



by DOUG SANDLER, CFA

THE RIVERFRONT WRITING TEAM

REBECCA FELTON
Senior Market Strategist

CHRIS KONSTANTINOS, CFA
Director of Investments |
Chief Investment Strategist

KEVIN NICHOLSON, CFA
Global Fixed Income Co-CIO |
Co-Head of Investment Committee

DOUG SANDLER, CFA
Head of Global Strategy

ROD SMYTH
Chairman of the Board of Directors

SUMMARY

- Global supply chains are currently clogged-up.
- We think it will be mid-to-late 2022 before things return to normal.
- Because we think inflation will be transitory, we remain overweight stocks.

11.15.2021

Inflation's Return is Not Surprising

Whether It's Structural or Transitory Remains the Million-Dollar Question

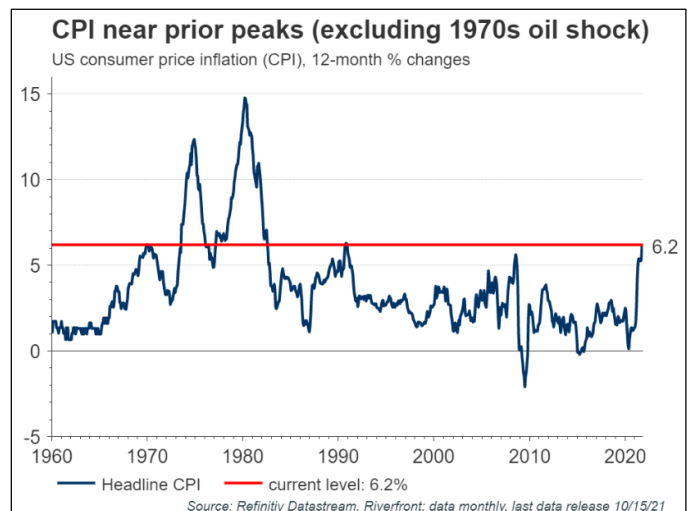
That 1968 Chevrolet Chevelle convertible in the picture used to be mine. I say 'used to' because owning it was a headache. Because I used it rarely, every time I went to take it for a spin, it would either not start or leave me stranded a long way from home. At first, I thought it was just 1968 engineering and that



old engines were not as technologically advanced and reliable as they are today. However, that thesis was quickly disproven when I had the same issue with a brand-new 2015 motorcycle. The simple fact is that machines are 'born to run' and regular usage keeps their many parts lubricated and in working condition.

Global economies and global supply chains are far more complicated and fragile machines. Therefore, we should expect some difficulty restarting them after leaving them dormant for 18+ months. Complications will occur and disruptions should be anticipated. It is natural to assume such issues will multiply if those machines are immediately placed

under stress before having ample time to 'warm up'. This is exactly what has happened across the world over the last 6 months. Just as producers were trying to get restarted and warmed up, consumers were leaving their COVID-19 quarantines with pockets full of savings and a desire to spend. This intersection of depleted supplies and torrential demand has caused prices to rise quickly and has stoked inflation fears. October's reading of the Consumer Price Index (CPI), released last week, noted that prices have risen by 6.2% over the past year, which was the highest annual inflation rate since August 1991 (see chart above).



Shown for illustrative purposes. Not indicative of RiverFront portfolio performance.

STRUCTURAL OR TRANSITORY?

The stakes are high regarding the answer to that question since structural inflation could severely damage investment values. Unfortunately, we do not believe that there is enough data to definitively answer that question yet. Complicating matters is the uniqueness of the COVID-19 shutdown making comparisons with other inflationary periods (especially the 1970's) problematic. For this reason, it is probably not appropriate to project today's difficulties into the future and assume that world economies are destined for 'stagflation' (low or no growth along with high inflation).

