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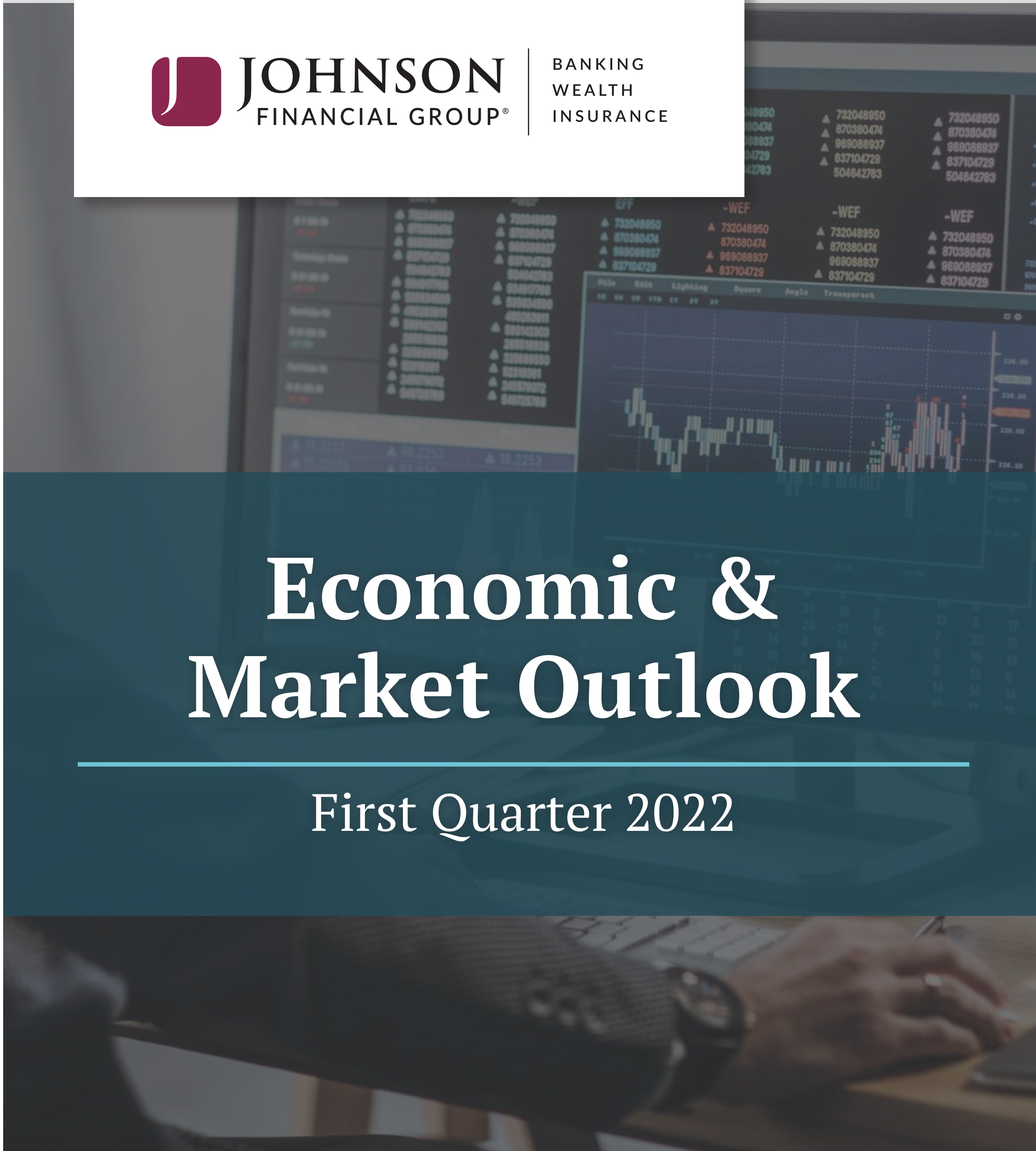


Economic & Market Outlook

First Quarter 2022

Investment Team Contributors

Brian Andrew, CFA
President & Chief Investment Officer

Ron Alberts, CFA
Senior Vice President, Director of Fixed Income Strategy & Portfolio Manager

David Carroll, CFA
Senior Vice President, Director of Complements Strategy & Portfolio Manager

Annette Hellmer, CFA
Senior Vice President, Portfolio Manager

Jason Herried, CFA
Senior Vice President, Director of Equity Strategy & Portfolio Manager

Brian Schaefer
Vice President, Portfolio Manager

Eric Trousil, CFA
Senior Vice President, Portfolio Manager

Executive Summary

Despite an extended pandemic and the uncertainty that comes with it, the economy and financial markets performed admirably in 2021. Stock returns exceeded expectations, rewarding investors with another year of excellent growth. As we enter 2022, we believe the economy is poised for another year of solid growth as the recovery transitions from stimulus-driven to one based on traditional fundamentals.

The Economy

- Following a very strong recovery in 2021, U.S. economic growth is expected to slow but remain robust. We expect GDP growth to exceed 4% in 2022.
- Consumer spending will continue to drive the economy. Despite record high home prices, the housing sector should continue to grow faster than the overall economy.
- Supply chain disruptions and a shrinking labor market have pushed inflation to the highest annualized level in nearly 40 years. We expect these pressures to ease in 2022. Inflation levels will remain elevated but closer to normal as the year progresses.

