

October 19, 2021

Dear Partners in Ministry,

Enclosed is the 2021 3<sup>rd</sup> quarter statement for your account(s) at the United Methodist Foundation (statements from 7/1/17 are accessible online). Net of fees, the returns of the fund models are:

As of 9/30/2021	3 <sup>rd</sup> Qtr 2021	Year to Date	Last 1 Year <sup>†</sup>	Last 3 Years <sup>†</sup>	Last 5 Years <sup>†</sup>	Last 10 Years <sup>†</sup>
<b>Aggressive Fund</b>	<b>-0.31%</b>	<b>10.30%</b>	<b>23.81%</b>	<b>12.97%</b>	<b>13.28%</b>	<b>10.58%</b>
Agg. Climate benchmark*	-1.33% -1.08%	8.41% 10.33%	19.35% 25.23%	n/a 12.30%	n/a 12.65%	n/a 11.10%
<b>Moderate Fund</b>	<b>-0.21%</b>	<b>6.93%</b>	<b>16.36%</b>	<b>10.39%</b>	<b>10.13%</b>	<b>8.16%</b>
Mod. Climate benchmark*	-0.87% -0.71%	5.62% 6.99%	14.00% 17.26%	n/a 10.13%	n/a 9.79%	n/a 8.76%
<b>Conservative Fund</b>	<b>-0.20%</b>	<b>3.17%</b>	<b>8.51%</b>	<b>7.25%</b>	<b>6.49%</b>	<b>5.84%</b>
Con. Climate benchmark*	-0.56% -0.34%	2.58% 3.36%	7.24% 9.05%	n/a 7.53%	n/a 6.62%	n/a 6.23%

\*"Benchmark" is a blend of benchmarks for the fund's underlying portfolios of stocks and fixed income, relative to the portfolio allocations within the fund's model. †Rates of return (1+ years) are annualized. See the monthly performance reports online: <https://umfnic.org/investment-performance-reports/>

### Market Commentary from Investnet | PMC

Brandon Thomas, Chief Investment Officer of Investnet | PMC, concluded their "Economic and Market Overview: Third Quarter 2021" report with the following observations and commentary:

"The global economy is moving forward in fits and starts, with varying results in different regions of the world. Covid-19 continues to be somewhat of a headwind for the economy, with the Delta variant raising concerns over a rise in new cases. At the same time, questions about the long-term efficacy of vaccinations and debates about vaccine and mask mandates are causing increased societal polarization. In the US, growth has been resilient, but expectations have been moderated in recent weeks due to the impact of the Delta variant. The euro zone is faring better than expected from the perspective of economic prospects, with analysts forecasting 4% growth in 2022. In Asia, lower vaccination rates have caused governments to re-impose restrictions, putting a damper on economies. Economists are increasingly focusing on consumer sentiment, because as the effects of fiscal stimulus fade, economies will need to rely on positive expectations about the future in order to sustain growth. Supply chain disruptions also remain a hurdle. Since Asia is a critical player in the supply chain, economists argue that improvement in supplies will be slow to come until the region sees a drop in Covid cases. In terms of central banks throughout the world, the expectation is that many will begin tapering soon, and that they will begin to raise rates in 2022, assuming growth is positive and inflation remains elevated. Despite stumbling into the end of the quarter, stock prices



are not far off all-time highs and still have valuations that are also near record levels. Historically, when valuations have been close to where they currently stand, forward returns have been muted.”<sup>1</sup>

**“Supply chain disruptions also remain a hurdle.”**

The media is constantly on the prowl for a causal narrative to entertain us and to explain to us what is going on with “the economy.” The latest dominant narrative is “supply chain disruption.” The narrative goes something like this: the lockdowns early on in the pandemic caused a profoundly deep and acutely brief global recession. Government stimulus injected trillions of dollars into the economy, much of it as cash deposited directly into the bank accounts of consumers. Due to the labor disruption of the pandemic and the rapid recovery of pent-up consumer demand (and stimulus to spend!), a perfect storm of short supply and increased demand brewed up bottlenecks in global supply chains.

When an economic story like this one makes its way into something superfluous like EOnline.com’s “Drew Barrymore-Approved Facial Spray Is On Sale”<sup>2</sup> article, we can assume the ubiquitous media coverage is signaling an apex in the exigent circumstances causing the media coverage in the first place, in this case, the supply chain disruption. I admit the boiling over media coverage indicator is not necessarily related to a climax in the issues themselves, but when this kind of coverage crowds out a headline like this one in the Financial Times, “US bank chiefs confident supply chain disruptions are ‘transitory’,”<sup>3</sup> we are probably safer in assuming the problems are, indeed, working themselves out. It will take time, but the probability is low that the supply chain issues will persist and derail the recovery of global economic growth.

