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First Quarter 2023 Market Commentary

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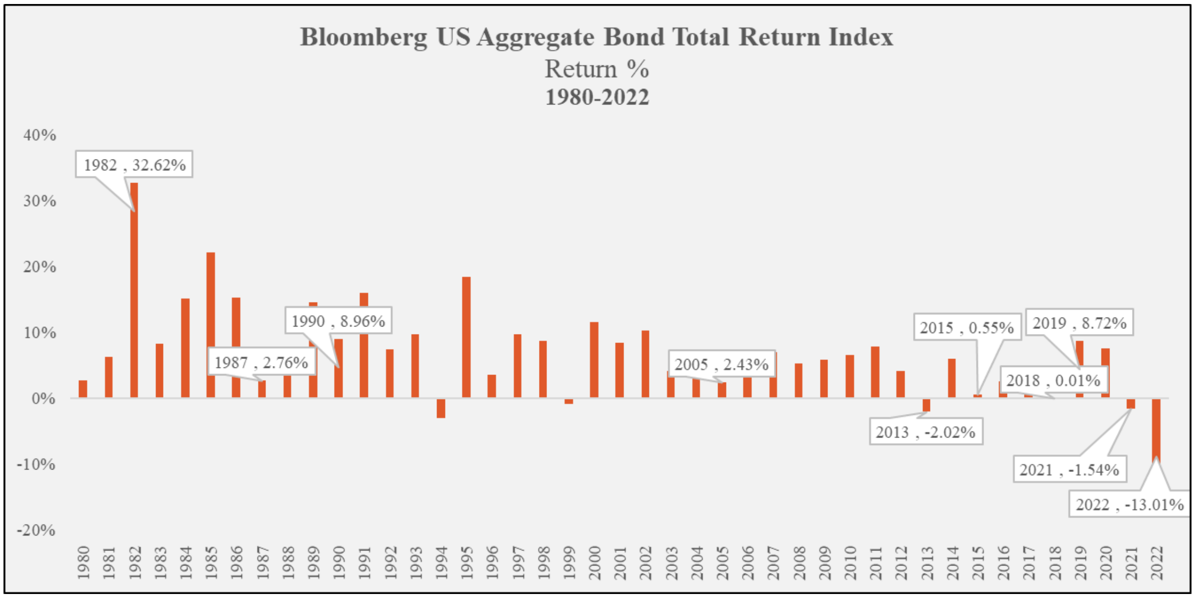
Some say the world will end in fire,
Some say in ice.
From what I've tasted of desire
I hold with those who favor fire.
But if it had to perish twice,
I think I know enough of hate
To say that for destruction ice
Is also great
And would suffice.
Robert Frost, December 1920

The symmetry of life is remarkable. Frost wrote *Fire and Ice* in an era when a global flu pandemic killed as many as 50 million people while a land war in Europe caused another 14 million military and civilian casualties. The global population was also much smaller than it is today, so it seems natural for many people who lived during this period to interpret these events as apocalyptic. A century later many investors seem to believe the world is not much different. The timing of Russia's invasion of Ukraine-just as the world was beginning to move past the deadly COVID-19 pandemic-has been a destabilizing force in markets throughout 2022. When a dramatic increase in inflation is added to the list of potential threats to the stability of the global economy investors have been historically pessimistic the last two years. In fact, our commentary from last quarter noted that consumer confidence has reached its lowest level in more than 70 years. Although many clients we speak with expect poor performance this year across most asset classes, we believe the worst may be behind investors.



It is our belief that opportunity exists across the fixed income landscape, particularly investment grade credit and mortgage-backed securities. The Bloomberg US Aggregate Bond Total Return Index, which measures the performance of investment grades issues, declined 13.01% in 2022, its worst performance since its 1976 debut, and possibly longer. By comparison, its second worst performance was -2.92% in 1994 which, coincidentally, was the first time the index experienced a negative calendar year return. The index has only experienced a negative return in five calendar years since inception, with two of them occurring over the last twenty-four months. Overall, the index has positive returns in 42 of 47 years. Mortgage-backed securities are another appealing option for their combination of attractive coupons and relative immunity from higher interest rates. Mortgage securities are most susceptible to prepayment risk, which we view as benign given the number of homeowners locked into long-dated mortgages issued at historically low rates. It is also worth noting that price discovery in real estate occurs at a slower pace compared to stocks and bonds which adds to their allure during a recession. We expect an orderly re-pricing of residential real estate over 2023 and possibly into 2024.

Our asset allocation heading into 2023 seeks to capture the opportunities previously discussed. The recent performance of our strategies has demonstrated that attractive risk-adjusted returns exist in the bond market. Investment grade bonds are a high quality, low volatility, and high yielding alternative to equities when seeking alpha. When our investment committee evaluates opportunistic areas of the market to increase risk-adjusted returns, we routinely ask ourselves "why assume the beta risk associated with equities when handsome returns are readily available in the fixed income market?" If you wish to learn more about our unique valuation-driven philosophy, please reach out to one of our advisors.