Ameriprise Financial

2022 Investment Outlook &Themes

An Ameriprise Global Asset Allocation Committee publication

December 15, 2021

David Joy | VP - Chief Market Strategist
Anthony M. Saglimbene | VP - Global Market Strategist
Brian M. Erickson, CFA | VP - Fixed Income Strategy
Russell T. Price, CFA | VP - Chief Economist
Justin H. Burgin | VP - Equity Research

Contents

NOTE: FOR IMPORTANT DISCLOSURES, INCLUDING POSSIBLE CONFLICTS OF INTEREST, PLEASE SEE THE DISCLOSURE PAGES AT THE END OF THIS DOCUMENT.

Key Points

2022 Outlook Summary

Reopening momentum across the globe could continue to see fits and starts due to ongoing pandemic effects. However, the economic expansion should broaden to more countries and regions as the year unfolds, in our view. Financial conditions should also remain favorable for risk assets, including stocks if more pent-up demand is satisfied, supply chains normalize, and inflation growth eases. Notably, central bankers in the U.S. and other large developed countries could tighten monetary policies in response to inflation pressures. Yet, interest rates should remain largely accommodative for most of the year. While investors should hold a fairly optimistic view for growth and returns in 2022, markets have traveled a long way since the depths of the pandemic. Therefore, we believe investors should review their financial plans carefully, ensure proper diversification based on risk, and set realistic return expectations given that market/economic trends could shift from "extraordinary" toward "ordinary" during the year.

2022 S&P 500 year-end price target: 4,950

Stock prices in the U.S. offer further upside as long as pandemic conditions improve, corporate earnings continue to grow, and inflation pressures do not materially erode profit margins. We forecast the S&P 500 to rise by roughly +7.0% in 2022, based on full-year earnings growth of +8% to +10%. Nevertheless, valuations remain elevated. We suspect stock prices could become more sensitive to monetary policies and changes in interest rates during the year. As a result, expect more modest returns across broad U.S. averages and the potential for more substantial returns internationally. Notably, stock selection could play a more significant role in 2022 than in recent years.

2022 U.S. Real GDP target: +4.5%

We believe consumer spending will likely remain fairly strong in 2022, particularly as consumers rebalance their spending allocations back toward services from the outsized allocations to goods in recent quarters. Consumers enter the year in sound financial shape, in our view, as does the businesses sector. U.S. growth could see a further boost from inventory restocking and increased government spending on infrastructure. After starting the year near multi-decade highs, we believe inflation could steadily subside beginning in the second quarter, and any increases in interest rates emerging from tighter Fed policy should be economically digestible.

2022 10-Year U.S. Treasury yield target: 2.00%

In our view, bond yields could drift higher in 2022 as monetary policies begin to normalize, pandemic effects fade, and inflation remains above longer-term trends. As a result, we believe the Federal Reserve could lift its Fed Funds target rate by two quarter point hikes in 2022.

Market Performance

Sector	Index	U.S. Dollar Terms 2020*	2021**
Equity	S&P 500	+18.4%	+25.1%
	Russell 3000	+20.9%	+22.0%
	MSCI World ex USA	+7.6%	+8.9%
Fixed Income	Bloomberg US Universal	+7.6%	-1.1%
	Bloomberg US Corp HY	+7.1%	+4.3%
	Bloomberg Global Trsy Ex-US	+9.5%	-7.4%
	JPM EMBI Global	+5.9%	-1.5%
Alternatives	Wilshire Liquid Alternative	+3.2%	+4.4%
	Bloomberg Commodity	-3.1%	+23.0%
	Gold	+25.1%	-6.5%
Oil & Currency	WTI Oil Prices ($ per barrel)	-24.4%	+46.3%
	US Dollar Index	-6.7%	+7.4%
Cash	FTSE Treasury Bill 3 Month	+0.6%	+0.04%

Sources: Morningstar Direct, FactSet, and American Enterprise Investment Services Inc. *Total return. ** Total return data as of 12/14/2021.

2021 Review

Much of what we outlined in our 2021 Market & Economic Themes (shown below) developed as the year unfolded. But as is the case every year, admittedly, the original script went through some edits along the way. Available COVID-19 vaccines indeed were a significant contributor to helping reopen the world this year, with areas such as the U.S., parts of Asia, and Europe leading the way out of the pandemic. Yet, economic growth accelerated across most of the globe in 2021 but was more pronounced in the developed world versus longer-term averages, particularly in countries and regions where vaccines were more readily available.

In combination with very easy monetary policies and the added fuel of fiscal stimulus, consumers in the U.S. were flush with cash, despite an employment backdrop that spent most of the year recovering the jobs lost in March/April of 2020. Ultimately, strong consumer balance sheets helped fuel pent-up demand, boost corporate profits and economic activity while driving dislocations across supply chains. As a result, inflation pressures became more pronounced as the year wore on.

Notably, companies across several industries and regions were able to raise prices, expand profit margins, and experience year-over-year earnings growth well above historical norms. In our view, that made the bullish narrative for overweighting stocks over bonds a relatively easy call through most of the year. With that said, more S&P 500 companies cited inflation pressures on their Q3 earnings calls than at any other time in the last ten years. As the degree of earnings outperformance has declined and supply chain/inflation pressures linger, investors are becoming more concerned about companies' ability to outperform profit expectations next year.

2021 Market & Economic Themes

• The global economy reopens as vaccine availability grows and treatments improve.	• Broad stock market returns should be positive, though valuations are high.
• Global growth returns unevenly based on local COVID-19 conditions and fiscal /monetary policy responses.	• U.S. small-caps and international equities offer investing opportunities.
• The Biden administration focuses on the pandemic and reengages with traditional allies to address common challenges.	• Bond yields are likely to remain compressed around the globe through 2021.
• Trade tensions ease. Developed economies slowly coalesce in a multilateral approach to address issues related to China.	• Cyclicals lead the way in both stocks and bonds. But don't abandon growth areas.
• Global growth accelerates. The U.S. and Asia lead the pandemic-period recovery.	• Defaults should peak in the first half of 2021.
• Monetary and fiscal policies offer tailwinds for economic growth and asset prices.	• Favor stocks over bonds, though a sound diversification strategy built on high-quality assets should help insulate from the unexpected.
• Inflation levels rise, and the U.S. dollar weakens — both moderately. Government policies adjust on the margins.	

