WINTER 2022 | VOL. 30 | NO. 1
QUARTERLY PERSPECTIVE

DVI
DAVID VAUGHAN INVESTMENTS

Will Williams *Chairman, President & CEO*

EXPECT THE UNEXPECTED

As an investment advisory firm, you have very little time, if any, to smell the roses at year end. Within a blink of an eye, the new year is upon you and the performance clock starts ticking away once again. It is a time of reflection for sure, trying to gain a better understanding as to what worked, what fell short of expectations and how that might impact future decision-making at Investment Committee meetings. David Vaughan often talked about the advantages of "being long in the tooth" and the fact that our clients benefited from the myriad of mistakes that we have collectively made in the past and hopefully have gained the wisdom and discipline to avoid making in the future. One thing is for sure, much like 2021, we can be quite confident as we roll into the new year, we should "expect the unexpected."

Inflation Expectations

If you polled economists in December of last year as to their forecast for inflation (CPI) in 2021, the average prediction would have been for an increase between 2 and 2 ½ percent. This would be in keeping with the year-over-year rate of inflation experienced in the U.S. over the prior decade. What these economists did not see in their crystal ball were two significant developments: 1) The significant recovery in energy prices from 2020 levels and 2) The increase in durable goods prices as demand recovered and COVID induced supply chain issues disrupted inventories. As the chart below depicts, well over half of the year-over-year increase in CPI of nearly 7 percent (the highest since 1982) was attributable to just these two factors. These CPI categories are described as flexible inflation indicators and tend to be cyclical and short-lived in nature. Sticky inflation factors such as rent and wage growth, tend to be more structural and persist in the economy for longer periods of time. Sticky indicators increased in 2021, albeit not at the significant rate of change of the flexible indicators.

If there is a consensus forecast for 2022, most economists are predicting a moderating inflation environment, especially in the back half of the year. The range appears to be an annual rate of increase between 3 and 3 ½ percent. The rational for this conclusion is that the supply chain bottleneck at the ports have and will continue to improve as the year progresses. In addition, the base rate for energy prices is now much higher than in 2020, and similar year-over-year price increases in 2022 will be difficult to replicate.

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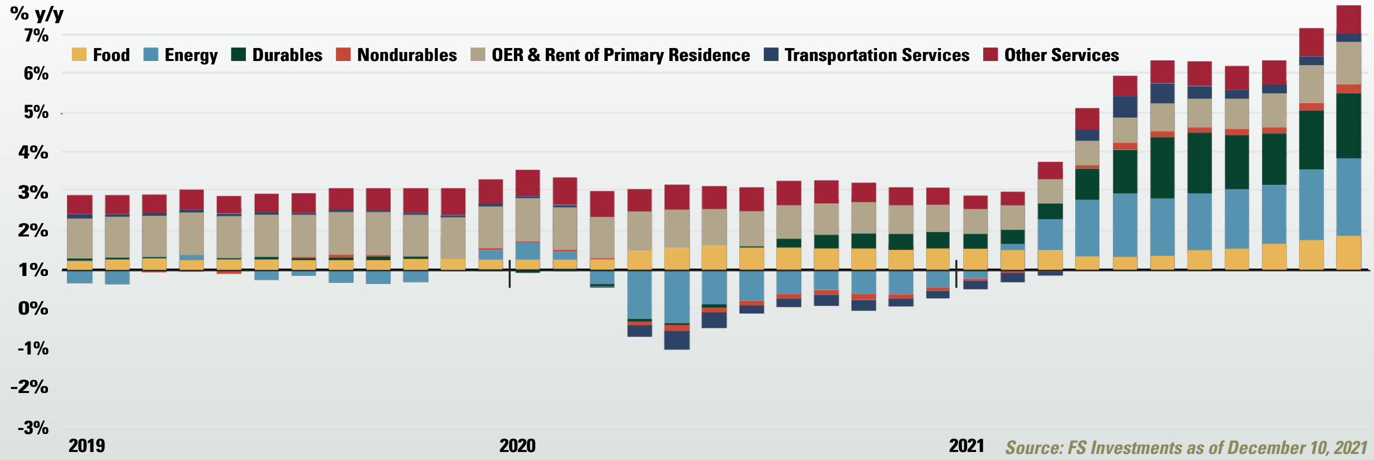
CONTRIBUTION TO THE CONSUMER PRICE INDEX



Source: FS Investments as of December 10, 2021

RISING INTEREST RATES – BULLISH OR BEARISH FOR STOCKS?

