The Gorton
Wealth Management Group
of Wells Fargo Advisors

2021 Annual Review

January 2022

An update of performance, trends, research, and topics for the long-term investor

Relevant rates of return a/o 12/31:	2021	vs.	2020
Russell 1000® Growth Index: Stocks within this index include: Amazon, Facebook, Google (Alphabet) Home Depot, Visa	+27.60		+38.49
Russell 1000® Value Index: Stocks within this index include: Berkshire Hathaway B, Exxon Johnson & Johnson, JP Morgan	+25.16		+2.80
Barclays U.S. Agg Bond Index:	-1.54		+7.51
S&P 500 Index:	+28.71		+18.40
Russell 2000® Value Index:	+28.27		+4.63
MSCI EAFE® Index:	+11.26		+7.82

Long Term Historic Returns, compounded annually (1970-2020)[1]

- Small Value +13.6%
- Large Value +10.3%
- Small Growth +9.9%
- Large Growth +9.4%

Growth and value stocks in this example are represented by the Ibbotson Associates Growth and Value Indexes for 1970–1997 and the Morningstar Style Indexes thereafter. Ibbotson Associates Growth and Value Indexes calculated based on data from CRSP US Stock Database and CRSP US Indices Database, Center for Research in Security Prices (CRSP®). The data assumes reinvestment of income and does not account for transaction costs or taxes.

Description of Indexes

An index is unmanaged and not available for direct investment.

S&P 500 Index - a market capitalization-weighted index, composed of 500 widely held common stocks, including reinvestment of dividends, that is generally considered representative of the US stock market.

Russell 1000 Growth Index - offers investors access to the large-cap growth segment of the US equity universe. The index is constructed to provide a comprehensive and unbiased barometer of the large-cap growth market. Based on ongoing empirical research of investment manager behavior, the methodology used to determine growth probability approximates the aggregate large-cap growth managers' opportunity set.

Russell 1000 Value Index - measures the performance of those Russel 1000 companies with lower price-to-book ratios and lower forecasted growth values. These stocks are selected from the 1000 largest companies in the Russell 3000 Index.

MSCI EAFE Index - the MSCI EAFE Index is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US and Canada.

Russell 2000 Value Index - measures the performance of those Russell 2000 companies with lower price-to-book ratios and lower forecasted growth values.

Barclays U.S. Aggregate Bond Index - an index comprised of approximately 6000 publicly traded bonds, including U.S. Government, mortgage-backed, corporate, and yankee bonds with an approximate average maturity of 10 years.

"The best way to predict the future is to create it."

—Abraham Lincoln[2]

"Prediction is difficult—particularly when it involves the future."

—Mark Twain[3]

Michael Gorton
Managing Director - Investment Officer

Predicting the Future

This fall Marin County, with our own water supply, was in the middle of a severe drought, with reserves in our reservoirs expected to last only through June. The season's weather forecast was for another dry year. As I write this our reservoirs are over 90% full after record early rains. So much for forecasting the weather...

2021 in review, what a surprise:

Lots of stimulus from the Fed, significantly higher markets, substantially higher inflation, and we ended the year with the Omicron variant keeping Covid with us into its 3rd year. I don't think any of those outcomes were expected as we headed into 2021...

2022 Forecast:

Let's see whether predictions fare any better for 2022. Wells Fargo Investment Institute has projected[4]:
(WFII 2022 Market Outlook included.)

- Stronger economy for 2022 with GDP growth of 4.5%
- Global inflation to moderate with US inflation target of 5.3%

- Earnings to continue to rise, up 12% for the S&P 500 in 2022, and with the price earnings ratio expected to be range bound translates to a 12-15% rise in the S&P 500
- Interest rates to rise with a target for the 10-year treasury of 2-2.5% vs 1.51% to end the year
- Oil prices to rise to $85-$95 a barrel vs $75.45 at year end
- And labor markets will continue to strengthen

What could cause the markets to be better or worse than the 2022 estimates?