In terms of markets, the S&P 500 Index has risen +25% for the year thus far. Nevertheless, market leadership in the U.S. ebbed and flowed throughout 2021, with cyclical value and small-caps performing well at the beginning of the year but giving back ground to growth areas, such as Technology, as the year wound down. Slowing growth trends, the rise of the Delta COVID-19 variant, and inflation concerns created bouts of uncertainty for investors throughout the year. This kept the tug-of-war for market leadership between industries tied directly to the reopening theme and industries more exposed to longer-term secular drivers front and center.

From a global perspective, the U.S. was an area of strength all year, showing it had the right mix of growth and value stocks tied to a dynamic economy leading the world in terms of reopening. And while returns in Europe were strong, its delayed start to emerging from the pandemic, more restrictive COVID-19 policies, and heavier reliance on global trade modestly weighed on stock performance. In Asia, stocks spent the better part of the second half of the year grappling with unexpectedly stricter regulations out of China, Beijing's zero-COVID-19 policies, and a debt problem across China's property market. These factors weighed on the Hang Seng Index this year, which is primarily where foreign investors gain access to China stocks. Slower growth in China also weighed on stock returns in the region, though India, Taiwan, and some inter-China stock indexes performed well. Overall, however, broader emerging market returns were hamstrung by developments in China this year.

Yields around the globe showed increased volatility but remained mainly compressed through most of the year. After spiking higher in the first quarter on rising inflation concerns, the 10-year U.S. Treasury yield essentially spent the year reacting positively to inflation concerns (i.e., the yield moving up) and negatively to slowing growth/pandemic concerns (i.e., the yield moving down).

At the close of the year, a new COVID-19 variant (Omicron), the potential for tighter central banker policies in 2022, and a slowing growth environment have given investors pause after a nearly +110% gain in the S&P 500 from the pandemic lows in March 2020. In our view, it's natural for markets and investors to take a pause given a still uncertain pandemic environment. However, as our themes and outlook identify in the coming pages, there is room for asset prices to modestly rise next year, particularly as more of the world emerges from the pandemic.

2022 Market & Economic Themes

Big Picture Themes	Why is it important?
A year of transition — moving from extraordinary toward ordinary.	The last two years marked a period of unusual developments and market/economic responses. The macro-environment could downshift toward more regular patterns in 2022 but remain conducive for growth.
Pandemic effects could fade with more of the world emerging from COVID-19.	Increased global vaccination rates could promote growth, more robust economic activity and help monetary/fiscal policies normalize over time.
Markets look past ongoing geopolitical issues and the U.S. mid-term elections.	Ongoing U.S./China tensions could simmer in the background, while the U.S. mid-term elections create a battleground for control of Congress. However, investors are likely to look past the drama given growth trends.

Economic and Policy Considerations	Why is it important?
Global supply chain pressures should ease as the year wears on. Notably, the pace of inflation is likely to moderate.	As bottlenecks clear, supply and demand should find a more balanced level as the year wears on. Easing base effects and increased supply/demand equilibrium should also help reduce price pressures in 2022. However, trends in wage inflation and ongoing pandemic policies (ex. COVID zero in China) are risks to a more normal environment.
Consumers enter 2022 in strong financial condition, a position that should support economic growth for some time.	In our view, consumers could shift their focus from goods to services in 2022. Excess savings, an improving labor market, and pent-up demand should help the U.S. economy grow above its longer-term potential.
The U.S. and Europe continue to grow above trend, as does the rest of the world.	The U.S. and Europe should continue to lead the world back toward normal. But economic growth could accelerate in other parts of the world, which could help broaden the expansion.
Monetary policies could become less accommodative but remain supportive throughout the year.	The Federal Reserve is "pot committed" and unlikely to materially surprise investors. However, the market may face increased challenges as accommodation is removed. With that said, we believe global monetary policy should help support above-trend growth next year.

Stock & Fixed Income Themes	Why is it important?
Stock returns should be positive. However, slowing profit growth and elevated valuations may limit gains.	U.S. equities could post high-single-digit total returns in 2022. Although global stock valuations largely reflect the favorable backdrop, slower to reopen international markets could offer opportunities.
Stay long cyclical stocks, but dividend payers may add value as growth normalizes.	Cyclical sectors continue to offer investors an attractive risk/reward trade-off with below-market valuations and above-market dividend yields. Dividend-paying stocks could provide downside protection, a hedge against inflation, and a yield substitute to bonds.
Stock Selection & Disruptive Distribution.	Equity valuations are elevated with little room for earnings shortfalls in 2022, making stock selection critical to performance. Post-pandemic, companies that can adapt to the new normal via enhanced distribution, onshoring, and reinventing "just-in-time" manufacturing could offer attractive opportunities.
Beyond Fed purchases and rate policy.	Though the Fed is likely to become less accommodative in 2022, we believe massive liquidity extends through the year in the form of repurchase market support, M2 money supply expansion, and elevated personal savings. Also, we anticipate G7 central bank balance sheets to expand rather than contract, marking a semi-permanent imprint on global bond markets.
The year for floating-rate bonds.	With the Fed removing asset purchases and looking ahead to potential rate hikes, next year may be the year of the floater – both for investment-grade bonds and senior bank loan funds.

Portfolio Theme	Why is it important?
Mitigate unwanted risks and diversify.	We believe the easy gains off the pandemic bottom have been made. Although accommodative financial conditions support a favorable outlook, investors should stick with the basics of sound portfolio management.

