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ASSET MANAGEMENT, LLC

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# A View from the Bevy – 1Q23

## Market Review

It was a tumultuous quarter for stocks. The year started out well with a strong rally in January, but reversed course in February in the face of stubborn inflation and rising Treasury yields. The roller coaster continued in March, as the failure of two U.S. regional banks, the largest bank failures since the Great Recession of 2008 – 2009, sparked fears of a new financial crisis. Stocks ultimately rebounded to finish March (and the first quarter of the year) in positive territory.

Banking crisis fears peaked when past accounting irregularities were disclosed at Credit Suisse. The situation quickly calmed, however, thanks to the combination of 1) quick actions by the U.S. Federal Reserve (Fed) and Federal Deposit Insurance Corporation (FDIC), to guarantee depositors of the two failed banks and create a backstop for other depositors; 2) larger money center banks stepping in to offer assistance to a third regional bank on the brink of collapse; and 3) a negotiated takeover of Credit Suisse by rival UBS with the help of the Swiss government and Swiss regulators.

The markets were able to shake off all the uncertainty by quarter-end, as the general feeling now is that the problems in the regional bank sector that brought the market to a crisis of confidence may in fact be contained. And a better-than-expected inflation report on the last day of the quarter sent the markets into the second quarter on a high note.

Despite the volatility most broad market indices ended the quarter in positive territory, as shown below. U.S. stocks were led by the NASDAQ, as technology stocks showed resiliency after a very tough 2022. The NASDAQ actually managed to re-enter bull territory by quarter-end (a 20% increase from its December 28, 2022 low). Other developed nations performed in line with the broader U.S. market, while emerging markets lagged slightly.

| Stock Market Indices | 1st Quarter 2023 |
|---|---|
| S&P 500 | 7.5% |
| S&P 500 (Equal-Weight) | 2.9% |
| Dow Jones Industrial Average (DJIA) | 0.9% |
| NASDAQ Composite | 16.8% |
| Bloomberg US Aggregate Bond | 3.0% |
| Russell 2000 | 2.7% |
| MSCI World | 7.7% |
| MSCI World ex U.S. | 8.0% |
| MSCI Emerging Markets | 4.0% |

Source: AJO. Data supplied by FactSet Research Systems.

The turmoil in the markets did not deter the Fed from continuing its fight against inflation, as it raised short term interest rates by 25 basis points (0.25%) at its March meeting. Expectations before the banking failures had been for a 50 basis points increase.

# Market Outlook

While fears surrounding the banking system have abated, we are not completely out of the woods yet. We expect market volatility to continue for the foreseeable future. We remain confident in the stability of the financial system, but some risk does remain that nervous depositors could cause additional disruptions in the regional and community banking sectors. Even if this happens, however, we feel the Fed and FDIC will do whatever is necessary to provide stability to the system.

The markets face several other headwinds that could add to market volatility this year. Inflation remains stubbornly high, and the Fed remains committed to fighting inflation with the hope of getting it close to the desired level of 2%. The Fed has also indicated that it doesn't foresee any interest rate cuts in 2023, a disappointment to many market watchers.

The looming showdown over the debt ceiling will also likely weigh on markets until a resolution is reached. Negotiations usually go down to the wire, but we expect as usual a compromise will be reached to avert a potential disaster, even if it is only a temporary extension.

Meanwhile, global tensions remain high, and relations with both Russia and China seem to be at low points of the recent past. The war in Ukraine continues, and domestic tensions in ally Israel have raised concerns that hostility could escalate.

Despite the headwinds facing markets we remain optimistic. While the Fed does not foresee any rate cuts this year, it appears to be nearing the end of its tightening cycle with one more 25 basis point increase likely at the next Fed meeting. Stocks have also re-entered a bull market, as signaled by two consecutive positive quarters for the S&P 500.

While the possibility of the economy going into recession still exists, we would expect it to be a short and shallow one, with growth picking up relatively quickly. The job market remains surprisingly strong, and consumers are still spending money (for now at least). The US economy has been remarkably resilient despite everything that has happened over the past 15 months.

We have confidence that many of the high-quality names that we hold will help moderate losses in client portfolios regardless of what transpires in the economy. We continue to position client portfolios to benefit from future market upside, and volatility in the shorter-term may in fact provide selective buying opportunities.

As always, we stand ready to adjust to any developments that affect our portfolio holdings.