Fixed Income

- Credit spreads continued to narrow during 2021, driving outperformance in the corporate bond sector. The resulting yields leave the sector open to bouts of volatility in 2022 should economic data disappoint.
- Improving fundamentals and the possibility of higher taxes have resulted in record flows into the municipal segment. This has driven after-tax yields below those of similarly rated corporate bonds for even those investors in the highest tax brackets.
- Chairman Powell has shown a willingness to pivot as economic conditions change, and we expect this will continue. While we expect strong economic growth and corporate fundamentals to endure, we are taking a slightly defensive posture within fixed income and have reduced interest rate risk with a below benchmark duration target.

Equity Markets

- The reopening of the economy led to an earnings boom and a 29% gain for the S&P 500 Index.
- Returns are likely to be more subdued in the coming year as investors adjust to an investment landscape with Fed rate hikes, limited fiscal stimulus and what may be stubbornly high inflation while growth rates slow from an elevated level.
- While recession risk remains low without reinstated pandemic restrictions, high inflation, U.S. mid-term elections and geopolitical risks bear watching in the coming year.

Economic Outlook

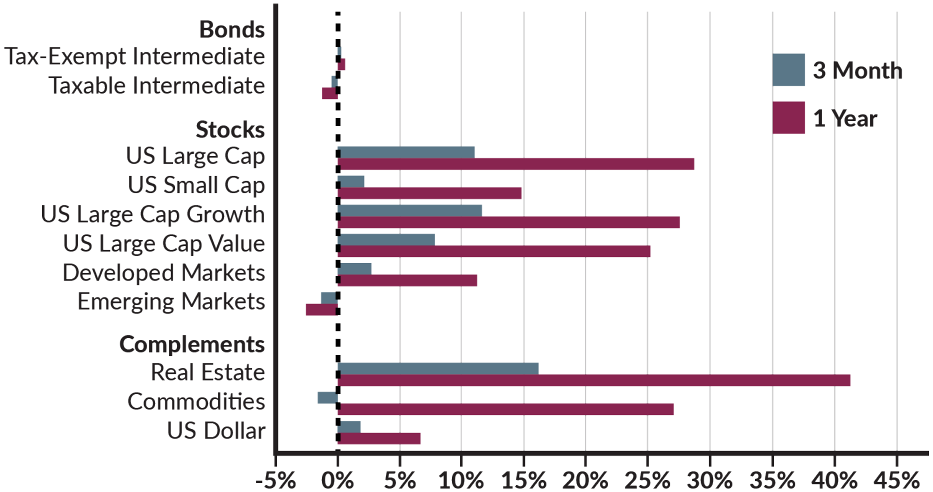
Economic growth is expected to remain strong in 2022 following robust gains in 2021. The recovery has been uneven thus far with varied results across different countries and economic sectors, still driven largely by the continued impact of COVID-19. The disruptive effects of the pandemic should continue to wane as progress is made on increasing vaccination rates and the availability of more effective treatments. We expect that growth in 2022 will be slower than 2021 — but still strong.

Consumer demand remains solid driven by household net worth (now near all-time highs), solid wage growth and accommodative financial conditions. The recent surge in coronavirus cases fueled by the omicron variant could potentially dampen growth in the early part of 2022. However, we expect any supply-constrained shortfalls in the early part of the year will eventually be made up by strong consumer demand.

Economic activity in 2022 will benefit from the continued reopening, pent-up consumer demand, and moderation of supply chain and labor constraints. The recent supply chain bottlenecks have resulted in a reduction of inventory levels that will need replenishing. This will further support economic growth.

Figure 1

3-Month and 1-Year Performance
As of December 31, 2021



Source: Morningstar Direct

Strong demand for housing will also contribute to growth in the coming year and likely beyond. Residential investment should remain robust as low mortgage rates, solid wage gains and demand from millennials—who are transitioning from renting to owning homes—continue to drive strong demand. Looking forward, we expect real GDP to post multiple quarters of growth higher than the pre-pandemic norm of 2.0-2.5, as shown in ***Figure 2***.

Labor shortages have been one of the biggest challenges impacting the business community, and the inability to hire workers has hampered growth.

- The Labor Force Participation Rate in the U.S. averaged 62.85% from 1948 until 2021, reaching an all-time high of 67.30% in January of 2000.
- At the onset of the pandemic, the level dropped from 63.3% to 60.2%. It has since recovered to 61.8% but remains near its lowest level in 45 years.
- Among prime-age people (between ages 25 and 54), the participation rate fell from 82.9% to a low of 79.8%. It has since recovered to 81.8% but remains depressed.

There are approximately 5 million fewer workers than at the pre-pandemic low for unemployment. Where have these workers gone? ***Figure 3*** tells the story.

