2023 Q1 IN REVIEW

An eventful Q1, a period characterized by heightened volatility that was primarily driven by uncertainty regarding the health of the regional banking system, a stubbornly hot labor market, and easing inflation, has finally ended. A strong January, weak February, and a March rally saw the S&P 500 and Russell 3000 finish the quarter up 7.5% and 7% respectively. Fixed Income markets saw positive signs as well, with the Bloomberg Aggregate Bond Index up 2.96% for the quarter and the US 10-Year Yield dropping to 3.48% by the end of March.

A liquidity crisis in regional banking stimulated by the Fed's campaign to raise rates in late Q1 served as the canary in the coal mine for Fed policy. As rates rose from near zero at the beginning of 2022, the value of securities held on bank balance sheets declined. The realization that some regional banks with undiversified deposit bases may not be able to adequately handle customer withdrawals without realizing large losses stimulated runs on several banks. These events, which threatened the faith in and function of the banking system, caused regulators to take steps to shore up liquidity for all banks. Those steps, however, came too late for Silicon Valley Bank and Signature Bank of New York.

The labor market, having shown incredible resilience, started to finally show signs of slowing as the quarter came to an end. January and February saw the addition of 517,000 and 311,000 jobs respectively, far above and beyond consensus estimates. The Job Openings and Labor Turnover Survey (JOLTS) that was released in early April showed February job openings fall to 9.93 million, the first time there have been fewer than 10 million openings since May of 2021. Nonfarm payrolls grew 236,000 for the month of March, slightly below the expected 238,000, but far below the 326,000 from the previous month. Wage growth, one of the key signals that the Fed has been watching, rose 30 bps, moving Y/Y growth to 4.2%, its lowest level since June 2021. While the unemployment rate fell to 3.5%, which was lower than the expected 3.6%, labor force participation increased to its highest level since before the outbreak of Covid-19.

The battle to tame inflation raged on during the first three months of the year. February CPI data showed inflation falling to 6% Y/Y while Core CPI, which excludes volatile energy and food prices, rose 5.5%. The release of the February report also showed that the driving force of inflation is now heavily within the shelter category. March data will be released on April 12.

The beginning of Q1 was characterized by the certainty that the Fed would continue to raise rates as aggressively and for as long as needed to tame inflation. As the quarter drew on, and cracks in the financial system and economy began to show, the prevailing opinion of the market is now the exact opposite.

See our recommendations and the economic forecast below for Q2. Or subscribe to our **Premium Newsletter** here to get up-to-date quality analysis on market conditions and stock ideas weekly.

RECOMMENDED PORTFOLIO WEIGHTINGS
AS OF APRIL 1, 2023

EQUITY SECTORS

OVERWEIGHT
- Energy
- Industrials
- Materials

NEUTRAL
- REITs
- Utilities
- Technology

UNDERWEIGHT
- Financials
- Health Care
- Consumer Discretionary
- Communications

ASSET CLASSES

OVERWEIGHT
- Short-Term Investment Grade Bonds
- Intermediate-Term Investment Grade Bonds
- Precious Metals
- Resource Commodities
- U.S. Mid Cap Equities

NEUTRAL
- Long-Term Investment Grade Bonds
- Cash Alternatives
- U.S. Small Cap Equities
- High Yield bonds
- Agriculture Commodities
- International Developed Equities
- Emerging Market Equities

UNDERWEIGHT
- U.S. Large Cap Equities
- International Developed Fixed Income

FIXED INCOME

OVERWEIGHT
- Municipal Bonds
- Corporate Bonds

NEUTRAL
- Bank Loans
- Agency Securities
- TIPS
- U.S. Treasuries

UNDERWEIGHT
- Preferred Securities
- Mortgage-Backed Securities

INDEXES

DATA POINT	CURRENT	YEAR-END PROJECTION
S&P 500	4,109	4,200-4,300
NYSE	15,375	16,500-17,500
10-Year Treasury Rate	3.49%	4.00-4.25%
WTI Crude Oil	$80.15	$95-100
Gold Priced in Dollars	$1,969	$2,200
Trade Weighted Dollar Index	115	110-115
Effective Fed Funds Rate	4.83%	4.00-4.25%

2023 Q2 ECONOMIC & MARKET OUTLOOK

01. Equities

Sentiment is positive, in spite of banks.

Although there was heightened volatility, equity markets finished the quarter higher than they began. Following a crushing end to 2022, Technology stocks were back in the limelight as household names like Meta and Nvidia rocketed off of December lows. Growth stocks broadly outperformed Value stocks for the quarter as well despite the fear in the aftermath of the regional baking crisis. Although markets have shown continuing optimism following the collapse of SBNY and SIVB, one should not assume that the run-up in growth stocks can continue indefinitely, as we see this as more of a countertrend rally. As the effects of the steep rise in rates begin to show, and the economy begins to crack, investing in companies that do not have balance sheets that are reinforced to weather economic headwinds would be ill-advised. Given economic dynamics, we would expect to see a shift away from growth and toward value as the year goes on. Industrial production, distribution, and transportation, which led the broad Industrial sector through Q1 may continue to show strength as we close out the first half of the year. Even as the conflict in Eastern Europe shows no signs of easing, neither does the demand for energy. Q2 2023 may be the quarter that sees the first Fed meeting in some time with no rate hike and equity markets are acting accordingly.

Schedule a Portfolio Review with one of our advisors to start planning your next best step.

02. Fixed Income

The end is near for rate hikes.