Ameriprise 2022 Year-End S&P 500 Scenario Forecast

Favorable Scenario Macro Conditions

- 2022 U.S. real GDP advances by +5.0% or more amid fading pandemic challenges
- Global activity grows by more than +6.0% in 2021; Growing COVID-19 vaccine availability fuels broader growth
- U.S. employment levels surge as businesses reopen; Unemployment rate drops below 3.5% by year-end
- Inflation steadily eases through the year and does not prompt central bankers in the developed world to tighten monetary policies more than expected
- The Fed remains accommodative; The market looks through marginally tighter policies in 2022
- Growing dispersion between developed and emerging market monetary policies
- 2022 U.S. corporate earnings increase by +10% or more; Pent-up demand is satisfied; Companies hold profit margins
- U.S. 10-Year Treasury yield approaches 2.50% on stronger growth and Fed policy trajectory
- Supply bottlenecks and labor constraints improve more rapidly through 2022; Companies ability to meet surging demand quickens
- Other Market Considerations: Geopolitical risks have little impact on asset prices; "Buy-the-dip" market reactions remain supportive for higher asset prices, despite tighter monetary policy; Company earnings surprises decline from 2021 levels but remain elevated versus history

Trailing Earnings Multiple Estimate (P/E) = 23x

5,300

+14.5% from 12/14/21 level

2022 EPS Estimate = $230.00

Base Scenario Macro Conditions

- U.S. real GDP rises by +4.0% to +5.0% amid improving virus conditions, financially sound consumers, and government infrastructure outlays
- The global economy grows by roughly +6.0% in 2022, as pandemic threats fade
- U.S. employment levels continue to rebound; The unemployment rate falls to about 3.5% at year-end
- Inflation should remain at elevated levels through the first half of 2022; A tail risk includes persistent inflation that prompts central banks to tighten policy more aggressively than expected
- The Fed remains accommodative; Bond tapering ends by Q2; Potential for rate hikes later in the year
- G7 central banks remain accommodative; Growing dispersion between developed and emerging market monetary policies
- 2022 U.S. corporate earnings grow by roughly +8% to +10%; Earnings growth slows versus 2021 but remains above longer-term trends; Companies weigh profit margins against market share
- U.S. 10-Year Treasury yield rises toward 2.00% at year-end
- Supply bottlenecks and labor constraints improve slowly through the course of the year
- Other Market Considerations: Geopolitical risks (e.g., China) simmer in the background; "Buy-the-dip" market reactions become less influential as Fed accommodation is withdrawn; Company earnings surprises moderate toward historical averages

Trailing Earnings Multiple Estimate (P/E) = 22x

4,950

+7.0% from 12/14/21 level

2022 EPS Estimate = $225.00

Adverse Scenario Macro Conditions

- 2022 U.S. real GDP advances less than +4.0%, as inflation and supply chains remain problematic
- Pandemic pressures linger and slow the global economic recovery
- U.S. employment levels recover slowly; The unemployment rate ends the year at 4.0% or above
- A rising price environment becomes "sticky," producing higher non-core inflation expectations; Central bankers aggressively raise interest rates, slowing growth
- The Fed remains accommodative; Tail risks include tighter policy to curb inflation or easy policies to help stem ongoing pandemic pressures
- Other global central banks remain accommodative; Provide additional support if needed
- 2022 U.S. corporate earnings grow by 5% or less; Earnings growth is weaker than expected based on supply/inflation pressures and ongoing pandemic issues
- U.S. 10-Year Treasury yield remains near 1.50% on slowing growth
- Companies weighed down by supply bottlenecks and labor shortages; Results in negative impacts on corporate profits
- Other Market Considerations: Geopolitical risks play a more significant role in shaping asset prices; Market sentiment sours given inflation pressures and/or lingering pandemic effects; Fewer companies surprise to the upside on earnings with more missing analyst estimates

Trailing Earnings Multiple Estimate (P/E) = 20x

4,300

-7.0% from 12/14/21 level

2022 EPS Estimate = $215.00

2022 Outlook

2022 S&P 500 year-end price target: 4,950

Our market outlook for 2022 anticipates a continuation of the uptrend in U.S. equities, yet with the pace of gains moderating toward their long-term historical average. Another year of strong economic growth, accompanied by expected solid gains in corporate earnings, should allow stocks to extend the cyclical bull market that began in March 2020.

There remains significant pent-up demand throughout the economy, hindered by supply-chain bottlenecks and the ongoing effects of the pandemic. But these headwinds should slowly dissipate throughout the year, allowing corporate revenue growth to remain strong. At the same time, due to increased pricing power, corporations have been able to maintain their profit margins. Consequently, we believe earnings could grow by roughly 8% to 10% in 2022. While that might seem disappointing compared to the 45% expected earnings growth of 2021, it should be remembered that 2021 benefited from a burst of federal stimulus and far easier comparisons to the prior year. In our view, stocks will also be starting the new year with high valuations compared to history, limiting the extent of their upside potential.

There are several developments that investors need to watch carefully in 2022 that could lead to a rise in market volatility. First, Federal Reserve policy is evolving. The Fed is mindful of rising inflationary pressures, and as a result, has already begun to slow the pace of its bond-buying program. Along with an increasingly tight labor market, these trends could persuade the Fed to start raising interest rates in 2022. However, it is important to remember that monetary policy is likely to remain exceedingly accommodative for some time. In addition, stocks can continue to rise if a cycle of rising interest rates is slow and orderly. Conversely, if the Fed pushes rates higher and faster than investors expect, stock prices could come under pressure.

The year ahead is also a mid-term election year, in which stock market returns are historically positive, albeit the lowest on average of any year in a presidential term. History also indicates that, on average, market volatility rises as summer approaches and the election comes increasingly into focus. On a positive note, stocks tend to enjoy relatively strong returns in the twelve months after the election. Yet, we believe the return prospects for bonds are less favorable. On most debt instruments, low interest rates offer little income. In addition, rates may rise somewhat in the year ahead, pushing bond prices lower, offsetting some or all of what little income they do offer. Of course, bonds can provide diversification and protect against downside volatility should equity markets come under pressure. For that reason, maintaining some exposure to fixed-income investments remains a prudent strategy for many investors, in our view.

In addition to our constructive outlook for the U.S., we believe that certain international markets may also offer upside potential. In particular, we find equities within the Eurozone attractive, owing to their less challenging valuations and greater sensitivity to a recovering global economy. In addition, monetary policy in the Eurozone looks poised to remain even more accommodative for longer than in the U.S. For that potential to be realized, however, the Eurozone must continue to make progress against the pandemic, and the strains in the global supply chain must dissipate over time as we anticipate. We are relatively less enamored of Asian markets and emerging markets more generally. Overall, we expect a well-diversified portfolio to achieve modestly positive returns in 2022. However, given the evolution of domestic monetary policy, mid-term elections, and the persistence of the pandemic, we may experience somewhat higher volatility. Making certain tactical adjustments within a portfolio may help mitigate those uncertainties while still allowing for a focus on the longer term.