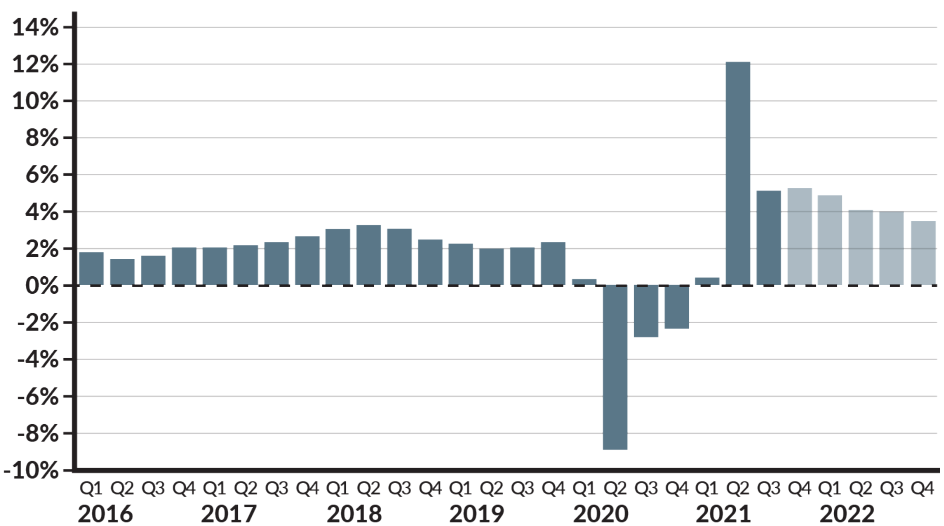
The decline in the workforce is attributable to several factors. Federal Reserve Chairman Jerome Powell said in recent testimony that strong asset and home price gains have likely caused some people to leave the workforce, particularly those who found that they now had the financial means to retire. These workers may never return. However, those leaving the workforce for other reasons such as fear of contracting COVID, childcare/home-schooling issues, and generous support programs may return as excess savings are depleted. Higher wage rates should create additional incentive for people to reenter the workforce, making it likely that labor force participation will increase in 2022.

Throughout the pandemic, businesses have learned to adapt to disruptions and pivot as needed to find solutions to deal with supply constraints and labor shortages. Adoption of new technologies has accelerated, and increased use of robotics and digitization may result in ongoing productivity improvements for years to come, ultimately increasing our country's economic output.

Figure 2

Real GDP Percent Change Year Ago

Quarterly, SAAR



Source: Bloomberg

Figure 3

Worker Shortages: Other Departures

Millions of Workers

Source: BLS, Census, GS, JPMAM, as of October 2021.

In the short run, the supply constraints and labor shortages are contributing to elevated levels of inflation. As these conditions improve, inflation should begin to move back toward trend levels, though both growth and inflation are likely to remain elevated in 2022 compared to long-term trends.

Fixed Income

Credit is King

Treasury yields rose off a low base in 2021, resulting in negative total returns for broad-based investment grade bond indices. The Bloomberg Intermediate US Aggregate Bond Index declined -1.29%, which was only its third negative annual return since 1987.

Short-term yields rose more than long-term yields, resulting in a flatter yield curve ***[Figure 4]***. The flattening confounded investors who expected above-trend growth and inflation to put upward pressure on long bond yields. Instead, with Core CPI running at 5% and the 10-Year Treasury yield finishing the year at 1.5%, real (inflation adjusted) yields turned deeply negative.

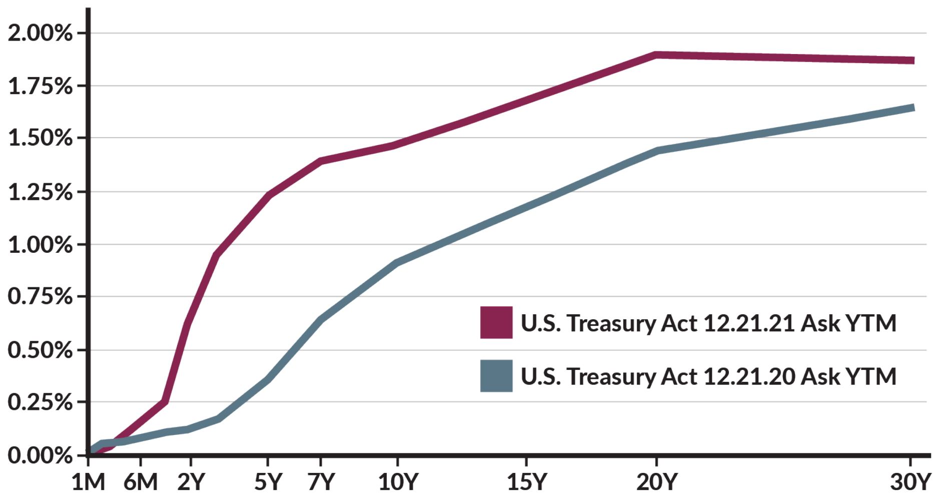
Corporate bonds outperformed as credit spreads narrowed, especially among below investment-grade issuers. Both high yield bonds and bank loans, their floating-rate cousins, rose more than 5% in 2021, driven by investor demand for their high coupons and improving fundamentals. Furthermore, investors expect few defaults among high yield issuers. We may even see the default rate test its all-time lows in 2022 with a drop below 2%. Still, tight spreads leave both investment grade and high yield corporate bonds subject to bouts of volatility in 2022 if economic data disappoints.

