



Quarterly Chartbook  
4Q2021

# Founder Comments

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When we started this firm back in 2016, we made a commitment to regular, transparent communication as one of our core principles. One of the core elements of that commitment has been our quarterly newsletters. The goals of our newsletter have always been to consolidate news relevant to your portfolio, review our decision-making process and highlight the research we do in a format that would be valuable and engaging to read.

Informally, however, we also made a commitment to ensuring that the content and format doesn't become robotic because we know that when it does, it immediately loses value. As a result, we are presenting the third iteration of our communication format to you this quarter. Compared to our last iteration, this will be the most dramatic overhaul we have undertaken.

We have taken the idea that "a picture is worth a thousand words" to heart and removed thousands of words in favor of a group of charts that capture the key factors influencing markets and our portfolio positioning.

We hope you find the content interesting and valuable. If you would like to jump to a specific idea, you can click on any of the links and ideas below. As always, we appreciate any feedback you might have.



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# Market Performance

## Annualized % Returns (As of 12/31/2021)

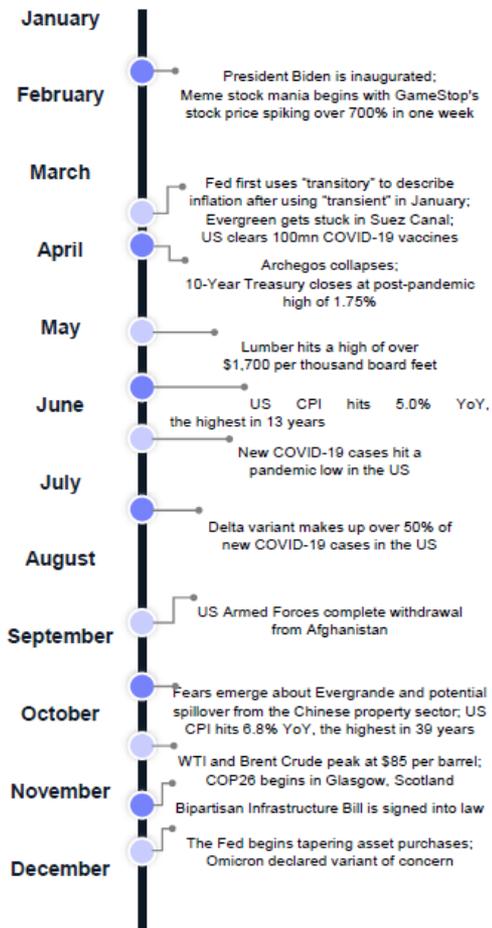
Index Name	Index Category	1 year	3 year	5 year	10 year
S&P 500 Index	Large Cap Stocks	28.71	26.07	18.47	16.55
Russell 1000 Index	Mid/Large Cap Stocks	26.45	26.21	18.43	16.54
Russell 1000 Growth Index	Growth Stocks	27.60	34.08	25.32	19.79
Russell 1000 Value Index	Value Stocks	25.16	17.64	11.16	12.97
Russell 2000 Index	Small Cap Stocks	14.82	20.02	12.02	13.23
MSCI EAFE Index	Non-U.S. Developed Market Stocks	11.26	13.54	9.55	8.03
MSCI Emerging Markets Index	Emerging Markets Stocks	-2.54	10.94	9.87	5.49
MSCI ACWI Ex USA Small Cap Index	Non-U.S. Small Cap Stocks	12.93	16.46	11.21	9.46
BofAML Preferred Stock Fixed Rate Index	Preferred Stocks	2.24	8.78	6.37	6.59
Barclays Municipal Bond Index	U.S. Municipal Bonds	1.52	4.73	4.17	3.72
Barclays Aggregate Bond Index	U.S. Bonds	-1.54	4.79	3.57	2.90
Barclays Intermediate U.S. Gov/Credit Index	Government/Corporate Bonds	-1.44	3.86	2.91	2.38
BofAML U.S. Treasury Master Index	Treasury Bonds	-2.38	4.17	3.14	2.22
BofAML U.S. Mortgage Backed Securities Index	Mortgage Backed Bonds	-1.21	3.08	2.53	2.29
BofAML U.S. Corporate Master Index	Corporate Bonds	-0.95	7.50	5.28	4.76
BofAML U.S. High Yield Master II Index	High Yield Bonds	5.35	8.53	6.08	6.71
BofAML Euro Broad Market Index	European Bonds	-9.66	2.16	3.16	2.27
BofAML Local Debt Market Plus Index	Emerging Markets Bonds	-6.53	4.38	4.41	1.77

## Calendar Year % Returns (QTD, YTD as of 12/31/2021)

	2021	2020	2019	2018	2017
S&P 500 Index	28.71	18.40	31.49	-4.38	21.83
Russell 1000 Index	26.45	20.96	31.43	-4.78	21.69
Russell 1000 Growth Index	27.60	38.49	36.39	-1.51	30.21
Russell 1000 Value Index	25.16	2.80	26.54	-8.27	13.66
Russell 2000 Index	14.82	19.96	25.52	-11.01	14.65
MSCI EAFE Index	11.26	7.82	22.01	-13.79	25.03
MSCI Emerging Markets Index	-2.54	18.31	18.44	-14.58	37.28
MSCI ACWI Ex USA Small Cap Index	12.93	14.24	22.42	-18.20	31.65
BofAML Preferred Stock Fixed Rate Index	2.24	6.95	17.71	-4.34	10.58
Barclays Municipal Bond Index	1.52	5.21	7.54	1.28	5.45
Barclays Aggregate Bond Index	-1.54	7.51	8.72	0.01	3.54
Barclays Intermediate U.S. Gov/Credit Index	-1.44	6.43	6.80	0.88	2.14
BofAML U.S. Treasury Master Index	-2.38	8.22	6.99	0.80	2.43
BofAML U.S. Mortgage Backed Securities Index	-1.21	4.09	6.51	1.00	2.45
BofAML U.S. Corporate Master Index	-0.95	9.81	14.23	-2.25	6.48
BofAML U.S. High Yield Master II Index	5.35	6.07	14.41	-2.27	7.48
BofAML Euro Broad Market Index	-9.66	13.35	4.11	-4.39	14.61
BofAML Local Debt Market Plus Index	-6.53	4.50	16.44	-4.90	14.71