We continue to believe that inflation will prove to be transitory. Importantly, however, we do not define transitory as 'quick'. Instead, we believe that inflation aftershocks will continue to reverberate into 2022. Our benign longer-term view is due to the following factors:

INFLATION MITIGATORS

For inflation to prove transitory, there must be mitigators to combat rising prices. Fortunately, there are a few which we are watching:

1. Supply:

- **Labor:** According to the Bureau of Labor Statistics' latest report, there are 7.4 million unemployed workers in the US. This means there are 1.7 million more unemployed workers than the number that existed prior to COVID-19 (February 2020). Getting those workers back to work will be a key in lessening supply constraints on the services sector. Rising wages for low-cost workers and the expiration of Federal enhanced unemployment benefits appear to be having a positive impact. For example, October's payroll gain of 531,000 jobs was well-above economist's forecasts and reversed a two-month trend of disappointing job growth numbers.
 - **Automation:** Unfortunately, getting the unemployment rate back to pre-COVID-19 levels may not be enough to completely reduce labor pressures. This is because roughly 2.3 million workers left the US workforce during the pandemic and are currently not seeking re-employment. Given that necessity is the mother of invention, the automation of labor-intensive tasks may be a solution. For example, according to Progressive Grocer, the delivery of self-checkout terminals surged by 25% in 2020 and can now be found in many non-grocery retailers, like drug and discount stores. Similarly, 'labor-light' solutions are beginning to be utilized throughout the economy in areas like food service (mobile ordering and check-out) and healthcare (wearable monitors and the utilization of robotic assistants).
 - **Logistics:** By now most of us have either heard of the logistical bottlenecks plaguing the recovery or have experienced it first-hand. Like many of the issues affecting the supply-chain there is no 'magic bullet'. However, a combination of several efforts should eventually ease some of these obstacles. One such effort is President Biden's October announcement that US ports would expand their operating hours to 24/7. The transportation industry is also attempting to address the trucker shortage by accelerating their testing of self-driving trucks. For example, Wal-Mart, the country's largest retailer announced last week that they were now operating two driverless box trucks near their Bentonville headquarters. While regulatory approval and full adoption is likely several years away, we are encouraged by the rising valuations and recent IPOs of companies that manufacture electric/autonomous vehicles. We think this influx of capital should provide the funds and the motivation to accelerate this timetable.
2. **Demand:** Inflation is often defined as 'too much money (demand) chasing too few goods (supply)', therefore, one inflation mitigator would be a decrease in demand. We can see this happening a couple of ways. First, as the economy fully re-opens, consumers will be able to increasingly spend on services, like travel and entertainment, which should alleviate some of the pressure on the supply-chain for goods. Second, we think pent-up savings from the economic shutdown will eventually be exhausted, returning spending to more normal levels.

DIFFERENT MESSAGES FOR DIFFERENT INVESTORS

Distribute & Sustain Investors: Inflation is called the 'thief in the night', because it can rob investors without detection. It goes undetected because it robs purchasing power, which generally is not noticed until it is too late. To put it into

perspective, when inflation is at 2%, a portfolio would have to grow by 49% over 20 years to maintain purchasing power. If inflation rises to 6%, that same portfolio would have to grow more than 4 times faster (221%) to keep up. Generating faster growth can be difficult given that distribute and sustain investors tend to have portfolios laden with bonds and little prospects for growth. **Our view on a potential remedy is to increase stock allocations, and to adopt a total return mindset where spending needs are met from portfolio income and systematic withdrawals of principal.** The degree of that adjustment and the appropriate balance of spending from income and/or principal is best determined by your financial advisor. **RiverFront's balanced portfolios remain significantly underweight fixed income and moderately overweight equities relative to their benchmarks.**

Accumulate Investors: Inflation can reduce the value of stocks and real-estate, especially if it is structural and significant. Furthermore, inflation can have an exaggerated effect on the growth stocks that accumulate investors tend to favor. This is because growth stocks tend to generate their earnings far into the future, and future earnings are less valuable when inflation is high. **Therefore, in our Advantage portfolios we have gradually added more cyclical stocks, whose earnings can be expected to benefit from inflationary trends, to complement the growth stocks we already own.**

Important Disclosure Information

The comments above refer generally to financial markets and not RiverFront portfolios or any related performance. Opinions expressed are current as of the date shown and are subject to change. Past performance is not indicative of future results and diversification does not ensure a profit or protect against loss. All investments carry some level of risk, including loss of principal. An investment cannot be made directly in an index.

Chartered Financial Analyst is a professional designation given by the CFA Institute (formerly AIMR) that measures the competence and integrity of financial analysts. Candidates are required to pass three levels of exams covering areas such as accounting, economics, ethics, money management and security analysis. Four years of investment/financial career experience are required before one can become a CFA charterholder. Enrollees in the program must hold a bachelor's degree.