State and local governments hauled in $500 billion of federal aid over the last two years, bolstering municipal balance sheets and emboldening investors to buy the debt of lower quality issuers. The S&P Municipal Bond Index rose 1.77%, while high yield municipals rose an astounding 6.82% in 2021.

In addition to improving fundamentals, expectations for possible tax increases continue to drive demand for tax-exempt municipals. Combined flows into municipal bond funds and ETFs exceeded $100 billion last year, the highest on record. The imbalance of supply and demand has left valuations stretched. After-tax yields for municipal bonds are below those of similarly rated corporate bonds even for investors in the highest tax brackets ***[Figure 5]***.

Figure 4

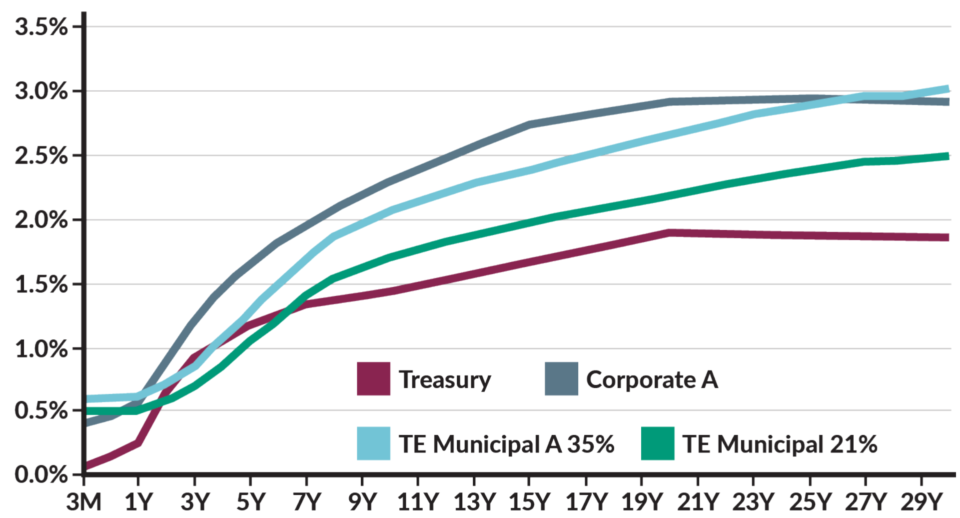
Flattening Yield Curve



Source: Bloomberg Finance L.P.

Figure 5

Tax Exempt Bonds Are Rich



Source: Bloomberg Finance L.P.

The combination of low interest rates, federal and monetary stimulus, and economic reopening has been a boon to borrowers of all stripes since the pandemic. Investors have been rewarded for dipping down in credit quality as corporate profits surged and tax revenues rebounded. Lofty valuations will vie with robust demand and strong fundamentals to determine if credit retains its crown in 2022.

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Powell Pivots (Again)

When criticized for changing his position, the famous economist John Maynard Keynes replied, "When the Facts Change, I Change My Mind. What Do You Do, Sir?"

Fed Chairman Jerome Powell appears to share the sentiment.

Powell's Fed raised interest rates and even began reducing its sizeable balance sheet in 2018 before pausing in the face of a slowing economy and stock market correction. The Fed then cut rates aggressively in 2020 in response to the pandemic and began a new round of bond buying that increased its balance sheet by more than $4 trillion. Powell later announced a new framework to reflect the Fed's commitment to an expanded definition of full employment and pledged to allow inflation to run above its 2% target for an undefined period. The Fed's price stability mandate appeared to be a second priority after a decade of benign inflation.

In his most recent pivot, Powell in November took a hawkish turn, abandoning the term "transitory" to describe the recent spike in inflation and accelerating the Fed's taper timeline. The Fed will now wind down its balance sheet expansion by March of this year instead of June, paving the way for rate hikes later in the year. In fact, the Fed now projects three quarter-percentage-point interest rate increases over the course of 2022, a marked contrast to its earlier forecasts.

Despite the hawkish change in direction, the Fed's actions merely brought its interest rate forecasts in line with market expectations ***[Figure 6]***. In fact, Treasury yields were largely unmoved in the wake of the decision, with short rates having already risen to yields last seen in early 2020.

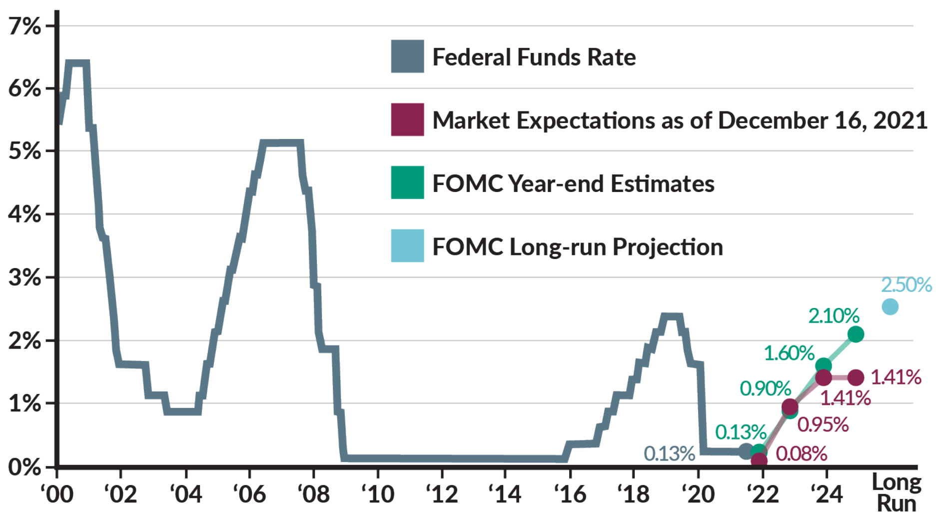
The Fed's shift in focus from unemployment to inflation makes sense when viewed alongside its most recent Summary of Economic Projections. The FOMC's median projection for inflation in 2022 moved up from 2.2% in September to 2.6% in December, while the committee forecast an unemployment rate of 3.5% by the end of 2022, down from the 3.8% projection in September.