Global Asset Allocation Committee 2022 Targets

Key Measure	2021 Actual	2022 Target	Implied Change
U.S. Real GDP	+5.5%*	+4.5%	-1.0 pp
S&P 500 Index**	4,634	4,950	+7.0%
10-year Treasury Yield**	1.44%	2.00%	+0.56%
Fed Funds Target	0.00% to 0.25%	0.50% to 0.75%	+0.50%

Source: American Enterprise Investment Services Inc.; FactSet
pp = percentage points
* Estimated, 2021 Actual based on year-end values
**as of December 14, 2021

Actions to Consider

- Incorporate a constructive investment view based on solid fundamentals but balance opportunities against elevated valuations.
- Improving reopening trends favor stocks over bonds.
- Overweight the U.S., but international investments increasingly look attractive as vaccination rates improve globally.
- Potentially tighter monetary policies warrant a tactical Underweight to Government bonds.
- Overweight credit.
- Favor cyclical over defensive areas.
- Incorporating a dividend focus could help balance growth and income needs.
- Companies across industries that can respond quickly to evolving pandemic conditions and meet demand needs offer investment opportunities.
- Set realistic return expectations for stocks and bonds — notably as the business cycle matures.
- Maintain a well-diversified portfolio.
- Continue to favor high-quality investments throughout your portfolio.

Economic Perspective

2022 Economic Outlook: Strong Growth, Stronger Inflation

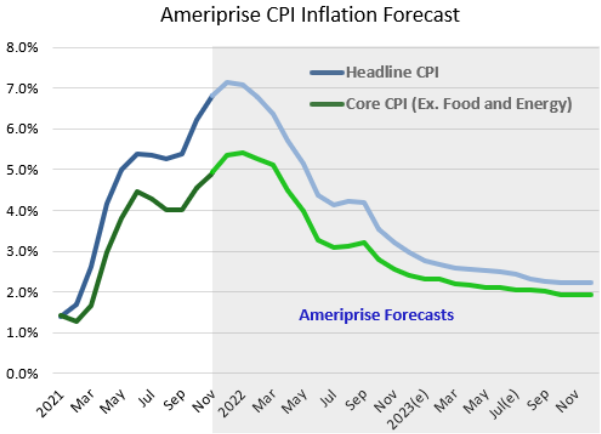
Economic prospects appear fairly strong as we approach 2022. In our view, consumer and corporate balance sheets are in a solid position thus likely able to support above-trend growth as supply allows. Consumer confidence should also benefit from a strong labor market. We currently project the unemployment rate to enter 2022 at a level of 4.0% and exit the year at approximately 3.0%, which would be the lowest since the early 1950s if achieved.

According to the Federal Reserve, consumers enter the new year with relatively low debt to income levels. A high savings rate, strong home values, and a buoyant stock market should also offer positive implications for consumer spending prospects. Added government spending on infrastructure, an improved trade picture, and the need to rebuild business inventories should each aid overall growth as well. Progress, of course, will remain dependent on COVID-19 conditions, supply-chain functioning, and what is likely to be higher interest rates. We currently project U.S. real GDP to expand at a +4.5% rate in 2022 versus what we expect will be a +5.5% rate for 2021.

Inflation a Dominant Theme

Inflation, however, poses a significant challenge to growth prospects. Higher prices have been sapping consumer purchasing power, and further gains could risk an over-tightening of financial conditions from the Federal Reserve. We believe year-over-year (y/y) inflation rates could begin to subside in the second quarter on tougher year-over-year comparisons, stabilizing costs for energy and housing and easing demand for goods relative to services.

Overall, however, inflation looks set to start 2022 at more than 40-year highs, with the headline Consumer Price Index recently at +6.8% (November) and a Core rate (excluding food and energy costs) of +4.9%. The recent string of "hot" inflation reports looks likely to accelerate Federal Reserve policy tightening. A few months ago, most forecasters expected the first Fed interest rate hike to come in early 2023. Today, expectations via Bloomberg's survey of professional forecasters suggest two or possibly three quarter-point hikes in 2022. Such actions should be economically digestible, in our view, but historically it's been financial markets that have been more reactionary to Fed rate hikes early in a cycle.



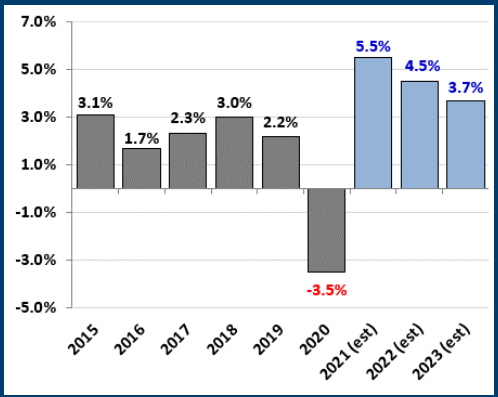
Source: Labor Department and AEIS Inc.

The International Outlook

Product shortages and delays caused by the COVID-19 Delta-variant outbreaks have been far from a U.S. story alone. More areas of the globe than not have seen their growth estimates cut in recent months as a result, but overall, the COVID-19 recovery continues. Unfortunately, as of this writing, Europe is seeing yet another severe outbreak – primarily of the Delta-variant with Omicron yet emerging. As a result, Austria and Denmark have again instituted national economic shutdowns, with Germany considering the same.

Though these developments should be expected to delay some growth to future periods, we believe the economic rebound in the region continues, nonetheless. In addition, much higher energy prices for gasoline, home heating, and electricity are also likely to trim near-term growth prospects in the region. Finally, virus-related shutdowns in Asia likely represent a greater direct risk to U.S. recovery prospects, particularly as it pertains to fledgling improvements in semiconductor supplies.

Ameriprise U.S. Real GDP Outlook



Source: Commerce Department for actuals and American Enterprise Investment Services Inc. for estimates.

IMF Global Economic Projections

	Actuals				Projections		Difference from July, 2021 projections.	
	2017	2018	2019	2020	2021	2022	2021	2022
World	3.8	3.6	2.8	-3.1	5.9	4.9	-0.1	0.0
United States	2.2	2.9	2.2	-3.4	6.0	5.2	-1.0	0.3
Euro Region	2.4	1.9	1.3	-6.3	5.0	4.3	0.4	0.0
Japan	1.9	0.3	0.7	-4.6	2.4	3.2	-0.4	0.2
Developing Asia	6.6	6.4	5.5	-0.8	7.2	6.3	-0.3	-0.1
China	6.8	6.6	6.1	2.3	8.0	5.6	-0.1	-0.1
India	7.2	6.8	4.2	-7.3	9.5	8.5	0.0	0.0
Russia	1.6	2.3	1.3	-3.0	4.7	2.9	0.3	-0.2
Brazil	1.1	1.3	1.1	-4.1	5.2	1.5	-0.1	-0.4
Mexico	2.1	2.1	-0.1	-8.3	6.2	4.0	-0.1	-0.2

Source: IMF World Economic Outlook, October 2021.

