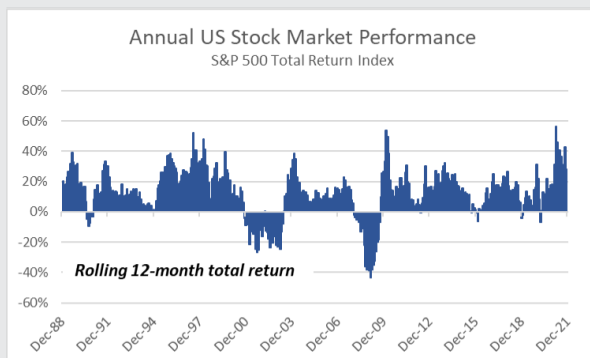


NEWSLETTER AND CAPITAL MARKETS REVIEW

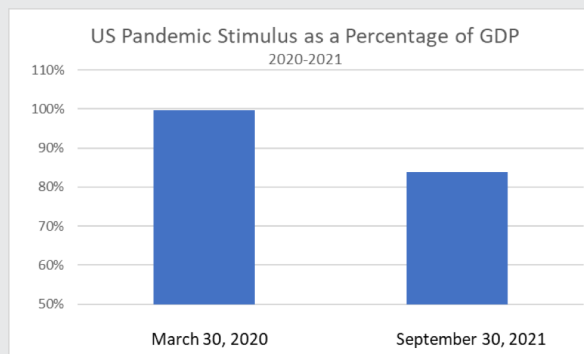
NOVEMBER - DECEMBER 2021

Through the end of November, the S&P 500 has delivered a robust 23.2% year-to-date total return, piling on to 2020's impressive full-year 18.4% clip. On its face, such strong stock market results would seem implausible given the disruptive forces of the pandemic, the multiple variants and building inflationary pressure here and abroad. The S&P 500 reached its pandemic bottom on March 23, 2020 and since then, the 20 month-end observations of rolling annual returns (shown on the chart) have averaged over 25.8%. To place that figure in context, the long-term average annual return since inception in 1987 is 12.38%. The low "base effect" climbing up from the pandemic bottom contributed to the relative strong % gains over the past twenty months, but there are also significant macro factors that have supported a booming US stock market that may prove to be headwinds going forward. [chart data courtesy Standard & Poors, Bloomberg LP © 2021]

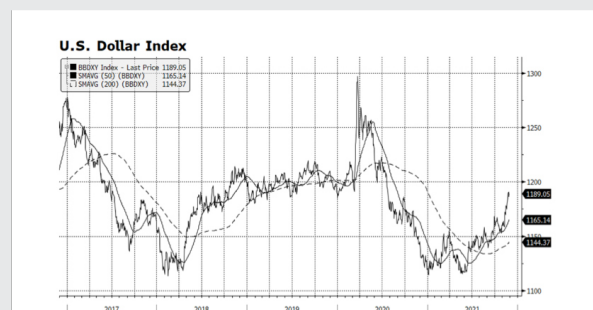


Over the past several quarters we have highlighted the role that unprecedented monetary and fiscal stimulus has had in supporting the economy and asset prices. Since the pandemic began, the US Federal Reserve has more than doubled the size of its balance sheet from \$4.2 trillion to \$8.7 trillion. In addition to those asset purchases, the Fed has maintained dovish interest rate policy and a benign regulatory environment.

Adding to that on the fiscal front, the US Federal government has injected at least \$15 trillion in stimulus through various programs (CARES Act, Exchange Stabilization Fund, Paycheck Protection



Program Liquidity Facility, etc.). As of the third quarter 2021, nominal US GDP amounted to just over \$23 trillion and the combination of monetary and fiscal stimulus amounts to at least \$19 trillion, with even more fiscal stimulus likely on the way. The combined government stimulus over the past twenty months amounts to over 83% of current US GDP. Compared to the recessionary bottom of June 2020, the total stimulus is nearly 100%, which provides ample explanation for why asset prices have risen and inflation is on the march.



Consumer prices in the US are observably on the rise across a broad array of products and services. The Federal Reserve's preferred inflation gauge, the PCE, last week registered a 4.1% annual increase, well above the Fed's target. The causes of higher prices are well known, ranging from supply chain bottlenecks to raw material scarcity to higher energy costs to a shortage of transportation personnel. Adding to the inflationary mix is strength in the US dollar which has recovered over 6% according to the Bloomberg US Dollar index, comprised of a basket of major currencies. The dollar has recovered to pre-pandemic levels and could strengthen further as the Fed begins to reign in liquidity towards the end of 2022 if not earlier. Continued dollar strength could provide some inflationary relief in the form of lower import prices and could be justified given strong US economic

growth and the interest rate differential between the US bonds and the rest of the world. As this week's chart illustrates though, currency movements are notoriously difficult to predict. [chart courtesy Bloomberg LP © 2021]



Heading into the new year both monetary and fiscal policy will likely be less supportive and inflationary pressure may persist. Investors should anticipate lower capital market returns and we would not be surprised to experience continued volatility or a consolidation of asset prices in the months ahead.