The facts are changing, and so is the Fed.

Figure 6

Federal Funds Rate Expectations

FOMC and Market Expectations for the Federal Funds Rate



Source: Bloomberg, FactSet, Federal Reserve, J.P. Morgan Asset Management

2022 Playbook. Same as 2021?

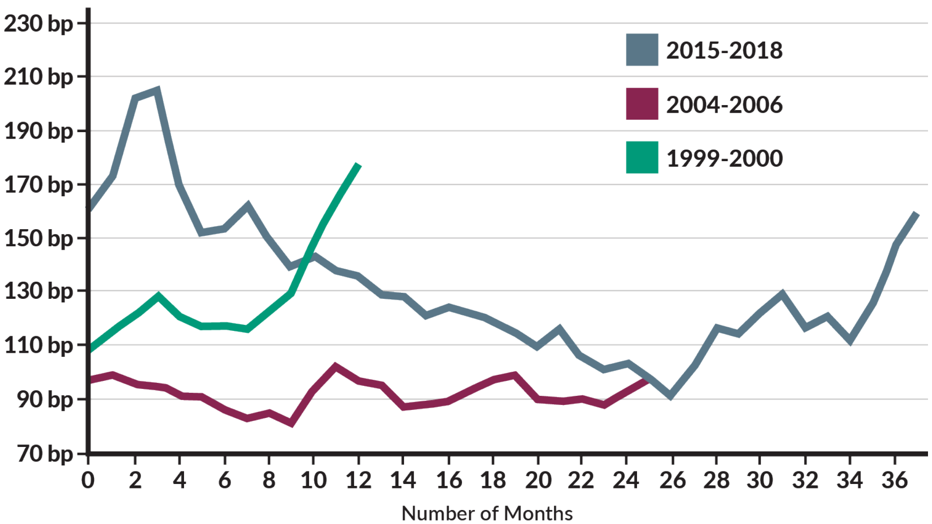
We have entered a new phase of this economic cycle. Less accommodative monetary policy is on the horizon as policymakers shift to focus on inflation. The Fed expects a gradual rise in the Fed Funds rate to 2.1% by the end of 2024. Fixed income performance in 2022 will depend in large part on how successful Powell and company are at maintaining a gradualist approach.

Recent rate hiking cycles suggest that rising rates alone do not cause credit spreads to widen. Investment grade credit spreads declined for much of the 2015-2018 hiking cycle and remained near current levels throughout the entire 2004-2006 cycle ***[Figure 7]***.

If the Fed is patient, as we expect, we believe economic growth and corporate fundamentals will remain robust and supportive of credit markets. Persistent inflation is the biggest risk to our outlook. If the Fed is forced to raise interest rates aggressively, credit markets will be volatile and bond investors will need to be nimble. We therefore remain modestly overweight corporate credit but maintain a quality bias. We also continue to favor non-traditional bonds including asset-backed securities and emerging market bonds, where valuations remain attractive.

Figure 7

Rising Rates and Credit Spreads



Source: CreditSights, FactSet, ICE Data Indices, LLC, Bloomberg, L.P.

We believe today's deeply negative real yields are unsustainable in the face of a strong economy and less Fed accommodation. Treasury demand from foreign investors, pension funds, and insurance companies should remain robust, but investors are unlikely to accept below inflation returns in perpetuity. Once tapering is complete, investors' focus will turn to potential reduction of the Fed's $9 trillion balance sheet, which could be the catalyst for higher long-term bond yields. We expect the 10-year Treasury to move gradually higher and approach 2% by the end of 2022.

Above-trend growth, rising yields, and strong fundamentals suggest to us that a modest overweight to credit and a bias toward short and intermediate-term bonds remains the correct positioning heading into the new year. Inflation and an overzealous Fed is the wild card that poses the biggest risk to our outlook. We will be watching the data closely, and if the facts change, so will we.

Equity Markets

U.S. Stocks

U.S. stocks finished with another year of very strong returns with large cap stocks up 29% and small cap stocks up 15%. The year started off strong as the reopening of the economy boosted company earnings. The positive earnings revision trend continued through the year despite a mid-year resurgence of the virus. In fact, positive earnings surprises nearly matched the calendar year return and added to what is expected to be a 50% increase in earnings in 2021 compared to 2020.

