ALL STAR FINANCIAL

Build Wealth. Retain Wealth.

QUARTERLY
REVIEW & PREVIEW

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December Surge Powers Stocks to Big Gains in 2021

After a decline in the S&P 500 in September and despite the uncertainties persisting in the global economy, the stock market finished strong with a December rally to end 2021. The S&P 500 returned 4.5% in December and 11% in the 4th quarter, finishing the year with a total return of 28.7%. This wrapped up a three-year rally for stocks that we have not seen since the late 1990s. The S&P 500 gained 31.5% in 2019 followed by 18.4% in 2020 and then 28.7% in 2021. These returns have been driven by a low interest rate environment, reduced corporate taxes, and soaring corporate earnings in the wake of fiscal stimulus enacted by governments in reaction to the COVID-19 pandemic.

With the stock market continuing upward, investors have continued to move funds into Fixed Income/Bonds. In 2021 investors added over $555 billion to bond mutual funds or ETFs. Despite those flows, the Barclays Global Bond Index declined 4.7% during the year. These returns impacted investors in diversified equity/bond portfolios. A 60% Global Equity / 40% Global Bond portfolio increased by 8.8% in 2021.

Elevated asset prices not only in equities but also in real estate and other financial assets have assisted wage growth in fueling significant consumer demand. Holiday retail sales between November 1st and December 24th grew 8.5% from 2020 to 2021, surpassing the markets expectations. We have more cash/liquidity in our system than ever before which has Americans feeling much more financially stable. Since 2019 (before the pandemic) American household wealth has increased by 19.6% to $141.7 trillion. As a point of reference, that figure has doubled since 2010, when household net worth hovered around $70 trillion. Thanks again to the Government funny money.

So the question is, what is the downside to all this growth in asset prices, consumer demand, and household wealth? The answer is inflation (rising prices). Despite the Federal Reserve's (the Fed) efforts to create inflation prior to 2020, the US economy has not experienced rising inflation above 3% for a sustained period since the 1980s but it appears we are entering 2022 with a solid expectation that we will observe inflation well above 4% for the next 12 months. At the end of October, the twelve month change in inflation (CPI) was 6.9%. Throughout the majority of 2021 the Fed Chairman, Jerome Powell, predicted that the inflation the US economy was experiencing was "transitory", meaning it was going to subside after a few quarters. That prediction was incorrect, and Mr. Powell decided to humbly retire the word "transitory" in a speech he gave toward the end of the year.

As we look ahead to 2022 the US economy is surging forward. Economists are predicting Gross Domestic Product (GDP) will increase by around 3.5% and the S&P 500 companies are forecasting earnings growth around 9%! Those two figures demonstrate the momentum in our economy created by the excess liquidity and low interest rates resulting from COVID-19 stimulus measures. The concern, however, is whether that momentum can overcome the risk factors created by supply chain issues, inflation, and labor shortages.

The past three years have been tremendous for those invested in stocks and other risky assets, but the long-term averages suggest that investors should be mindful of risk looking forward. Toward the end of growth cycles the emotion of greed tends to accelerate demand for risk, but disciplined investors should stay mindful of their overall financial goals and maintain diversification within their portfolio to allow them to navigate the next few years of uncertainty.

Bob's Corner
2021 Closes with a Bang

After focusing on funding the economy with trillions of dollars in 2020 (pandemic concerns), the government has created a monster that concluded with a phenomenal 4th quarter (+11.0%), an exceptional 2021 year at 28.7% for the S&P 500. We believe that the big upside to the market is close to being in the rearview mirror. After unprecedented 3-year compound average returns for the S&P 500 of 26%, the Russel 1000 at 26.2% (growth + 34.1% and value +17.6%) and the Bloomberg US Aggregate Bond Index at + 4.8% (-1.5% for 2021), the market needs a break.

The expectation is that we are in store for lower rates of return going forward after this inflation surge in the economy slows down. As we have stated in the past, the paradigm shift in bonds has created an asset class that will not give us much upside going forward. With the teeth of inflation (rates bouncing higher) just starting to eat away at the total returns for bonds, investors are looking to equities to fill the void. This is a good decision now, but might come back to bite the market later as our disrupted economic cycle continues to change.

