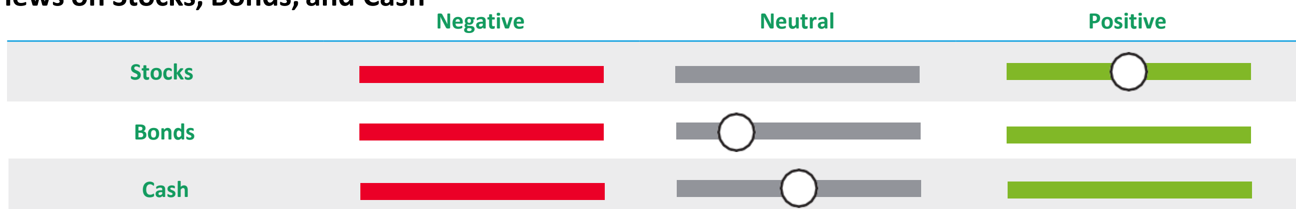
Two significant variables have impacted the investment landscape over the past 60 days. The Fed has clearly signaled they intend to be much more aggressive in their fight against inflation and tensions related to Russia's potential military conflict are being evaluated minute by minute. While interest rates are still historically low, investors have rapidly bid up rates anticipating the Fed's likely actions. Two years ago, the Fed rolled out policies that aimed to prevent a financial and economic meltdown. In a rather dramatic turnabout, they are now forced to confront almost unbridled growth and inflation which is at 40-year highs. They are projected to raise the Fed Funds Rate four to five times (1.00% to 1.25%) in 2022. Less than 60 days ago, it was anticipated the Fed would raise rates only two to three times (.50% to .75%). Investors have already priced in much of the projected rate move, with yields on the 2-year U.S. Treasury bill doubling since the start of the year. Russia is creating dangerous conditions with their military buildup at Ukraine's borders. This has led to increased volatility in global financial markets. Rising energy prices, bond yields and inflation have contributed to short-term instability. Socio-political events are common. Some are rather mundane and ineffectual, while others may have significance. It is too early to draw a conclusion as to the eventual outcome of this activity. United portfolios are constructed to be diversified and to withstand adverse conditions.

INVESTMENT TAKEAWAYS

- Despite January's volatility and modestly higher interest rates, we continue to overweight equities within our total global asset allocation. We continue to favor stocks relative to bonds based on our expectation that strong economic fundamentals remain in place and will continue to drive record-setting earnings even higher. We expect this growth to extend well into 2022.
- We favor a combination of growth and value large cap stocks. Our value bias better protects portfolios during volatile periods as was just experienced in January. Companies with strong balance sheets often pay higher dividends and are preferred during less certain environments. Growth stocks typically generate strong earnings and revenues. While subject to somewhat higher volatility, they can perform extremely well during an economic expansion.
- Our positive view of mid and small cap stocks is supported by historical evidence from prior recoveries. Our analysis shows that the current mid-cycle economic position should prompt investors to remain favorably disposed to both segments. Though valuations are in line with historical averages, mid and small companies are generally subject to higher volatility than large-cap stocks.
- Cyclical vs. defensive stocks established leadership across the globe during much of the recovery. Much like the U.S., rising global interest rates and inflation will, from time to time, play a part in destabilizing investor sentiment. Though developed nations' equity markets have generally outperformed those of emerging markets (EM), both segments have considerably lagged the U.S. We remain comfortable with our modest international exposure and prefer to wait for more evidence suggesting a higher allocation is warranted.
- We continue to underweight our allocation to fixed income. Rates have recently moved appreciably higher over the last several months, which has contributed to recent fixed income underperformance. We expect rates will move modestly higher from here. We believe much of the anticipated rate increase has already been seen.
- We favor a blend of short to intermediate bonds with an emphasis on high credit quality.

BROAD ASSET CLASS VIEWS

Views on Stocks, Bonds, and Cash



EQUITY ASSET CLASSES

The factors that influence our decision to overweight equities remain in effect. We continue to favor stocks relative to bonds. Economic strength has been maintained as we move into 2022 despite escalating interest rates and occasional short-term equity volatility. The record setting domestic earnings of 2021 will carry forward into 2022. We see little evidence suggesting earnings growth will be curtailed, but the rate of earnings growth will be well less than last year. Our U.S. equity preference has proven to be both prudent and profitable through much of the COVID pandemic and subsequent recovery. We continue to favor the U.S. but are encouraged by signs of economic growth globally. We continue to monitor political/economic activities in both Russia and China as authorities in both countries engage in activities contrary to worldwide economic stability. Investor enthusiasm has waned for international equities, but should détente prevail, investors will likely eventually be rewarded.