While earnings growth was strong and above expectations, full year returns diverged across different segments of the stock market. U.S. small cap stocks and value stocks traded largely sideways after the robust gains in the first quarter. These more economically sensitive segments of the market faced growth headwinds from a resurgence of the virus and falling interest rates.

Contrarily, after mediocre returns in the first quarter, U.S. large cap growth stocks resumed leadership for the balance of the year as investors sought the comfort found with the low debt levels, strong cash flow generation and secular growth for the large technology companies that dominate the category. While this rotation made for a resilient year for a diversified index like the S&P 500, concerns are mounting that too much money is crowding into a small number of stocks.

The top 10 stocks in the S&P 500 make up 31% of the index, which is up from about 20% at the beginning of this bull market (2008). For context, at the peak of the technology bubble in 2000, this figure was roughly 28%.

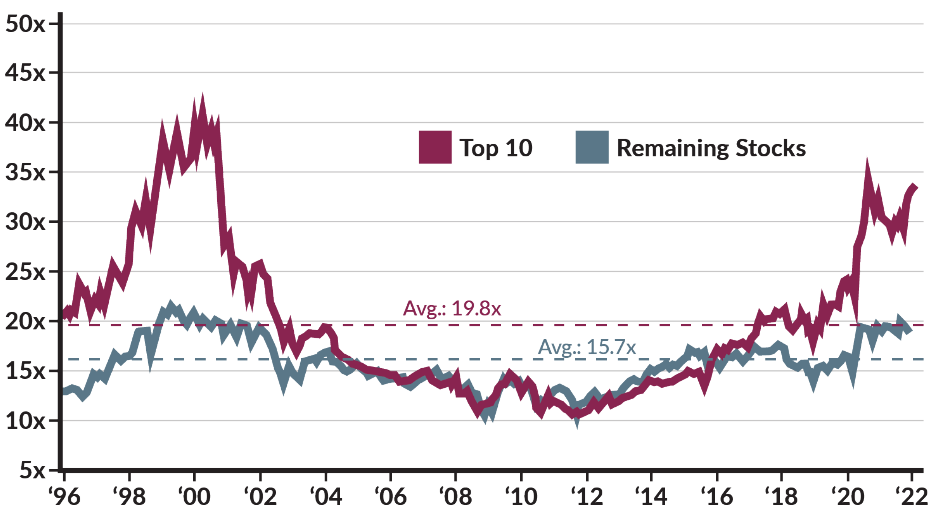
This concentration is partially due to tremendous earnings power, as these companies contribute 26% of the earnings of the index. The remainder is explained by price appreciation, which has pushed the valuation of the top 10 stocks to a price-to-earnings (P/E) ratio of 33.2x compared to 19.7x for the remaining stocks in the index.

Figure 8 shows the historical valuation of the top 10 stocks and the remainder. At present, valuations are high for both segments, but here our focus is primarily on the gap, which illustrates the significance the top 10 stocks have made to overall index performance… and suggests a risk to valuations should strong sentiment wane.

Figure 8

P/E Ratio of the Top 10 and Remaining Stocks in the S&P 500

Next 12 Months



Top 10 S&P 500 Stocks: Apple 6.8%, Microsoft 6.5%, Amazon 3.9%, Tesla 2.3%, Alphabet Cl A 2.2%, Alphabet Cl C 2.1%, Meta 1.9% (f.k.a. Facebook), NVIDIA 2.1%, Berkshire Hathaway 1.3%, JPMorgan Chase 1.2%, Johnson & Johnson 1.2%

Source: FactSet, Standard & Poor's, JPMorgan Asset Management, as of December 31, 2021

International Stocks

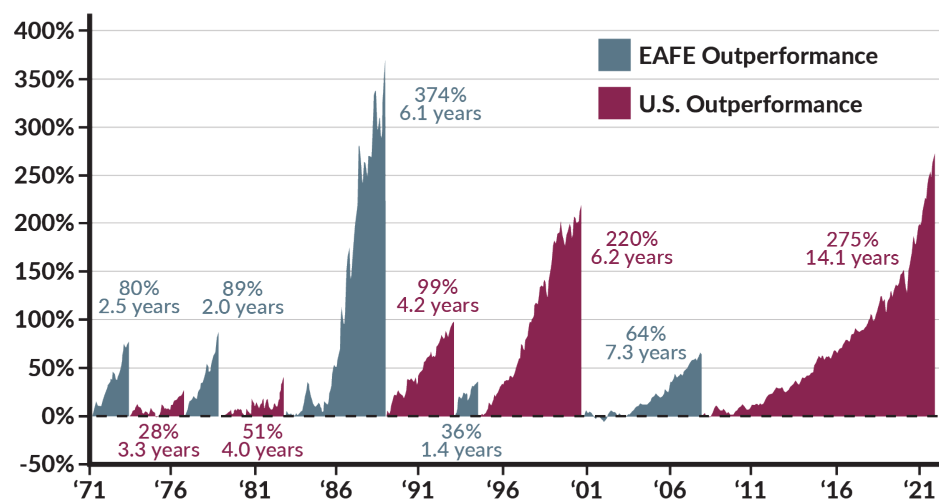
Like small cap and value stocks, international stocks had a good start to the year with double-digit returns heading into late May. However, international equity markets were pressured by disappointing economic growth as governments reimposed restrictions related to the Delta variant mid-year and, more recently, the Omicron variant. In addition, Chinese markets fell double-digits due to a troubled real estate sector and a regulatory crackdown that cut the stock prices of many of the largest Chinese technology stocks by 50% or more.