Source: Morningstar Direct

# 2021 Year in Review



<b>~8.5bn</b>	COVID-19 vaccines administered globally
<b>Energy</b>	Best performing global sector after being the worst performing one in 2020
<b>&gt;\$530bn</b>	Equity-capital market issuance, the most on record
<b>\$1tn</b>	Global ETF inflows reach for first time in history
<b>+20%</b>	Record spread between mutual fund and hedge fund performance
<b>70 ATHs</b>	All-time highs hit by the S&P 500, second to only 1995 with 77
<b>1 week</b>	Median time US homes spent on the market before a contract was signed
<b>\$69k</b>	Bitcoin reached a new high in November

Capturing the essence of a year is difficult, but some trends stood out more than others....

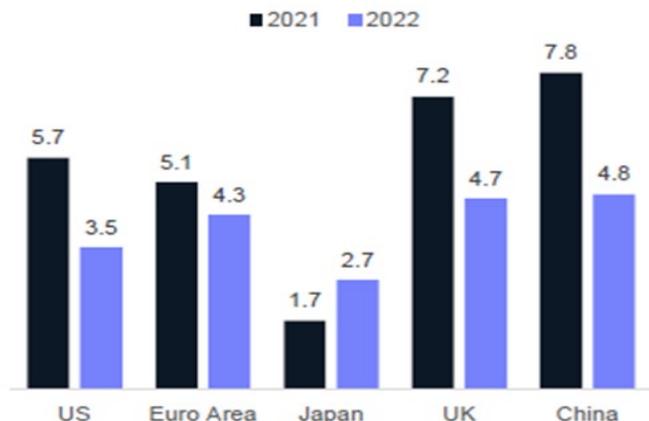
- Treasury bond yields moved higher.
- Covid variants and vaccination trends were closely monitored.
- U.S. stocks continued to visit all-time highs.
- Home buying demand was very strong.
- Inflation became a regular point of discussion.

and provided a potential preview for 2022.....

Source: Goldman Sachs

# Fixed Income – Global Economic Growth

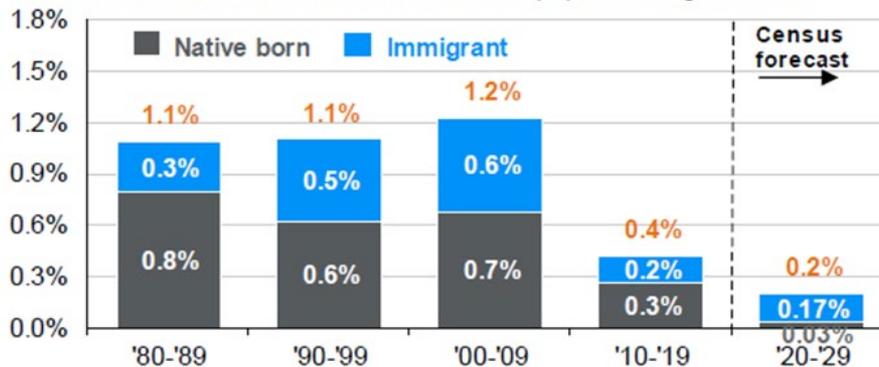
Forecasted Real GDP (% YoY Annualized)



Source: Goldman Sachs

Growth in working-age population

Percent increase in civilian non-institutional population ages 16-64



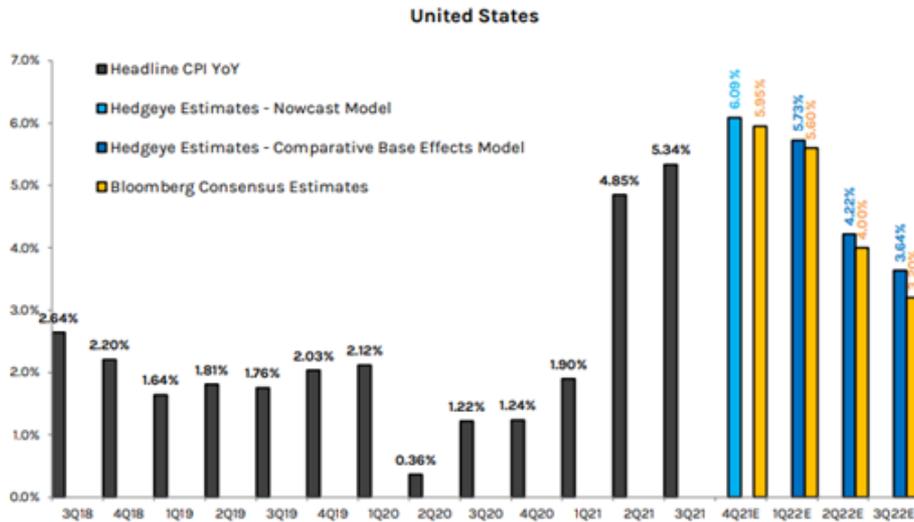
Source: JPMorgan

Global economic growth is expected to slow in 2022.

- Projections for GDP growth in 2022 are expected to range from 5-6%.
- Long-term growth drivers, such as an increase in the working-age population (or lack thereof), are among the factors putting pressure on estimates.

If the market prices in lower economic growth expectations, the U.S. Treasury bond yield curve has the potential to flatten. We believe this creates the potential for longer-term maturity bonds to outperform. Portfolios are now slightly overweight longer-term maturity bonds.

