



# SilverOak

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WEALTH MANAGEMENT LLC

**Third Quarter 2021 Market Summary**

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## Third Quarter 2021 Market Summary

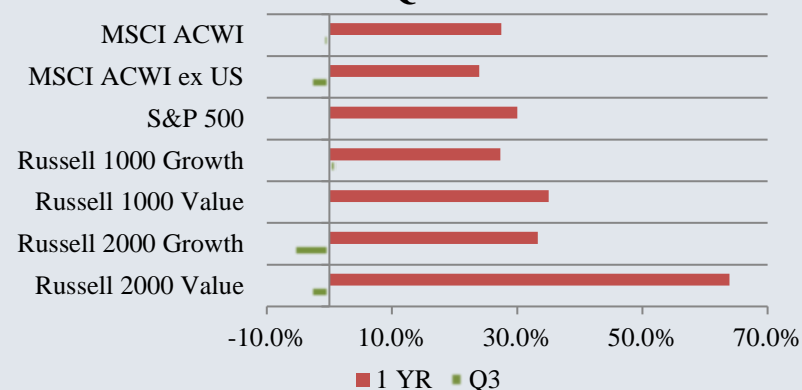
Throughout life, we experience many transitions. Some of these transitions can be very exciting, such as marriage or the birth of a child, while other transitions can be more difficult, such as divorce or the passing of a loved one. Many of us are currently experiencing a major transition in life as we continue to adjust to a world that has been interrupted by a pandemic. The economy and markets have certainly not been immune to this interruption, and are experiencing their own transition into a new post-pandemic world. Although the economy continues to recover, growth is naturally shifting to a lower gear. In this phase of the transition, “post-initial rebound”, it is normal for the weekly economic data to exhibit mixed signals rather than being one-directional. Even though mixed data is common, we all know the current economic cycle has not been normal due to economic shutdowns and record stimulus that led to a condensed decline and rebound. The economy has been and will continue to be dictated largely by personal health and safety – both individual decisions and larger policy changes. We see this born out with distorted labor markets and an inconsistent demand for goods and services, which are causing issues in the supply chain from factories, to shipping and ports, and trucking as well.

Other transitions that are affecting markets include monetary policy that will begin tapering asset purchases, fiscal policies from the new administration, and labor markets that are adjusting to priority shifts. On a personal level, many are going through some transitions as well – a hybrid work environment, back to school, potentially resuming traveling and other social activities. While some people have transitioned back to pre-2020 ways of life, others are adapting to a “new normal”. These factors are impacting economic data and influencing the expectations of market participants, which can seem to be a moving target.

The transition from recovery to the unknown path ahead allows for greater focus on ancillary topics such as the debt ceiling, fiscal stimulus, tax policy, inflation, growth concerns, tail risks, etc. New reports on inflation data are an example of how perceptions of reality can change. Initially forecasted as “transitory”, inflation may be sustained longer than expected due to labor imbalances that are in part causing supply chain issues and higher wages. The supply chain was expected to revert to pre-pandemic efficiency; however, as we are finding out in all parts of life, a return to “normalcy” is not as easy as expected. The pandemic has been a wrench thrown into society’s gears and many people and businesses have decided to rebuild differently than before.

Equities were largely flat-to-negative during the quarter. U.S. large company stocks, represented by the S&P 500 Index, were up 0.6% during the quarter. U.S. small company stocks, represented by the Russell 2000 Index, were down 4.4% during the quarter. The S&P 500 had not endured a 5% correction for the entire year until the last day of September finally tipped the index over the negative 5% threshold. However, there have been plenty of transitions underneath the surface, as over 90% of U.S. equities have had a correction of greater than 10%. Many growth and small cap equities have been down 30% at one point this year. Nonetheless, corporate earnings have been exceptionally strong this year due to revenue growth and margin expansion.

### Broad Market Index Returns Third Quarter 2021



International stocks, represented by the MSCI ACWI ex US Index, were down 3.0% during the quarter. Emerging market equities were down meaningfully, led by China, which is going through its own transitions. Recent regulatory policies instituted by government leaders are aimed at promoting affordability and social stability. China is also moving away from construction of property and infrastructure and towards strengthening its domestic economy in segments such as health care, technology and consumption. These changes have caused market volatility and have, in-part, slowed economic growth.

## Third Quarter 2021 Market Summary (continued)

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The Bloomberg Barclays U.S. Aggregate Bond Index, which represents a broad basket of bonds, was up 0.1% during the quarter. Interest rates declined slightly at the beginning of the quarter, but rallied late and ended the quarter slightly higher. Credit spreads have tightened to historical lows; however, history has shown they can persist at low levels for an extended period of time as long as the economy continues to expand.

The Federal Reserve is expected to announce a plan to taper its balance sheet by year end. The transition in reducing its purchases may cause mild short-term volatility as we saw in 2013, the last time the Fed began the process of shifting away from stimulus. Other central banks around the world are also slightly tightening monetary policy. These actions likely mean interest rates will slowly go higher over the next few years.