- Higher Markets
  - Inflation wanes more than expected and the fed is softer with their rate increases
  - Covid finally becomes an annual endemic, masks come off and we go back to business as usual with annual flu shots to include the latest covid variant
  - More people come back to work easing the labor shortages
  - Stimulus bill creating more fiscal spending and excess liquidity in the system
  - Positive outlook — Mood, Money and Momentum drive the markets, which have driven stocks and real estate markets this last year.
  - Social Security benefits to rise 5.9% in 2022 and I assume pension COLA's will be similar
- Lower Markets
  - The higher market cases being worse than expected
  - China, Russia, or the Middle East destabilizing the world
  - Then of course there is always what does not even show up on the radar!

Since we are asked all the time, let's discuss some popular topics: Cryptocurrency, Green Energy vs Oil (the new exciting technology).

Cryptocurrency

I believe blockchain technology is, and will be, part of our future. I am not sure if blockchain will use any of the existing currency. A currency is used for two purposes: a store of value and a medium of exchange. When I ask crypto investors why Bitcoin is priced at $65,000 a month ago or $42,000 today, I have not found anyone who has a definitive answer. So let's say I put the down payment for my house in Bitcoin a month or so ago when it was trading at $65,000 and went to close escrow and can now only get $42,000. I am sure you get the picture. This is why most crypto currencies are not a good store—or even short-term exchange—of value in the present form and markets. This just feels a bit like the dot.com days where folks were being temporarily rewarded for their purchases, right before the majority of the companies collapsed. I believe at some point our government will regulate and establish both a medium of exchange and/or a store of value using cryptocurrency. I just don't understand why it would need to be one of the existing cryptocurrencies. Interestingly enough, gold has underperformed expectations in this more recent inflationary environment as many folks have probably used cryptocurrency as a substitute, keeping the gold price down and possibly undervalued.

Green Energy and Electric Cars

A well known electric car manufacturer estimated that electric cars would double global energy demand. Where will that come from? 10% of US energy production in 2020 was from wind and solar, 40% from natural gas which both have made up for the decline in coal generation.[5] If it comes from wind and solar, we will need to increase our battery storage significantly so that you can charge your car on dark windless days. If it comes from the alternate sources, oil, coal, natural gas, it does not move us towards a green energy goal. Then there is the issue of transmission and infrastructure to get the electricity from where it is generated, wind farm, solar farm, etc. to where you plug in (home solar is very inefficient in the national energy grid picture). This would require the transmission infrastructure to be rebuilt to handle the significantly higher demand, which means digging up every city to replace and upgrade electric transmission lines. Therefore, the technology still needs to advance to make it a reality. And yes, 6% of the population can drive electric cars and not overtax the system. Many people who can afford a Tesla can also afford to put solar panels and battery storage in their homes. I am not sure the average person can. So, if we want electric cars to be greener and generate the doubling of power from alternate energy, then we would have to increase the wind and solar production by 10x. Why? Right now, we cannot increase hydroelectric nor nuclear energy, as it is difficult, if not impossible, to get approved. So, that leaves wind and solar (and yes, geothermal, but that power generation is minimal). Increasing wind and solar by 10x would necessitate a lot more storage (batteries) which are expensive, have a limited life, and not environmentally-friendly with lithium and cadmium mining in addition to the transportation energy cost (still need to charge your car when it is dark and windless). Maybe storage is the place to look to invest?

Like with cryptocurrency, early automobiles (there were originally 300 manufacturers), early computers, software etc., we are just too early in the development cycle to know who the leaders in green energy will be 10 years from now.

So, where should one invest? Does it make sense to guess and hope we picked right or wait until a few clear winners begin to emerge and then commit?

We plan to stick to our knitting and buy good quality companies at a fair price and be willing to hold them for the long term. We are always looking for cutting edge companies that can earn money and are trading at a reasonable price for what they earn and how fast the business can grow. It does not mean that you can't put some money into/invest in something you are passionate about, but don't let it negatively affect your portfolio if you over invest and it does not work out.

We are headed into annual review time and look forward to our discussions over the coming months....

Happy New Year! May it be a good one...

Michael Gorton
Managing Director – Investment Officer

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4 Wells Fargo Investment Institute. Asset Allocation Strategy. 2022 Outlook: Which Way to the Recovery. Dec 21, 2021 (CAR# 1221-04221)
5. U.S. Energy Information Administration. Total Energy. Retrieved 1/7/22 from www.ela.gov/totalenergy/data