We've had more than a few phone calls from clients asking what will happen to our portfolios if the market corrects again another -30%+? Well first, we don't think that will happen any time soon, but a 10-20% correction is possible. In this last quarter we had a couple of days that dropped 3% in one day, and our models averaged approximately a 1.2% downturn. Remember, it is fear and greed that will sink the ship.

Rest assured we have your portfolios ready for more volatility and uncertainty. Thank you for your continued trust in the All Star Financial Team!

– Bobby K.

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All Star Financial is passionate about providing strategies for a safer way to a successful retirement for people who are serious about their money but uncertain about how to nurture it.

The Economy

Inflation Proves Stickier Than Expected

- The current projections of GDP growth for the 4th quarter currently stands at a 7.4% annualized growth rate.
- At its December meeting, the Fed presidents revealed their intentions to double the pace of tapering starting in January to end their asset purchases by March 2022.
- Congress passed a $1.2 trillion bipartisan infrastructure bill in mid-November. Much of the bill's allotted spending will be used to improve our nation's transportation, power, and water infrastructure.
- Core CPI (excluding food and energy) rose by 4.6% year-over-year in October and by 5.0% in November, which was the highest reading since the early '90s.
- ***We are cautiously optimistic about the economic growth in 2022 as we see multiple global challenges. Fiscal policy will be much less supportive going forward and the pandemic continues, but with less disruptive economic effects. In the US, the labor market continues to be very tight and elevated inflation persists.***

Bond Markets

The End of Peak Liquidity

- The US Aggregate Bond Index had a flat return, 0.0%, for the quarter while the Global Aggregate Bond Index fell 0.7%.
- The yield on the 10-Year Treasury Note started the quarter at 1.47%, bottomed at 1.36% in early December, ahead of the Fed meeting, before finishing the year at 1.51%.
- The yield curve flattened throughout the quarter, as a sign that the fixed income market is pricing in reduced economic growth going forward.
- The US Corporate Credit Index returned 0.2%, and the US High Yield Index posted a 0.7% return as yield spreads compressed.
- ***Due to massive global stimulus, sovereign debt levels are increasing, and we believe central banks will keep interest rates low for as long as possible. However, with global yields near or below zero, we do see rates going up. Therefore, our forecast for fixed income continues to be muted and investors must focus on its diversification and stability effects vs. performance.***

Domestic Stocks

Omicron Fails to Spook Equity Rally

- The S&P rose 11.0% in Q4 with the Real Estate (17.5%) sector leading all sectors, followed by Information Technology (16.7%), while the worst performing sectors were Communication Services (0.0%) and Financials (4.6%).
- The current S&P 500 P/E ratio is 21.2, 9% lower than its peak in September 2020, but well above the 25-year average ratio of 16.8.
- Large cap stocks (Russell 1000) outpaced small cap (Russell 2000) stocks, returning 9.8% vs 2.1%.
- The Russell 3000 Growth and Value indices returned 10.9% and 7.5%, respectively.
- ***With the US markets forecasting several interest rate hikes in 2022, and the valuation gap between growth and value stocks still persists at historically high levels, we believe there are opportunities in mostly the cyclical sectors as we move into 2022 (Financial and Energy).***