Portfolio Positioning

Policy status quo has kept us at portfolio status quo. Central bank policy and the surges of inflation are dragging on but not causing a crisis for fixed income. We continue to hold an overweight allocation to equities overall as well as a modest underweight in fixed income, also leaving cash meaningfully underweight. Within global equities, we are overweight with respect to the US, underweight in Emerging Markets, neutral with respect to Eurozone stocks and underweight Japan. Within fixed income, we are overweight in the US with a preference for mortgages and investment grade corporate credit. We have little to no exposure to non-US fixed income except through Green Bonds in our ESG series portfolios. All portfolios holding fixed income maintain lower duration than the benchmark.

Risk Outlook

- **Inflation** – The headlines are troubling, but inflation does not seem to be systemic. In many regards it is surprising, maybe even astonishing, that inflation has not been more of a concern for years now. We are more than a decade in to post-Crisis easy monetary policy and a booming stock market only briefly interrupted by the pandemic. But, the market may be the answer. As noted earlier in this newsletter, the coordinated government response to the economic damage of the pandemic has been massive. Had all of that stimulus settled into the “real” economy, inflation would be on a tear. We believe that the capital markets have been serving as a pressure relief valve, with stimulus settling out of the real economy and in to the capital markets inflating asset prices. Correlation does not equal causation, but there seems to be a relationship of some sort between the magnitude of the stimulus and the increase in aggregate value in just the public markets. We have seen spikes in prices of building materials and scarcity of new cars for purchase as examples. But, while we cannot discount those observations entirely, we principally

see them as graphic examples of how interdependent world economies and supply chains are and how fragile they were with just-in-time inventory management. While investors have extolled just-in-time since Toyota popularized it, it introduced an inelasticity into global supply chains that was not capable of absorbing the blow of COVID. We liken this to everyone on the highway cruising at 70 Mph riding bumper-to-bumper and doorhandle-to-doorhandle. It works fine until somebody swerves or stamps on their brakes. This was further exacerbated by climate-related issues with beetle infestation and fire affecting Western timber stocks and storms knocking petro-chemical production capacity off line among several other challenges. The results were issues such as a microchip shortage affecting the ability of factories to finish automobiles for delivery. We believe as major parts of the global economy get back on pace that the current situations will self-correct, but as investors and market watchers we are looking longer term at the confluence of business practices that are not sustainable, resilient or adaptive and externalities like global health and climate change which can and will disrupt businesses and markets again.

- **Rates** – Benign conditions do not always result in benign outcomes. As discussed elsewhere, even a slight normalization of the rate environment, which would reflect stabilizing economic conditions, could have profound effects in fixed income markets, severely dragging down assets like 30-year Treasury Bonds which are normally seen as safe harbors from risk. Wall Street has been cautioning about the risk of rising rates since the end of the Financial Crisis in 2009, but we have yet to actually have to live with those risks because a slow grind recovery followed by a series of crises including COVID have conspired to hold central bank policy where it has been – accommodative. A mild turn of phrase by the Fed Chair has resulted in temporary shocks in the bond and even equity markets, so we can anticipate that rising rates are not welcome in markets that have enjoyed easy money for more than a decade now. This compels us to think about risk in globally diversified portfolios differently, where the traditionally more conservative parts of asset allocations may actually represent more material risk in the nearer term.



Risk Outlook [cont'd]

