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Nauset Market Commentary
Fourth Quarter 2021

Market Performance Recap: **Strong Finish for Stocks**

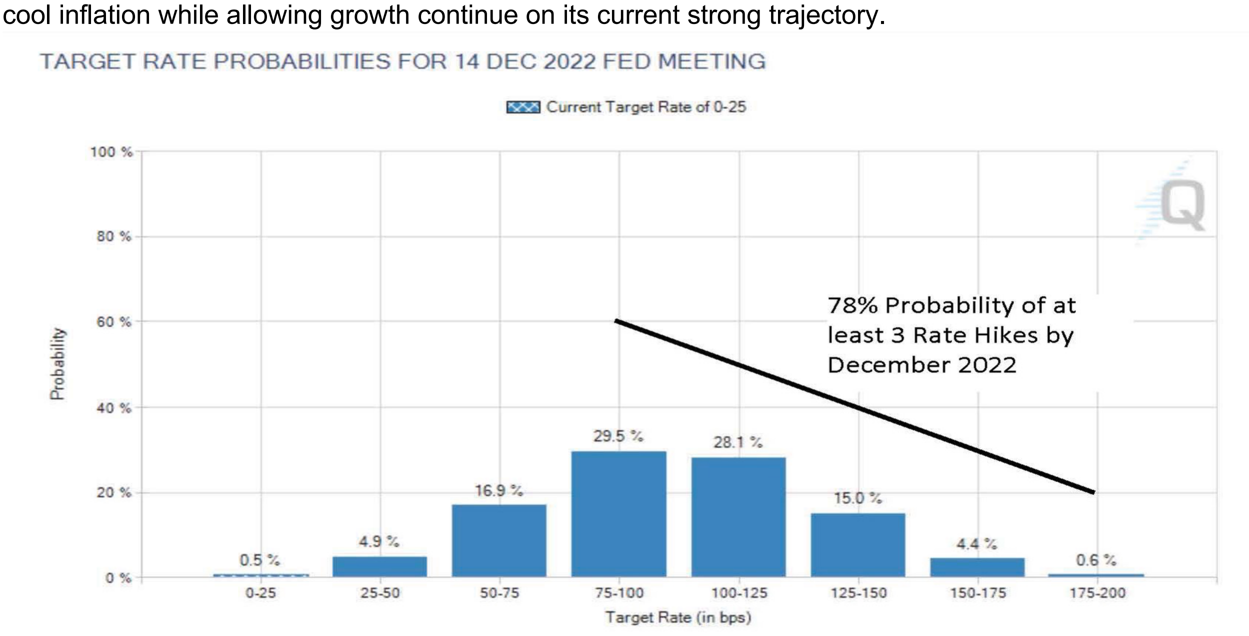
Despite news of another Covid variant, US stocks ended 2021 on a high note as investors drove the Russell 1000 up +9.9% in the quarter to finish the year at +26.4%. Energy, tech and real estate stock sectors were market leaders in 2021, while telecom and utilities lagged. The best gains were in large caps as the small cap Russell 2000 rose a more moderate +14.3% for 2021. In international stocks, the developed-country EAFE index posted 2021 gains of +11.3%, while Emerging Markets index slid -2.5% as China policy changes hurt EM stocks. Bonds slipped further in Q4 to finish 2021 off -1.4% as measured by Barclays Intermediate Gov't/Credit bond index.

Economic & Market Discussion: **2022 – A Year of Transitions**

We enter 2022 in a similar way to 2021 with a new wave of Covid infections causing investor anxiety. However, there are key differences. We are starting the year from a different base medically as most people have some vaccination protection, markets are at higher valuations, inflation is spiking to highs not seen since the 1980s, and the Fed is poised to increase rates this year. Welcome to a year of transition.

- The Great Moderation – Following last year's pandemic-recovery GNP growth of +5.6%, we expect the US economic growth to moderate in 2022 with estimated GNP growth at +3.8%, still well above pre-pandemic levels. Along with solid, albeit slower growth, high inflation over +5% will likely persist for a while, then also moderate in our view to around +3% by the end of 2022. We believe Fed rate hikes, fewer supply-chain constraints and moderating economic demand will help cool inflation.

- Hut, Hut, Hike – The level of US growth and inflation moderation this year will most likely be tied to action by the Federal Reserve. The pace and timing of the next Fed rate hike cycle will be a key driver of market sentiment in 2022. As shown below, investors expect the Fed to hike rates at least three times in 2022 starting as early as its March meeting. The Fed will be walking a fine line as it aims to cool inflation while allowing growth continue on its current strong trajectory.



CME FedWatch Tool, January 10, 2022

- Buckle Up – The transitions we are likely see this year in the economy and financial markets are unique to the pandemic environment and difficult to model. The constantly evolving pandemic and anticipated Fed funds hikes will cause investor sentiment gyrations and market volatility almost certainly greater than last year. As such, this action can create opportunities and lead to tactical shifts in our portfolio strategy. We will monitor developments closely and make adjustments as events unfold this year.

Portfolio Strategy: **Steady as We Go**

While we expect a year of transition featuring plenty of ups and down, we remain positive on the equity markets. However, with stocks fully valued and close to all-time highs, gains will depend on solid growth and will likely be lower than returns during the past three years.

- Favor Equities over Bonds – We continue to favor equities over bonds, especially given current inflation levels, growth expectations and the Fed's plan to increase short-term rates this year. Within equities, we are maintaining our diversified allocation to positions in large, mid and small cap US stocks, and international developed and emerging markets stocks. While interest-rate sensitive bonds may struggle this year, we do see opportunity in high-yielding securities tied to economic growth and middle market lending.
- Non-Equity Allocations – Our managed-risk strategy includes portfolio elements that have low or no correlation to US and international equity holdings. These holdings have return streams that differ from equities and serve as sources of funds to rebalance portfolios during equity market declines. Holdings include real assets, high yield and income positions as well as cash.
- Rebalancing, Not Market Timing – With expected volatility this year, we are often asked how we prepare for a potential market decline. We don't market time in the classic sense of selling stocks at an arbitrary market high and then hold a chunk of cash awaiting a market drop. We believe no one can time both an exit and an entry well enough. Instead, we actively rebalance each quarter according to our market view. In the case of a market decline, we will actively rebalance, again in line with market conditions and each portfolio's investment policy.

Market Performance **% Change for Periods Ended 12/31/2021**

Market Index	Fourth Quarter	2021 YTD	1-Year	3-Year Annual.	5-Year Annual.
Russell 1000	9.78	26.45	26.45	26.21	18.42
MSCI EAFE – Non-US	2.69	11.26	11.26	13.54	9.55
Russell 2000	2.14	14.82	14.82	20.02	12.02
MSCI Emerging Markets Equity	-1.31	-2.54	-2.54	10.94	9.87
DJ US Real Estate	14.58	38.99	38.99	19.28	12.34
NASDAQ Composite	8.45	22.18	22.18	34.26	24.97
Barclays Gov't/Credit Interm. Bond	-0.57	-1.44	-1.44	3.86	2.91
Wilshire Liquid Alternative	0.57	4.68	4.58	4.84	3.00
3-Month T-Bill	0.01	0.05	0.06	0.95	1.11