International Stocks

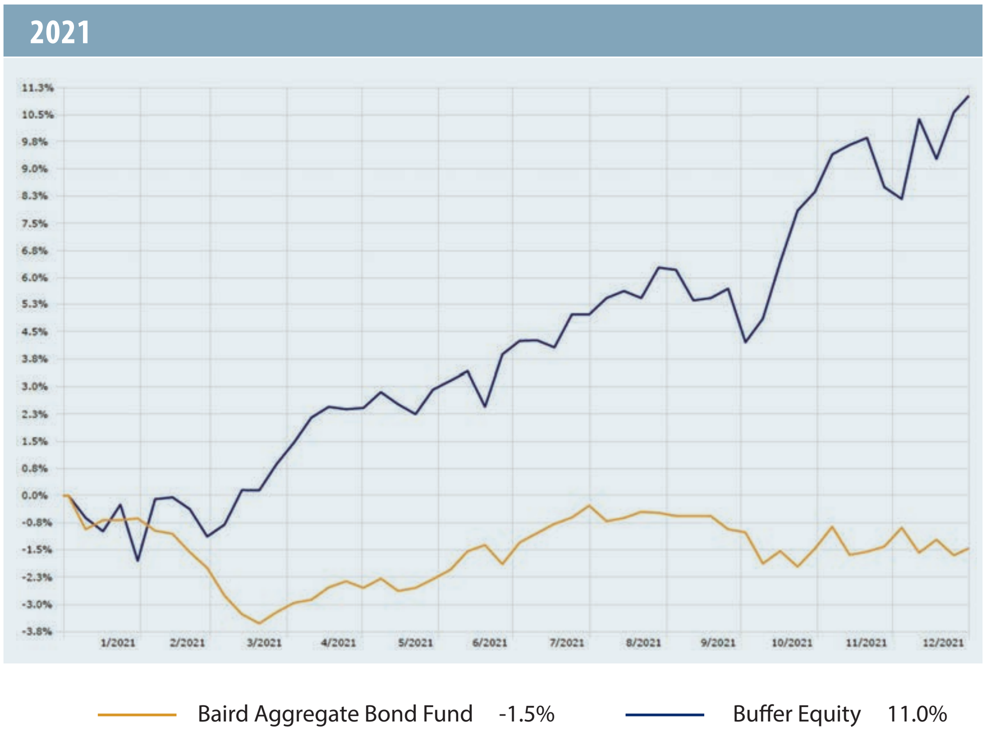
Emerging, China Concerns Remain

- Non-US stocks (MSCI ACWI ex-US Index) returned 1.8% in the fourth quarter and 7.8% for the year, drastically underperformed US stocks (Russell 3000 Index), which gained 9.3% and 25.7%, respectively.
- Developed markets (MSCI EAFE Index) returned 2.7% while Emerging markets (MSCI EM Index) returned -1.3%, and ended -2.5% for the year.
- From a style perspective, the MSCI ACWI Ex US Value and Growth index returned 1.2% and 2.4%, respectively.
- Looking at valuations, the MSCI ACWI ex-US Forward P/E ratio is at a historically wide discount to the S&P 500 Forward P/E ratio, over 30% cheaper.
- ***With continued out-performance of US vs. International equity markets, the valuation gap between them has increased. Therefore, we believe there are compelling opportunities outside the US equity markets for patient investors going forward.***

Sources: All economic data is from JP Morgan's Guide to the Markets, December 2021 (https://am.jpmorgan. com/us/en/asset-management/gim/per/insights/guide-to-the-markets/viewer#/share-by-email) and all rate of return data is from Morningstar.com, unless otherwise noted by citation.

Buffer vs. Bonds

With interest rates near all-time lows entering 2021, the All Star Financial Investment Committee decided to take an active role in reducing the overall allocation to fixed income/bonds. In early January one of our core bond funds, Baird Aggregate Bond, was sold and the proceeds were reinvested into equity buffer ETFs. These ETFs capped the upside opportunity but more importantly minimized the downside risk. It seemed reasonable that the total return opportunity was greater than the Baird Aggregate Bond fund, and we were right. Mid-year we adjusted the buffer strategy by moving out of the buffer ETF and into a hedged equity fund that was similar but also provided us a dividend yield. **In total, these strategies gained 11% in 2021 compared to the -1.5% return of Baird Aggregate Bond. This trade is an example of how active portfolio management can add value within a diversified portfolio.**



The Mighty *"usually"* Fall

In 2021, only 5 stocks accounted for 51% of the gain in the S&P 500. These stocks: Apple, Microsoft, Meta (formerly Facebook), Alphabet (Google's parent company), and Amazon drove a substantial part of the performance over the past few years. It almost seems like those are the only stocks you should own. However, history tells another story. If we look at the top 10 largest companies as of March 2000, 6 of the 10 declined in price over the next 20 years. **The lesson is that diversification is the best long-term path to investing in the stock market. Following the herd can hurt you!**

Where Are They Now?