	Sector	Overall View	Relative Trend	Rationale
Market Capitalization	Large Caps			U.S. large cap stocks have been the most predictable and reliable equity segment for the last several years. The record setting earnings generated in 2021 influenced investors to continue holding and buying large-cap cyclical value and earnings-driven growth stocks. We remain well positioned in this segment and believe investors will be rewarded by holding quality names.
	Mid Caps			Mid-cap companies have grown dramatically with economic expansion. Despite some recent short-term volatility due to interest rate increases, mid-cap valuations remain attractive as strong earnings continue to be reported.
	Small Caps			The U.S. small cap sector was among the strongest performers of 2021. Continued economic expansion and strong earnings generated increased investor demand despite recent short-term volatility. Valuations remain attractive based on strong earnings growth prospects through 2022. We remain overweight small caps.
Style	Growth			We believe large cap growth stocks will continue to garner investor support from strong current and future earnings and revenue expectations. We are mindful that growth equities may be somewhat restricted by inflation and higher interest rates. But we do not feel rates will move high enough to be a long-term obstacle.
	Value			We expect most domestic cyclical value stocks to outperform defensive value stocks as the economy expands. Value stocks have lagged their growth counterparts for over a decade. We believe a reversion to the mean began in late 2020 with both mid and small-cap companies experiencing this transition more rapidly.
Region	United States			We see the potential for more gains in the U.S. stock market during 2022. In response to the pandemic, trillions of stimulative dollars were circulated into the economy. This will have long reaching effects. Though modestly higher interest rates have already occurred, strong earnings are likely to be reported as the economy moves forward with momentum. For these reasons we continue to favor U.S. stocks as our dominant position in equity portfolios.
	Developed International			Developed countries around the world have faced economic concerns since the start of the COVID pandemic. Though most of the world is now in a sustainable recovery, investors have favored countries with appropriate health protocols but also allowed for economic growth. Geographic constraints have made health management a more difficult task. Therefore, economic development has been compromised. As the pandemic abates, economic activity will improve.
	Emerging Markets			Chinese government intervention and continued EM pandemic health concerns cast a shadow over EM in 2021. EM vaccination rates should see a considerable increase this year which should have a positive impact. China's governing body is unlikely to soften its internal position, but some hints of a compromise seem to be possible. We have a slight overweight to EM.

FIXED INCOME

Limit Rate Sensitivity with Intermediate Focus

The 10-year Treasury yield has increased another 25 basis points just over the last 30 days. Now standing at over 2%, this is the highest rate seen since the summer of 2019. This aggressive rise is completely attributed to bond investors demanding higher fixed income returns in light of Federal Reserve comments regarding how swiftly and intensely they intend to fight inflation going forward. We have stated for some time that the 10-Year Treasury rate would eventually rise and find stability between 1.75%—2.00%. We are now at, and slightly exceed, that level. We further believe that the slight premium over our expected range is due to inflationary pressures lasting longer than the Fed had predicted. The market is suggesting the Fed is somewhat "behind the curve" and is demanding slightly higher rates to compensate for the Fed's lagging action. Fixed income investors have responded rather quickly to Fed statements and decisively moved both short and long rates higher. This will stem some growth and lessen inflationary concerns. The Fed continues to enact their "taper" policy which should be completed over the next few months. In our view, compensation for longer-maturity and rate-sensitive bonds remains unattractive as rates will likely move modestly, but not substantially higher from current levels. We continue to suggest a blend of high-quality short-to-intermediate bonds in all fixed income portfolios.

The continued economic expansion allows for high yield bonds issued by stable but growing companies to be a productive use of fixed income capital. We remain committed to a modest high yield position in both corporate and municipal bonds. As previously stated, inflation has risen as the expanding global economy has experienced many COVID related supply chain shortages. We believe this will continue for the time being but will lessen at some point in 2022. Thus, we continue to promote inflation protection in fixed income portfolios.

We favor municipal bonds for tax-sensitive accounts. Federal stimulus, infrastructure spending and the potential for higher personal tax rates provide support to municipal markets.

Positioning		Low / Medium / High	Rationale
	Credit Quality	High (indicator between Medium and High)	Credit spreads have increased slightly of late and still suggest stable, but not excessive, economic growth.
		Short / Int. / Long	
	Duration	Short (indicator between Short and Int.)	Concerns over rising interest rates/inflation remain viable with the prospect of a return to normalized economic growth with reduced government stimulus.

COMMODITIES

Our precious metals view remains neutral with gold prices seemingly range bound between the mid-1700s and the mid-1800s. The recent price increase in precious metals was almost exclusively attributed to the global uncertainty created by the military threat posed by the potential Russia/Ukraine conflict. Should diplomatic channels prevail, we would expect gold, precious metals and oil to decline.

The global demand for goods and services has clearly improved over the last year. Energy prices rapidly escalated in late 2020 and continued moving higher for much of 2021 due to relatively low and controlled supply. After a slight pullback late in 2021, West Texas Intermediate Oil has once again risen to multi-year highs at well over $90 per barrel. However, much like gold, oil has recently risen as a direct consequence of the potential Russian conflict. Should the threat abate, prices are unlikely to remain this elevated.

CONCLUSION

In most respects, a full economic recovery has been obtained. The Fed would not be reducing financial support and contemplating rate increases should significant economic peril be anticipated. We know inflation and tightening monetary policy may contribute to bouts of uncertainty. However, the U.S. consumer and the corporate world have been steadfast in their resolve to move forward.

As we examine market risks, we continue to believe these risks are generally known, manageable and will not likely impact the continued expansion. The market will continue to look forward to a prosperous, post-pandemic environment despite occasional volatility.

Disclosures

The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual security. To determine which investment(s) may be appropriate for you, consult your financial advisor prior to investing.

All performance referenced is historical and is no guarantee of future results. All indexes are unmanaged and cannot be invested into directly. Unmanaged index returns do not reflect fees, expenses, or sales charges. Index performance is not indicative of the performance of any investment.

Economic forecasts set forth may not develop as predicted.

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