As these transitions play out over the coming quarters, it would not be surprising to see greater volatility than we have seen year-to-date. Potential unknowns should be kept in perspective and not steer investors away from the process of promoting their long-term plans. The low interest rate and low inflation environment of the past 5-10 years, coupled with recent stimulus, has helped put many households in a favorable position. Financial asset price inflation has led to strong equity returns and real estate appreciation. Along with reduced debt, many households' balance sheets have been strengthened. Those in that situation may be able to take on less risk to meet their goals, as they are closer to reaching them.

Life transitions can often take us to unexpected places. Not every exciting possibility manifests as we hope it will, and perceived setbacks can sometimes be opportunities in disguise. The economy and the markets are no different. With so many competing forces, correctly predicting the outcome of the current economic and market transitions is improbable. Hence, it is important to maintain a diversified investment strategy in order to take advantage of whatever comes to be. Maintaining a sound financial plan and a calm, measured approach through economic and market transitions will allow for more options and flexibility in reaching long-term goals.

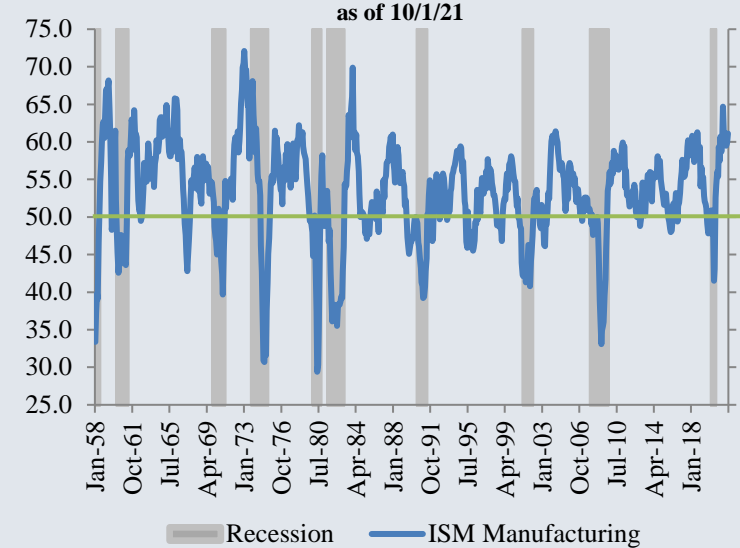
## MACROECONOMICS

- The Bureau of Economic Analysis released the advanced estimate of third quarter 2021 real GDP, an annual rate increase of 2.0% from the preceding quarter. This deceleration of lower GDP growth, from 6.7% in the second quarter, was caused by both weaker personal consumption expenditures and final sales of domestic product.
- GDP is expected to be about 5.5% in 2021 for the full year, which is lower than previously expected. Many economists are expecting 2022 GDP to remain above recent historical trend at around 4%.
- The ISM Manufacturing Index remained elevated during the quarter, finishing at 61.1 versus 60.6 in June. Typically, when the ISM Index is above 55 it is bullish and when it is below 45 it is bearish. The ISM Non-Manufacturing Index was also strong during the quarter and finished at 61.9 in September.
- In September, the Conference Board Leading Economic Index increased 0.2% month-over-month to 117.5. The index, which is a composite of leading employment, housing, manufacturing, and market indicators, continues to increase over the past year.
- The price of WTI Crude Oil was \$75.22 at the end of September, which is 2.3% higher than \$73.52 at the end of June. The price of Brent Crude Oil ended the quarter at \$77.81, which is 1.1% higher than at the end of June. Supply of oil has been constrained, while demand for oil has rebounded in the past year. Natural gas prices have risen considerably as well.
- Inflation has increased over the past year. In September, headline CPI increased 5.4% year-over-year. Core CPI, which does not include food and energy, had a 4.0% increase. Used and new vehicles, airline fares, and energy prices have seen the highest increase in prices over the past year. Wages, rents and input costs have risen as well.

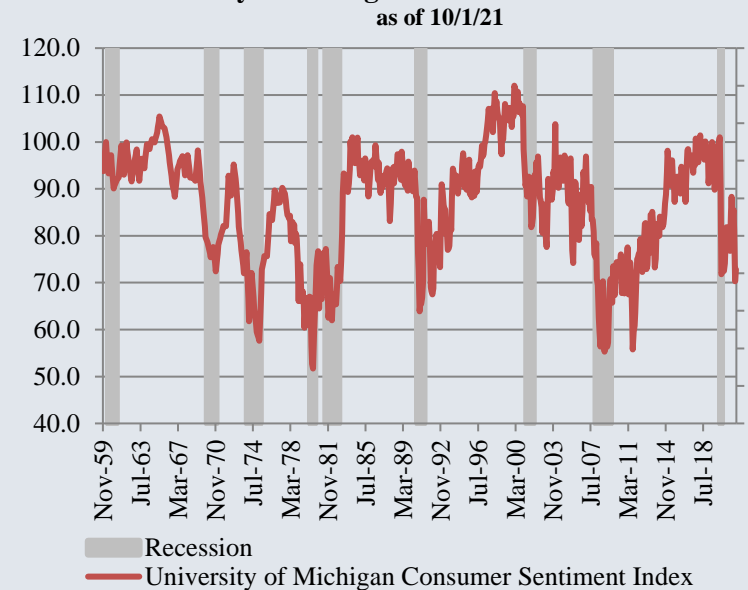
## CONFIDENCE METRICS

- Consumer confidence has moderated over the past few months as fiscal stimulus declined, inflation increased and the delta variant raised concerns of economic growth.
- The University of Michigan Consumer Sentiment Index final reading for September was 72.8, which is lower than 85.5 in June.
- The Conference Board's Consumer Confidence Index September reading was 109.3, down from 128.9 in June.