History says stock investors shouldn't fear rising interest rates. No question, there have been time periods in history where rising interest rates have coincided with poor stock market returns. The 1970's was certainly an era when stocks suffered significantly from higher interest rates. However, I believe today is quite different simply for one reason. The level of interest rates today is far lower than those seen in the 1970's. If, in fact, the economy is staging for a lengthy surge in inflation, which forces the Fed to raise rates more aggressively, we are starting from a significantly lower base than what we experienced in the 1970's. Having the yield on the 10-year Treasury Bond go from 1.5% to 3.0% (the range of Wall Street predictions for 2022) does not have the same impact as going from 6% to 11% as was experienced between 1971 and 1979.

The relationship between interest rates and stock prices can be seen in the two tables below.

10-Year Treasury Yield and Stock Prices

Rising Rates Start Date	Rising Rates End Date	Duration (Months)	Change in 10-Year Treasury Yield	S&P 500 Gain/Loss
12/26/1962	8/29/1966	44.7	1.70%	18.3%
3/16/1967	12/29/1969	34.0	3.60%	1.3%
3/23/1971	9/16/1975	54.6	3.20%	-18.1%
12/30/1976	9/30/1981	57.8	9.00%	8.7%
5/4/1983	5/30/1984	13.1	3.90%	-7.9%
8/29/1986	10/16/1987	13.8	3.30%	11.8%
10/15/1993	11/7/1994	12.9	2.90%	-1.4%
1/19/1996	7/8/1996	5.7	1.50%	6.7%
10/5/1998	1/21/2000	15.8	2.60%	45.8%
6/13/2003	6/28/2006	37.0	2.10%	26.0%
12/30/2008	4/5/2010	15.4	1.90%	33.3%
7/24/2012	12/31/2013	17.5	1.60%	38.1%
7/8/2016	10/5/2018	27.3	1.90%	35.5%
3/9/2020	2/25/2021	11.8	1.00%	39.4%
	Average	25.8	2.90%	17.0%
	Median	16.6	2.40%	15.0%
	% Positive			78.6%

Source: LPL Research, FactSet

According to Sam Stovall, CFRA's chief investment strategist, history shows that prior Fed tightening led to minor price increases for stocks over the ensuing year. Since 1946, the Fed has launched seventeen rate-tightening cycles. Thirteen of them consisted of three or more rate increases, with nine occurring within a 12-month period. From the date of the first rate hike until the third, the S&P 500 rose a median of roughly 3.5% and gained in price 56% of the time. The table on page 3 highlights data back to 1983 which supports Mr. Stovall's position.

While textbooks will suggest that the relationship between interest rates and stocks is negatively correlated, the data tells a different story. Why?

In theory, higher interest rates should lead to lower stock prices as corporate earnings and future cash flows get discounted with a higher interest rate. But as witnessed time and again, theory often gets surpassed by reality. In this case, the trump card is often economic and earnings growth. Simply, if interest rate increases are a function of faster economic growth leading to better corporate earnings, stocks will

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FED RATE INCREASES AND STOCK PRICES

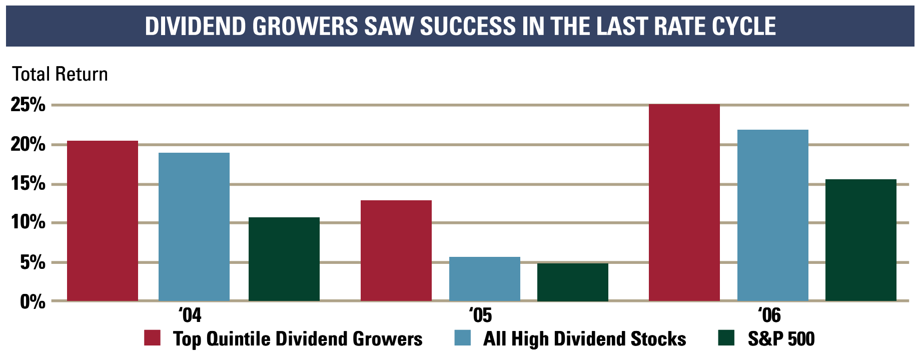
FED RATE INCREASES						S&P 500		
Start Date	End Date	Start Rate	End Rate	Increase	Number of Raises	Start	End	% Change
3/31/83	8/11/83	8.50%	9.56%	1.06%	6	152.96	161.55	5.62%
3/29/84	8/9/84	9.38%	11.50%	2.13%	4	159.52	165.54	3.77%
1/24/85	3/28/85	8.13%	8.50%	0.38%	3	176.71	179.54	1.60%
7/25/85	9/6/85	7.69%	8.00%	0.31%	3	192.06	188.24	-1.99%
4/2/86	4/2/86	7.25%	7.32%	0.07%	1	235.71	235.71	0.00%
5/22/86	6/5/86	6.75%	6.88%	0.13%	2	240.12	245.65	2.30%
1/5/87	5/22/87	5.88%	6.75%	0.88%	3	252.19	282.16	11.88%
8/27/87	9/24/87	6.63%	7.31%	0.69%	4	331.38	319.72	-3.52%
3/30/88	5/17/89	6.50%	9.81%	3.31%	16	258.07	317.48	23.02%
2/4/94	2/1/95	3.00%	6.00%	3.00%	7	469.81	470.4	0.13%
3/25/97	3/25/97	5.25%	5.50%	0.25%	1	789.07	789.07	0.00%
6/30/99	5/16/00	4.75%	6.50%	1.75%	6	1372.7	1466	6.80%
6/3/04	6/29/06	1.00%	5.25%	4.25%	17	1116.6	1272.9	13.99%
12/16/15	12/19/18	0.25%	2.50%	2.25%	9	2073.1	2507	20.93%
							Avg S&P 500 Return	6.04%
							Median S&P Return	3.04%

