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Looking back at 2021

As I look back on 2021, I am reminded of a day about 28 years ago (January 17th, 1994) when I was living in Santa Monica, California. The weather was simply amazing. Sunny, blue skies, temperatures in the low 80's with low humidity. Unfortunately, this beautiful day was impossible to enjoy given the incredible destruction that surrounded me. Earlier that morning, the Los Angeles area had experienced one of its worst earthquakes ever — the so-called "Northridge" earthquake. The damage to the house in which I was living, and the surrounding area was enormous.

Last year felt like that day in California. The weather (e.g., the performance of our investments) was excellent (the stock market, as represented by the S&P 500 index including dividends, was up 26.9%) while the surrounding situation that we have lived through (e.g., the COVID-19 pandemic) was awful for so many people.

On the positive side of this paradoxical situation, 2021 represented the third straight year of double-digit growth of the S&P 500 index. This string of strong results has only happened three other times in the 65 years since the modern S&P 500 index was created in 1957. During those other three occasions, the return in next year (e.g. year four) has varied from -10% to 1% to 29%, leaving us with no obvious pattern for 2022 to follow.

Inflation Fears Persist

Given the strong connection between interest rates and stock valuations, it is not surprising that inflation continues to be the major topic in investment circles. At its December 2021 meeting, the Federal Reserve Bank decided to eliminate the word "transitory" in its description of current inflation trends. The Bank also indicated that they were likely to raise interest rates sooner and more frequently than they had previously expected due both to unexpected strength in our economy and increased concerns about inflation. Even with these changes, Fed members continue to believe that inflation will remain under control over the longer-term. Only one member of the Bank's Open Markets Committee expected interest rates to exceed 3% by 2024 and only two members expected interest rates to exceed 2.5% in the "long run" (e.g. beyond 2024). If these predictions came true, our stock holdings would likely benefit.

Our current inflation seems to be caused by a supply-demand imbalance largely due to the pandemic. Recent one-time government support meant that folks had extra money with few places to spend it. People bought more goods than normal while supplies were constrained due to Covid-related factors. Most of the Covid-related one-time government spending has ended while many of

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the supply chain bottlenecks seem likely to be resolved in the months ahead. If this forecast is correct, the main issue going forward is whether inflation expectations became locked into our economy before these transitory issues were resolved.

Latest RMD News

As I mentioned in my last newsletter, effective January 1, 2022, the tables used to determine the amount of Required Minimum Distributions from retirement accounts for anyone who is at least 72 years old by 12/31/22 were adjusted for changes in average life expectancy. This means that 2022 RMD's are lower than they would have been without these changes. Of course, since these are simply minimums; you can always take larger distributions, if desired.

Preventing Financial Fraud

The ease with which we can move money from one financial institution to another makes our financial lives much easier to manage. At the same time, this convenience also makes it easier for swindlers to steal our funds. Recently, one of my clients had their account impacted by fraud. Someone called Schwab, impersonated my client and requested that Schwab send a large amount of money to a brand-new bank account. Fortunately, this situation was discovered in a timely fashion and the client's funds were quickly returned.

One way we can help prevent this type of fraud involves the use of a voice identification system. Schwab has created a process that enables you to establish a voice print that allows them to technologically confirm your identity when you call in. The one-time setup is easy. During a call with Schwab (800-515-2157), you are asked to answer a few questions to establish your identity. Then, you are instructed to repeat the phrase "At Schwab, my voice is my password" a couple of times. Using biometric technology, Schwab can then positively identify you by analyzing your voice when you repeat this phrase during future calls. The system even works when you have a cold!

What's Next?

After three years of strong stock market returns, history gives us no sense of what the stock market will do in year four. My own feeling is that interest rate *expectations* will largely influence the stock market's future direction during 2022. As the year has begun, this prediction seems to be playing out. Of course, what really matters is what happens to interest rates over time rather than in the short run. If interest rates normalize and return to historical levels (e.g. pre-2009), stock market returns could be reduced going forward. If interest rates stay subdued, as the Fed is currently predicting, the stock market's growth could continue. My strategy will be to take advantage of whatever path unfolds.

Thank you for your confidence.

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