# Fixed Income – Inflation

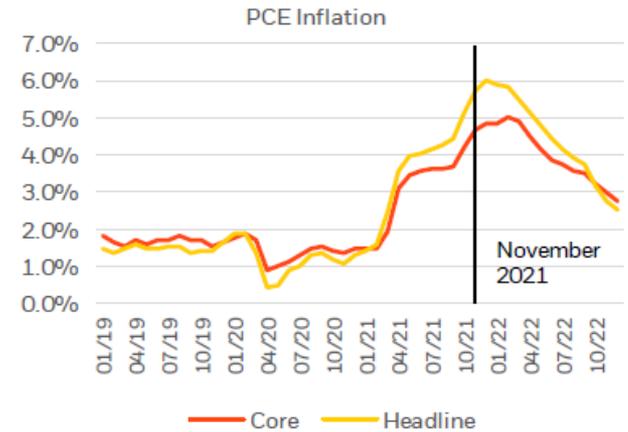


Source: Hedgeye

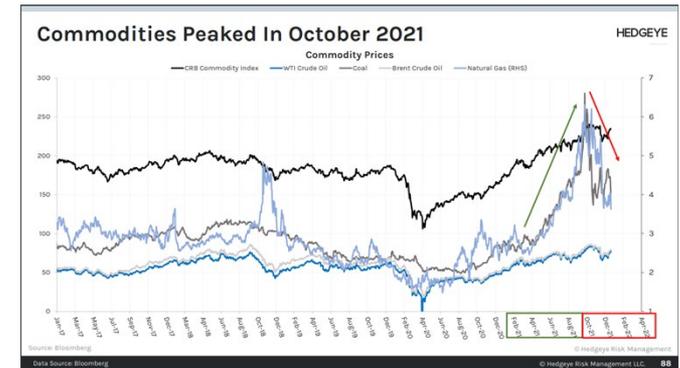
Inflation is expected to moderate in 2022 but remain above post financial crisis averages.

- Commodity prices appear to have rolled over.
- Supply chain disruptions seem to be abating.
- Long-term inflation trends are well-anchored.

We are underweight Treasury bonds relative to the broad market, but recently increased our investment due to potential risk in spread sectors (non-government bonds) in a risk-averse environment.

