

Quarterly Commentary: Market Series Quantitative Portfolios (QPs) Large Cap Dividend Income

Fourth Quarter (Q4) 2021

Market Environment

The US economy delivered slowing growth in the quarter, having been adversely affected by the Delta variant of Covid-19 as well as fading economic stimulus. The results were somewhat weaker than the numbers indicated, as consumer spending rose at its slowest rate since the recovery began. Against this backdrop, the Bureau of Economic Analysis released the third estimate of the third-quarter 2021 real GDP, a seasonally adjusted annualized increase of 2.3%, slightly higher than the prior estimate, but a significant decline from the 6.7% increase in the prior quarter. The employment situation disappointed in the quarter, as gains were far below expectations. The November report showed that employers added 210,000 jobs in the month, and that the unemployment rate fell to 4.2%. The Federal Open Market Committee (FOMC) maintained its federal funds rate target range of 0% to 0.25%. However, the central bank increased the amount of its tapering program from \$15 billion to \$30 billion in an acknowledgement that it has underestimated the level and persistence of inflation. In addition, the FOMC removed the word “transitory” from its accompanying statement in describing the high inflation rate. The FOMC’s “dot plot,” a forecast of future rate changes, indicates the Committee now expects three 25-basis-point rate hikes in 2022, and another three in 2023.

Portfolio Commentary

The Market Series Large Cap Dividend Income strategy generated robust positive absolute returns in the quarter, but performance slightly lagged the benchmark on a relative basis. The strategy generated a total return of 8.12% compared with the 9.33% return of the CRSP US Large Cap Value Index. For the full year, the strategy delivered a total return of 24.35% compared with the 26.51% return for the benchmark. At the end of the quarter, the portfolio offered a dividend yield of 3.92% compared with a yield of 2.15% for the benchmark.

The CRSP US Large Cap Value Index’s quarterly return trailed the 10.74% return for the CRSP US Large Cap Growth Index. The portfolio is designed to provide beta exposure and returns similar to those of the benchmark, but with a substantially higher dividend yield. Portfolio holdings include dividend-paying stocks that rank highly according to quality metrics, which underpin a company’s ability to continue payments to shareholders.

Sector selection has a relatively minor effect on performance, as the QPs are constructed to be sector neutral at rebalancing. Accordingly, the portfolio’s relative performance was driven primarily by individual security selection. Sector allocation detracted 21 basis points from performance, whereas stock selection within sectors detracted 100 basis points during the quarter. The sectors in which positive stock selection occurred included Financials and Real Estate. Sectors that experienced negative stock selection included Communication Services and Energy.

Positively contributing to the Market Series Large Cap Dividend Income strategy’s performance during the quarter was an overweight to AbbVie Inc. (ABBV), which gained about 27%. The stock also outperformed the 11% return of the Health Care sector.

The portfolio also benefited from having an overweight to Pfizer Inc. (PFE). The pharmaceuticals giant surged almost 37%, and contributed 44 basis points to performance.

Having no exposure to Comcast Corp. Class A (CMCSA) resulted in a 28-basis-point contribution to the portfolio. The media company’s stock dropped approximately 9% on the quarter.

An overweight position to Annaly Capital Management Inc. (NLY) detracted 56 basis points from the portfolio’s active return. The stock of the mortgage real estate company declined about 3% during the quarter.

Citizens Financial Group Inc. (CFG) gained a mere 1% during this quarter, detracting 32 basis points from the portfolio as a result of its overweight allocation.

The portfolio also suffered during the quarter from having an overweight to AGNC Investment Corp. (AGNC). The mortgage company’s stock declined about 1% in the quarter, detracting 26 basis points from portfolio performance as a result of its overweight allocation.

The economy’s growth slowed somewhat during the quarter, as supply chain issues and the effects of the Omicron variant of the COVID-19 virus caused disruptions. Earnings growth was strong in the third quarter, bringing down stock valuations from all-time highs, even as the market itself closed the quarter near record levels. Analysts expect increased volatility in 2022 as the Federal Reserve seeks to normalize monetary policy.

Model Portfolio Attribution

	Performance Driver	Active Return Contribution	Portfolio Exposure	Average Weight in Model	Comments
Contributors	AbbVie Inc. (ABBV)	+66 bps	Overweight	4.97%	The biotechnology company's stock gained about 27%.
	Pfizer Inc. (PFE)	+44 bps	Overweight	3.29%	The pharmaceutical giant's stock surged almost 37%, outpacing the broader health care sector's gain of 11%.
	Comcast Corp. Class A (CMCSA)	+28 bps	No exposure	0.00%	The stock of the media company dropped by about 9%.
	Citigroup Inc. (C)	+19 bps	No exposure	0.00%	The banking giant's stock performed poorly, falling by more than 13%.
	Eaton Corp PLC (ETN)	+15 bps	Overweight	2.96%	The electrical equipment manufacturer gained more than 15%.
Detractors	Annaly Capital Management Inc. (NLY)	-56 bps	Overweight	4.43%	The stock of the mortgage real estate company declined about 3% during the quarter.
	Citizens Financial Group Inc. (CFG)	-32 bps	Overweight	4.08%	The stock gained a mere 1% during this quarter, detracting 32 basis points from the portfolio as a result of its overweight allocation.
	AGNC Investment Corp. (AGNC)	-26 bps	Overweight	2.37%	The mortgage company's stock declined about 1% in the quarter, detracting 26 basis points from portfolio performance as a result of its overweight allocation.
	Antero Midstream Corp. (AM)	-24 bps	Overweight	1.69%	The oil and gas company's stock fell by more than 5%, detracting 24 basis points from performance.
	Broadcom Inc. (AVGO)	-23 bps	Underweight	0.29%	The stock of the semiconductor manufacturer rose by about 17%.

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Disclosure

The **Russell 1000 Index** is a market capitalization weighted benchmark index made up of the 1000 largest U.S. companies in the Russell 3000 Index. The **Russell 1000 Value Index** refers to a composite of large and mid-cap companies located in the United States that also exhibit a value probability. The **CRSP US Large Cap Index** includes U.S. companies that comprise the top 85% of investable market capitalization.

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