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OBERMEYER WOOD **NEWS**

FALL 2021

MARKETPOINT

FOCUSED ON THE LONG RUN

Broad market indices are up in the low double digits for the first nine months of the year. September's market declines were an anomaly in what has otherwise been an incredibly bullish 2021. Shifting into the last quarter of the year, we see several potential catalysts on the horizon. First, we are watching the Fed walk a thin line as it seeks to normalize a still-recovering American economy that is showing signs of inflation as it reboots. Second, we are processing moves from Congress, where Democratic leadership juggles its goal of spending on traditional and human capital infrastructure while preventing a default on U.S. debt if the debt ceiling is not increased. Finally, we are monitoring China's fiscal stability and the global economic effects of COVID-19 variants. Near-term catalysts will likely create market volatility, yet the focus for investors remains on the long run. By understanding and processing these events, we gain confidence to stay steady by owning high-quality investments, while being nimble if emotions and headlines create mispriced opportunities.

As investors, we appreciate the role that liquidity plays in market returns and watch the Fed closely. The Fed has signaled it will begin tightening at the end of this year by reducing its buying in the open markets. By the end of 2022, Fed governors expect one interest-rate increase, moving up the timeline they previously communicated. Chairman Powell has been more hawkish in recent weeks, stating that the Fed is "turning to the process of normalization" at September's ECB Forum on Central Banking. Yet in the same forum, Powell restated dovish themes, including reinforcing his view that inflation is transitory and the Fed is still some way from raising rates.

The central bank is in a tough position. Supply chain constraints are causing prices to rise as companies struggle to meet elevated consumer demand. Bottlenecks did not resolve by the third quarter, as most investors and the Fed thought they would, and some indications suggest they are worsening. For example, 64 cargo freighters are now anchored off the coast of California waiting to unload.[1] While many factors have contributed to the strain, a sudden spike in demand is the primary driver. Volume at the Port of Los Angeles, the busiest port in the country, is up 30.3% so far this year.[2] As consumers spend more time at home, they have shifted spending from services toward goods. The pace of change required to retool supply chains cannot keep up with the pace of change in consumer preferences.

The Fed's toolkit is designed to stimulate demand and has no direct control over supply. If consumers are unwilling to spend, the Fed will engage in open market operations and decrease interest rates. This action makes it easier for consumers to borrow money and gives them confidence and encouragement to make purchases. Conversely, the Fed will increase rates and make capital scarce when the economy risks overheating. Yet no one is debating the current level of demand. After last year's decline in economic activity, the most severe pullback in a century, consumer spending should be above average. The difference today is that the demand is centered around goods rather than services. In the pre-Covid era, consumers would have spread out their spending between items, like new cars and televisions, and services, like concert tickets and gym memberships.

For a continued recovery, the U.S. will need to either resolve the supply chain bottlenecks or consumers will ›

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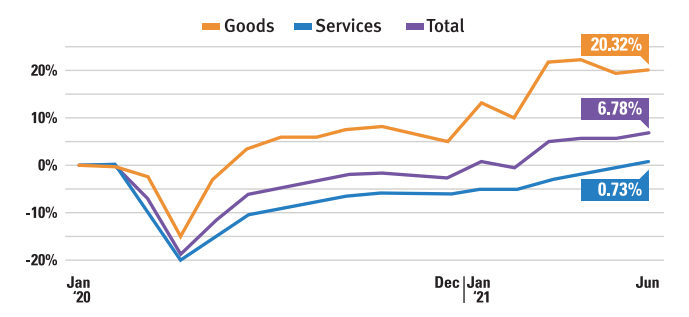
U.S. Spending on Goods Outpaces Services

Change in personal consumption expenditures on goods and services in the U.S. since January 2020*



Source: U.S. Bureau of Economic Analysis
*Underlying monthly spending data is seasonally adjusted at annual rates.

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have to shift their spending back to services. We consider this unlikely with an only partially vaccinated nation that remains wary of eating at restaurants, getting haircuts, and visiting family and friends with the prevalence of the Delta variant.[4] Covid-19 fears also affect the labor side of the equation since workers are uneasy providing these services. "It is frustrating to acknowledge that getting people vaccinated and getting Delta under control 18 months later still remains the most important economic policy that we have," Powell says. "It is supply side constraints that are really holding back the economy at this point." Effectively, there is little the Fed can do to improve the economic environment as supply chains are under stress and consumer spending is focused on goods.