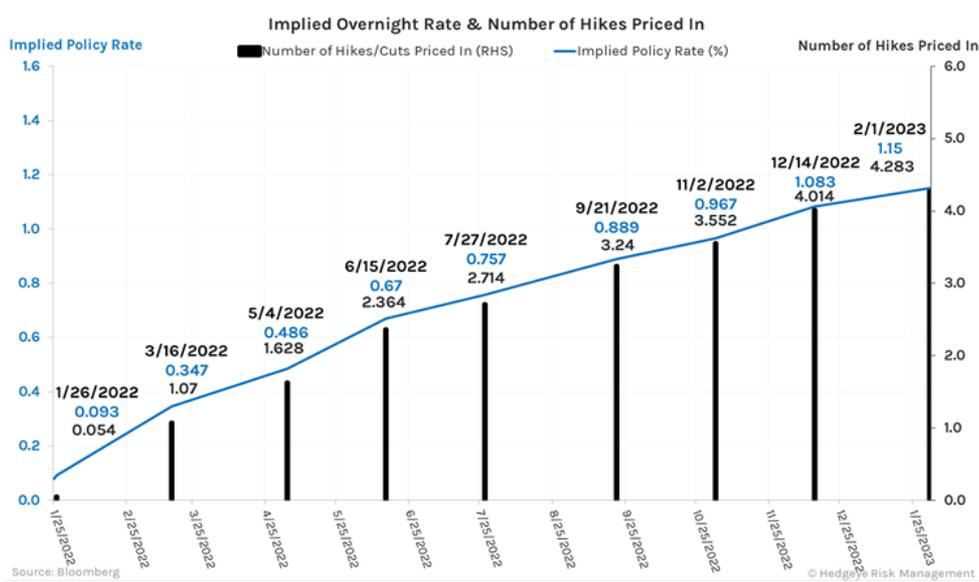


Source: Blackrock



Source: Hedgeye

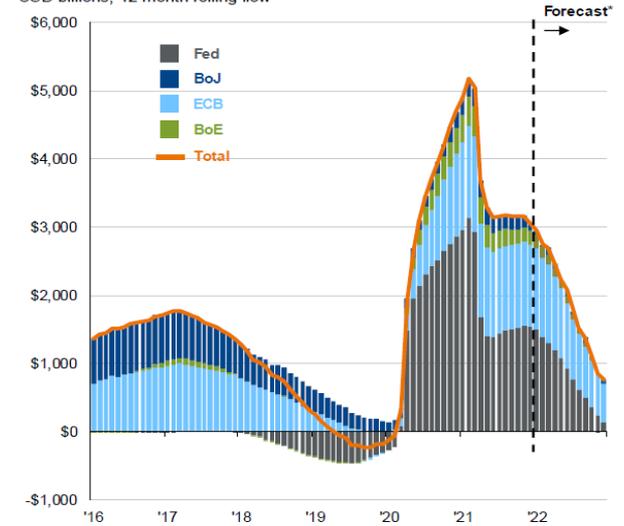
# Fixed Income – Interest Rates



Source: Hedgeye

## Developed market central bank bond purchases

USD billions, 12-month rolling flow



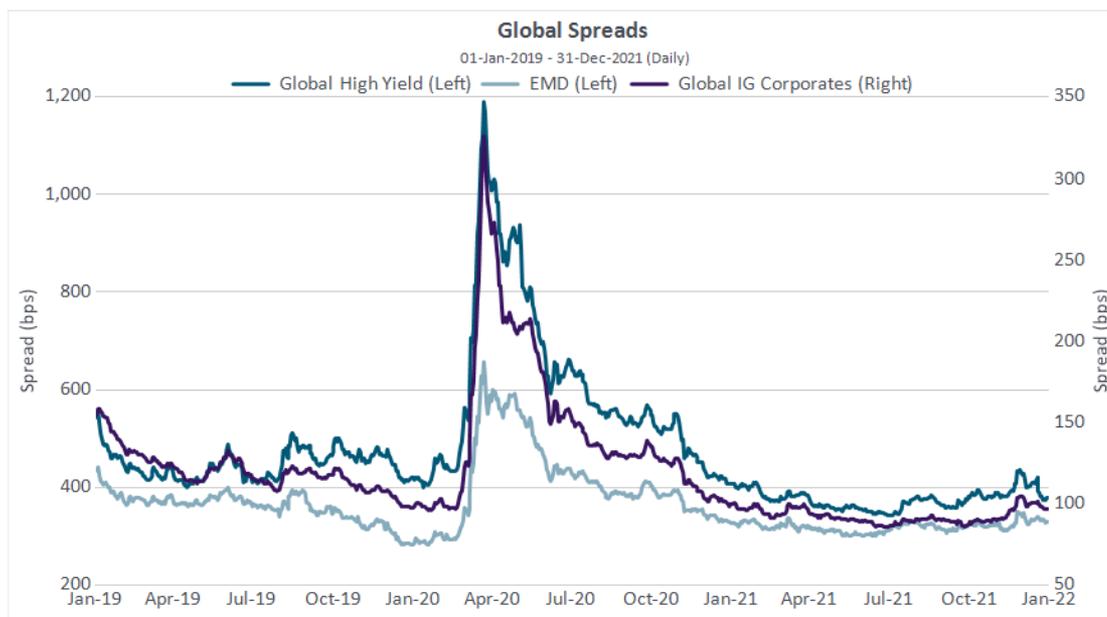
Source: JPMorgan

The U.S. Federal Reserve (Fed) is expected to meaningfully tighten policy in 2022.

- Most Fed members are projecting three interest rate hikes in 2022.
- The Fed is also planning to reduce the size of its balance sheet (quantitative tightening).
- The Fed has already begun to reduce the size of its monthly asset purchases.
- Simultaneous rate hikes and tightening is creating market volatility.

Early this year, we increased the duration (bond price sensitivity) of client portfolios to a level that is similar to broad benchmarks. We did this because of a sudden rise in interest rates in anticipation of Fed activity.

# Fixed Income – Credit Spreads



Source: MFS Investment Management

The spread between U.S. Treasuries and global credit sectors is very narrow.

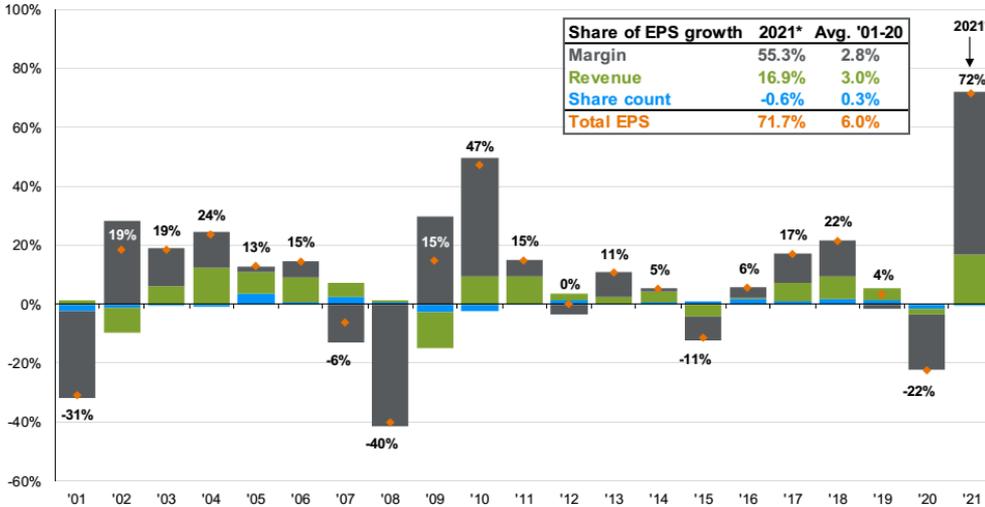
- Higher yielding sectors generally mitigate inflation pressure, but if spreads widen, these sectors represent an area that could experience significant pricing pressure.
- Securitized assets generally offer higher yield per unit of risk than other spread sectors.

We recently reduced our investment in corporate bonds because of very tight spreads, compared to similar Treasury bonds, and historically long maturities. We have small allocations to high-yield bonds and emerging markets bonds through actively-managed mutual funds. We have also reduced investment in municipal bonds because of their strong outperformance and lower relative value compared to the recent past. We prefer to pursue yield in securitized assets.

# Equity – Earnings

## S&P 500 year-over-year operating EPS growth

Annual growth broken into revenue, changes in profit margin & changes in share count



Source: JP Morgan

## Labor share of income and profit margins\*

Compensation and adjusted after-tax corporate profits, SAAR



Source: JP Morgan

Corporate profit margins and revenue growth are two of the largest determinants of overall earnings per share (EPS) growth.

- In 2021, the primary driver of earnings growth was a spike in margins.
- Historically, earnings growth driven by large margin gains has been difficult to maintain for multi-year periods.
- Wage pressure has been one of the primary causes of margin compression in prior timeframes.

We believe a reduction in profit margins has the potential to limit earnings growth in 2022, which may lead to weaker than expected returns for the broad equity market.