Information or data shown or used in this material was received from sources believed to be reliable, but accuracy is not guaranteed.

This report does not provide recipients with information or advice that is sufficient on which to base an investment decision. This report does not take into account the specific investment objectives, financial situation or need of any particular client and may not be suitable for all types of investors. Recipients should consider the contents of this report as a single factor in making an investment decision. Additional fundamental and other analyses would be required to make an investment decision about any individual security identified in this report.

Stocks represent partial ownership of a corporation. If the corporation does well, its value increases, and investors share in the appreciation. However, if it goes bankrupt, or performs poorly, investors can lose their entire initial investment (i.e., the stock price can go to zero). Bonds represent a loan made by an investor to a corporation or government. As such, the investor gets a guaranteed interest rate for a specific period of time and expects to get their original investment back at the end of that time period, along with the interest earned. Investment risk is repayment of the principal (amount invested). In the event of a bankruptcy or other corporate disruption, bonds are senior to stocks. Investors should be aware of these differences prior to investing.

Investing in foreign companies poses additional risks since political and economic events unique to a country or region may affect those markets and their issuers. In addition to such general international risks, the portfolio may also be exposed to currency fluctuation risks and emerging markets risks as described further below.

Changes in the value of foreign currencies compared to the U.S. dollar may affect (positively or negatively) the value of the portfolio's investments. Such currency movements may occur separately from, and/or in response to, events that do not otherwise affect the value of the security in the issuer's home country. Also, the value of the portfolio may be influenced by currency exchange control regulations. The currencies of emerging market countries may experience significant declines against the U.S. dollar, and devaluation may occur subsequent to investments in these currencies by the portfolio.

Foreign investments, especially investments in emerging markets, can be riskier and more volatile than investments in the U.S. and are considered speculative and subject to heightened risks in addition to the general risks of investing in non-U.S. securities. Also, inflation and rapid fluctuations in inflation rates have had, and may continue to have, negative effects on the economies and securities markets of certain emerging market countries.

When referring to being "overweight" or "underweight" relative to a market or asset class, RiverFront is referring to our current portfolios' weightings compared to the composite benchmarks for each portfolio. Asset class weighting discussion refers to our Advantage portfolios. For more information on our other portfolios, please visit www.riverfrontig.com or contact your Financial Advisor.

For each outcome category (accumulate, sustain and distribute) RiverFront's portfolio management team has assigned one or more RiverFront product(s) based on their assessment of the product's investment objective as it relates to a typical client's return and risk objectives when seeking investment outcomes of accumulating wealth, sustaining wealth and distributing wealth. The team has also designated RiverFront product alternatives for those clients looking to take more or less risk with the outcome category. The 'more aggressive' (or more risk) alternatives will generally have greater equity and international exposure as well as longer time horizon targets, while those designated as 'more conservative' (or less risk) will have fewer equities, a lower exposure to international and shorter time horizon targets. Since the risk assessments are dependent on the outcome category selected, RiverFront products may fall in multiple categories. All investments carry a risk of loss and there is no guarantee that an investment product or strategy will meet its stated objectives.

RiverFront Investment Group, LLC ("RiverFront"), is a registered investment adviser with the Securities and Exchange Commission. Registration as an investment adviser does not imply any level of skill or expertise. Any discussion of specific securities is provided for informational purposes only and should not be deemed as investment advice or a recommendation to buy or sell any individual security mentioned. RiverFront is affiliated with Robert W. Baird & Co. Incorporated ("Baird"), member FINRA/SIPC, from its minority ownership interest in RiverFront. RiverFront is owned primarily by its employees through RiverFront Investment Holding Group, LLC, the holding company for RiverFront. Baird Financial Corporation (BFC) is a minority owner of RiverFront Investment Holding Group, LLC and therefore an indirect owner of RiverFront. BFC is the parent company of Robert W. Baird & Co. Incorporated, a registered broker/dealer and investment adviser.

WEEKLY VIEW

To review other risks and more information about RiverFront, please visit the website at www.riverfrontig.com and the Form ADV, Part 2A. Copyright ©2021 RiverFront Investment Group. All Rights Reserved. ID 1921991