Q2 2023 Asset Management

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Index	1st Quarter Return	2022 Return
S&P 500 Index	7.50%	-18.11%
Nasdaq Composite Index	16.77%	-33.10%
US Aggregate Bond Index	2.96%	-13.01%
Russell 2000 Small Cap Index	2.74%	-20.44%
Bloomberg Commodity Index	-6.47%	13.75%

Markets started the year in a roaring mood led by the beaten down growth sectors of Communication Services, Technology, and Consumer Discretionary. It was a very eventful three months as market sentiment went through five unique phases.

- **Recession fears** – the first few weeks began with growing fears of a recession as economic indicators continued to come in weaker and earnings were expected to begin to show signs of weakness

- **Soft-landing optimism** – sentiment then shifted abruptly as earnings came in better than expected and though the economy was slowing there was growing confidence that the Fed would be able to nail the soft landing

- **The No Landing/reheating shift** – February brought inflation numbers that were stickier than hoped. The Fed raised rates and alluded to future rate hikes and no rate cuts for 2023. The Fed was determined to stomp out inflation even if risking a recession.

- **Fears of a bank crisis** – We then had a bank run as some regional banks with flighty depositors had poor asset-liability matching. In Switzerland Credit Suisse was folded into UBS overnight and fears were spreading that we were beginning to see cracks in the financial system.

- **Optimism that the banking crisis was contained** – The Fed stepped in and backed depositors as well as some struggling regional banks. Any crisis in

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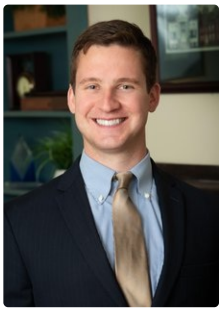

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Schedule a meeting

March came to naught and equities rallied to end out the quarter led by large gains in mega-cap tech.

I believe the Fed is stuck in what they are doing. It is hard for them to pivot when trend inflation is still stubbornly high for their liking. Their only chance to pivot is in case of a hard landing or emergency scenario. The Fed is too focused on the 1970s inflation narrative and by doing so is increasing credit risks in the economy.

Equity Risk Gauge

I will use this space to fill you in on where there is optimism and where there is pessimism in the markets.

Bullish indicators

Sentiment – sentiment continues to be overly bearish and tends to be a contrarian indicator. Both institutional and individual investors show record levels of pessimism and this bodes well for 1 year future returns.

Technicals – we have begun a short-term uptrend led by Mega-Cap tech. Also seeing positive performance from an economically sensitive sector in Semiconductors.

Bearish indicators

Internals – market breadth to start the year was flat as most performance came from mega-cap tech. Regional banks struggled and 4 of 11 sectors were down for the quarter including Financials, Energy, and Industrials.

Valuations – valuations have come back in line to historical averages but with expectations of continued earnings recession these multiples may continue to contract. With interest rates surging in 2022, fixed income and cash are now alternatives to generate some return.

Market Cycle – we are still in a bear market and have seen market performance come in flat since June of 2022.

The Fed – as mentioned previously, the Fed continues to remain hawkish with their policy as they fight yesterday's battle with inflation instead of having concerns over tightening financial conditions.

Economy – Leading indicators have begun to turn negative, and we have seen cracks in the employment numbers as they have continued to be revised down over the ensuing months (again Fed stuck looking at old/incorrect data). The yield curve is inverted across the curve and has historically been a telltale sign of a looming recession.

Model Changes

- We continue to maintain a defensive positioning and used the quarter to rebalance our models after large swings in certain sectors.

- We continue to hold an overweight position in cash, which now provides meaningful yield, as we believe markets have yet to bottom and continue to wait for better opportunities to add back to positions in cyclical sectors.

- We will look to add more fixed income exposure this quarter as we believe the Fed hiking schedule will soon be coming to an end and recession fears will be heightened.

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