Shifting to fiscal policy, the long-awaited infrastructure bill, key to President Biden's agenda, could help with future economic growth. There are many long-term advantages of an affordable, sustained spending program to the economy. Spending on infrastructure is gradual and often takes years to realize the benefit of an investment. For example, improving an airport today may lead to higher air traffic in the future, resulting in an economic boost to the communities it serves. Upgrading a power grid prevents disruptions like the one Texas experienced during winter storm Uri, which supports growth in a different way. The U.S. economy will benefit from thoughtful investment in our nation's infrastructure.

Yet Congress is at an impasse. The Democratic majority is operating with self-defeating factions. Legislators carved out spending on hard infrastructure to increase the likelihood of passage, hoping that Republicans would offer their support. The $1 trillion bipartisan legislation earmarks dollars for investment in roads, bridges, rail, power grids, and broadband internet. The bill would be paid for with offsets from unspent coronavirus relief funds, Medicare rebates, and increased revenues from cryptocurrency regulation. As of this writing, there still has not been a vote on the proposed legislation.

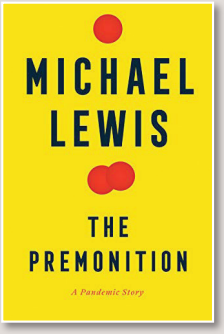
The $3.5 trillion human capital infrastructure legislation faces more headwinds to passing. This package focuses on four key areas: 1) spending on childcare and tuition for families, 2) increasing healthcare benefits for seniors and other Americans, 3) investment in public and sustainable housing, Veteran's Administration facilities, and job training projects, and 4) funding to support clean energy, manufacturing for green projects, and transforming the federal fleet into electric vehicles.[5] Republicans and moderate Democrats object to the plan's scope, saying it is too expensive and would put our nation's financial footing at risk. In addition, even with a recent short-term agreement, the U.S. is still only months away from hitting the debt ceiling, a self-imposed cap on how much the U.S. government can borrow to pay off its existing legal obligations. Without resolution on the debt ceiling, the infrastructure legislation in its proposed form is unlikely to move forward.

Investors are looking for clarity, both from the Fed and from Congress. Mixed economic data mean less insight into how quickly the Fed will normalize, and this gives investors lower confidence in the current forecast of interest rates. If inflation persists, the Fed will have no choice but to tighten monetary policy even if the broader economy is not ready for it. Meanwhile, inaction from Congress on the infrastructure bill and resolution of the debt ceiling cause uncertainty and angst in the financial markets. Percolating under the surface are unexpected catalysts, such as whether China's debt issues will worsen and whether new Covid-19 variants will hamper growth.

We are in a period of transition where the near-term outcome is not clear. Despite challenges, the U.S. is on much stronger footing than it was a year ago. Consumer excess saving remains at $2.2 trillion, substantially higher than long-term averages. Employment has strengthened, and capital spending is elevated. The most important thing investors can do is to continue to own companies that are competitive in a technology-driven economy, have access to large and growing markets, can invest even if capital becomes scarce, and are led by adaptable management teams. Investors will get clarity in the months ahead; until then, stay steady and focused on the long run.

[1] https://www.wsj.com/articles/california-ports-24-hour-operation-is-going-unused-11633018532
[2] https://www.reuters.com/world/us/record-60-cargo-ships-wait-unload-busiest-us-port-complex-2021-09-15/
[3] https://www.statista.com/chart/23574/consumer-spending-on-goods-and-services/
[4] https://evercoreisi.mediasterling.com/document/1621195D-71C6-47D4-8B44-D8B3EDC4B428
[5] https://www.usbank.com/investing/financial-perspectives/market-news/how-infrastructure-investment-may-affect-the-economy.html

RECOMMENDED READING: *The Premonition*, by Michael Lewis



In his latest work, *The Premonition*, Michael Lewis examines the political, institutional, and scientific conditions of the last 20-odd years that led to the U.S. government's feeble response to the COVID-19 pandemic. The author's penchant for using individuals and their experiences to explain complex events is on full display in this book, as is his style of fast-paced storytelling seen in his earlier publications *The Blind Side*, *Liar's Poker*, and *The Big Short*, among others.