Key Equity Themes

Stay Invested; But Dial Back Expectations

We remain bullish on stocks despite expectations for more modest returns in 2022, thus cautioning equity investors to temper expectations. If earnings for 2022 come in as expected, it would again mark another record high for the Index as current expectations call for +9% y/y earnings growth. Factoring in very healthy consumer balance sheets (i.e., low debt), the strong employment picture, and easing supply chain disruptions, our view is that the overall market backdrop is favorable. We believe companies in more cyclically-oriented sectors (e.g., Financials and Technology) with solid fundamentals, stable growth prospects, and attractive valuation levels (i.e., GARP, or Growth at a Reasonable Price) could provide opportunities for relative outperformance in 2022. For international equity investors, the 'lag effect' of reopening efforts (versus the U.S.) could also offer attractive investment opportunities as their benchmark indices are heavily weighted towards the cyclical sectors of Financials and Industrials.

In 2021, corporate expense discipline and strong consumer demand resulted in record profit margins for the S&P 500. However, we believe the impact of rising raw materials costs, supply chain disruptions, and higher wages may not be fully reflected in current profit margins. As we move through 2022 and prices ramp higher, including in raw materials pricing, wage growth, rising freight costs, etc., we believe these factors could work to pressure corporate profit margins.

Reopening 2.0 — Cyclicals with Dividends

Despite the potential for new COVID variants (and a return to lockdowns and mandates), we believe the more cyclical areas of the economy could provide attractive risk/reward opportunities in 2022. Our macro equity outlook includes a gradual rise in interest rates as economic growth resumes, with inflation peaking sometime mid-year. This backdrop should act as a tailwind for key sectors of the economy such as Financials (e.g., benefit from higher rates) and Technology (e.g., the digital transformation continues).

In addition to our cyclical bias for 2022, we believe dividend-paying companies could act as a potential inflation hedge, an attractive equity-income opportunity, and a defensive equity strategy should volatility spike higher. In our view, high-quality dividend-oriented companies can help flatten out volatile periods, much as they did in 2020 during the height of the pandemic. While dividend companies lagged post the pandemic as investor focus turned to momentum and growth, we believe the risk/reward is favorable for low-beta dividend names heading into 2022. Sometimes you can have your "growth cake and eat it too." FactSet data indicates Technology dividend growth could top that of the S&P 500' bond proxy' sectors such as Consumer Staples and Utilities in 2022.

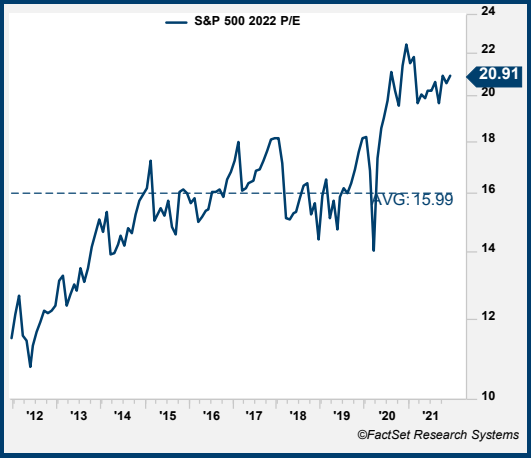
We would further narrow the focus in the dividend space to quality companies (i.e., low debt, high ROE, etc.) that consistently grow their dividend (versus just paying a dividend). In our view, these higher-quality dividend growers with strong free cash flow are less impacted by share price volatility as they seek to reward shareholders with increased quarterly dividend distributions.

Disruptive Distribution is Here to Stay; Stock Selection Makes a Comeback

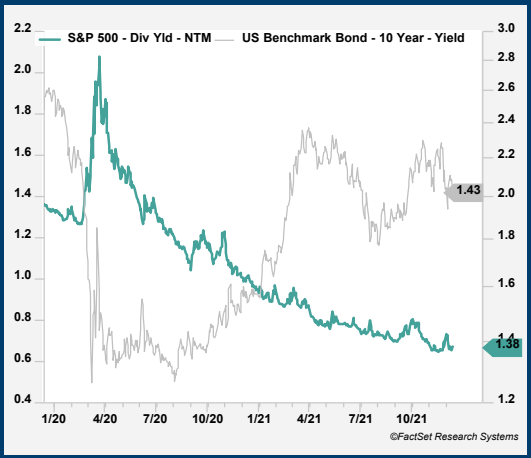
While nearly all industries experienced some level of operational disruption during the pandemic, companies are learning to grow and thrive in this "new normal." Examples include the hybrid office for information workers, onshoring, leveraging digital services (i.e., Zoom, Teams, etc.), accelerating an online presence, and adopting omnichannel marketing and service delivery. While this list just scratches the surface of structural changes taking place across almost every sector, change is happening, and we believe it sets the stage for more robust long-term growth for companies ready to adapt.

We believe there are periods in the market when it is relatively "easier" to passively invest in an index versus trying to construct a portfolio to beat an index. These periods are typically when there is a relatively narrow range of returns between the top performers and bottom performers in a particular index. Conversely, when there is a wide range of returns between stocks in an index (and thus dispersion is higher), the proverbial 'stock pickers market' is considered to be in play. The current investing environment reflects the latter scenario where dispersion is rising, which we believe can offer attractive total return opportunities for stock investors in 2022.

S&P 500 Forward P/E Elevated

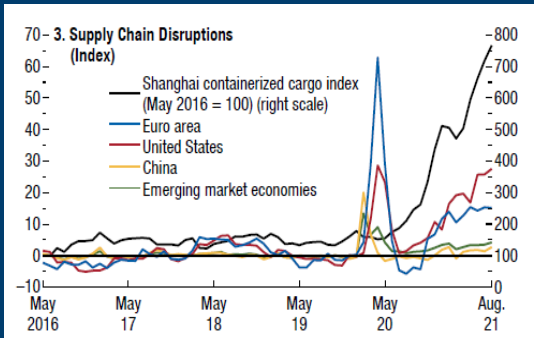


Dividends Offer Potential Benefits in 2022



Sources: FactSet American Enterprise Investment Services Inc. Data as of 12/13/20.