### ISM Manufacturing Index



### University of Michigan Consumer Sentiment Index

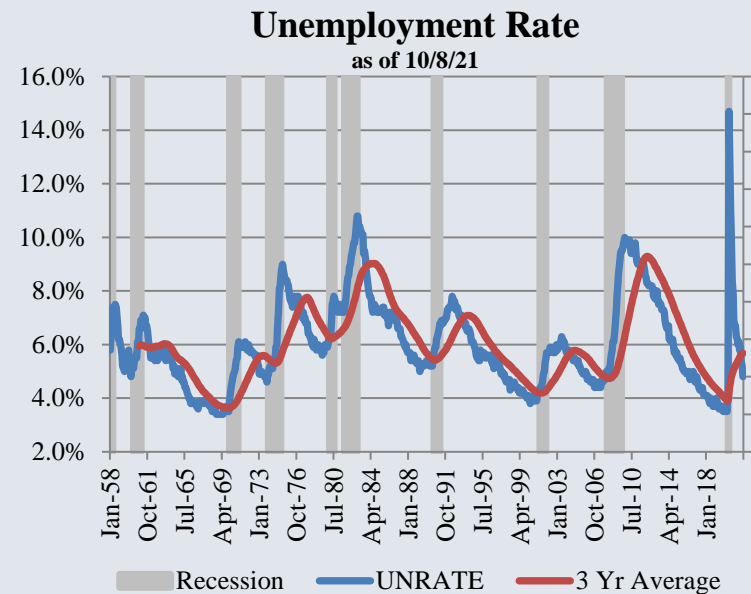
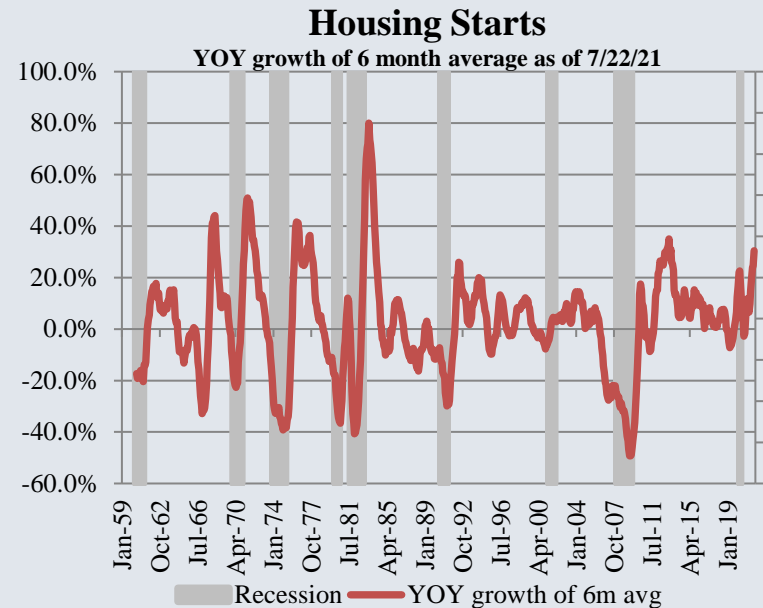


## HOUSING

- The housing sector has been very strong over the past year with pent-up demand fueled by low interest rates and low inventory levels. Low mortgage rates should continue to support the sector. However, home sale prices have soared, as have input costs, which will be a headwind for the housing sector going forward.
- Preliminary existing home sales increased in the quarter, with a monthly average annualized rate of 6.06 million units, up from 5.83 million units in the second quarter. Unsold home supply remains at historic low levels.
- The preliminary existing home sale prices for the quarter were 17.5% higher than the levels of one year ago. Prices have accelerated higher this year as demand has greatly outstripped the constrained supply.
- New home sales were down during the quarter on a year-over-year basis. However, median new home prices were significantly higher during the quarter on a year-over-year basis.
- S&P Case-Shiller 20-City Home Price Index (seasonally adjusted) showed home prices rose over 19.7% year-over-year in August. Of the locations in the Index, home prices in many major cities in western states have risen the most over the past five years, while many major cities in eastern states have seen weaker growth. Housing trends will continue to shift as workforces become more mobile and millennials start buying homes.
- Housing starts continued to be strong to meet high demand. However, permits, which are a leading indicator, have declined from very high levels in the first quarter. Higher input costs, higher home prices and a lack of labor may impact demand short-term.

## EMPLOYMENT

- The labor market has seen mixed data but generally the trend has been positive. There is currently a mismatch of high labor demand and weaker labor supply.
- During the quarter, nonfarm payrolls averaged 550,000 jobs added per month. JOLTS Job Openings have risen considerably as employers are having trouble filling positions.
- The unemployment rate decreased during the quarter to 4.8% in September from 5.9% in June. Initial Jobless Claims have now declined to March 2020 levels. However, the labor participation rate is currently 61.6% in September, down from 63.4% in January 2002, indicating many people have left the job market.