# Equity – U.S. Valuations

## S&P 500 Index at inflection points

GTM U.S. 4

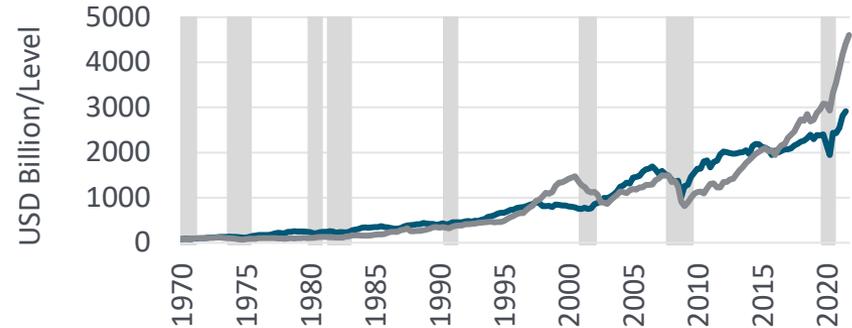
### S&P 500 Price Index



Source: Compustat, FactSet, U.S. Federal Reserve, Refinitiv Datastream, Standard & Poor's, JP Morgan Asset Management

— US Corporate Profits (Before Tax) - USD Billion

— S&P 500 Price Index - Level



Source: Haver Analytics

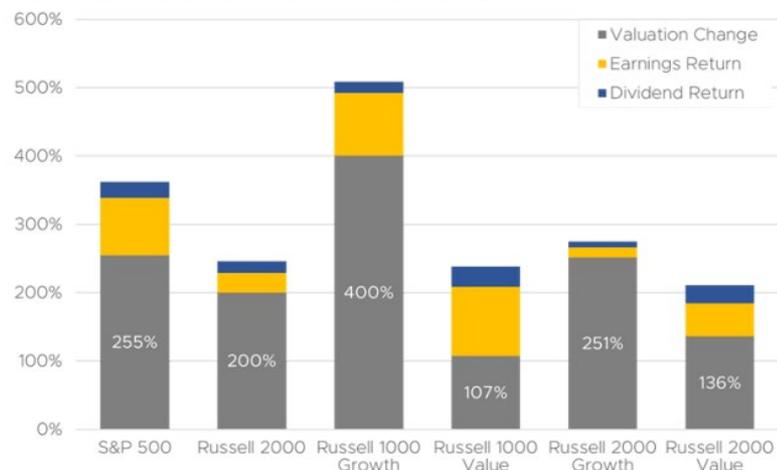
Valuation levels remain elevated relative to history.

- The forward P/E of the S&P 500® Index was 21.2X at year-end. The only other time the market was at a higher inflection point was the height of the technology bubble in March 2000 when it was 25.2X.
- Equity prices generally revert to fundamentals (profits) over the long-term despite minimal short-term correlation.

Based on relative valuations and the potential for relatively weaker earnings growth, we believe future U.S. equity returns will be lower than what investors have experienced since the depths of the global financial crisis.

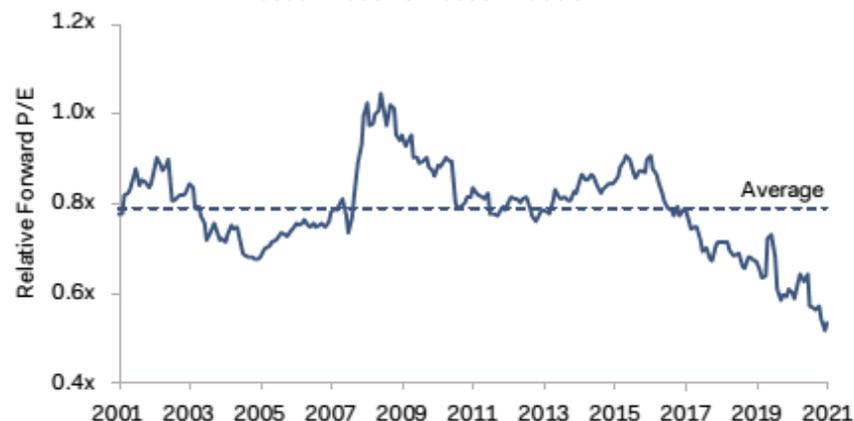
# Equity – U.S. Style

Breakdown of Total Return (Annualized) 2011-21



Source: Bloomberg, Cresset Capital

Relative Forward P/E Ratio  
Russell 1000V / Russell 1000G



Source: Bloomberg, FactSet, Russell

Within U.S. equity markets, growth stocks have held a distinct advantage compared to value over the recent past.

- U.S. equity market returns over the last 10 years have been driven, in large part, by the expansion of valuation multiples (P/E ratios growing). This is particularly true among large- and small-cap growth stocks as represented by the Russell 1000® Growth and Russell 2000® Growth indices.
- Historically, growth stocks have traded at a valuation “premium” to value stocks. At year-end, this “growth premium” was the largest we have seen in the past 20 years.

U.S. value stocks have not experienced the same degree of valuation expansion as the other sub-asset classes shown and are attractively priced compared to growth stocks. We believe this may result in relatively better downside protection and more attractive return potential for these stocks over the intermediate-term.

# Equity – Non-U.S. Valuations

## International: Price-to-earnings discount vs. U.S.

MSCI AC World ex-U.S. vs. S&P 500 Indices, next 12 months



Source: JP Morgan

Fig 6: EM trade at historic lows compared to developed markets

MSCI EM / MSCI World forward price to earnings ratio



Source: Ashmore, Bloomberg. Data as at 30 November 2021.

Source: Bloomberg, Ashmore

Non-U.S. stocks have been out of favor relative to U.S. stocks.