Supply Disruption Intensifies Globally



Sources: Baltic Exchange; Haver Analytics; IMF, Primary Commodity Price System; Organisation for Economic Co-operation and Development; and IMF staff calculations.

Key Fixed Income Themes

The Transition from Extraordinary Toward Ordinary

After a less than graceful Fed policy pivot to catch up with sticky inflation at the end of November, we look for Fed policy to transition away from extraordinary accommodation in 2022.

Fed Policy: We anticipate Fed policy will evolve significantly by the end of 2022. We expect the Fed to reduce its bond purchases from $90 billion per month in December to $60 billion in January at its December policy meeting. At that pace, purchases would end in March, concluding monthly cash infusions the Fed thought necessary through Covid-19 driven business disruptions.

Our Forecasts: Allowing bond markets to adapt to diminished liquidity and progress toward full employment likely fill the Fed's dashboard in the first half of 2022. Our current forecast incorporates a quarter-point hike in July and another in December. As the Fed contemplates potential hikes in the back half of the year, inflation forces may be easing given year over year comparisons. With inflation potentially past peak levels, we anticipate the Fed to be more measured with rate hikes than the nearly three quarter-point hikes priced into 2022 fed futures markets as of December 10. We set our year-end 2022 10-year Treasury yield target at 2.00%, up half a percent from where it likely ends 2021. Our target considers both retreating Fed policy intervention and moderate levels of sticky inflation.

Nominal Returns Depressed, Real Returns Depressing

More than 20% of the $63 trillion Bloomberg Global Aggregate Index traded at a negative yield on December 10. In 2022, low coupons offer meager support for total returns, while price returns likely come in negative given the potential for higher yields. At the end of November, 10-year Treasury yields provided a -3.5% real yield relative to November's core CPI reading of 4.9%. While nominal U.S. yields remain positive, U.S. Treasury investors do not expect their investments to keep up with inflation today. We believe the Fed and its G7 brethren are "pot-committed" or willing to go all-in to sustain an expansion and avoid a deep contraction. Thus, low yields likely persist.

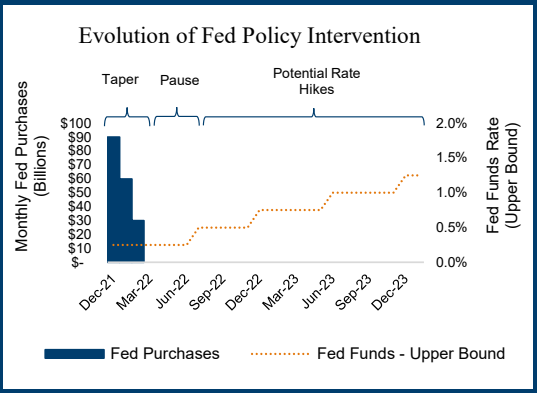
Liquidity Boosted Through 2022

We anticipate the Fed adjusts the pace of its bond purchase program, ending purchases by March. While the program may soon end, the impact of past purchases likely persists as a positive impulse in our view. Beyond active bond-buying programs and rate policy, two pillars of liquidity likely persist through next year:

- **Central bank balance sheets:** G7 central banks hold $21 trillion of assets, including $8.2 trillion at the Fed. Asset purchase programs exchange bondholder debt investments for cash, reflecting trillions of long-term liquidity added since the Financial Crisis and $9 trillion added since the beginning of 2020.
- **Pent-up Demand:** Fiscal and monetary policy flooded the consumer and credit channels with cash, which takes time to work its way through the economy. Among the factors supporting markets: $3.7 trillion of above-trend U.S. M2 money supply, $2.7 trillion of above-trend commercial bank deposits, and $1.7 trillion of above-trend assets in money market accounts. See chart at right.

We believe liquidity likely remains a force through 2022, supporting risk assets and providing stability through potential dislocations that arise.

Ameriprise's Forecast for Fed Policy



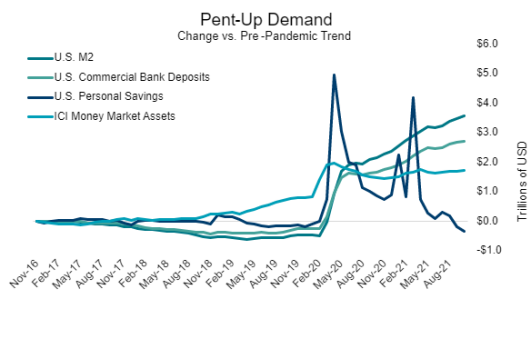
Source: American Enterprise Investment Services Inc.

Ameriprise 2022 Year-End Rate Forecasts

Favorable Scenario Macro Conditions	Base Scenario Macro Conditions	Adverse Scenario Macro Conditions
Fed Funds Target Range 0.75% - 1.00%	Fed Funds Target Range 0.50% - 0.75%	Fed Funds Target Range 0.00% - 0.25%
Ten-year Treasury 2.50%	Ten-year Treasury 2.00%	Ten-year Treasury 2.50%+ or 1.50%

Source: American Enterprise Investment Services Inc.

Pent-up Policy Impulse = Easy Credit
$ in Trillions



Source: Bloomberg L.P., Federal Reserve, Investment Company Institute (ICI), American Enterprise Investment Services Inc.

Positioning: Our View on Segments and Strategies

We believe U.S. Treasuries continue to offer valuable diversification against tail and event risks that might arise. In our view, U.S. Treasuries remain a global safe-haven destination and likely benefit from any Fed emergency policy response that may prove necessary. Another form of Treasuries, Treasury Inflation Protected Securities (TIPS), may outperform fixed-rate Treasuries in scenarios where inflation becomes unanchored and other asset prices, including Treasuries, fall. Following the Fed's policy pivot toward inflation risk at the end of November, breakeven rates suggest TIPS as an attractive diversifier against higher inflation. We recommend investors consider a buy and hold approach, holding positions until maturity to navigate the challenging return environment. Laddered strategies of individual bonds or target maturity funds use this approach. Alternatively, looking at the total return of a fund investment over a longer period of time than one quarter or one year takes into account the negative returns of rising rates and also the benefits resulting from higher yields on future fund holdings. Finally, mandate flexibility for active fixed income managers, such as an absolute return strategy, could prove helpful at times next year if properly geared with an investor's risk profile.