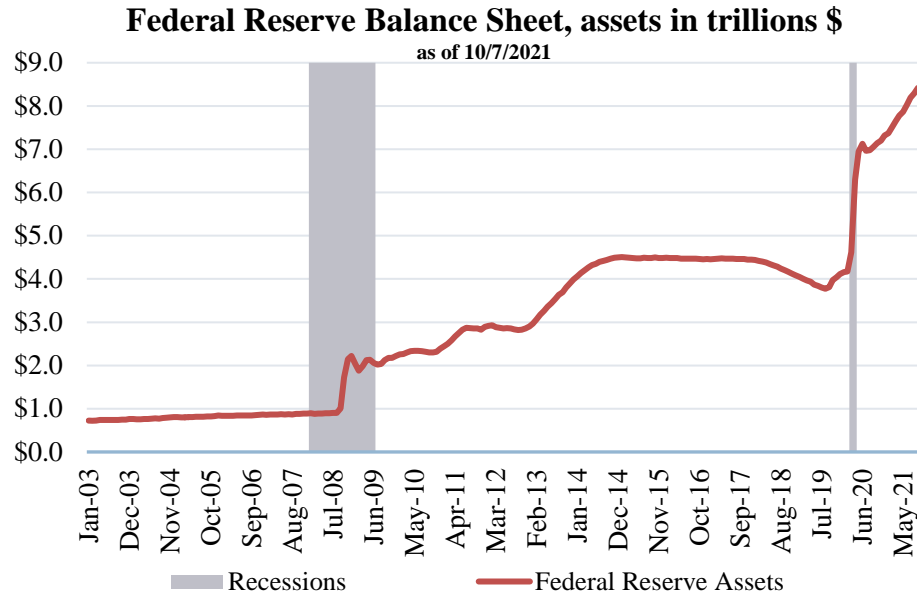


## FED POLICY

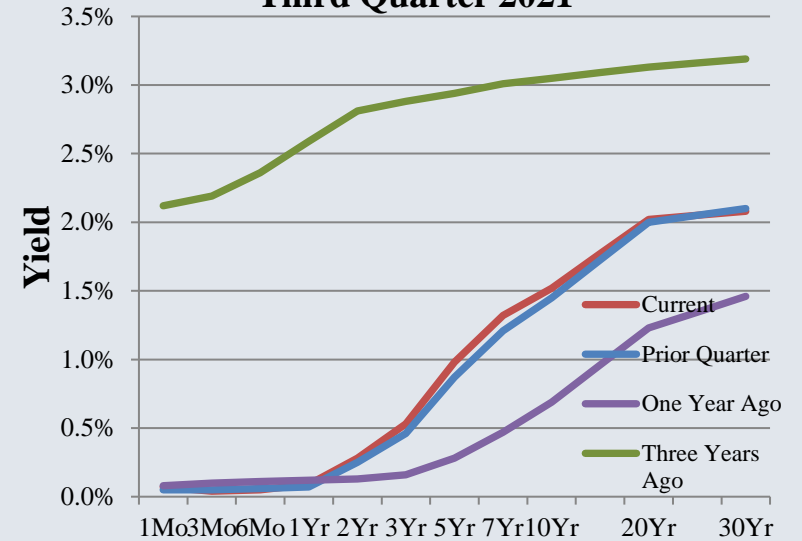
- The Federal Open Market Committee (FOMC) kept the federal funds rate at a target range of 0.00% - 0.25% in September. The Fed indicated they will likely commence tapering asset purchases before the end of the year but did not announce a specific plan.
- Based on the Fed's comments, the FOMC may start hiking rates in late 2022 or early 2023. However, as always, Fed policy is dependent on economic and labor data.
- Federal Reserve Chairman Jerome Powell's four-year term ends in February and thus there could be changes amongst members of the FOMC.

## FIXED INCOME

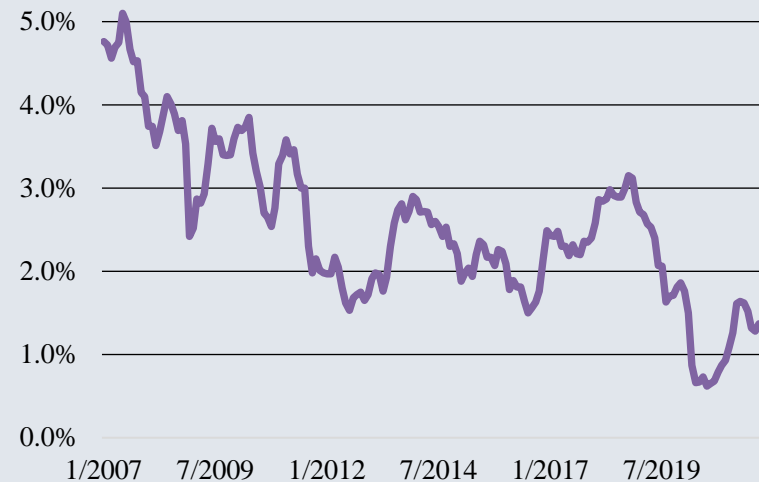
- Yields across the U.S. Treasury curve were essentially unchanged during the quarter but intermediate and long-term rates have been trending higher over the past year.
- Short-term interest rates are controlled or heavily influenced by central banks, whereas long term interest rates are controlled by market forces and economic growth.