**“stock prices are not far off all-time highs”**

The S&P 500 closed September down 5.2% from its all-time high early in the month. I view this pullback as a sign of health in the stock market. Investors are constantly looking to trim from stocks with elevated valuations and to reallocate to other stocks that present a better “value.” This is a normal and healthy function of the market, to rebalance, which is an important part of the ongoing optimization of the investment models offered by the Foundation.

Stock “prices” are near all-time highs, but let us remember the old adage from Ben Graham, Warren Buffett’s teacher: “Price is what you pay. Value is what you get.” We naturally pay attention to prices as they go up and down, but we need to focus on the value of what we’re paying for. So, where are U.S. stock “valuations?”

**S&P 100<sup>4</sup>** (9/30/2021)

P/E (TRAILING)	P/E (PROJECTED)	P/B	INDICATED DIV YIELD	P/SALES	P/CASH FLOW
26.01	21.11	5	1.41%	3.43	30.05

How about international stock valuations?

**S&P/BNY Mellon Developed Markets 100 ADR Index<sup>5</sup>** (9/30/2021)

P/E (TRAILING)	P/E (PROJECTED)	P/B	INDICATED DIV YIELD	P/SALES	P/CASH FLOW
17.3	11.79	1.62	2.93%	1.9	7.77

Based on the fundamentals above, international stocks are trading at more attractive valuations than U.S. stocks. Also, consider this, during the past 30 years, the average PE ratio of the S&P 500 was 25.<sup>6</sup> Even throwing out the 11 months during the financial crisis of 2008-2009 when the the S&P 500’s PE ratio ranged from 59 to 124, the average PE ratio of the last 30 years was 23. Current stock valuations do not

look worrisomely overvalued in this 30-year context. Often sources cite the long-term average of the S&P 500's PE ratio at about 16. Compared to this long-term average, stocks do look overvalued. But there are good reasons to view the stock market of recent history as providing better contextual clarity for valuations. Specifically, stock dividend yields have historically been much higher.

A more contextual way to assess valuations is to divide the current dividend yield by the forward-looking earnings yield (the inverse of the PE ratio), which is the payout ratio of forecast earnings. For example, the S&P 500's dividend yield on 9/30 was about 1.3% and the one-year forward-looking PE was about 21, which equates to a 4.8% earnings yield. The payout ratio of forecast earnings, in this current case, is then 27% ( $1.3 / 4.8$ ). The S&P's long-term average earnings yield is 7.3%<sup>7</sup> and the average dividend yield is 4.3%.<sup>8</sup> Using these metrics, the average payout ratio of stock earnings is 59%. This means that currently companies retain more earnings to reinvest in growth and to, perhaps, buyback shares. By this metric, the payout ratio of earnings, stocks do not look overvalued and may be considered undervalued.

**“when valuations have been ... where they currently stand, forward returns have been muted”**

The past 10 years in the stock market have seen healthy double-digit annualized returns. As Mr. Thomas reminds us, considering historical patterns, the next 10 years are less likely to continue the same significant annualized gains as the previous 10 years. This does not mean the stock market is overheating simply because stock prices are near their recent all-time highs. Valuations are elevated, but reasonable, and the economic recovery looks stable as we turn the pages of the pandemic toward its conclusion.

As always, it is a good thing to reevaluate investment allocations at least once a year. How about reevaluating toward the end of this year or the beginning of next year? The number one thing that should determine your overall investment allocation is your time horizon for distributions. If you would like to gain more clarity of your church's investments and the factors that should shape your collective decision-making regarding investment allocation, please contact me.

Be safe and be blessed,



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<sup>1</sup> [https://www.investpmc.com/sites/default/files/documents/PMC\\_QuarterlyMarketEnvironment.pdf](https://www.investpmc.com/sites/default/files/documents/PMC_QuarterlyMarketEnvironment.pdf)

<sup>2</sup> <https://www.etonline.com/this-drew-barrymore-approved-facial-spray-is-on-sale-at-amazons-holiday-beauty-haul-173091>

“Many shippers are citing delays due to supply chain issues, which means even though we might still be in the midst of gathering Halloween costumes and candy buckets, it's not too early to shop for Hanukkah gifts, Christmas presents and other festive holiday decor.”

<sup>3</sup> <https://www.ft.com/content/0dd1622d-883a-44a8-80c4-079fc5e90fab>

<sup>4</sup> <https://www.spglobal.com/spdji/en/indices/equity/sp-100/>

<sup>5</sup> <https://www.spglobal.com/spdji/en/indices/equity/sp-bny-mellon-developed-markets-100-adr-index/>

<sup>6</sup> <https://www.multpl.com/s-p-500-pe-ratio/table/by-month> (average of the S&P 500's PE by month for the previous 30 years)

<sup>7</sup> <https://www.multpl.com/s-p-500-earnings-yield>

<sup>8</sup> <https://www.multpl.com/s-p-500-dividend-yield>

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