These lackluster returns of 2021 add another year to what's now a 14-year stretch of international-market underperformance to U.S. stocks—substantially longer than the historical cycle of three to seven years ***[Figure 9]***. This record run is due to an extended period of outperformance by large U.S. technology companies in addition to the slower recovery for the global economy after the Great Financial Crisis in 2008.

Figure 9

MSCI EAFE & MSCI USA Relative Performance

U.S. Dollar, Total Return, Cumulative Outperformance



Source: FactSet, MSCI, Standard & Poor's, JPMorgan Asset Management, as of December 31, 2021

Equity Outlook

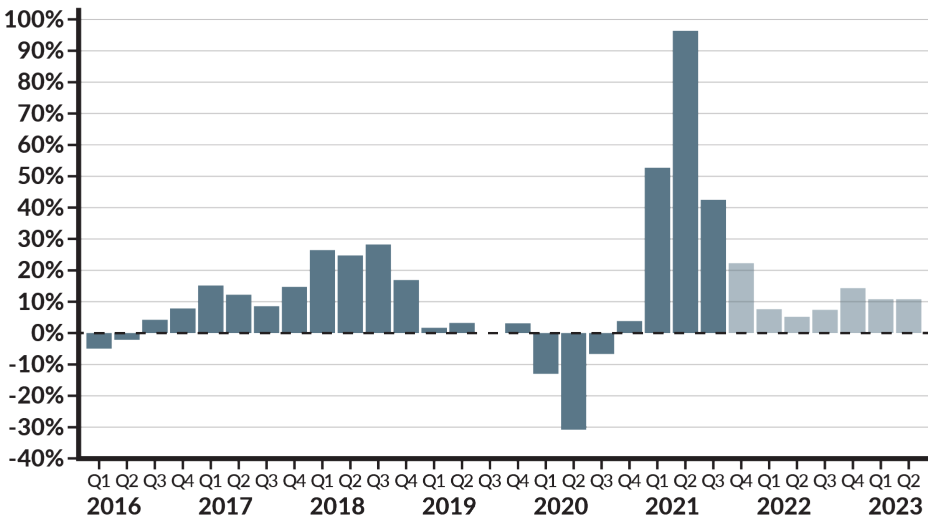
As we turn the corner into 2022, stocks are facing increasing turbulence as many facets of the investment environment are changing. While the headwinds are more significant in 2022, as detailed in ***Figure 10***, we nonetheless expect another positive year on the back of continued earnings growth and an economic cycle likely to last multiple years. S&P 500 earnings are forecast to increase a solid 8-10% in 2022, which would be a solid rate of increase on top of the gaudy growth rates of 2021.

While the earnings picture serves as the foundation for equity returns in the long-run, remember that back-to-back years of fiscal stimulus and accommodative monetary policy—and bullish sentiment—have led to elevated valuations. Investors faced a relatively smooth ride in 2021 with the largest decline for the S&P 500 Index just over 5%.

Figure 10

S&P 500 Operating Earnings Growth

vs. Year Ago Period



Source: Refinitiv, as of December 17, 2021

2022 may be less smooth. The following are some of the risk factors that may trigger higher volatility in the coming year.

PANDEMIC

While we are hopeful that the pandemic will have a smaller impact on our lives in 2022, Omicron is a good example of how quickly the outlook can change.

EARNINGS GROWTH

S&P 500 earnings are expected to increase 8-10% in 2022. However, if economic growth underwhelms while inflation pressures remain high, both earnings and stock returns may disappoint.

FEDERAL RESERVE

If the pace of Fed rate hikes is slow, as is currently projected, the stock market typically moves higher as financial conditions tighten only moderately. However, if growth and inflation remain high, the Fed may be forced to take more aggressive action to tighten financial conditions.

MID-TERM ELECTIONS

Stock market returns have historically been below average in mid-term election years due to uncertainty and because economic growth is often slowing after the actions taken to boost growth in years one and four of the President's term.

GEOPOLITICS

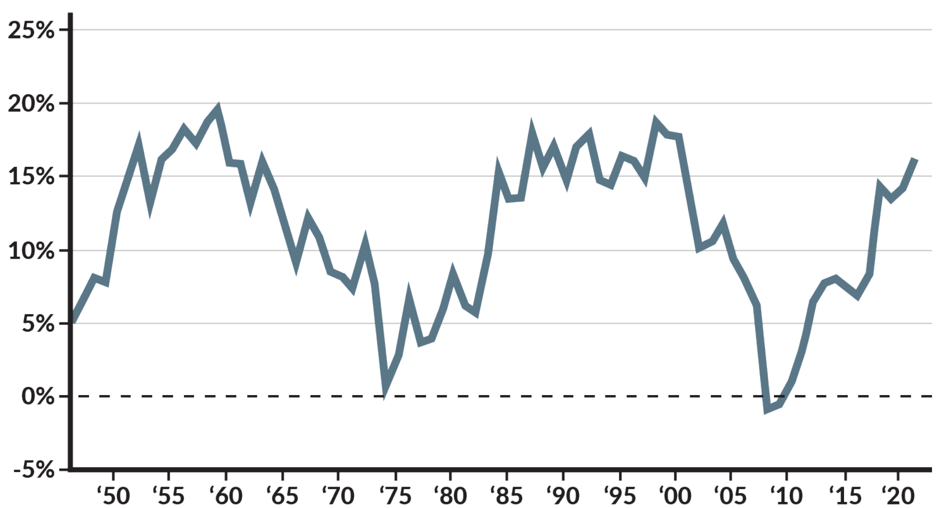
The pandemic has suppressed many of the tensions facing the globe. Tensions with Russia and China are among the areas that we are watching.

