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Kevin P. Barr
Head of SEI's Investment Management Unit

Dear Client,

We've come a long way over the last 12 months. Following a narrative set by the pandemic, 2021 was a lot more like a rollercoaster ride with its attendant ups and downs than a straight drive out of the COVID-19 wilderness. Capital markets tracked the world's changing economic fortunes throughout the year, delivering impressive returns for the full year even as the final months were marked by choppy conditions attributable to the emergence of the Omicron variant, multi-decade-high inflation rates and anticipation of rising interest rates.

Looking at the year as a whole, I think investors have plenty to be pleased about. Developed-market stocks generated average to well-above-average gains depending on geography and market cap. Emerging markets were challenged by the lag in vaccine availability, a raft of regulatory changes and setbacks to the Chinese economy and inflation sensitivity.

Rising price pressures were more beneficial elsewhere, with broad commodity gains in line with some of the year's best equity performances. Inflation-indexed bonds led in fixed income, while high yield had the only other notable bond market gains.

We shared our expectations last January that growth and inflation would accelerate in 2021, along with our guidance on the types of assets that should be expected to thrive in this regime. Indeed, investors have begun to reprice expensive, less-profitable companies as the specter of higher interest rates diminishes the present value of their long-term growth prospects.

As we stated last year, "rather than seeking to time the market, we remained focused on quality companies selling at reasonable valuations." These types of equities have been upgraded as more expensive stocks have started to fall out of favor. Value-oriented shares have led growth stocks around the world since November 2020, most markedly within U.S. small caps and emerging markets, and at the closest margin within U.S. large caps.

2021 Performance

U.S. equities were the top-performing major market in 2021. Our commitment to owning quality companies at reasonable valuations boosted many of our equity strategies over their benchmarks, both within the U.S. and elsewhere.

Our U.S. equity strategies all earned double-digit absolute returns with an array of relative performance. Most strategies beat their benchmarks.

- Active large-cap strategies saw mixed relative results. Tax-managed and value-satellite versions outperformed, while core and growth-satellite versions lagged.
- Active small-cap strategies generated remarkably high alpha across the board. Investors reawakened to the benefits of owning companies with strong cash flows and balance sheets, positive earnings revisions and reasonable valuations. Our avoidance of companies with no earnings, cash flows, or those that were otherwise expensive and speculative was also quite important.
- U.S. factor-allocation equity strategies also outperformed by a wide margin due to a value overweight, which was bolstered by the presence of secondary momentum exposure. With valuation dispersion levels hovering close to the peak of the internet bubble of the late 1990s, we have a favorable outlook for value. Rising interest rates and inflation are expected to provide a further boost to the outperformance of this factor family.

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Overseas, our equity strategies managed to generate above-benchmark performance in most instances despite facing a less-favorable market backdrop than that of the U.S.

- Emerging-market stocks struggled, but our strategies were able to improve on benchmark performance. Some of the largest technology stocks in emerging markets were adversely affected by China's regulatory changes, so our underweight exposures were beneficial.
- Our active ex-U.S. strategies were the outliers, producing flat-to-negative relative performance. Stock selection detracted, offsetting favorable tailwinds from our positioning within the value, momentum and quality alpha sources. Businesses in the retail and leisure sectors have faced unprecedented challenges, while autos and industrial companies have confronted supply chain disruptions, so our exposure to these segments came under pressure in 2021.

The range of outcomes on the income-oriented side of the portfolio was much narrower than within equities. Our strategies mostly performed in line with their benchmarks as bond markets struggled with the prospect of rising interest rates at various points during the year. Our relative performance shined brightest in strategies where we could capitalize on inflation and credit opportunities, and we were able to generate alpha in several portfolios.

- Our multi-asset real return strategy's emphasis on commodities exposure was its most significant contributor to outperformance in the high-inflation environment. Allocations to credit sectors also contributed. Credit spreads are relatively tight, but we believe corporate fundamentals coupled with strong technicals will remain supportive.

- Our high-yield bond strategy outperformed by a considerable margin in one of the only bright spots within fixed income. A long-standing focus on structured credit, along with selection in energy and basic industry, were the primary drivers of outperformance.
- Our opportunistic fixed-income strategy also produced above-benchmark performance resulting from exposure to securitized sectors, including asset-backed, residential mortgages, and commercial mortgages. Many of these securities have floating rate structures, which we would expect to produce higher yields once the Federal Reserve (Fed) begins raising the funds rate.