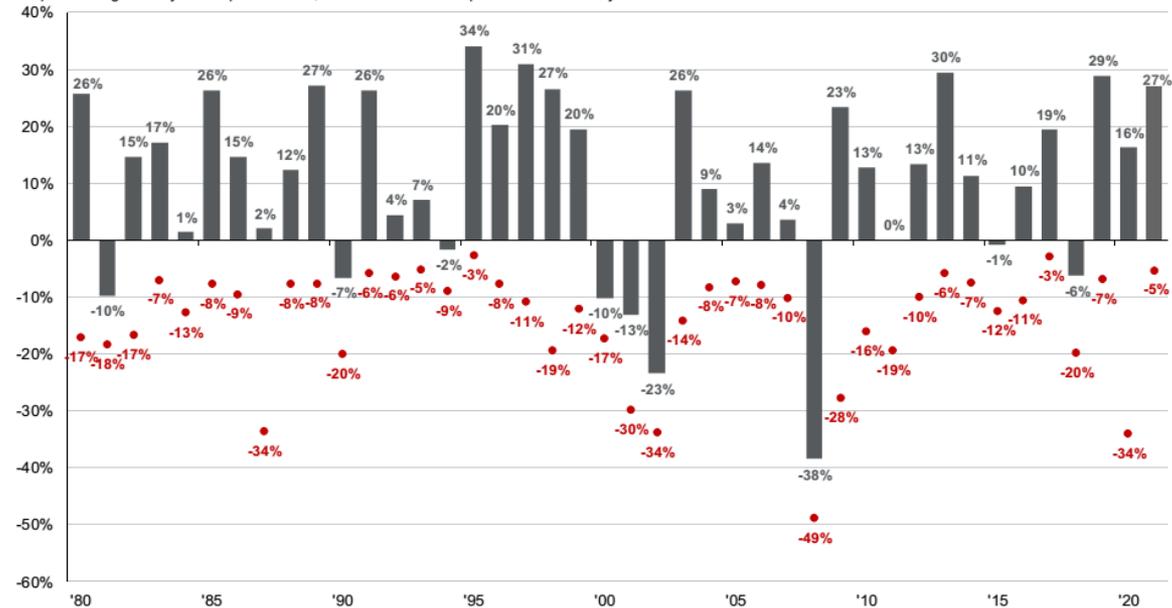
- U.S. stocks have outperformed foreign stocks (developed and emerging) by a wide margin for over a decade. The outperformance has led to an historically large valuation difference between the two sub-asset classes.
- Emerging markets equities are priced at a large “discount” to developed markets.

Based on relative valuations, earnings outlook, and a positive macroeconomic backdrop, we believe foreign equities, particularly emerging markets equities, may provide investors with relatively attractive returns over the intermediate- to long-term.

# Equity – Volatility

## S&P intra-year declines vs. calendar year returns

Despite average intra-year drops of 14.0%, annual returns were positive in 32 of 42 years



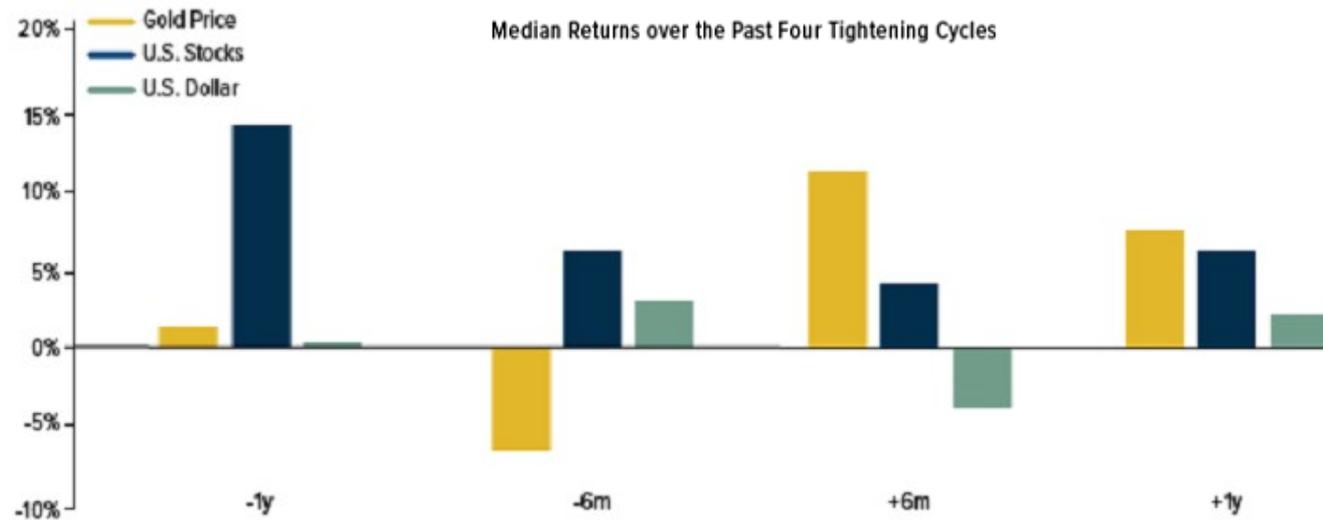
Source: FactSet, Standard & Poor's, JP Morgan Asset Management

U.S. equity market corrections, even in positive calendar years, are very common.

- The chart displays calendar year returns for the S&P 500<sup>®</sup> Index back to 1980 (grey bars), along with intra-year declines (red dots).
- We expect equity market volatility to remain elevated.

An expectation of heightened volatility has caused us to have relatively defensive equity allocations in client portfolios (notably in the U.S.).

# Commodities – Gold



Source: MWGC, Bloomberg, U.S. Global Investors

Gold has historically performed well following the initiation of Fed interest rate hikes (+6 months and +1 year).

- Historically, gold has had relatively low (or negative) correlation with many global equity market sub-asset classes and has proven to be resilient during periods of increased market turmoil.
- The combination of these factors may improve diversification in portfolios and may also provide investors with a more attractive risk-adjusted return profile for their portfolios.
- We view gold to be a short- to intermediate-term holding in portfolios.

