

The Legacy Group, Inc.

Dear Legacy Clients,

With the arrival of the new calendar year, we thought it would be in your best interest for us to send you this timely investment update. In this letter, we will be detailing our thoughts on the current investment landscape, reflecting on the investment year of 2021, and providing our general economic/investment outlook going forward.

So far, we believe that the most impactful difference between this year's and last year's investment landscape is market sentiment surrounding inflation. Whereas last year was almost defined by a popular debate about whether or not the high Covid-related inflation numbers would subside or persist, this year seems to have been met by a general feeling of surprise that inflation is still so high. This in turn can bring about more consideration for the idea that high inflation might be here to stay. Even though many blamed this high inflation on "short-term" Covid-related supply chain problems, there are a number of reasons why it could make sense that we see more elevated and lasting inflation going forward. One reason could be increased wage growth fueled by labor shortages and low unemployment; another could be the unprecedented amount of liquidity that now exists as a result of the Federal Reserve increasing the money supply by 30% during the year 2020. It is impossible to know for sure.

What is important however, is how the Federal Reserve has responded to these high inflation prints, and what these changes in Fed policy imply for the future of interest rates. At their December 2021 meeting, the Federal Reserve drastically altered policy in order to accelerate their plan to increase interest rates, and they specifically cited higher and more persistent than expected inflation as their primary reason for doing so. The reason why this is so significant is because up until this point, the Federal Reserve's uncertainty and doubt regarding the inflationary landscape allowed them to prioritize accommodative monetary policy, which tends to coincide with lower interest rates. Now, not only has this buffer against rapidly rising interest rates dissipated, but the fact that the Federal Reserve made such a drastic reversal in both their policy and outlook regarding inflation indicates that they may have waited too long to address it, which only further pressures rates to go up. The primary takeaway from this is that from here forward, we can reasonably expect higher and more consistent upwards pressure on interest rates than we have seen in the previous two decades, because up until now, inflation like this had been virtually absent.

Regardless, we still believe that 2022, similarly to 2021, will exhibit strong underlying economic conditions as a result of continued low unemployment and stable GDP, which should weigh favorably on equities. However, unlike in 2021, the U.S. economy and stock market will not be able to benefit so heavily from 2021's timely global events (i.e. record levels of stimulus, the first covid vaccine, reopening the economy). Instead, it seems that 2022 will have to persevere through rising interest rates and the threat of consistently elevated inflation. Given this, we believe that U.S. equities will fall noticeably short of their 2021 performance, but nevertheless, 2022 will still likely be another positive year for U.S. stocks. We also maintain a constructive outlook on international equities, which were positive last year but still underperformed U.S. equities once again. Whereas U.S. stocks benefited from the Federal Reserve's unprecedented levels of Covid stimulus during the reopening of the economy, international equities did

The Legacy Group, Inc.

not have this advantage. However, this means that valuations on U.S. stocks have become more stretched, indicating that international stocks may be undervalued by comparison.

Overall, we remain balanced in our allocation, with no heavy overweight to any given sector, as the current economic environment is relatively unpredictable given the circumstances of recovering from a global pandemic. In other words, this isn't exactly something that happens very frequently. However, we do believe that the economy will remain strong in the coming years, which should have a net positive impact on equities.

Sincerely,



Austin Smith
Analyst for The Legacy Group, Inc.

Resources used:

<https://www.cnbc.com/2022/01/05/fed-minutes-december-2021.html>

<https://www.investors.com/news/2022-stock-market-forecast-investor-risk-inflation-stocks/>

<https://www.fidelity.com/learning-center/trading-investing/international-investing-2022-outlook>