- **The National Balance Sheet** – Continuing on the related themes of inflation and rates, the Federal Reserve has begun to signal their intent to start winding down the extraordinary measures they have been taking through asset purchases. That has a couple implications – one is telling the markets that the training wheels can come off. The Fed feels like their additional help is no longer as needed. That is positive in tone which should be good for market sentiment, but offset by the disappointment of losing a major bond investor. This does mean a more orderly bond market where institutional investors are not competing with the government for bond inventory. Again, this is good, but it also means less liquidity. This is a slow turn of the battleship of state. They are not really shrinking the balance sheet. Just growing it less fast, so most of the market reaction will be sentiment-driven rather than based on real stresses from lower liquidity.
- **Spending** – We cannot get away from the not-so-invisible hand of government in how markets are functioning. It may not be a risk per se, but we are mindful of the legislative efforts around major spending initiatives coming out of Washington DC. Discussions around infrastructure have been bipartisan and bicameral, and the President signed the legislation in to law on November 15th. The \$1 trillion will be more fundamental to the economy because it is being spent on “stuff”, and that spending will take time to deploy (5 years) and for the bridges, roads, broadband, etc. to be built or restored. That spending becoming a sure thing does get discounted into the market so it has an immediate effect on asset prices, but in a more durable way than the sugar buzz of pure cash stimulus we have been getting. Next up is Build Back Better, which may or may not happen since it does not enjoy the bipartisan support of infrastructure. As we have been saying since the election, an evenly split government means a lot of triangulation and not a lot of surprises, so we do not think the market will either jump or drop materially on the outcome.
- **COVID-19** – We are now looking at the global transition of SARS CoV-2 and COVID-19 from pandemic to endemic, and what that means for progress and prosperity in developed and developing economies. Vaccine deployment continues and close on its heels the promise of new therapies in pill form that may make addressing severe illness as simple for COVID as Tamiflu does for influenza. New strains of the virus may contest the efficacy of those vaccines, but after two years the world has become more adaptive to the challenge and the need to hit the “off switch” on the world economy is far less than the early stages when the virus represented all danger with no defense. As we have previously expressed, the global community remains vulnerable to a have/have-not dichotomy based on access to virus-fighting resources. Indications are that pricing will be calibrated according to economic capacity, which is a promising development that may help to reduce the gap between developed and developing nations in the same way COVAX is working to do so through access to vaccinations. With these developments we may be less than a year away from COVID no longer being a meaningful factor in global economies.
- **China and Russia** – One of our long-term risk themes continues to be our focus on Chinese Communist Party actions which have not materially shifted for the better in the COVID era. From aggression in the Asia-Pacific region to military tension along the border with India to suppression of Hong Kong citizens’ rights and the interests of the Uighur population and the lack of contrition for their early role in failing to stop COVID-19 in its tracks, all may contribute to China-directed backlash or retaliation. There does seem to be regional coherency in the response as nearly all Pacific nations have aligned with the US against Chinese aggression. From lack of respect for intellectual property rights to involvement in global criminal drug trafficking to financial crimes and human rights abuses bordering on genocide, the country is finding it harder to get the global community to look the other way. We view this as a risk to investment in China and investment in companies reliant on a Chinese supply chain, but likely bullish for other parts of the Asia Pacific interested in usurping China’s role as the manufacturing floor for the world. Meanwhile Russia continues to operate from other pages in the same playbook, manipulating natural gas markets in Europe and massing troops on the Ukraine border.



ESG Considerations

Disappointment is in the air

COP-26, shorthand for the 26th (United Nations Climate Change) Conference of the Parties took place in Glasgow through the first half of November. Coming out of COP-25 in Madrid, in the weeks before COVID-19 brought everything to a standstill, UN Secretary General António Guterres tweeted “I am disappointed with the results of #COP25. The international community lost an important opportunity to show increased ambition on mitigation, adaptation & finance to tackle the climate crisis. But we must not give up, and I will not give up.”

In anticipation of the 26th climate conference, Secretary General Guterres said 2021 was the “make it or break it year”.

At the conclusion of COP-26, disappointment came back for a stage call. “I know you are disappointed”. That was Guterres’ message to “young people, indigenous communities, women leaders, and all those leading the charge on climate action”. From the perspective of those four groups, representing a large percentage of the planet’s population, “disappointed” might be the diplomatic understatement of this century as they cling to the edge of an existential cliff.

Can an institution that by design is meant to move (extremely) slowly and deliberately and with total consensus actually address something with this much urgency?

We blogged regularly throughout COP (see our series of “Charting COP” posts at <https://wildecapitalmgmt.net>) examining the explanatory data behind various initiatives undertaken in Glasgow, from national pledges for climate finance to deforestation to Net Zero pledges to regenerative agriculture and sustainable aviation. We started with a simple thesis – the UN and individual nation-states are not the right parties to solve the climate crisis. The short-termism of individual political

regimes juxtaposed against the long-termism of a convening body like the UN results in stasis. Good for preventing war. Not good for solving immediate and urgent global problems.