## U.S. Treasuries Yield Curve Third Quarter 2021



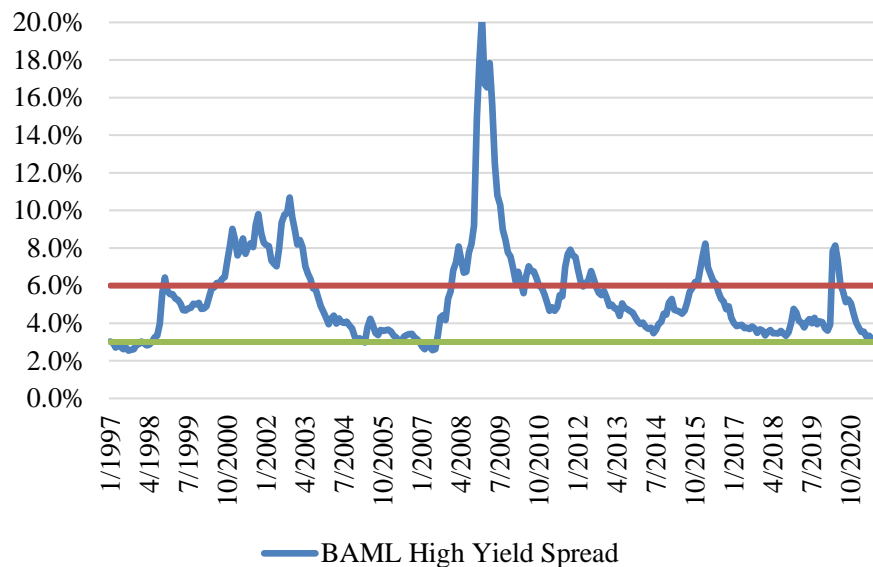
## 10-Year Treasury Yield as of 10/1/2021



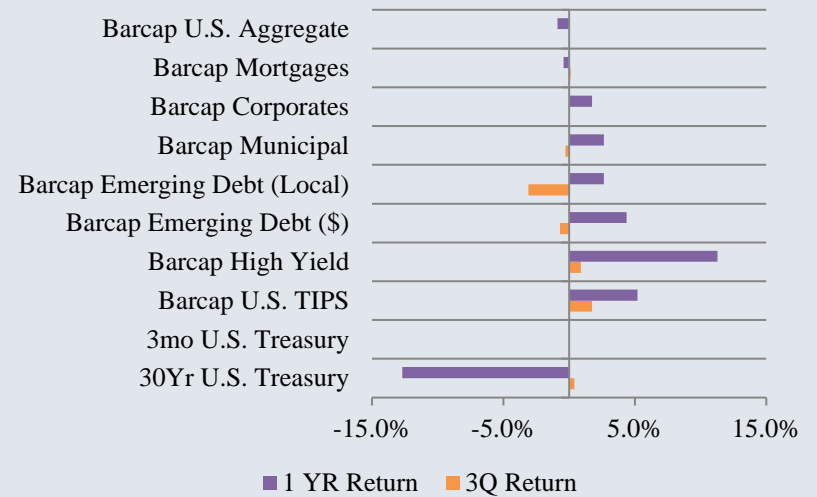
## FIXED INCOME (continued)

- During the quarter, the Bloomberg Barclays U.S. Aggregate was up 0.05%. U.S. high yield and U.S. TIPS had the strongest returns, while emerging market debt saw negative returns as the U.S. dollar appreciated relative to many other currencies.
- Municipals had negative returns during the quarter, as tax-exempt yields rose.
- Securitized sectors appear more favorable than many sectors as they currently exhibit better valuations and fundamentals. They currently offer a yield advantage with lower interest rate risk.
- Demand for credit remains strong which has supported rich valuations in most sectors.
- Credit spreads are near their historic lows, indicating that a lot of the positive economic growth and earnings are baked in and there is not a lot of room to tighten further. Thus, returns in many fixed income sectors could be lower over the next year relative to last year's returns.

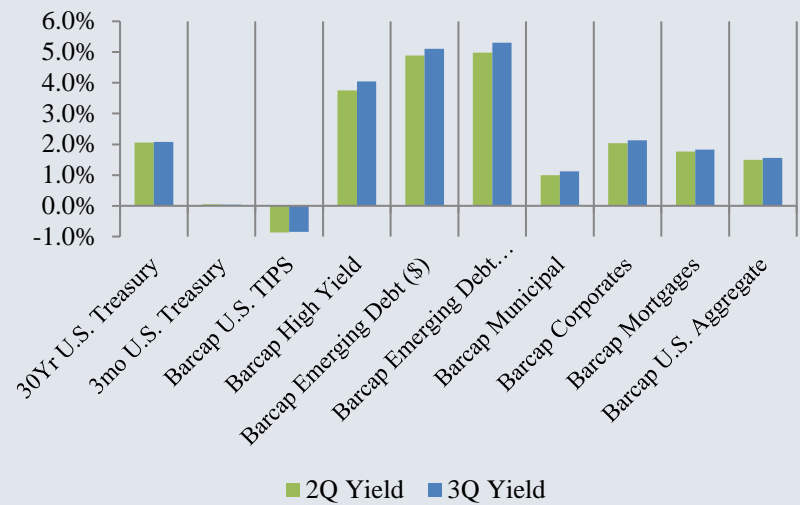
### Credit Spreads - High Yield as of 10/1/2021