10 Largest Russell 1000 Companies as of 3/31/2000 (Prices Adjusted for Splits)

	Price as of 3/31/2000	% Change 5 Years Ending 3/31/2000	Price as of 9/30/2021	% Change 3/31/2000–9/30/2021
Cisco Systems	$77.31	3550.2%	$54.43	-29.6%
General Electric	$398.92	476.4%	103.03	-74.2%
Intel	$65.97	1143.6%	$53.28	-19.2%
Microsoft	$53.13	1095.1%	$281.92	430.7%
Exxon Mobil	$38.97	134.0%	$58.82	50.9%
IBM	$118.00	474.7%	$138.93	17.7%
Citigroup	$418.84	597.6%	$70.18	-83.2%
Lucent Technologies	$61.25	N/A[2]	$2.34[3]	-96.2%
AT&T	$42.13	100.6%	$27.01	-35.9%
Oracle	$39.03	1586.2%	$87.13	123.2%
Russell 1000	1536.33	200.7%	4,648.47	202.6%
S&P 500	1498.58	199.3%	4,307.54	187.4%

Sources: All economic data is from JP Morgan's Guide to the Markets, December 2021 (https://am.jpmorgan. com/us/en/asset-management/gim/per/insights/guide-to-the-markets/viewer#/share-by-email) and all rate of return data is from Morningstar.com, unless otherwise noted by citation.

Performance Update

Fourth Quarter 2021

Market Index	4th Qtr	Year to Date	3 Year	5 Year
MSCI ACWI All Cap NR	6.03	18.21	20.19	14.11
S&P Global BMI NR	5.75	17.70	19.91	13.96
MSCI ACWI Ex USA NR	1.82	7.82	13.18	9.61
Russell 3000 TR	9.28	25.66	25.78	17.97
S&P 500 TR	11.03	28.71	26.06	18.48
DJ Industrial Average TR	7.87	20.95	18.48	15.52
Russell MidCap TR	8.00	24.76	21.40	13.09
Russell 2000 TR	2.14	14.82	20.02	12.02
NASDAQ Composite TR	8.45	22.18	34.25	24.98
MSCI EAFE NR	2.69	11.26	13.54	9.55
MSCI EM NR	-1.31	-2.54	10.94	9.88
Bloomberg Global Aggregate TR	-0.67	-4.71	3.59	3.36
Bloomberg US Government TR	0.15	-2.28	4.06	3.07
Bloomberg US Credit TR	0.22	-1.08	7.17	5.05
Bloomberg US Agg Bond TR	0.01	-1.54	4.79	3.57
Bloomberg High Yield Corporate TR	0.71	5.28	8.83	6.30
JPM EMBI Global Diversified TR	-0.44	-1.80	5.94	4.65

*The above after-fee annualized total returns, betas, and alphas represent All Star Financial composite model performance. Your portfolio's actual returns, betas, and alphas may differ depending on your specific holdings and timing of cash flows.

Diversification, asset allocation, and value investing do not assure or guarantee better performance and cannot eliminate the risk of investment loss.

All Star Financial works on a "best efforts" basis and does not promise or guarantee any results. Past performance does not represent future results.

Summary

Asset Allocation Decisions in 2021

Using the All Star Financial dynamic asset allocation approach, our Investment Committee made the following decisions in 2021 that benefited our clients' portfolios:

1. Reduced fixed income exposure to address the paradigm shift of rising interest rates.

2. Utilized hedged/buffer equity strategies to obtain a higher total return than fixed income while maintaining equity risk minimization.

3. Continued to sell growth stocks and purchase value stocks based on current valuations.

4. Maintained international equity exposure for diversification while continuing conviction to be underweight to global equity benchmarks.

5. Addressed major risk factors in the global economy but maintained a long-term and risk-based approach to avoid the greed and fear cycles of investing.