Portfolio Positioning & Wrap-Up

Consider How Far Markets Have Come Already

As our outlook details, investors should remain constructive on growth and overall prospects for higher returns in 2022. However, economic and profit growth is likely to slow as the year wears on, and changes in monetary policy could create periods of greater volatility for risk assets, including stocks and bonds. As a result, in our view, returns could look more modest, and it may be harder to simply lean on macro themes to generate portfolio returns in 2022. As such, we believe investors should incorporate the following views into their portfolios for the new year.

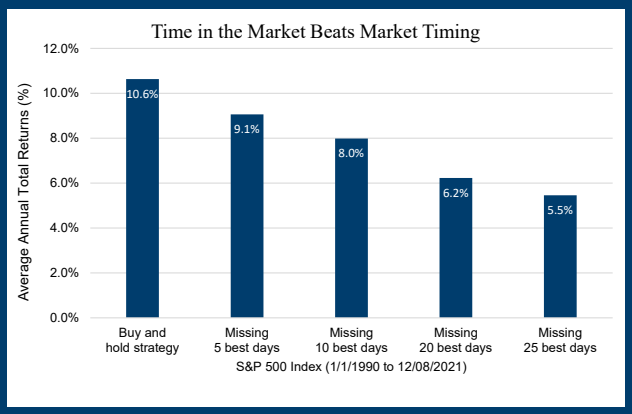
Overweight stocks, but be mindful of overall diversification properties. Investors should overweight stocks and underweight bonds as more of the world reopens. However, we believe the potential for outsized gains relative to history has diminished. Elevated valuations, a maturing business cycle, and tighter monetary policies could create headwinds for assets during the year. We believe this is the time to evaluate risk tolerances, ensure proper diversification, and temper expectations for future price appreciation.

Interest rate risk is a growing threat to portfolios — Alternative Strategies could offer tactical opportunities. The potential for higher interest rates in 2022 could create crosscurrents for both stocks and bonds. To help reduce portfolio volatility, investors should modestly increase Alternative Strategies exposure over strategic targets. Strategies that reduce equity volatility or hedge interest rate risk may offer a prudent way to manage through added volatility and/or stay prepared for the unexpected.

The U.S. and Europe could continue to shine. Developed markets, including the U.S. and Europe, should continue to recover from the pandemic, allowing for above-trend economic growth and still strong corporate profitability. Each area poses a unique set of risks and opportunities. While the U.S. offers more exposure to growth areas, it is also more richly valued and sensitive to interest rates. Europe offers more concentrated exposure to reopening areas, like Financials, but is more susceptible to pandemic pressures and slowing growth. However, we believe both regions provide a healthy mix of cyclical opportunities that should continue to benefit from a world emerging from the pandemic.

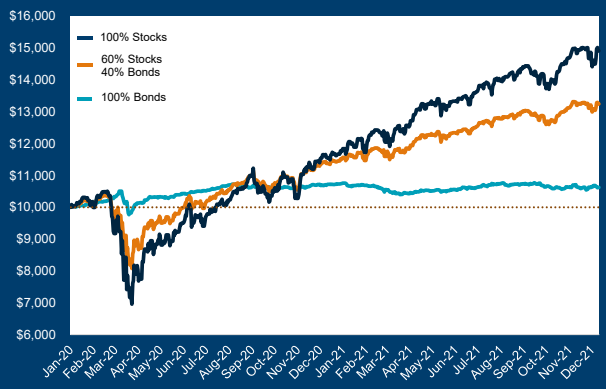
Sector exposure can still guide portfolio allocations, though security selection will likely play a more prominent role in returns. We believe cyclical industries, such as Financials, could continue to perform well in 2022 — particularly against a rising rate backdrop. But easing supply chain pressures, improved economic activity, and more pent-up demand being satisfied during the year should also provide tailwinds for Industrials, Energy, and Consumer Discretionary sectors. And while interest rate risk is a concern for Technology, strong secular industry drivers provide growth opportunities against a normalizing economic backdrop. Health Care may also offer an attractive balance between growth, safety, and dividend yield at the start of the year and help diversify portfolios. Notably, we believe focusing on high-quality companies with the ability to grow, navigate a still challenging business environment, and adapt to change quickly are likely to be attributes rewarded with higher stock prices. As a result, investors should place a stronger emphasis on underlying investment choices in 2022. Of course, a good dividend yield to help cushion some downside risk also doesn't hurt.

Time in the Market Beats Market Timing



Sources: Bloomberg, S&P Dow Jones Indices, American Enterprise Investment Services Inc. S&P 500 Total Return Index since 1990 as of 12/08/2021. Calculations assume no fees or transaction costs. Past performance is not a guarantee of future results.

Portfolio Values for Different Asset Mixes (Initial Value = $10,000 on December 31, 2019)



Sources: Bloomberg, S&P Dow Jones Indices, American Enterprise Investment Services Inc. S&P Total Return Index as of 12/8/2021.

Tying it All Together

After such an intense period of returns for a range of assets (including stocks) since the depths of the pandemic, we believe investors should take a more prudent approach regarding risk and portfolio construction. In our view, the next leg higher in the market is likely to be more discriminate across regions, companies, and investments. And while our outlook for 2022 is generally favorable for higher stock prices, investors should expect the unexpected along the way, given moderating growth trends and potentially tighter monetary policies. ■

Global Asset Allocation Committee

Led by top Ameriprise strategists, the Ameriprise Global Asset Allocation Committee is a team of experienced investment professionals focused on delivering strategic and tactical asset allocation guidance and actionable investment strategies. Each quarter the Committee publishes a comprehensive outlook on the markets along with its recommendations in the Quarterly Capital Market Digest.