### Fixed Income Returns Third Quarter 2021



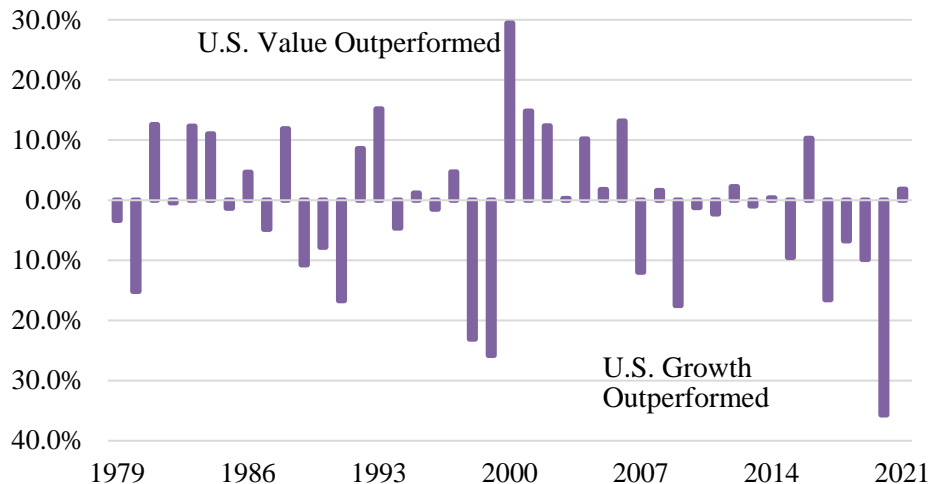
### Fixed Income Yields Third Quarter 2021



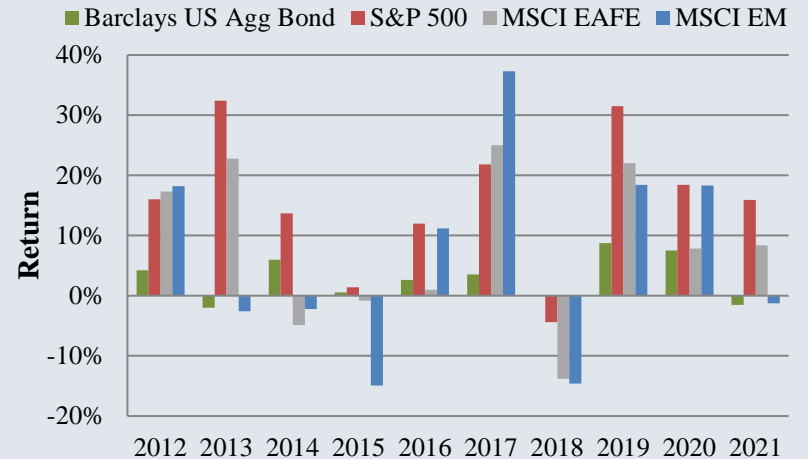
## MARKET COMMENTARY

- Equity markets started the quarter strong but sold off in September. However, the S&P 500 had positive returns for the sixth quarter in a row.
- There are many positives that are supporting the markets, including more fiscal stimulus coming, accommodative monetary policy, healthy consumer balance sheets and resilient consumer and business spending.
- Global supply chains are still disrupted, which has caused an increase in prices in certain parts of the economy such as autos and commodities.
- Health care continues to influence global economic and social policies.
- Commodities had the strongest returns this quarter amongst asset classes.

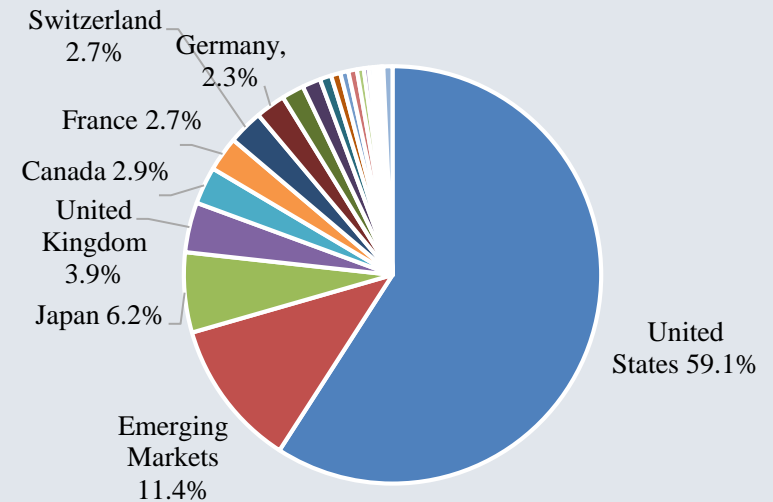
### U.S. Value vs. Growth Relative Equity Performance (as of 9/30/21)



