INVESTMENT
UPDATE

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December 2021

2021: A MARKET FOR THE AGES

With Thanksgiving behind us and the holiday season in full swing, this is the extended time of year where we count our blessings and ponder what the upcoming New Year has in store for us. After a period of volatility and disruption due to Covid in 2020, you are likely feeling more financially secure this year given the market's runup virtually out of the gates and without interruption during 2021. As of November 29, the Dow is above 35,000, up 14% from year end.

While we are all grateful for a market that has surpassed even our wildest expectations amidst a pandemic, I know based on conversations with many of you we are all wondering the same thing: How long can it last?

No one has a crystal ball of course but experience serves as our guide. Having been an investment professional during the dot com blowup of 2000-2002 and the burst of the housing bubble and the resulting Great Recession in 2008, I, like many of you that were our clients during those years, have a wealth of perspective. This market has one main parallel to the run up in stock prices before those declines: fundamentals, or price valuations, didn't seem to matter and stocks soared to nosebleed levels. Until they didn't...

Ponder this, thanks to Andy Kessler of *The Wall Street Journal:*

Airbnb is worth more than **Marriott** and **Hilton** combined.

Coinbase, the crypto-currency exchange is worth more than the **NASDAQ.**

Joby Aviation, planning an air taxi service starting in 2024, is worth more than **Lufthansa, EasyJet** or **JetBlue.**

Beyond Meat, whose patties are made with pea protein, is worth more than the entire market for peas eaten globally.

Tesla, which recently reached a $1 trillion market cap (to put that in perspective—that's 1,000,000 million), is larger than the next nine largest auto companies *combined.*

New Sheriff in town? **Rivian,** the EV truck maker, is now the largest company by market value with *no revenue,* larger than Mercedes Benz maker **Daimler, GM** or **Ford.**

In case you were wondering, Mr. Kessler's article is aptly titled "The Stock Market Fails a Breathalyzer."

Sure, these are great and innovative companies and deserve respect. But as I've learned, sometimes painfully, great companies aren't by definition great investments, particularly when their prices are disconnected from reality.

So when will fundamentals matter yet again? There are no set rules on timing. Also, as I've learned from experience, the market can be irrational long after I, or Andy Kessler, for that matter think it is irrational. He wrote that piece three months ago on September 12, 2021.

The good news is that the market is somewhat bifurcated. While as a whole the market is not cheap, we continue to focus on stocks that pay good dividends and represent attractive values. True, they have not been fully appreciated in this market, but they offer real cash flow and should maintain their value when this market cycle inevitably ends, and fundamentals again rule the day.

As we embark upon our 60th year in business, let me reiterate that we manage risk not return, and we welcome a conversation with you about your own portfolio or just to share good cheer. Best to you and your families this Holiday Season and the coming New Year!

Joe Romano
PRESIDENT

TREASURY INFLATION-PROTECTED SECURITIES (TIPS)

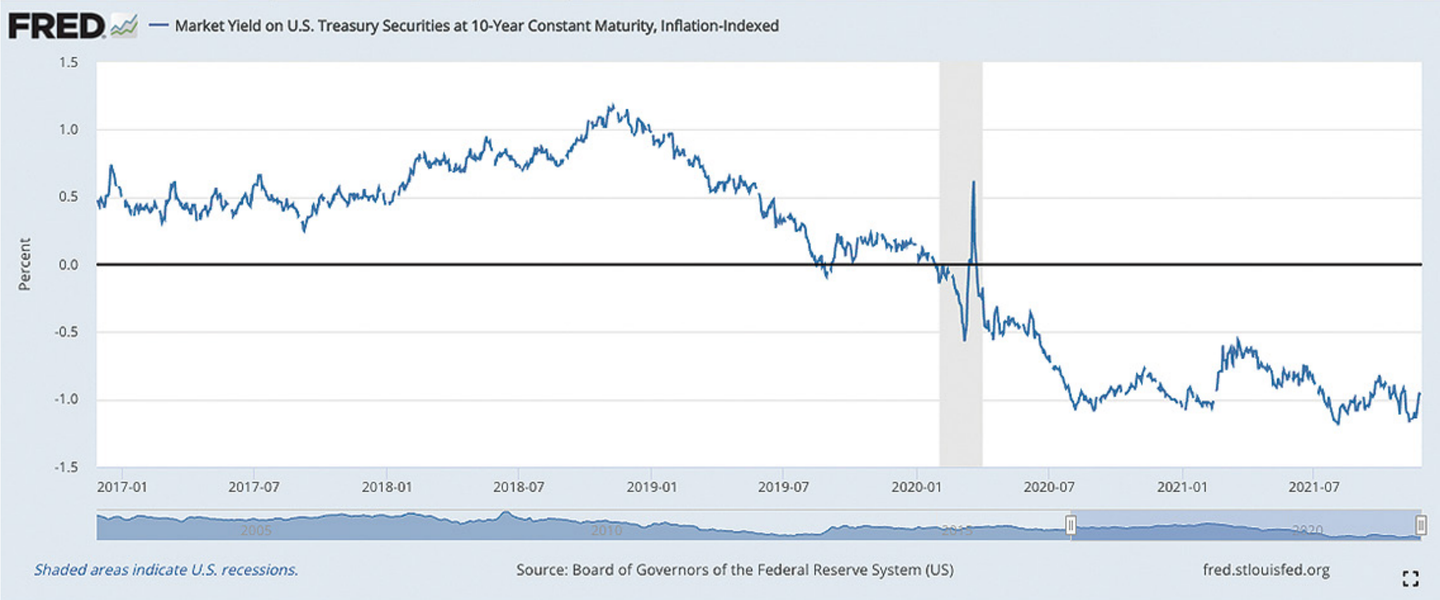
How do they work and are they a useful investment in an inflationary environment?

