Market Comment

No one can know for sure if the current pull-back in stocks will continue, but we realize "I don't know" is not a helpful forecast. As such, we will attempt a more revealing answer as follows:

1) Identify the two primary risk factors we are monitoring
2) Share our current expectations for each risk factor
3) Describe any relevant actions we have taken in our investment strategies

Primary Risk Factors

We believe the recent downturn in stocks has been driven by two primary risk factors:

1) Fear of tighter monetary policy from the Federal Reserve (Fed)
2) The possibility of a military conflict in Ukraine

Our current expectations for both issues are on the optimistic end of the range of possibilities, which we will explain below. Even so, we have already taken steps to address these risks in our investment strategies, and we stand ready to do more if conditions evolve in a more troubling direction.

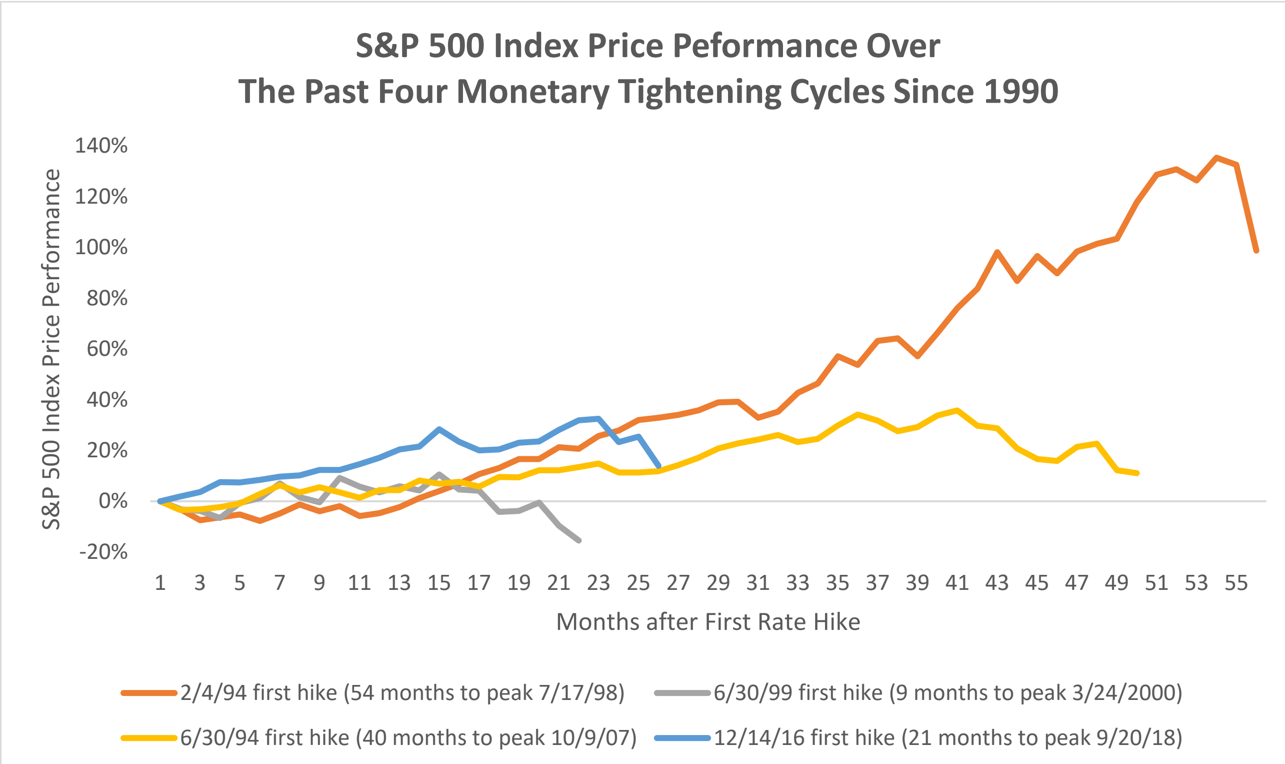
Fed Policy

Last November the Fed abandoned its premise that inflation would prove to be "transitory," thereby ushering in its own transition toward tighter monetary policy. Investors fear monetary tightening cycles because they have historically ended when policy makers go too far and trigger a bear market in stocks (defined as a drop of 20% or more).

We showed in our year-end *Overview* that stocks have historically been resilient during the early stages of past tightening cycles because the economy is typically strong when these cycles begin, and because it usually takes time for monetary policy to become restrictive once the process starts.

So far, the stock market is not following its historical script, as stocks are down sharply before the Fed has even started its pending tightening campaign.

> *Note: The Fed began to "taper" its monthly asset purchases (known as quantitative easing, or "QE") in December. However, these asset purchases are expected to continue at a declining rate until March, when the first interest rate hike is also penciled in.*



Source: Bloomberg; Standard & Poor's; St. Louis Fed; The peak-to-trough decline in 2018 was just under the 20% threshold for a bear market, but it is included here as a representative example of a monetary tightening cycle. It is not possible to invest directly in the index.

We suspect the recent drop in stocks reflects investors' fear that the Fed might overdo it more quickly this time because inflation is currently running much higher than past tightening cycles. The logic here is that the Fed may have less flexibility to respond to stock market volatility by pausing or reversing its tightening campaign because the Fed's mandate is to promote stable inflation, not to stabilize the stock market.

In contrast, when the Fed's last tightening campaign was launched in December 2016, inflation was already stable near the Fed's 2.0% target.[1] This condition enabled flexibility for a rapid course correction from the Fed once it became clear that their policies were destabilizing the equity markets.

