4TH QUARTER 2021 MARKET OVERVIEW

THE DOWNSIDE OF UP

There is a downside to a rapidly rising stock market. The age old idiom of investing, "buy low, sell high" is rendered unattainable in so many circumstances. Valuations become inflated and investors are herded into assets at nose bleed levels.

As stock prices approach their zenith, the runway for making money, shortens. Investing is more perilous and finally, what is inevitable occurs, and the market falls.

<u>So far, the market has not done that.</u> The further and longer the market runs,however, the higher the probability that a decided drop is drawing nearer. It makes for worrisome conditions. This is the "downside of up".

Currently, evidence suggests the market is inflated. Broad measures of valuations for stocks are elevated. Large technology companies comprise most of the heady gains for the indices over the past year, but these stocks are stretched and extended to the point that it is difficult to merit a case for further investment.

High valuations for stocks carry reality defined in the laws of physics, oddly, rather than finance. Therefore, a steep rise indicates a concurrent, pending, rapid descent. At this point, this risk should be heeded.

The S&P 500 fell 5% in September. This was actually good because it set the stage for a terrific fourth quarter for the market. The market needs another of these corrective whacks to happen. We do not want the stock market to get too frothy, less a longer term tailspin would occur. We also do not want to see the market become exhausted, unable to make further progress because valuations are too high.

A proper correction in the market could return valuations to reasonable levels and then would facilitate a more healthy investment environment with more reasonable price levels.

We are accustomed to cheering for the market to rise. People invest more into stocks and are gratified to have gains. Assets grow and exceed projections. It is reassuring. The cautionary measure, however, is that the more the market rises, the more risk looms.

THE FED CHANGES ITS POLICY

The investment environment promises to be drastically different in 2022. Asset values face a stiff challenge. You will remember, the Fed has fueled the market with a rampant money printing expedition of a stupendous proportion. Finally, the Fed has signaled it would end this stimulus. The Fed has also promised a series of interest rate hikes. This is referred to as a *tightening of monetary policy.* Usually, Fed tightening is not favorable for the stock market.

Persistent, accelerating inflation along with a return to near pre-pandemic employment has emboldened the Fed to finally reverse its policy. The Fed finally believes that the economy and the markets can stand on their own, sans supportive measures. This shift, however, threatens to unnerve investors in the early months of 2022.

The Fed pivot renders interest rates as the focal point for investors in 2022. Most credible investment analysts feel a gradual, modest interest rate increase would be tolerable for stocks. Sharper increases would be more detrimental.

PEREGRINE HOLDINGS AND STRATEGY

Peregrine client accounts are designed to be **resilient**. This implies achieving consistent returns in conjunction with defensive characteristics that are supportive during bear markets.

A contributing factor to **resilience** is for client accounts to carry investments in sectors that are non-correlated. For example, what promises to be a good environment for energy stocks, would be negative for travel stocks. Positive developments for economic reopening stocks like airlines, travel, and hotels would be negative for consumer staples companies, like General Mills. Disparate price movements provide stability during market volatility.

Client holdings have continued to provide consistent dividend income to bolster investment returns. Alternate assets such as gold and crypto currency can potentially capture gains separate from the stock market. Lastly, fixed income ETFs are utilized for diversification.

Overall, at the outset of 2022, the stage seems to be set for more volatility and shifting trends. It might be a bad time to "fall in love with our stocks". Conditions promise to change rapidly. The perceived worst areas of the market could enjoy brisk rebounds while favored categories sour quickly.

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