### Equity & Fixed Income Market Annual Returns (as of 9/30/2021)



### Country Weighting in MSCI ACWI (as of 9/30/2021)



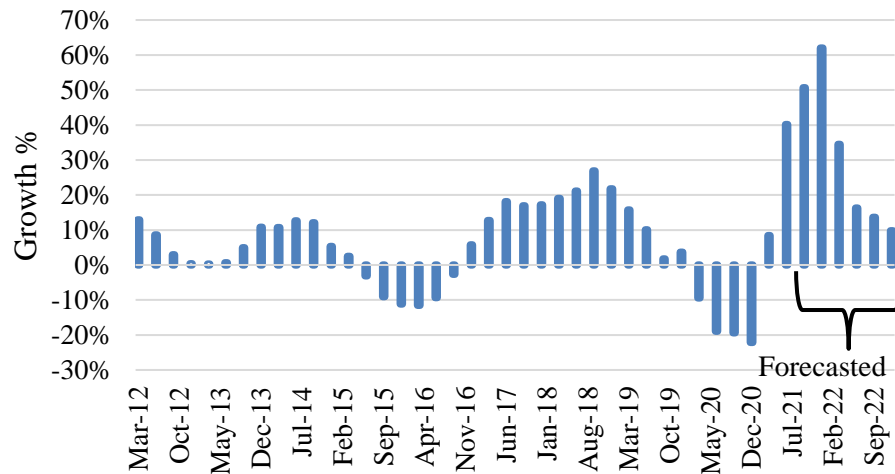


## DOMESTIC EQUITIES

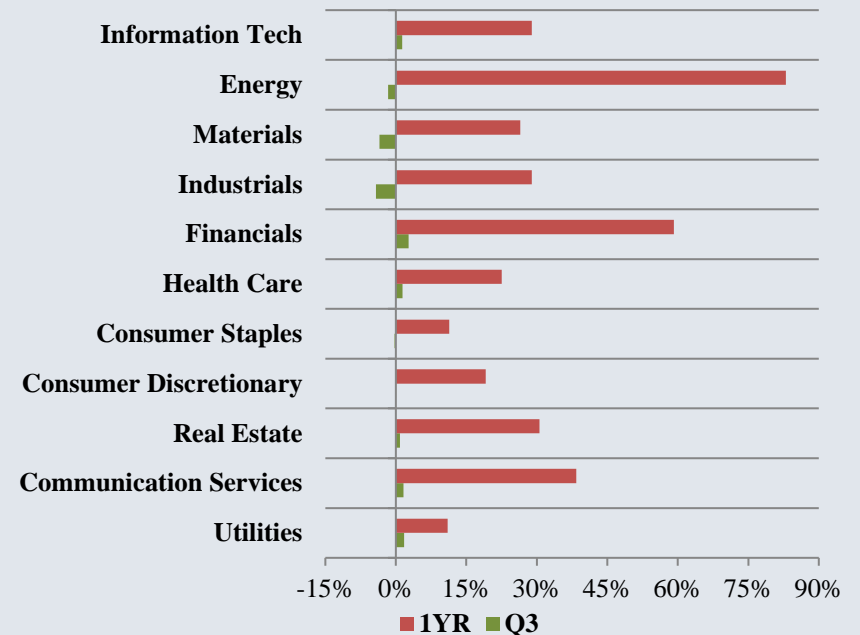
- The Russell 1000 Index, comprised of large and mid-capitalization stocks, posted a total return of 0.2% during the third quarter. This was the sixth quarter in a row with positive gains. On a year-over-year basis, the Russell 1000 Index has increased 31.0%.
- Small capitalization stocks, as represented by the Russell 2000 Index, decreased 4.4% during the third quarter. On a year-over-year basis, the index has increased 47.7%. Historically, small caps have led coming out of recessions.
- Corporate earnings are having an exceptionally strong year. Growth is expected to continue into 2022, but at a slower pace.
- During the quarter, Financials and Utilities outperformed, while Industrials and Materials lagged. Sector rotation will likely continue as global economic conditions shift.

Third Quarter 2021 Returns			
	Value	Core	Growth
<b>Mega Cap</b>		1.91%	
<b>Large Cap</b>	-0.78%	0.21%	1.16%
<b>Mid Cap</b>	-1.01%	-0.93%	-0.76%
<b>Small Cap</b>	-2.98%	-4.36%	-5.65%
<b>Micro Cap</b>	-1.82%	-4.98%	-9.09%