As we enter a year in which volatility will likely be higher, it is a good time to put equity investments in perspective. Over the last 10 years, returns have averaged 16% annually, compared to the long-term average of 10% ***[Figure 11]***. Investors have bid up valuations to achieve the above average return over the past 10 years. A return toward more normal valuation levels would mean below average returns over the next 10 years. Based on our outlook for equity returns over the next 10 to 15 years, we expect equities to return 4 to 6% on average per year.

Looking shorter term, it is also important to remember that equity returns are positive in about 7 out of 10 years despite experiencing one or two 5% to 10% corrections each year ***[Figure 12]***. The years in which stocks experience large declines are typically those in which earnings decline, such as during a recession.

Figure 11

S&P 500 Rolling 10-Year Returns



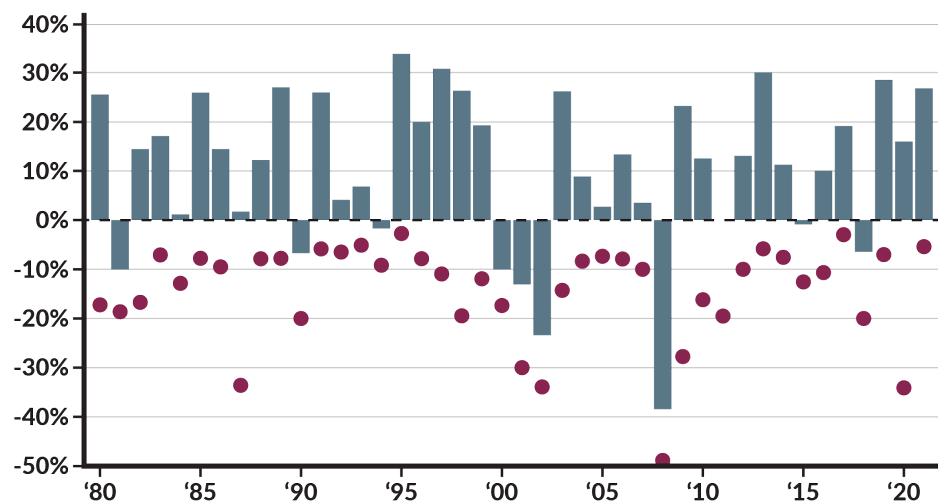
Source: Morngingstar Direct

We believe the odds of a recession in the foreseeable future are low. Other circumstances that could lead to an above average correction (15-20%) include high valuations, high inflation that impacts profit margins, an oil price shock and geopolitical events. Despite some of these headwinds, we continue to believe that a diversified allocation to equities remains a relatively attractive investment over the coming three to five years.

Figure 12

S&P 500 Intra-Year Declines vs. Calendar Year Returns

Average Intra-Year Drops of 14.3%, Annual Returns Positive 31 of 41 Years



Returns are based on price index only and do not include dividends. Intra-year drops refers to the largest market drops from a peak to a trough during a year. For illustrative purposes only. Returns shown are calendar year retuns from 1980 to 2020, over which time peroid the average annual return was 9.0%.

Source: FactSet, Standard & Poor's, J.P. Morgan Asset Management.

Portfolio Positioning & Summary

Given our expectations of above trend economic growth in 2022 and upward pressure on interest rates, we favor equity investments over traditional fixed income at this time. Within equities, we think the wide gap in valuations between U.S. and international stocks should narrow during 2022, which favors international stocks. Overseas economies have not recovered at the same pace as the U.S., primarily due to slower adoption of the vaccines. Within fixed income, we have taken a slightly defensive posture and have reduced interest rate risk with a below benchmark duration target.

For portfolios with an allocation to complements, we have an overweight to the asset class. The allocation to complements is funded 30% from equities and 70% from fixed income and cash. Within complements, we favor private credit and infrastructure. Private credit should benefit from a stronger economy (healthy merger and acquisition activity) and higher interest rates. Most private loans carry floating rates based on a short-term index. Infrastructure assets (real estate, commodities, transportation) should also benefit from an improving economy and further government spending focused on infrastructure.

To summarize, we believe the economy is on solid footing as we move into 2022. Fed policy and inflation will be key components to watch as the economy transitions from the very accommodative policies of the pandemic. The positive news of the past year is currently reflected in both equity and fixed income markets. So, expect surprising economic data of an unpleasant nature to cause sharp volatility. We will be watching the data closely and will adjust as needed.

We thank you for your partnership and trust in Johnson Financial Group. We look forward to working with you in 2022.