S&P 500 Outpaces COVID-19 Woes, Soars More Than 25% in 2021

While the traditional end-of-year Santa Claus equity rally may not have been as pronounced as we typically see, it may have just come early. Thus far, we've seen both the Dow Jones Industrial Average and the S&P 500 notch new highs in December with underlying market sectors firmly in the green.

Despite the challenges posed by coronavirus variants and extreme weather events, 2021 saw the best economic growth since 1984, muted market volatility and the S&P 500 delivering a return of approximately 27% over the course of the year. Raymond James Chief Investment Officer Larry Adam expects inflation to peak by early next year, which should alleviate pressure on the Federal Reserve (Fed) in the upcoming tightening cycle and would be supportive of domestic equity markets overall. The situation remains fluid, but there's general optimism that the global reopening will continue and inflationary pressure will subside. Both will be key factors for markets, economic growth and corporate earnings throughout 2022.

This year-end equity boon didn't come easy. We saw some volatility amid faltering negotiations to advance President Joe Biden's Build Back Better legislation and rising geopolitical tensions between Russia and the Ukraine, which have the potential to escalate in the near term. We believe that U.S. lawmakers may eventually unlock a deal in the new year, says Washington Policy Analyst Ed Mills. However, investors can expect to see short-term economic headwinds emerge in the meantime, and consumer sectors may stumble as the monthly child tax credit payments are set to expire as well.

Let's look at the longer-term numbers:

	12/31/20 Close	12/31/21 Close	Change Year to Date	% Gain/Loss Year to Date
DJIA	30,606.48	36,338.30	+5,731.82	+18.73%
NASDAQ	12,888.28	15,644.97	+2,756.69	+21.39%
S&P 500	3,756.07	4,766.18	+1,010.11	+26.89%
MSCI EAFE	2,147.53	2,336.07	+188.54	+8.78%
Russell 2000	1,974.86	2,245.31	+270.45	+13.69%
Bloomberg Aggregate Bond	2,392.02	2,355.14	-36.88	-1.54%

Performance reflects price returns as of market close on Dec. 31, 2021.

As we close out the month, quarter and year, here are a few trends we're keeping an eye on:

Energy policy

As negotiations in D.C. drag out, clean energy companies in the U.S. market may not be able to count on a decade-long extension of the wind and solar tax credits, a more generous electric vehicle tax credit, or new tax credits for low-carbon fuels and green hydrogen. These provisions may be revived in some form but that remains to be seen. This is a sharp contrast to the European Union climate policy, notes Energy Analyst Pavel Molchanov. For example, Germany's new coalition government announced plans to phase out coal and mandate 80% renewables in the electricity mix by 2030.

Inflation and interest rates

The overall market feel has not changed a great deal. Inflation is rooted in select products/industries, yet interest rates remain subdued for a myriad of reasons that include inflation longevity doubts, global interest rate disparity, sovereign bias toward amassing debt levels and more complex demographic rationales.

The Fed began to taper the pace of its monthly asset purchases and financial markets seem to have priced in rate hikes sooner than later. The central bankers have stated hikes won't occur until tapering is complete, most likely around May. Given that monetary policy has been so influential to equity markets post-credit crisis, the Fed's hawkish pivot from ultra-lenient policy could come with more moderate returns and normal volatility/choppiness over the coming year, notes Joey Madere, senior portfolio analyst, Equity Portfolio & Technical Strategy.

Around the world

Overseas markets faced similar challenges (e.g., a sharp rise in COVID-19 cases; higher gas prices; heightened inflationary pressures), yet European equity markets hit new 2021 highs during December. Corporate earnings growth for 2022 is anticipated to be above 10%, aided by a combination of general global export recovery and the current low level of both the euro and the pound against both the dollar and the Chinese yuan.

During 2021, over 40 global central banks raised interest rates, predominantly in the emerging markets, reflecting both economic recovery and higher inflation. With economic growth rates in China continuing to slow, we believe the world's largest emerging market is more likely to reduce its interest rates further during 2022.

The bottom line

We expect normal volatility and pullbacks in the year ahead, along with continued sector rotation. Overall conditions are likely to remain healthy, and investors can use these periods to opportunistically and thoughtfully add vetted positions. If you have any questions about your financial plan, this letter – or anything else – please reach out at your earliest convenience.

I hope the buoyant mood of the domestic stock markets carries into 2022 and that you and yours enjoy a healthy and prosperous new year! Thank you for your continued trust in me.