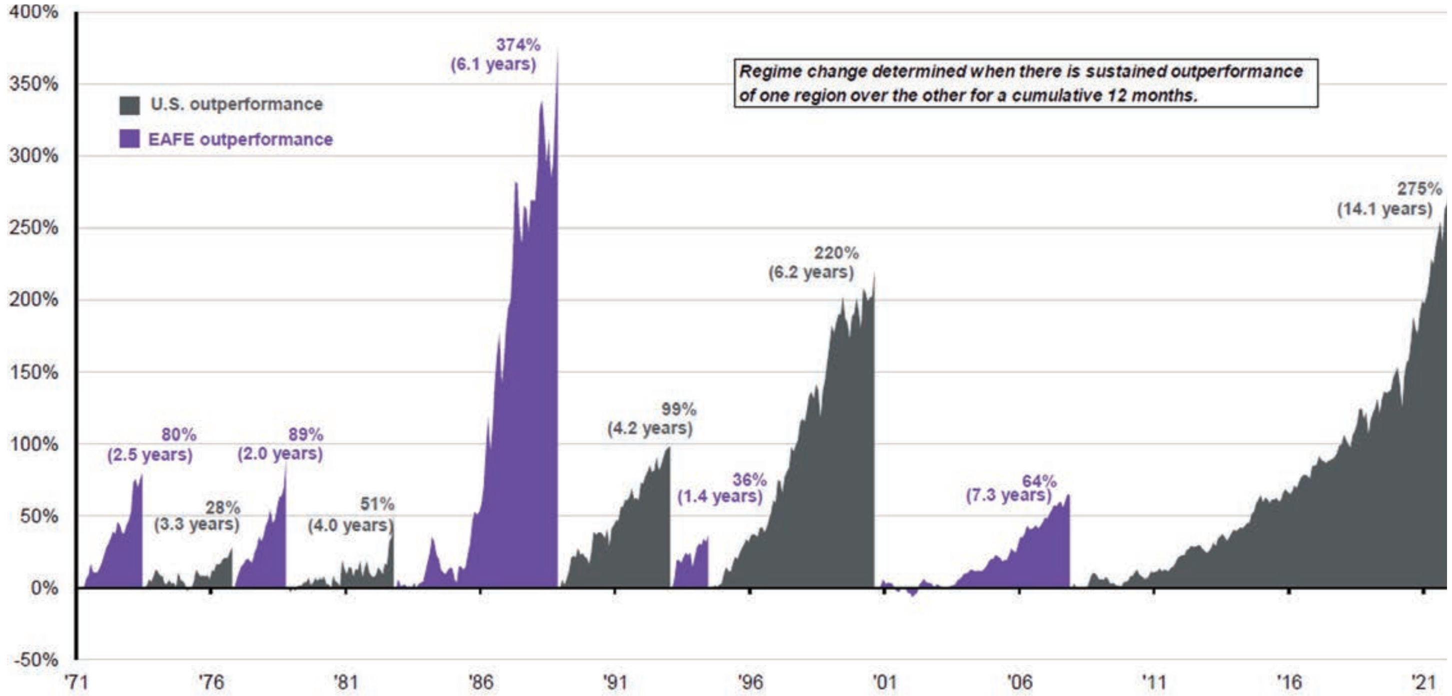
"It's not how much you make, it's how much you keep!"

Asset Allocation & Diversification with International Equities

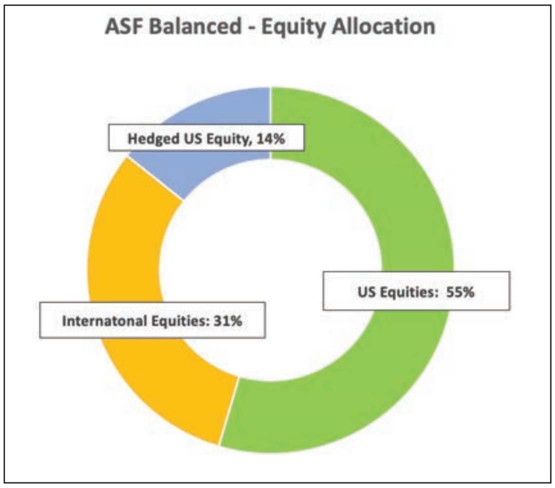
Over the past 50 years, throughout the emergence of globalization and democratization of our world, there have been periods where US equities and International (EAFE – Europe, Asia, Far East) equities have outperformed one another. The past 14 years of that time period we have experienced the most prolonged out-performance as US equities have increased in value by 207% MORE than their EAFE counterparts. Many investment professionals and economists have been predicting a reversion back to the mean of this theme over the past few years and that opinion has only grown as the trend continues.