David M. Joy
Vice President
Chief Market Strategist

Russell T. Price, CFA
Vice President
Chief Economist

Thomas Crandall, CFA, CFP®, CAIA, CMT
Senior Director
Asset Allocation

Christine A. Pederson, CAIA, CIMA
Senior Director
Manager Research

Brian M. Erickson, CFA
Vice President
Fixed Income Strategy

Justin H. Burgin
Vice President
Equity Research

Jon K. Cartwright
Senior Director
Fixed Income

Dan Garofalo
Director
Equity Research

Frederick M. Schultz
Senior Director
Equity Research

Anthony M. Saglimbene
Vice President
Global Market Strategist

Cedric Buermann Jr., CFA
Quantitative Analyst
Asset Allocation

Patrick S. Diedrickson, CFA
Director
Equity Research

Mark S. Phelps, CFA
Director
Manager Research

The content in this report is authored by American Enterprise Investment Services Inc. ("AEIS") and distributed by Ameriprise Financial Services, LLC ("AFS") to financial advisors and clients of AFS. AEIS and AFS are affiliates and subsidiaries of Ameriprise Financial, Inc. Both AEIS and AFS are member firms registered with FINRA and are subject to the objectivity safeguards and disclosure requirements relating to research analysts and the publication and distribution of research reports. The "Important Disclosures" below relate to the AEIS research analyst(s) that prepared this publication.

Each of AEIS and AFS have implemented policies and procedures reasonably designed to ensure that its employees involved in the preparation, content and distribution of research reports, including dually registered employees, do not influence the objectivity or timing of the publication of research report content. All research policies, coverage decisions, compensation, hiring and other personnel decisions with respect to research analysts are made by AEIS, which is operationally independent of AFS.

Important disclosures

As of September 30, 2021

The views expressed regarding the company(ies) and sector(s) featured in this publication reflect the personal views of the research analyst(s) authoring the publication. Further, no part of research analyst compensation is directly or indirectly related to the specific recommendations or views contained in this publication.

A part of a research analyst's compensation may be based upon overall firm revenue and profitability, of which investment banking, sales and trading, and principal trading are components. No part of a research analyst's compensation is based on a specific investment banking transaction, nor is it based on sales, trading, or principal trading. A research analyst may have visited the material operations of one or more of the subject companies mentioned in this research report. No payment was received for the related travel costs.

This information is being provided only as a general source of information and is not intended to be the primary basis for investment decisions. It should not be construed as advice designed to meet the particular needs of an individual investor. Please seek the advice of a financial advisor regarding your particular financial concerns. Consult with your tax advisor or attorney regarding specific tax issues.

Tactical asset class recommendations mentioned in this report reflect The Ameriprise Global Asset Allocation Committee's general view of the financial markets, as of the date of the report, based on then current conditions. Our tactical recommendations may differ materially from what is presented in a customized long-term financial plan or portfolio strategy. You should view our

recommendations in conjunction with a broader long-term portfolio strategy. Not all products, services, or asset classes mentioned in this report may be available for sale at Ameriprise Financial Services, Inc. Please consult with your financial advisor.

Product Risk Disclosures

Asset allocation and diversification does not assure a profit or protect against loss.

Alternative investments cover a broad range of strategies and structures designed to be low or non-correlated to traditional equity and fixed-income markets with a long-term expectation of illiquidity.

Alternative investments involve substantial risks and are more volatile than traditional investments, making them more suitable for investors with an above-average tolerance for risk

Commodity investments may be affected by overall market and industry- and commodity-specific factors, and may be more volatile and less liquid than other investments.

Risks are enhanced for **emerging market issuers**.

There are risks associated with **fixed-income** investments, including credit risk, interest rate risk, and prepayment and extension risk. In general, bond prices rise when interest rates fall and vice versa. This effect is usually more pronounced for longer term securities.

Growth securities, at times, may not perform as well as value securities or the stock market in general and may be out of favor with investors.

Non-investment-grade (high-yield or junk) securities present greater price volatility and more risk to principal and income than higher rated securities.

International investing involves increased risk and volatility due to political and economic instability, currency fluctuations, and differences in financial reporting and accounting standards and oversight. Risks are particularly significant in emerging markets.

Investments in **small- and mid-capitalization companies** involve greater risks and volatility than investments in larger, more established companies.

The **U.S. government** may be unable or unwilling to honor its financial obligations. Securities issued or guaranteed by federal agencies and U.S. government-sponsored instrumentalities may or may not be backed by the full faith and credit of the U.S. government.

Value securities may be unprofitable if the market fails to recognize their intrinsic worth or the portfolio manager misgauged that worth

Financial products that utilize complex investment strategies (including investments in sectors, commodities, currencies, derivatives or other nonconventional assets) involve substantial risks, may be more volatile than products that only use traditional investments, and may not be suitable for all investors.

Definitions of Terms

Price/Earnings: An equity valuation multiple calculated by dividing the market share price, as of a certain date, by earnings per share. Trailing P/E uses the share price divided by the past four-quarters' earnings per share. Forward P/E uses the share price as of a certain date divided by the consensus estimate of the future four-quarters' EPS.

The **Standard Deviation** measures how concentrated the data are around the mean; the more concentrated, the smaller the deviation.

Index Definitions

An index is a statistical composite that is not managed. It is not possible to invest directly in an index.

Definitions of individual indices mentioned in this report are available on our website at ameriprise.com/legal/disclosures/ in the **Additional Ameriprise research disclosures** section, or through your Ameriprise financial advisor.

Disclaimer Section

Except for the historical information contained herein, certain matters in this report are forward-looking statements or projections that are dependent upon certain risks and uncertainties, including but not limited to, such factors and considerations as general market volatility, global economic and geopolitical impacts, fiscal and monetary policy, liquidity, the level of interest rates, historical sector performance relationships as they relate to the business and economic cycle, consumer preferences, foreign currency exchange rates, litigation risk, competitive positioning, the ability to successfully integrate acquisitions, the ability to develop and commercialize new products and services, legislative risks, the pricing environment for products and services, and compliance with various local, state, and federal health care laws. See latest third party research reports and updates for risks pertaining to a particular security.

This summary is based upon financial information and statistical data obtained from sources deemed reliable, but in no way is warranted by Ameriprise Financial, Inc. as to accuracy or completeness. This is not a solicitation by Ameriprise Financial Services, LLC of any order to buy or sell securities. This summary is based exclusively on an analysis of general current market conditions, rather than the appropriateness of a specific proposed securities transaction. We will not advise you as to any change in figures or our views.

Past performance is not a guarantee of future results.

Investment products are not federally or FDIC-insured, are not deposits or obligations of, or guaranteed by any financial institution, and involve investment risks including possible loss of principal and fluctuation in Value.

Ameriprise Financial, Inc. and its affiliates do not offer tax or legal advice. Consumers should consult with their tax advisor or attorney regarding their specific situation.

Ameriprise Financial Services, LLC. Member FINRA and SIPC.