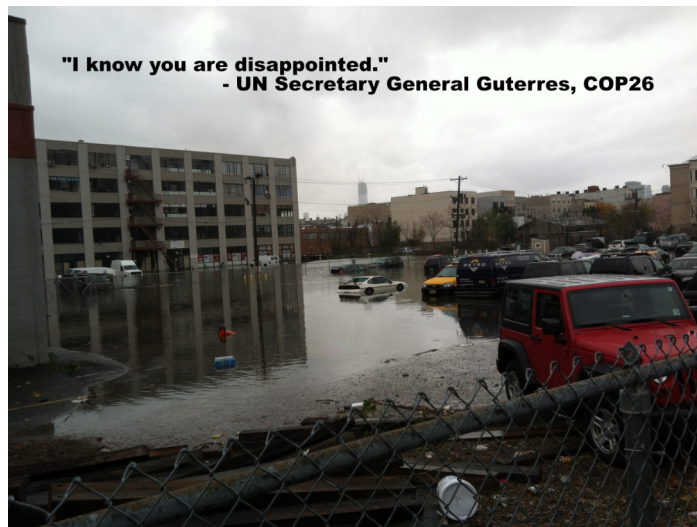
In fact, large convenings like COP seem to be providing aircover for everyone to do nothing. Grand statements and large pledges give permission for other stakeholders to hang back since the problem has been “dealt with”. Just one example of why that does not work out in reality is that prosperous industrialized nations already pledged \$100 billion annually to address the climate crisis and then failed to live up to the commitment. A commitment, as it happens, that is at least a 10X undershoot to what is actually needed to

avoid exceeding the 1.5-degree scenario and address the damage that has already been done to environmentally marginalized communities and infrastructure globally.

Rather, our perspective is that the highest and best use of the aggregate power convened in Glasgow would have been to remove as many obstacles as possible from the path of private enterprise, private

citizens, academia, and not-for-profits. Legislation, regulation, facilitation.

As we blogged, perhaps the issue is one of framing. From the UN’s perspective, if they were presented with an international conflict where food systems were to collapse, millions of lives were to be at risk, millions were to become refugees, hundreds of billions of dollars of infrastructure were to be destroyed, and this catastrophe would know no borders and respect no nation, law, or military might, what would the UN do? Guns pointed at each other is actually one of many societal byproducts of climate change, but for this thought experiment we should focus on the magnitude of devastation and hardship that is happening without a shot being fired.



ESG Considerations [cont'd]



**UN CLIMATE
CHANGE
CONFERENCE
UK 2021**

IN PARTNERSHIP WITH ITALY

If slowing things down is the UN's true nature, what can it slow down to forestall the full impact of this emerging catastrophe while society finds a permanent fix? What resources would it mobilize?

197 nations are signing the "Glasgow Climate Pact", but the two most populous countries insisted on a language change from "phase out" to "phase down" coal. That fundamentally changes the coal question from one of "when" to one of "if". Again, looking at other activities that pose imminent threat to life and land that bring UN involvement, say, nuclear weapons development or massing troops on a national border, the distinction between "phase out" and "phase down" would be of monumental import. We are mired in process over outcome.

Opportunity from disappointment

On the UN's news feed for November 3rd, they reported "It's 'Finance Day' at COP26, and the spotlight is on a big announcement: nearly 500 global financial services firms agreed on Wednesday to align \$130 trillion – some 40 per cent of the world's financial assets – with the climate goals set out in the Paris Agreement, including limiting global warming to 1.5 degrees Celsius." At the UN above all other institutions, words mean something. What does "align" mean? Is this another "phase down" vs. "phase out" situation?

For what we do on a regular basis as allocators of capital within this ecosystem of global financial services firms, we are forced to ask if this is a commitment to the largest greenwashing campaign in history. As we have written and spoken about repeatedly, we are looking to

see whether this is the first step of many along a path to more sustainable capital allocation, or window dressing to manage optics. Intentionality is everything. Too much was made of the \$130 trillion based on the actual (lack of) commitment made, but the potential is enormous. The tone is shifting on Wall Street, particularly as the mythology of concessionary returns from sustainable investment collapses on itself. There is a new moral hazard attached to squandered opportunities to invest proactively in public and private markets for climate adaptation, resilience and justice. The risk is both missing a historic moment to activate capital for good and missing a historic opportunity to invest in and profit from the third great economic revolution – from industrial to technology to regenerative systems.

The right response to disappointment is for the more responsible parties to seize the initiative. Waiting for elected (and un-elected) governments to solve these problems has cost decades of lost time and treasure. It is going to take the mobilization of private and not government capital to reach the intensity and scale of development necessary to forestall the worst effects of the climate crisis and walk us back from the edge. Shifting capital to a regenerative model for food, energy, water, and infrastructure should unlock an economic boom and broaden participation in a way which would be historic in defining the 21st century.