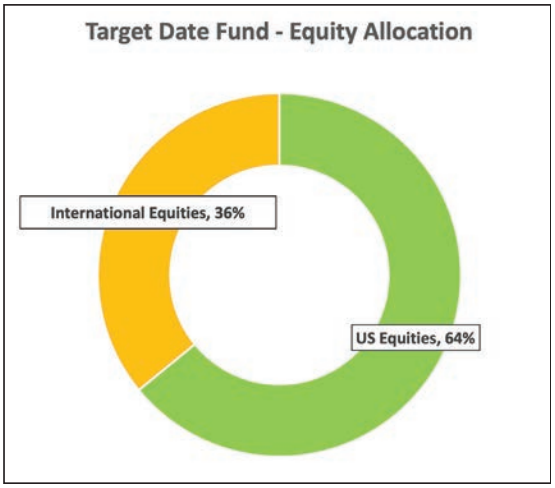
MSCI EAFE and MSCI USA relative performance

U.S. dollar, total return, cumulative outperformance*



Using our dynamic asset allocation approach, the All Star Financial (ASF) investment committee has always maintained some allocation to US and non-US international stocks. However, in the wake of the pandemic the overall allocation was shifted away from International equities toward an overweight to US equities and hedged US equities. Over the past 12 months, the S&P 500 has increased by 28.7% and the EAFE index has increased by 11.8%. Compared to a similar Target Date Fund, the ASF overweight to US equities and hedged US equities has added value to clients in the past 12 months. However, we do believe that a sustained exposure to international equities continues to provide diversification and upside opportunities as well.





ALL STAR FINANCIAL

Build Wealth. Retain Wealth.

OUR MISSION IS TO HELP YOU ACHIEVE YOUR DESIRED STANDARD OF LIVING AND FINANCIAL PEACE OF MIND.

The experienced All Star team of professionals is dedicated to understanding your individual needs and objectives, offering a comprehensive wealth management platform that is designed with one purpose in mind — to serve you, our valued client.

New Team Member Spotlight

Amanda Giliotti – Director of Tax Services - JD, CPA

Amanda joined All Star Financial in 2021 as the Director of Tax Services. She is a trusted advisor and always strives for better results and more valuable service. Amanda is an attorney and CPA with 29 years of tax experience and has been featured in numerous publications including Forbes and the Wall Street Journal as one of the best in her field. She has also been featured on local news stations as a tax expert speaking on tax law changes.

Amanda attended the University of Houston as well as William Mitchell College of Law in St. Paul. She is a veteran of the Gulf War, a master scuba diver and avid motorcyclist. She splits her time between her two homes, Minneapolis and San Antonio, and enjoys watching the Minnesota Vikings.

Joleen Giliotti – Tax Advisor and Operations Coordinator

Joleen joined All Star Financial in 2021 as a Tax Advisor and Operations Coordinator. Prior to joining All Star, she was the second in command at Giliotti Tax and Legal Services where she created the infrastructure and processes that enabled a high standard of service for their clients. Before that Joleen worked as a manager at RBC Wealth Management. She brings over 10 years of tax experience and operational support to All Star Financial.

Joleen attended Gustavus Adolphus for her undergraduate degree and received her master's degree from Carlson School of Management. In her free time, Joleen enjoys traveling the world and scuba diving.

Please join us in welcoming the team from Giliotti Tax Services to the All Star Financial family!

Advisory services are offered through All Star Financial, a SEC Registered Investment Advisor.

Meet Our Team

Robert Klefsaas, CFP , AIF , CFDA® – CEO, Senior Wealth Advisor
Brian Senske, MA, CPA (inactive) – CFO, COO, Senior Wealth Advisor
Kaitlin Buckley – 2IC, Wealth Management Associate
Matt Berhow CFP®, AIF® – Senior Wealth Advisor
Sam Sexton CPA, CFP® – Senior Wealth Advisor
Mark Potter, CPA – Associate Advisor
Elliot Syverson – Associate Advisor
J. Alexander Källebo, CFA® – Portfolio Manager
Caleb Findell – Investment Analyst
Amanda Giliotti , JD, CPA – Director of Tax Services
David Osterberg, CPA – Tax Advisor
David Engelsgaard, CPA – Tax Specialist
Joleen Giliotti – Tax Advisor & Operations Coordinator
Linda Davis – Tax Assistant
Lucelia Husby – Client Service Associate
Haley Ziemke – Client Service Associate
Paula Zilka – Operations Manager
Nicole VandenPlas – Executive Assistant

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