Lewis begins the book by taking readers back to 2005, when then-President George W. Bush ordered the Department of Homeland Security to formulate a federal pandemic response plan. Bush read a chronicle of the 1918 Spanish flu outbreak and saw a need for a modern-day government playbook for containing an outbreak in the absence of an existing vaccine. It wasn't until 2009 and the occurrence of the H1N1 pandemic that the government had a chance to implement the plan. In hindsight, the government's response was mixed. The Centers for Disease Control and Obama administration ignored recommendations and actions central to the pandemic reaction plan while benefiting from the fact that the flu strain was less lethal than initially believed. The reader comes to realize that the weak federal response to H1N1 is what Lewis alludes to in the book's title: the lack of decisive action by a federal public health agency should have served as a warning that the government was not ready to confront a more dangerous outbreak.

After setting the scene, Lewis transports readers into a world coming to terms with the COVID-19 outbreak and the resulting pandemic. In classic Lewis style, he follows a group of ragtag public health experts working as a team to lobby the federal government into taking aggressive measures to stop the spread in the early months of the pandemic. The group, dubbed "the Wolverines," works tirelessly to reach the decision-makers in federal agencies and the Trump administration, albeit to no avail.

The personal stories of the members of the Wolverines, combined with the big-picture lessons that we hope policymakers will learn from the COVID-19 pandemic, make this a timely and interesting read. In particular, we think the one takeaway most vital to the wellbeing of future generations of our country is that we need public leadership that is proactive about solving problems on the horizon, in addition to dealing with the problems of today. Please let us know if you are interested in *The Premonition*, and we can send you an audiobook or physical copy.

FIRM UPDATE: OBERMEYER WOOD RECOGNIZED

BARRON'S | Forbes | DENVER BUSINESS JOURNAL

We are delighted and humbled to share that our team was recognized in three industry rankings in September.

Wally Obermeyer, representing our firm, was ranked No. 49 in the nation and No. 1 in Colorado in *Barron's* annual ranking of Top 100 Independent Wealth Advisors. Obermeyer rose 13 places from his 2020 ranking. This is his sixth straight year appearing on this prestigious list, which considers both quantitative and qualitative factors in determining who appears in the Top 100.

Later in the month, Dana Nightingale was named to the *Forbes* and SHOOK Research list of Top Next-Generation Advisors for the fifth consecutive year. This year, Dana was chosen out of nearly 3,000 nominees and ranked No. 86 in the country and No. 1 in Colorado. We are especially proud of this recognition because it demonstrates our keen focus on working with Gen Xers, Millennials, and multigenerational families who seek the benefit of including their adult children in their financial lives and wealth planning.

Our Team

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President and Co-Founder

Ali Flynn Phillips
Executive Vice President

Lee (Skip) W. Dines, Jr.
Senior Vice President

George F. Wood, CFA
Co-Founder (Emeritus)

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Bret Hirsh
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Nick Barnes, CFA
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Senior Associate, Client Services and Compliance

Jody Dible
Associate, Client Services and Technology

Brooke Gais
Associate, Client Services

Luke Jones
Associate, Client Advisory

Naomi Seldin
Associate, Client Services and Communications

Efrata Kirose
Assistant, Client Services and Marketing

Finally, our firm was recognized by *The Denver Business Journal* as one of the Top Denver-Area Wealth Management Firms.

We are incredibly proud of our team and believe these accomplishments reflect the collective efforts of everyone at Obermeyer Wood. We also know that none of this would be possible without our clients' partnership and support. More details on these recognitions are available under the News section of our website.

YEAR-END REMINDERS: RMDS AND GIFTING

As we approach the final months of 2021, we would like to provide you with a few year-end reminders related to required minimum distributions (RMDs) and gifting.

As many of you know, 2020 was a year of changes for RMDs. The SECURE Act raised the minimum age for RMDs from 70 1/2 to 72, and the CARES Act waived RMDs for 2020. There is no RMD waiver this year, so anyone age 73 or older as of December 31, 2021, must take their annual RMD by the end of this year to avoid penalties. Individuals who turn 72 in 2021 must take their first RMD by April 1, 2022, and their second RMD by December 31, 2022. For these 72-year-olds to avoid having both amounts included in their income for 2022, they may want to consider taking their first RMD by December 31, 2021, instead of waiting until April 1, 2022. We will be reaching out to clients in the coming two months to coordinate distributions. If you have any questions in the meantime, please get in touch with our team.

The holiday season and end of the year are popular times for many clients to consider charitable or family gifting. Those interested in giving to a charity can satisfy all or part of their RMD with a charitable gift using a qualified charitable distribution (QCD). If you are considering gifting cash or securities, either to charity or to a family member, and would like our help in strategizing or coordinating such gifts, please let us know. Keep in mind that many custodians have mid-December transaction deadlines for various gifting practices, so we urge you to coordinate with your tax professional and plan ahead.

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