Like other treasury notes and bonds, Treasury Inflation-Protected Securities (TIPS) pay a fixed interest rate coupon twice a year. However twice per year, the principal value of a TIPS increases with inflation and decreases with deflation, as measured by the Consumer Price Index. The fixed coupon rate is applied to the adjusted principal value and can increase or decrease your semiannual payment. When a TIPS matures, you are paid the greater of the adjusted principal or original principal value. TIPS are typically issued once a year with maturities of 5, 10 and 30 years. However, older issues with various maturities can be purchased in the secondary market at the current price and adjusted principal values.

Unlike typical Treasury issues, the par (face) value of TIPS is constantly changing as it is adjusted by changes in CPI. As an example, if you purchase a new 10-year issue for $1,000 and the CPI changes by 3% in the first year, the par (face) value of the bond would increase by $30 to $1,030. In 10 years if inflation increased by 3% annually for the life of the bond, the maturity value would be $1,344 ($1,000 compounded at 3% for 10 years). The result is that when you purchase a TIPS bond there is no way to know what the full value will be at maturity. Semiannual coupon payments increase along with the principal. If the TIPS coupon rate was 1%, the last semi-annual payment in year 10 would be $6.79 (1% x $1,344 face/2). Federal income tax owed on TIPS is not only on the coupon payment but also annually on the inflation that accrues to the principal.

Current market rate and inflation expectations determine the pricing of new and secondary market TIPS. Because TIPS have a potential additional return with an increase in CPI, the current market coupon rate is always less than their fixed rate Treasury counterparts. The difference between the TIPS coupon rate and the similar maturity fixed coupon rate is known as the 'breakeven rate'. The breakeven inflation rate is calculated by subtracting the yield of an inflation-protected bond from the yield of a nominal bond during the same time period. This number represents what inflation would have to be in order for investors to "break even" (or earn the same) when buying one bond type over the other. For 10-year TIPS the breakeven rate has averaged about 2.25%, nearly identical to the annualized CPI increase since TIPS were first issued in 1997.

Market Yield on U.S. Treasury Securities at 10-Year Constant Maturity



What are some of the offsets to investing in TIPS? The first is the lower coupon yield than their fixed rate counterparts. Currently the fixed rate 10-year treasury yields 1.65%. The current yield on the 10-year TIPS is a NEGATIVE -1.0%. An investor would lose -1% annually if there was no inflation. The 10-year TIPS yield has been negative for the past 20 months and has only averaged 0.40% in the ten years prior to that.

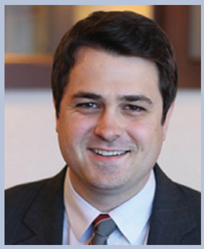
In addition, price sensitivity to changes in rates is similar with TIPS as it is with their fixed rate counterparts. If rates move higher, the price of each security will fall and have an impact on total return if an issue is sold prior to maturity.

With a 10-year nominal Treasury trading at 1.65% at the time of this writing, the TIPS gets an inflation breakeven rate of 2.65%, near the top of the Treasury's history of the 10-year breakeven rate. At this level TIPS look historically expensive. However, if inflation continues at a rate of 4% to 5% or higher over the next 10 years, TIPS will end up being a reasonable investment versus fixed rate bonds. Then again, no 10-year inflation period since 1990 has run higher than 2.9%. If that were to hold true again, 10-year TIPS total return is estimated to be the same as holding cash.

Doug Geisser, *VP Fixed Income Principal*

ROMANO NEWS

Peter Hemwall Completes Level II of CFA Exam



Seven-year Romano veteran Peter Hemwall completed the second stage of the Chartered Financial Analyst exam this fall. Level II centers on financial analysis and asset valuation, culminating in a nearly five-hour exam. The entire Romano team congratulates Peter both on his accomplishment and continued ambition. Peter will sit for Level III, the final stage prior to being named a CFA institute member, in May.

Best Wishes to Wendy Ek

Please join us in applauding Wendy Ek on her December retirement. Wendy has been an enthusiastic and dedicated member of Romano's Operation Team for over 14 years. She says she will miss her coworkers and Romano clients alike, proclaiming, "It really is a great group of people across the board." Wendy plans to enjoy the winter free from her long commute and is looking forward to planning a trip this spring to celebrate.

Where's My Holiday Gift?

Chances are you may have witnessed 2021's supply chain disruptions firsthand. The pandemic lead global manufacturing shutdown collided with spiking consumer spending on goods like furniture, appliances and electronics, rather than traditional services....and we had ourselves a perfect storm. Add in a semiconductor plant fire and a ship stuck in the Suez Canal, and adults were acting like children scorned over missing holiday gifts!

It's early to call it a comeback, but macro data and a quick office poll both yield the same results. That thing you asked Santa for might *finally* be on its way. **Doug Geisser** needed a simple coil for his AC unit, but a three-month delay meant he ended up with an entirely new system. **Scott Miller** is enjoying his evenings in an off-the-floor recliner he waited nine months for, and **Nicole Kustok** is expecting a gas range ordered in March this week. At print, there are 51 ships anchored off Long Beach down from a July high of 76 and rail delays have been cut in half. Just like in the movies, we might have a Christmas miracle after all.

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HAPPY HOLIDAYS FROM ROMANO

'Tis the season for gratitude and reflection here in Evanston. Thank you to our clients, family and friends for all you do to make us who we are. This is more than a job for us because of the people we serve, it's you who makes the work matter and worthwhile. Here's to reaching all of our goals in the coming year!