**S&P 500 Earnings Growth**  
Trailing 12-Month Operating Earnings Growth YOY  
(as of 10/7/2021)



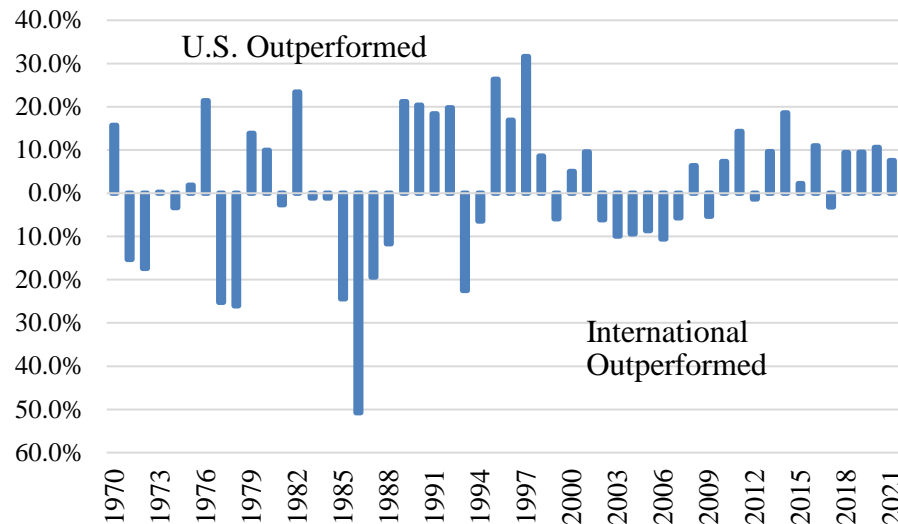
**U.S. Equity Market Returns by Major Sector**  
(Securities in S&P 500, Third Quarter 2021)



## INTERNATIONAL EQUITIES

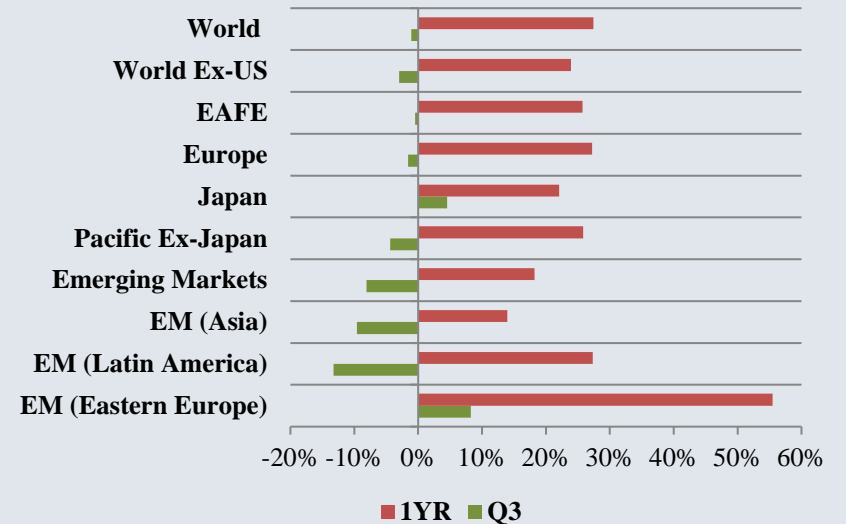
- Developed international stocks, as represented by the MSCI EAFE, were down 0.5% during the quarter. On a year-over-year basis, the EAFE is up 25.7%, lagging the performance of U.S. domestic equities.
- Emerging market stocks underperformed developed markets during the third quarter as the MSCI Emerging Markets Index was down 8.1%. On a year-over-year basis, emerging market stocks are trailing developed markets with a return of 18.2%.
- China's regulatory policy changes have caused volatility as the government focuses on social stability and national security. The MSCI China Index was down 18.2% during the quarter, as a result.
- Japanese equities rebounded after underperforming in the second quarter. In the past few months, Japan has accelerated its COVID-19 vaccinations program, which helped improve sentiment.
- The past few years have seen the rise of populism and de-globalization pressures. Going forward, global asset diversification may provide more benefit than it has over the previous decade.

### U.S. vs. International Equity Performance (as of 9/30/21)

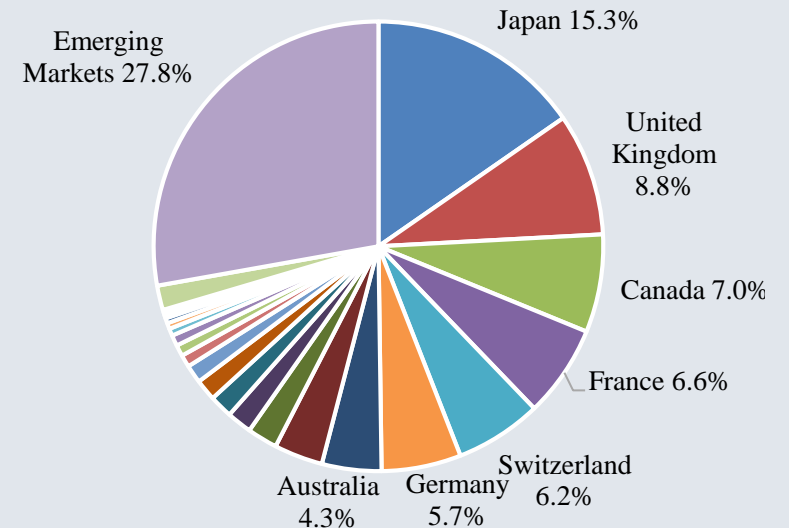


S&P 500 TR vs. MSCI EAFE NR

### Non-U.S. Equity Market Returns Third Quarter 2021



### Country Weighting in MSCI ACWI ex US (as of 9/30/2021)



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