Grant Street Asset Management, Inc.

INVESTMENT ADVISORS

GRANT STREET ASSET MANAGEMENT, INC.
QUARTERLY LETTER
4TH QUARTER 2021
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As we reflect on the fourth quarter and the full year 2021, we can be grateful for another year of strong equity market returns, a solid economic recovery, continued improvement in employment and a state of the world that, compared with 2020, is arguably in a better place overall given the widespread availability of vaccines and improved therapeutics/treatments related to the COVID 19 virus. On the economic front, there has also been a tremendous amount of fiscal and monetary stimulus to propel the economic recovery from March 2020 lows. Consumer spending has increased 15% over the past two years compared to a historical average of 2-3% per year. Similarly, corporations are expected to post earnings growth of 45% in 2021 compared to a 10-year historical average of 5% per year.

Within equities, U.S. stocks enjoyed yet another period of decidedly strong gains throughout the capitalization spectrum (large, mid, and small companies). While inflation concerns and uncertainty surrounding the jump in Omicron COVID cases led to some downside volatility in the fourth quarter, most markets ultimately shrugged off those worries and finished the year well in the positive. Notably, emerging market stocks continued to struggle due to regulation and growth concerns in China along with a surprisingly strong dollar. Overall, corporate earnings outlooks for next year have been mostly positive, yet recently restrained. We believe that restraint is attributed to on-going supply-chain bottlenecks and uncertainty around how long elevated inflation levels will persist, both risks companies had to address throughout 2021 as well.

Equity Index	**1Q 2021**	**2Q 2021**	**3Q 2021**	**4Q 2021**	**2021**
S&P 500 (Large Companies)	6.2%	8.6%	0.6%	11.0%	28.7%
Nasdaq 100 (Technology-heavy)	1.8%	11.4%	1.1%	11.3%	27.5%
S&P 400 (Mid-sized Companies)	13.5%	3.6%	-1.8%	8.0%	24.8%
Russell 2000 (Small-sized Companies)	12.7%	4.3%	-4.4%	2.1%	14.8%
MSCI EAFE (Europe, Australia & Far East)	3.5%	5.2%	-0.5%	2.7%	11.3%
MSCI Emerging Markets	2.3%	5.1%	-8.1%	-1.3%	-2.5%
MSCI ACWI (All Country World Index)	5.2%	7.2%	-1.1%	6.0%	18.2%

Fixed Income Index	**1Q 2021**	**2Q 2021**	**3Q 2021**	**4Q 2021**	**2021**
Bloomberg U.S. Aggregate Bond	-3.4%	1.8%	0.1%	0.0%	-1.5%
U.S. 10-year Treasury	-7.0%	3.0%	0.0%	0.8%	-3.7%
Bloomberg 1-3 yr. U.S. Treasury	-0.1%	0.0%	0.1%	-0.6%	-0.6%
U.S. 3-month T-Bills	0.0%	0.0%	0.0%	0.0%	0.0%
Bloomberg U.S. Corp. High Yield	0.8%	2.7%	0.9%	0.7%	5.3%
Bloomberg Municipal Bond	-0.4%	1.4%	-0.3%	0.7%	1.5%

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Shifting our focus to fixed income, broadly speaking, bonds experienced another lackluster period of performance for the quarter with just slightly positive performance across most sectors. For the year overall, the negative returns experienced in the first quarter were difficult to recoup through year end. Only the lowest credit quality bonds kept pace with inflation, and tax-free municipals outperformed taxable bonds. Consistent with past communications, the low interest rate environment continues to challenge bond investors to achieve low risk returns in a higher inflation world.

However, this may change soon as the Federal Reserve indicated at its most recent meeting that it is likely to raise interest rates by the middle of 2022 and may even raise rates multiple times in 2022. The hope is that higher interest rates will translate into higher yields within fixed income, but the timing, frequency and messaging of rate hikes is crucial. If the Fed raises rates too fast, it risks stunting growth and stymieing the recovery. If it raises too slowly, it risks inflation continuing to climb and becoming even more difficult to contain. The messaging and investor expectations from the Fed are also very important. Over the years, the Federal Reserve has attempted to telegraph its policies and any potential changes well in advance of those actions so as not to surprise investors with unexpected monetary shifts. While the Fed controls the short end of interest rates, investors' demand (or lack thereof) for bonds of various maturities controls the rest of the interest yield curve. Investors caught off guard may lead to knee-jerk reactions that shift the yield curve and cause bond prices to fall. We expect the Fed to clearly communicate its intention to move rates this coming year, and our strategy of diversification to include defensive core bonds, multi-sector bonds for higher yields and low-volatility alternatives on the defensive side has been very successful despite the challenging environment. We anticipate that this strategy will continue to be resilient in a gradually rising rate environment.

It is worth taking a moment to discuss two key pieces of legislation in the U.S. that will impact 2022 and beyond. A $1.2 trillion bipartisan infrastructure bill was passed in mid-November after months of negotiations. The bill dedicates more than $550 billion over five years to our nation's infrastructure. This includes bridges, airports/seaports, public transit, rail networks, broadband, electric and water infrastructure, zero/low-emission public transport and EV charging networks. Although this bill fulfills a key piece of President Biden's agenda, it is not without cost. While the White House has stated that costs would be covered using unspent COVID-19 relief funds, strengthened tax enforcement, new revenues and other bipartisan measures, the Congressional Budget Office estimates the infrastructure bill may add $256 billion to the nation's budget deficit over the next 10 years. Regardless of how paying for the bill works out, the bill should be positive for the economy and markets in the near term, as it represents additional stimulus and spending.

The second piece of legislation, the "Build Back Better" bill, focuses on social and climate spending and new tax provisions. While it passed in the House in November, dissent within the democratic party stopped it from going to vote in the Senate prior to Christmas. This social spending bill has been controversial and could potentially include significant tax changes that would impact wealthy individuals and corporations alike. If and when a version of this legislation is passed, it seems likely that it will have implications for some clients' tax and estate planning strategies, and this will be a point of discussion with clients.

As we consider portfolio construction in the midst of equity markets near all-time highs, we continue to prefer a diversified portfolio of large, mid and small-sized companies, predominantly through U.S. equity, but also including an increasing allocation to international stocks. Going back to the 1970s, U.S. and foreign developed equity markets have traded periods of outperformance over one another on average every four years. Most recently, the U.S. period of outperformance over foreign stocks has lasted for over fourteen calendar years, nearly three times the historical average. Couple this unusual outperformance with historically low relative valuations within foreign equity markets, and we continue to expect a regime shift where U.S. stocks underperform foreign stocks in the future. A weakening dollar, which tends to result in a rising interest rate environment, will only help U.S. investors investing overseas. We are also seeing attractive valuations in certain sectors, such as financials and other value sectors at this time.

In terms of an outlook for 2022, we anticipate another year of positive U.S. GDP and market growth, albeit at a slower pace that will likely not repeat our experience in 2020 and 2021. We continue to favor a diversified portfolio in which equities generate growth and the defensive/fixed income side of the portfolio contributes downside protection with modest upside to offset inflation. Although supply chain, inflation and policy risks are not without warrant, the resilience of consumer spending coupled with increasing wages, ongoing government stimulus and pockets of investment opportunity give us optimism as we head into a new year. We wish you and your family a healthy, happy and prosperous 2022.