CONTINUED FROM PAGE 2

respond positively. Rising interest rates do not have to be the death knell for equity markets. The trend in corporate earnings is key.

So, where should stock investors be focused when interest rates are on the rise? We would expect the Energy, Financial, and Basic Material sectors to lead. Also, companies that can increase prices with little or no impact on demand for their products and services will be leaders.

Finally, the chart to the right provides perspective on the stock performance of companies able to grow dividends during rising rate cycles. These companies will be more desirable as the growing stream of income from the dividends is a valuable tool in maintaining purchasing power.



Source: Bloomberg, Neuberger Berman. High-dividend stocks and top dividend growers include constituents of the Russell 3000 Index with at least a 2.5% dividend yield and $2 billion in market capitalization.

Despite enjoying exceptional investment returns, 2021 has been a year of many challenges. May we all be blessed with peace and good health in the new year. Thank you for your continued confidence in DVI.

CNBC RANKS DVI #21

David Vaughan Investments, LLC (DVI) is pleased to announce that CNBC has ranked our firm 21st out of the top 100 Registered Investment Advisory (RIA) firms in the United States. Annually, CNBC publishes their "FA 100" list, which ranks advisory firms across the nation that provide comprehensive planning and financial services. CNBC stated that the intent of the FA 100 list is to highlight various factors that an investor should consider when hiring a financial advisory firm, such as fiduciary responsibility, range of services, investment strategy and compensation.

The analysis started with an initial list of 38,302 RIA firms. The ranking methodology considered many factors, such as number of years in the business, number of employees, disclosures, ratio of investment advisors to total number of employees, total assets under management, percentage of discretionary assets under management and total accounts under management. CNBC also applied weighted categories to further refine and rank each firm.

Will Williams, DVI's President and CEO remarked, "2021 is the third consecutive year in which we have been recognized as an RIA industry leader, each year making considerable progress in our overall ranking. We are honored and humbled with this recognition, but we continue to understand the ultimate gauge of firm success is the achievement of financial goals and objectives by our valued clients. We are passionate about "Building a Firm to Last" and serving as a trusted advisor to our clients for decades to come. This ranking is simply validation as we continue to make progress towards this end goal."

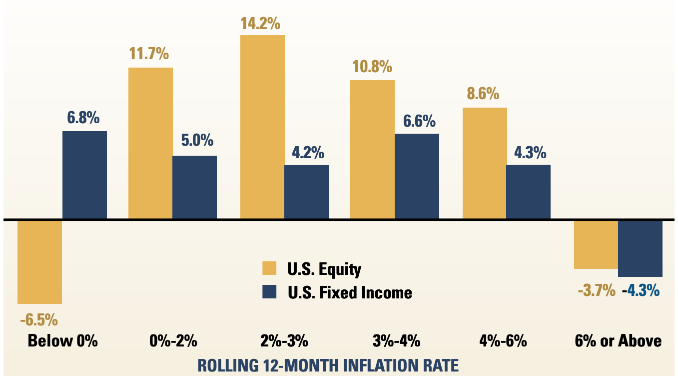
This rating is not indicative of DVI's future performance. The analysis for the CNBC FA 100 rating was conducted by CNBC with the assistance of AccuPoint Solutions, and neither the participating firms nor their employees pay a fee in exchange for inclusion in it. For more information regarding the CNBC FA 100, including the methodology and how the firms were selected, visit www.cnbc.com/top-rated-wealth-management-firms/.