# Our Team

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## We are an investment firm, founded by investors.



**Bob Batchelor, CFA®**, **CFP®** is Co-Founder and Chief Executive Officer of Entasis Asset Management. Bob has 22 years of experience in the investment industry. Prior to founding Entasis, Bob worked at Artisan Partners where he held a variety of roles including Head of Corporate Communications, Managing Director, Head of Marketing and Technology and Head of Marketing and Communications. He also served as a member of Artisan Partners Executive Committee. Before Artisan Partners, Bob worked at Strong Capital Management as Client Account Manager and Director of Investment Research and Communication.

Bob holds an M.B.A. from Marquette University and a B.B.A. from the University of Wisconsin-Madison. He has earned the right to use the CFA designation. Bob is a member of the CFA Institute and CFA Society of Milwaukee. Bob has also earned the right to use the Certified Financial Planner™ certification.



**Charles (C.J.) Batchelor, CFA®** is Co-Founder and Chief Investment Officer – Equity of Entasis Asset Management. C.J. has 17 years of experience in the investment industry. Prior to founding Entasis, C.J. worked at Cleary Gull, a multi-billion dollar investment advisory firm, as Director of Investment Research. He also served as a voting member of Cleary Gull's Investment Policy Committee, Investment Committee and Equity Strategy Group.

C.J. holds a B.B.A. in Finance from the University of Wisconsin-Milwaukee. He has earned the right to use the CFA designation. C.J. is a member of the CFA Institute and CFA Society of Milwaukee, where he currently serves on the Board of Directors.



**Mike Peters, CFA®** is Co-Founder and Chief Investment Officer – Fixed Income of Entasis Asset Management. Mike has 17 years of experience in the investment industry. Prior to founding Entasis, Mike worked at Cleary Gull, a multi-billion dollar investment advisory firm, as Fixed Income Portfolio Manager. In his role he served as a voting member of Cleary Gull's Fixed Income Strategy Group and Complement (Alternative) Strategy Group. Before Cleary Gull, Mike worked for several years at Madison Investment Advisors, a multi-billion dollar asset management firm, as a Fixed Income Analyst.

Mike holds a B.B.A. in Finance from the University of Wisconsin-Milwaukee. He has earned the right to use the CFA designation. Mike is a member of the CFA Institute and CFA Society of Milwaukee.

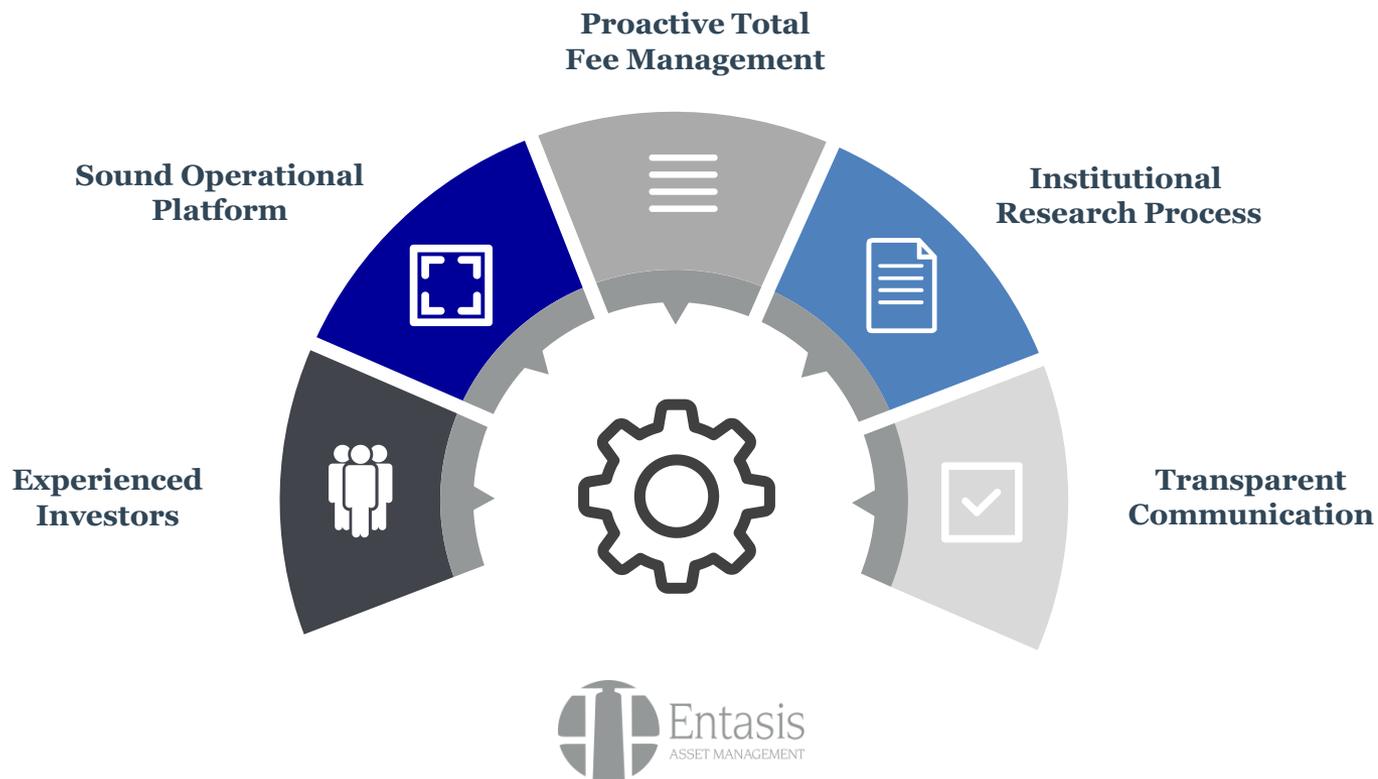


**David LaCroix** is a Senior Financial Advisor at Entasis Asset Management. David has more than 49 years of experience in the investment industry. Prior to joining Entasis, David worked at Cleary Gull Advisors, a Johnson Financial Group Company, and Cleary Gull Inc., a prior affiliate of Cleary Gull Advisors, where he most recently served as Vice President, Relationship Manager responsible for high net worth clients. Before Cleary Gull, David worked in a variety of portfolio management and client relationship management positions with A.G. Edwards and M&I Capital Markets Group.