Hawkish Fed rhetoric in January briefly brought the 10-year treasury yield back above 4%, but rates failed to surpass the October highs, which was an indication that the bond market was not buying their ability to raise rates much further. By early March, the bond market was vindicated as a banking crisis forced the Fed to create a new lending facility that ballooned their balance sheet back to levels of early Fall. The 2-year Treasury yield briefly broke the 5% level in early March but quickly moved below 4% by the end of the month as markets began pricing in Fed rate cuts by year's end. As the economic data comes in light, the odds of credit events rise, therefore you have to be careful and not step in front of markets that are resetting, like office real estate. There are many opportunities out there as broad sectors enter crisis, and related industries come under pressure. For example, many non-bank financial bonds were hit during the recent crisis that brought opportunities. Overall, the recent rally in long-duration assets is a good opportunity to take profits and shorten your duration exposure. We expect any easing cycle to be short-lived as structural inflation is here to stay due to fiscal deficits, demographic trends, and geopolitical tensions, therefore it would be an error to assume rates will go back to pre-COVID levels.

Check out our Stable Income Investment Strategy.

03. Commodities

Upward pressure on commodity prices is possible.

As volatility increased throughout the quarter, so did precious metal prices as the hawkish Fed rhetoric of January turned into dovish action during the banking crisis in early March. Gold topped $2,000 an oz for the third time in less than three years. The dynamics of lower bond yields, a weaker dollar, and rising geopolitical tensions, all point to a bullish market for precious metals. Oil spent most of the quarter in a trading range after a large pullback in 2H22, but prices perked up late in the quarter on dwindling global supply and a production cut from OPEC+. Natural gas prices languished near multi-year lows as LNG exports were limited due to the shutdown at the Freeport LNG terminal that came back online late last month. Other major commodities like copper traded mostly sideways for the quarter despite a clearly decelerating economy, which bodes well for prices once Fed policy truly turns accommodative. Layer on rising Geopolitical tensions that limit the free flow of supply, and we are likely to see structurally higher commodity prices over the coming years.

Want to learn what your best investment strategy will be this quarter? Explore our Investment Programs.

CONCLUSION

Q1 ended on a positive note across the board and investors are hoping for the positive momentum to be carried into Q2. As we dive into April, the Federal Reserve appears to be at the end of its tightening cycle given that cracks are beginning to show in the economy. Geopolitically, while Russia and China are drawn ever closer, tensions between Washington and Beijing are running hotter. A weakening dollar is likely to begin to boost commodities in the long run and drag companies that source, transport, and distribute those commodities with it. The recession that was once seen as inevitable may either be mild in the near future or become a thing of the past as we move toward the end of the year. Similar to last quarter, the market will continue to closely watch key indicators such as the Consumer Price Index (CPI), and Personal Consumption Expenditure (PCE) to help forecast fed policy. With inflation likely to be a structural reality for some time, and the second-order effects of not just Fed policy but the self-induced banking crisis are felt, one should expect Q2 to be just as choppy as Q1.

DISCLAIMER

There is no assurance that any of the target prices or other forward-looking statements will be attained. Any market prices are only indications of market values and are subject to change. Past Performance is a no guarantee of future results.

The prices of small and mid-company stocks are generally more volatile than large company stocks. They often involve higher risks because smaller companies may lack the management expertise, financial resources, product diversification and competitive strengths to endure adverse economic conditions.
Technology and internet-related stocks, especially of smaller, less-seasoned companies, tend to be more volatile than the overall market.

There are special risks associated with investing in preferred securities. Preferred securities generally offer no voting rights with respect to the issuer. Preferred securities are generally subordinated to bonds or other debt instruments in an issuer's capital structure, subjecting them to a greater risk of non-payment than more senior securities. In addition, the issue may be callable which may negatively impact the return of the security. Preferred dividends are not guaranteed and are subject to deferral or elimination.

Income from municipal securities is generally free from federal taxes and state taxes for residents of the issuing state. While the interest income is tax-free, capital gains, if any, will be subject to taxes. Income for some investors may be subject to the federal Alternative Minimum Tax (AMT).

Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in interest rates can result in the decline of the value of your investment. Investing in fixed income securities involves certain risks such as market risk if sold prior to maturity and credit risk especially if investing in high yield bonds, which have lower ratings and are subject to greater volatility.

All fixed income investments may be worth less than original cost upon redemption or maturity.

Although Treasury Inflation-Protected Securities (TIPS) are considered free from credit risk, they are subject to other types of risk. These risks include interest rate risk, which may cause the underlying value of the bond to fluctuate, and deflation risk, which may cause the principal to decline and the securities to underperform traditional Treasury securities. TIPS have special tax consequences, generating phantom income in the "inflation compensation" component of the principal. A holder of TIPS may be required to report this income annually although no income related to "inflation compensation" is received until maturity.

The yield, average life and the expected maturity of mortgage-backed securities are based on prepayment assumptions that may or may not be met. Changes in prepayments may significantly affect yield, average life and expected maturity.

Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability, and different accounting standards. This may result in greater share price volatility. These risks are heightened in emerging markets.

Investments in the energy sector are subject to the adverse economic events within that industry. A downturn in the energy sector of the economy, adverse political, legislative or regulatory developments or other events could have a large impact on a portfolio's investments in this sector.

Exposure to the commodities markets may subject an investment to greater share price volatility than an investment in traditional equity or debt securities. Products that invest in commodities may employ more complex strategies which may expose investors to additional risks.

Real Estate investments have special risks, including possible illiquidity of the underlying properties, credit risk, interest rate fluctuations, and the impact of varied economic conditions.

Additional information available upon request.

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