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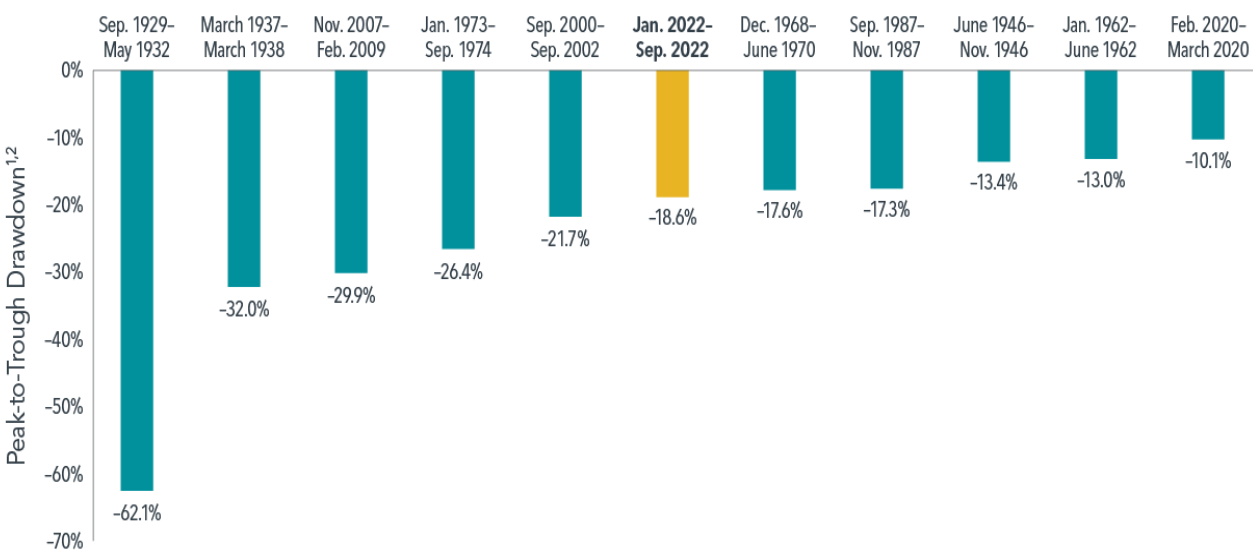
# Of Interest: Balanced Portfolios: Down but Not Out

2022 was a challenging year for investors, as there were few places to hide. On top of a large drop in stocks, unanticipated losses in bonds were especially unnerving, leading some to question whether the balanced portfolio is dead and if diversification still works. We believe that it does.

Although 2022 saw the worst start to a year in history for many bond indices, the overall performance for the common 60/40 portfolio (60% stocks/40% bonds) did not even crack the top (or, alternatively, worst) five historical drawdowns of the last century, as shown in Exhibit 1. While a 19% loss of wealth is not fun, it's only two-thirds of the drawdown investors suffered during the financial crisis of 2008–2009.

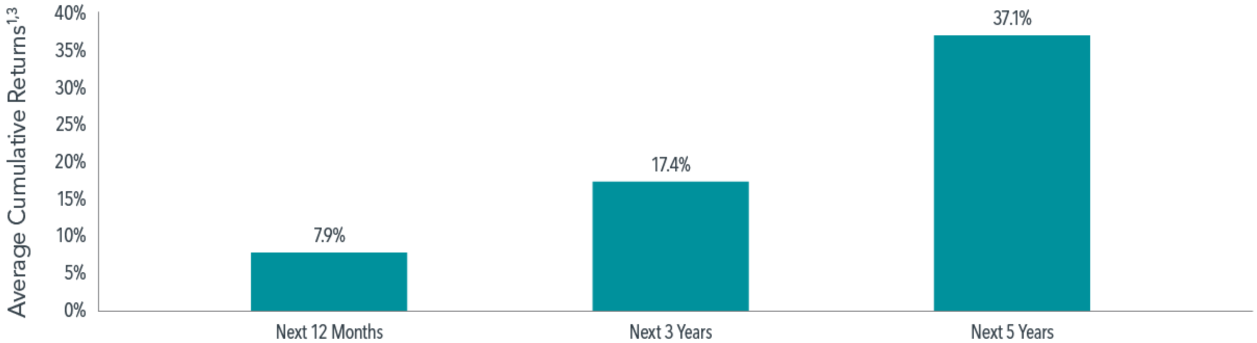
Exhibit 1 – Not Such a Low Blow
(60% S&P500 Index / 40% Five-Year U.S. Treasury Notes
January 1926 – September 2022)




Note: Past performance is not a guarantee of future results. Indices are not available for direct investments; therefore, their performance does not reflect the expenses associated with the management of an actual portfolio. Source: Morningstar Direct.

It is important, especially when market conditions are volatile, to not focus solely on where returns have been but also on where they could be going in the months and years ahead. Looking at the performance of the same 60/40 portfolio following a decline of 10% or more since 1926, as shown in Exhibit 2, you can see that returns on average have been strong in the subsequent one-, three-, and five-year periods. History makes a strong case for you to stick with your longer-term investment plan. It should also serve as a reminder that large declines shouldn't derail you from the expected long-term benefits of investing.

Exhibit 2 – Still in the Fight
(60% S&P500 Index / 40% Five-Year U.S. Treasury Notes
January 1926 – September 2022)




Note: Past performance is not a guarantee of future results. Indices are not available for direct investments; therefore, their performance does not reflect the expenses associated with the management of an actual portfolio.

Markets have proven quite resilient over the long run. The most important thing is to roll with the punches and not get sidetracked by short-term moves. If history is any guide, there's reason to believe that the balanced portfolio is alive and well and poised to deliver healthy returns going forward.