Asset classes aside, our alternative strategies also performed commendably in 2021. Our multi-strategy alternative strategy outperformed its benchmark amid a mix of opportunities and challenges depending on the sub-strategy. While equity hedge strategies struggled in a narrow market where shorting was difficult, our relative value and distressed debt strategies performed well.

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2022: Our View

Although there have been pockets of speculative behavior in some areas of the financial world—meme stocks, special purpose acquisition companies (SPACs), cryptocurrencies and non-fungible tokens (NFTs), for example—we do not see the sort of fervor that would point to a serious equity correction in 2022. The economy would have to slow precipitously for reasons other than the temporary impact stemming from COVID mobility restrictions, and the trend in earnings would need to flat-line or turn negative.

We expect a gain in overall U.S. economic activity of around 4% in 2022—appreciably above the economy's long-term growth potential of 2%. We also expect other countries to continue to post above-average growth as they recover from the past two years' worth of lockdowns and shortages.

China's performance in 2022 is one of the key unknowns that will influence global economic growth. Consensus expectations call for a soft landing of the Chinese economy, with GDP growing by about 5% in 2022 versus 8% in the past year.

The year ahead promises to be another one of extremely tight labor markets. In the short term, we expect wages to continue their sharp climb in the U.S. as businesses bid for workers.

We are skeptical that the Fed will be sufficiently proactive as it struggles to balance full and inclusive employment against inflation pressures that are starting to look more entrenched. This will be its biggest challenge in 2022 and beyond.

Even the major central banks that are most likely to taper their asset purchases and raise their policy rates in the months ahead will likely do so cautiously. Policy rates in emerging economies, by contrast, have already jumped, and the pace of tightening is picking up. The shift in Fed policy will probably represent a formidable headwind for emerging-market economies in 2022.

Earnings growth in 2021 for developed- and emerging-market equities both exceeded the earnings gain for the U.S. As a consequence, the relative valuation of international markets versus the U.S. has become only more attractive in the past year.

Yet the emergence of the Omicron variant has further delayed what we believe is an overdue rotation to cheaper, more cyclical stocks.

The trajectory of S&P 500 earnings growth probably will slow next year, but a gain in the 8%-to-12% range seems consistent with our macroeconomic call for continued above-average growth and inflation.

In our view, the real anomaly in the financial markets is the ultra-low levels of interest rates in the face of higher inflation and above-average growth in much of the world. This may force central banks to adopt more aggressive interest-rate policies than they and market participants currently envision.

We expect a 50- to 75-basis-point rise in 10-year U.S. Treasury bond yields for 2022. That gain could be the catalyst for a shift away from the most highly-valued, interest-rate-sensitive areas of the market into the broader grouping of stocks that have been neglected for the past several years

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Our Focus

Prior to 2021, the dominant theme in equity markets over the last several years favored concentration in a small group of high-priced mega-cap stocks at the expense of diversified fundamental-oriented strategies. Nevertheless, we stuck to our philosophy since history has shown that diversification and a focus on positive company fundamentals can be an enduring strategy for long-term wealth generation.

We believe that our performance in 2021 serves as evidence that the pendulum is swinging back in favor of our approach, and that it has only just begun. Moreover, our calls on higher inflation, coupled with portfolio construction that prioritizes positive inflation sensitivity, helped to prepare our investors' portfolios for the most aggressive price increases in almost 40 years.

Frankly, years of easy monetary policy have resulted in unsustainable market imbalances that are just beginning to unwind. We expect this trend to accelerate as bond yields rise in tandem with a more normal interest-rate cycle. Elevated valuation dispersions should allow managers to identify value opportunities, while the environment remains positive for those able to identify companies able to exceed market expectations. This is an environment that should reward skillful stock selection.

Looking ahead, the energy we invested in reorganizing the Investment Management Unit in 2021 should begin to bear fruit in the New Year as we focus on developing new strategies, solutions and capabilities.

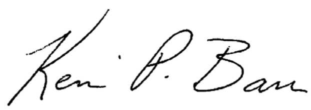
We saw early indications of this with the success of our managed account solutions (MAS) program in 2021. We experienced tremendous asset growth across MAS as advisors sought to deliver greater customization for their clients.

Demand has been driven by the opportunity for advisors to capitalize on tax-loss harvesting of individual assets within client portfolios, as well as the flexibility to tap into important trends including investments focused on environmental, social and governance and sustainability factors.

We are looking forward to building on this momentum in the year ahead, and as always, we remain committed to fostering an innovative culture focused on helping investors meet their objectives.

We thank you for your ongoing support and wish you a prosperous New Year.

Sincerely,



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