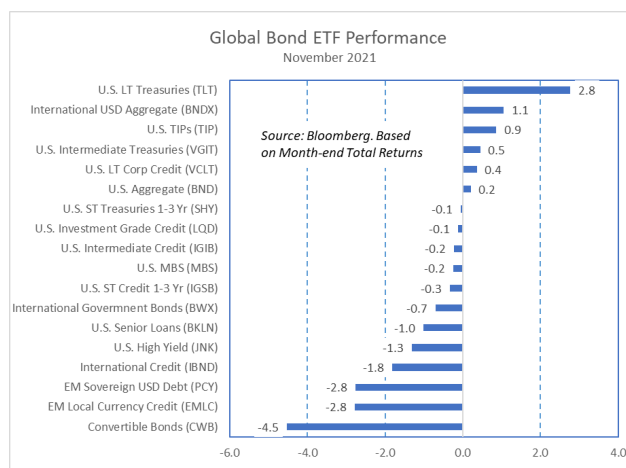
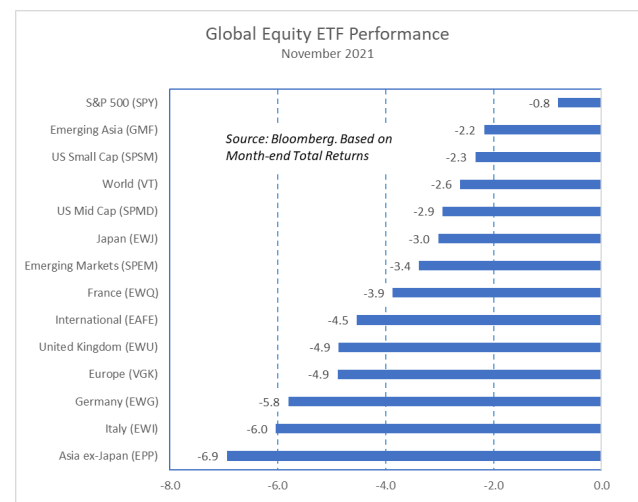


November 2021 Capital Market Review

Inflation is topping the charts for concerns for the economy and the market. The year-over-year comparisons put us at a multi-decade high harkening back to the 1970's. Conditions are different though. The world economy looks very different, we are still in a negative rate environment, and the hot spots for inflation are largely episodic and explainable. The principal concern would be whether these hot spots fade out or touch off more wide-spread inflation even after supply chain and other issues resolve. We continue to see what has become the new normal in the persistently low-rate environment in which we have operated for more than a decade. Skittish markets react adversely to even the implication that central bank policy might become less accommodative much less hawkish. New COVID variants "of concern" cause immediate and sharp reactions. November concluded with both to punctuate a volatile and generally negative month. The broad top-down pressures are not affecting all markets equally. We have seen larger departures between asset classes (bonds vs. equities for instance), geographies, and industries and sectors, and active fundamental management has continued to shine since the rising and falling tide is not moving all metaphorical boats equally.

Equity Markets

The overall direction of equity markets was down for November, but perhaps the most meaningful observation is that dispersion continues and has even increased. Rather than everything moving up and down more or less in lock step, we are seeing differences in capitalization (small cap and mid cap underperforming large cap by 150bp or more), and regionally, with Germany underperforming France by nearly 200bp and Asia ex-Japan underperforming Japan by nearly 400bp and the US by more than 600bp. We are in a period where allocation decisions matter across sectors, geographies and asset classes more than they have in recent periods.



Bond Markets

Becoming more of a steady drumbeat, bonds continued to not provide safe harbor for investors in November much as in September as equities fell again. Again here in the bond markets dispersion is higher with more than a 500bp spread between the ultimate safe harbor of the US Long Term Treasury vs. a go-to risk asset like local currency Emerging Market debt. The equity-like behavior of certain bond types like Convertibles and High Yield also pulled spreads farther apart. TIPS performed decently given concerns about inflation but still came up well short of the long-term Treasury and did not add a lot of value relative to the short and intermediate Treasury.

The returns cited reflect total return performance of exchange traded funds listed in the corresponding bar charts



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ETFs included in portfolios may charge additional fees and expenses in addition to the advisory fee charged for the Selected Portfolio. These additional fees and expenses are disclosed in the respective fund/note prospectus. For complete details, please refer to the prospectus.

For additional information regarding advisory fees, please refer to the Fee Summary and/or Fee Detail pages (if included with this report) and the program sponsor's/each co-sponsor's Form ADV Part 2, Wrap Fee Brochure or other disclosure documents, which may be obtained through your advisor.

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