Our View on Fed Policy

We recognize there is risk of a policy error from the Fed, but we assign a lower probability to this outcome relative to more bearish commentators. *This perspective is highly dependent upon our expectation that the news on inflation will improve soon*. We believe this is likely for two reasons.

[1] Source: Bloomberg

First, the so called "fiscal cliff" should relieve certain inflationary pressures due to its downward impact on aggregate demand. For instance, the expiration of various Covid relief programs represents the removal of more than $25 billion *per month* in consumer spending power over the course of 2022.[2]

The second reason is math. Year-over-year comparisons for inflation should improve due to the lapping of higher prices one year ago.

For financial markets, the absolute condition of a particular variable is frequently less important than its direction of change. As it relates to inflation, provided the incoming data on inflation can transition from being incrementally-worse to being incrementally-better, we suspect investors' fears about a monetary policy mistake might subside materially.

Ukraine

We believe the second major risk factor driving recent stock market volatility is the possibility of a military conflict in Ukraine. With the Pentagon having joined NATO allies to organize military resources around Ukraine, the risk of military conflict with Russia seems very real.

Our View on Ukraine

As with Fed policy, we are on the optimistic side of the spectrum regarding potential outcomes in Ukraine. We currently subscribe to the view that if Russia really wanted a confrontation, it would have done it quietly. Instead, the well-advertised military movements Russia has been executing for *many months* served to *lower* Russia's probability of a successful military operation by providing time for Ukraine and its allies to prepare defenses. Our baseline expectation is for the conflict to be diffused before it escalates into a military conflict.

Investment Considerations

I. We entered the recent rise in interest rates with a relatively short duration in our **Fixed Income** strategies to improve their resilience to higher rates.
II. We have been migrating the **Managed Equity Growth** strategy toward a broader mix of factor exposures beyond "growth" for more than a year. Examples include the trimming (not selling completely) of leading growth stocks like **Apple** (AAPL), **Nvidia** (NVDA), and **PayPal** (PYPL), while increasing positions in sectors like industrials, financials, energy, and commodities (growth stocks can be particularly vulnerable to rising interest rates).
III. In the **Managed Equity Dividend** strategy, we recently sold **Ares Management** (ARES) and reduced the position in **Blackstone** (BX) to prepare for an expected shrinking of the Fed's balance sheet. Both companies are leading players in private equity, which has been a major beneficiary of central bank asset purchases (QE) by serving as a major transmission channel for this massive wave of liquidity.

---

[2] Source: St. Louis Fed; Moody's Analytics; Barron's

IV. We have also established a meaningful a meaningful position in energy within the **Managed Equity Dividend** strategy, while adding to companies that produce industrial metals like copper, iron ore, aluminum, and lithium.

V. The **Dynamic Allocation** strategy entered 2022 with 40% of its allocation in short-term Treasuries and cash reserves. We expect this strategy to shift toward an even more defensive posture over the next two weeks if domestic equity markets remain near current levels (international equities were sold in 2021).

VI. The recent market environment serves as a reminder of the value of balance in a diversified portfolio. **Fixed Income** may be boring, but it serves its purpose to protect capital and reduce volatility when the stock market hits a pothole.

VII. The resilience of **Fixed Income** is cause for celebration in times like these, but we do not believe investors need to increase their allocation to bonds at this time – assuming one's asset allocation was thoughtfully designed in the first place, stick with it.

VIII. For investors working their way into stocks from a position of cash, we believe the right approach is to keep going. We combine a systematic process with discretionary "rifle shots" when we migrate portfolios into the stock market from a position of cash. We have been firing rifle shots throughout the downturn and anticipate doing more if it continues.

Disclosures

Security Recommendations: The investments presented are examples of the securities held, bought and/or sold in the Capital Advisors strategies during the last 12 months. These investments may not be representative of the current or future investments of those strategies. You should not assume that investments in the securities identified in this presentation were or will be profitable. We will furnish, upon your request, a list of all securities purchased, sold, or held in the strategies during the 12 months preceding the date of this presentation. It should not be assumed that recommendations made in the future will be profitable or will equal the performance of securities identified in this presentation. Capital Advisors, Inc., or one or more of its officers or employees, may have a position in the securities presented, and may purchase or sell such securities from time to time.

This commentary does not purport to be a statement of all material facts relating to the securities mentioned. The information contained herein, while not guaranteed as to accuracy or completeness, has been obtained from sources believed to be reliable. Opinions expressed herein are subject to change without notice.

The **S&P 500 Index** seeks to track the performance of 500 large companies listed on stock exchanges in the United States. It is one of the most commonly followed equity indices.

As with any investment strategy, there is potential for profit as well as the possibility of loss. Capital Advisors does not guarantee any minimum level of investment performance or the success of any portfolio or investment strategy. All investments involve risk (the amount of which may vary significantly) and investment recommendations will not always be profitable. The investment return and principal value of an investment will fluctuate so that an investor's portfolio may be worth more or less than its original cost at any given time. The underlying holdings of any presented portfolio are not federally or FDIC-insured and are not deposits or obligations of, or guaranteed by, any financial institution.

Past performance is not a guarantee of future results. Capital Advisors, Inc. does not provide tax or legal advice and recommends you consult with your tax and/or legal adviser for such guidance.

Additional information, including management fees and expenses, is provided on Capital Advisors' Form ADV Part 2, available upon request or at the SEC's Investment Adviser Public Disclosure site, https://adviserinfo.sec.gov/firm/summary/104643

Presentation is prepared by: Capital Advisors, Inc. and is considered to be supplemental to a compliant presentation.
www.capitaladv.com

2022.01.26