David received his M.B.A. and B.B.A. in Finance from the University of Wisconsin-Madison. He has served as a member of the Archdiocese of Milwaukee Investment Committee, as a Trustee for the Village of Shorewood and as Director/Treasurer of Milwaukee Summerfest.

# The Entasis Difference

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# Disclosure

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The **Dow Jones Industrial Average**<sup>SM</sup> is a price weighted index that measures the performance of thirty component large-cap U.S. stocks. The **S&P 500**<sup>®</sup> **Index** is a market capitalization weighted index that measures the performance of 500 leading companies in leading industries of the U.S. economy. The **Russell 1000**<sup>®</sup> **Index** measures the performance of roughly 1,000 U.S. large-cap companies. The **Russell 1000**<sup>®</sup> **Growth Index** measures the performance of U.S. large-cap companies with higher price/book ratios and forecasted growth values. The **Russell 1000**<sup>®</sup> **Value Index** measures the performance of U.S. large-cap companies with lower price/book ratios and forecasted growth values. The **Russell 2000**<sup>®</sup> **Index** measures the performance of roughly 2,000 U.S. small-cap companies. The **MSCI EAFE**<sup>®</sup> **Index** is a market capitalization weighted index that is designed to measure the performance of developed markets, excluding the U.S. and Canada. The **MSCI Emerging Markets Index** is a market capitalization weighted index that is designed to measure equity market performance of emerging markets. The **MSCI ACWI Ex USA Small Cap Index** is a market capitalization weighted index that represents the performance of smaller capitalization companies in developed and emerging markets excluding the U.S. The **Barclays Aggregate Bond Index** tracks the performance of intermediate-term government bonds, investment grade corporate debt securities and mortgage-backed securities with at least one year to final maturity. The **Barclays Intermediate U.S. Gov/Credit Index** tracks the performance of intermediate U.S. government and corporate bonds. The **Barclays Municipal Bond Index** is considered representative of the broad market for investment grade, tax-exempt bonds with a maturity of at least one year. The **BoAML Fixed Rate Preferred Securities Index** tracks the performance of fixed rate U.S. dollar denominated preferred securities in the U.S. domestic market. The **BoAML Treasury Master Index** tracks the performance of the direct sovereign debt of the U.S. Government. The **BoAML U.S. Mortgage Back Securities Index** tracks the performance of U.S. dollar denominated fixed rate and hybrid residential mortgage pass-through securities publicly issued by U.S. agencies in the U.S. market. The **BoAML U.S. Corporate Master Index** tracks the performance of U.S. dollar denominated investment grade corporate debt publicly issued in the U.S. domestic market. The **BoAML High Yield Master II Index** is a broad based index consisting of all U.S. dollar-denominated high-yield bonds with a minimum outstanding of \$100 million and maturing over one year. The **BoAML All Convertibles All Qualities Index** measures convertible securities' performance of U.S. dollar denominated convertible securities not currently in bankruptcy with a total market value greater than \$50 million at issuance. The **BoAML Euro Broad Market Index** gives exposure to euro-denominated investment grade debt publicly issued in the Eurobond or euro member domestic markets including government, quasi-government, corporate, securitized and collateralized securities. The **BoAML Local Debt Markets Plus Index** is a broad composite designed to track the performance of local currency sovereign debt of emerging markets countries. Past performance is no guarantee of future results. All indices are unmanaged. Investors cannot invest directly in an index. Index returns do not include expenses.

### *Investment Terms*

**Valuation levels** are typically shown by calculating the price level of an index or a company relative to any number of characteristics of an index or company. For instance, the price-to-earnings valuation metric looks at the price of an index (or stock) divided by the total earnings of an index (or stock). Based on the multiple (in this instance, the multiple is how much investors are willing to pay – the price – for a given amount of earnings), it provides investors with a general sense of how expensive, or cheap, the overall market is at the present time. While there are a significant number of valuation metrics that are used in practice, and many ways to vary/modify the calculation of the price-to-earnings ratio, in this summary we are focused on the price investors are willing to pay (the level of the S&P 500<sup>®</sup> Index) divided by earnings expectations for the equity market (S&P 500 Index) over the next 12 months. This valuation metric is referred to as the forward P/E. A **yield curve** is a line that plots the interest rates, at a set point in time, of bonds having equal credit quality but differing maturity dates. The most frequently reported yield curve compares the three-month, two-year, five-year and 30-year U.S. Treasury debt. A **basis point** is a common unit of measure for interest rates and other percentages in finance. One basis point is equal to 1/100<sup>th</sup> of 1%, or 0.01% (0.0001). **Interest coverage** is a measure of a company's ability to meet its interest payments on its debt. **Federal funds rate** is the interest rate at which a depository institution lends funds maintained at the Federal Reserve to another depository institution overnight. It is one of the most influential interest rates in the U.S. economy, since it affects monetary and financial conditions, which in turn have a bearing on key aspects of the broad economy including employment, growth and inflation.

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To learn more please visit us at  
[www.EntasisAM.com](http://www.EntasisAM.com)

Entasis Asset Management  
300 N Corporate Drive  
Suite 220  
Brookfield, WI 53045  
262-754-5299  
[Info@EntasisAM.com](mailto:Info@EntasisAM.com)

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