Source: David Vaughan Investments, LLC

EXPECT THE UNEXPECTED | CONTINUED FROM PAGE 1

As investors tend to view inflation as a headwind for equity prices, the chart below is a historical reminder that moderate inflation as a sole factor is not an impediment for positive investment results. In fact, so long as you avoid deflation or hyperinflation, average annual rates of return for the equity market tend to be consistently positive.

AVERAGE ANNUAL RETURNS AT DIFFERENT INFLATION RATES | 1970-2021



Source: Capital Group as of November 30, 2021

Valuation Divergences

Another trend that persisted in 2021 was the valuation divergence between high P/E (Price /Earnings) stocks and the rest of the market. As illustrated in the chart below, the top 100 companies traded on average at next twelve-month (NTM) market multiples nearly three times that of the rest of the S&P 500. So, when we look at market multiples of the broad market, it is heavily influenced by these high-priced growth stocks rather than inflated prices for all index constituents.

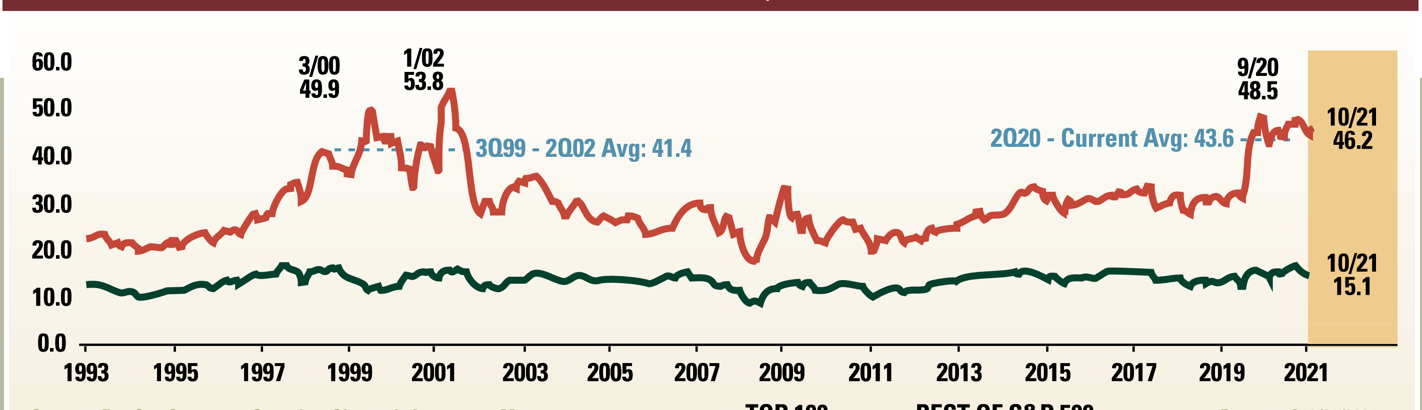
It is hard to argue against the fact that there is a speculative element in the U.S. stock market today. Record inflows into the U.S. equity market, stock option trading volumes exceeding stock trading volumes for the first time ever, crowded trades on certain mega cap technology stocks, all these facts point to the same conclusion. However, all stocks are not priced to perfection, and the ten stocks that now represent more than 30% of the market capitalization of the S&P Index might behave much differently than their lesser valued peers.

The Rest of the Story

No different than in past years, there is no shortage of items to worry about as we enter into 2022. COVID-19 continues to exist as a Pandemic in the form of the Omicron variant and is surging to record numbers of positive cases every day. Fed Policy makers have communicated their intent to reduce quantitative easing measures in the first quarter of 2022 and have indicated the growing possibility of increasing the Fed Funds target rate three times (.75 of 1%) throughout the year. Corporate Earnings are expected to show growth in 2022 (+9.2%), but down significantly from the (+45%) calendar year results anticipated for 2021. China's economic growth prospects are waning as they continue to struggle with the fallout from their speculative real estate bubble. A slowing China will have a material impact on the demand for global goods and services and overall economic activity. Lastly, mid-term elections will soon be upon us, with all the fiscal and tax policy unknowns that are part and parcel with that process.

With that as our investing backdrop, we once again set the stage for a year that will undoubtedly be full of challenges and unexpected outcomes. There is a real benefit in DVI embracing a fundamental road map towards investing. Rather than focusing on things that do not make logical sense, we can always navigate towards investment strategies that we not only understand but also provides our valued clients with meaningful peace of mind.

100 MOST EXPENSIVE COMPANIES BY NTM PRICE/EARNINGS VERSUS REST OF S&P 500



Sources: FactSet, Compustat Snapshot, Glenmede Investment Management
Past results are not indicative of future performance
Data as of 10/31/2021