TRIVANT

CUSTOM PORTFOLIO GROUP, LLC

April 2022

Quarterly Insights

EXECUTIVE SUMMARY

Stocks And Bonds Down In Q1

In the First Quarter, the domestic S&P 500 Index was down 4.60% but out-performed all major regions. The Russian invasion of Ukraine (February 24), sky-rocketing oil prices, inflation concerns, and trepidation regarding Fed rate hikes elevated market volatility. To combat high annual inflation (7.9% in February), the Fed initiated a 0.25% rate hike in March and signaled several future rate hikes. This wreaked havoc on bond prices. In Q1, the Bloomberg US Aggregate Bond Total Return USD Index fell 5.93%, the largest quarterly bond decline since 1980.

Risk Management In A Down Market

If you felt nervous at times in Q1, you were not alone. Be calm. Stick to your game plan:

1. Don't let your emotions get the best of you.
2. Remember the "baseline"!
3. Periods of market volatility are normal.
4. Return volatility falls over longer time frames.
5. There are dire consequences when investors act on their emotions.
6. Amidst market volatility, maintain discipline in asset allocation strategies.

First Quarter 2022

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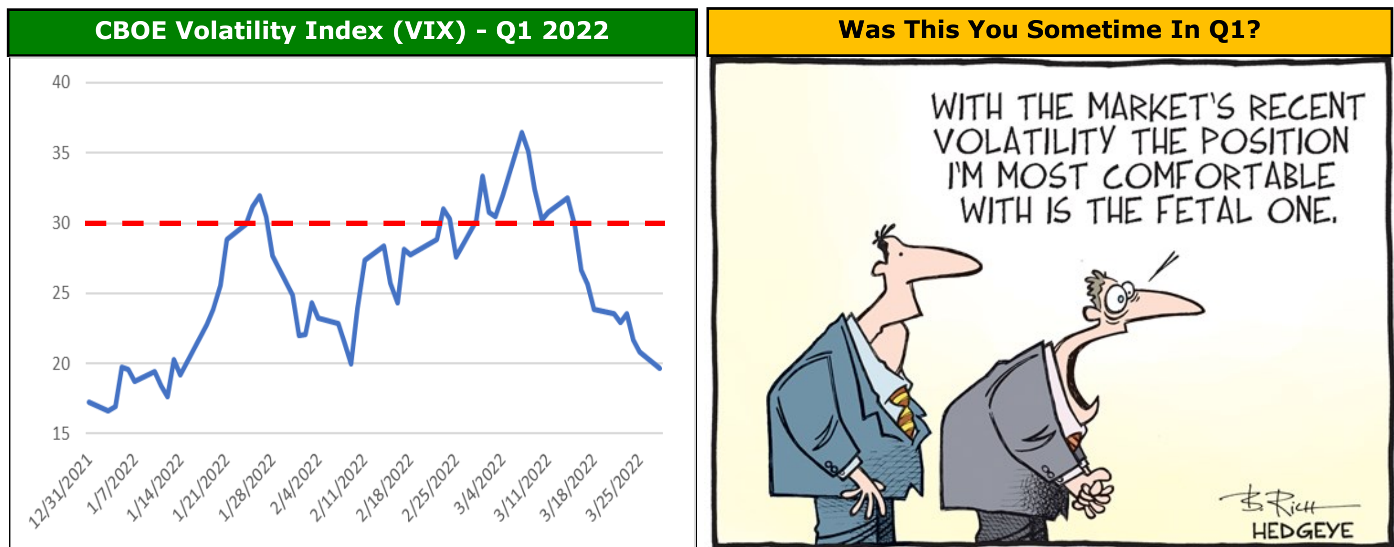
If You Felt Nervous At Times In Q1, You Were Not Alone

The First Quarter was marked by the Russian invasion of Ukraine (February 24), sky-rocketing oil prices driving further inflation concerns, and continued market trepidation regarding impending Fed rate hikes. Positive news regarding the US economy and employment got lost in the mix. In an unusual occurrence, both US stocks and bonds fell in Q1, bonds by more than stocks.

It was not unusual to see the stock market fluctuate plus or minus 3% within a single day in Q1. The Chicago Board Options Exchange (CBOE) Volatility Index (symbol: VIX) is a measure of market sentiment. Unofficially nicknamed the "fear index", the VIX shows the expected level of price fluctuation in the S&P 500 Index options over the next 12 months. A VIX value of less than 20 generally corresponds to stable, stress-free periods in the markets. A VIX value of greater than 30 indicates large volatility from increased uncertainty and perceived risk. The VIX exceeded 30 many days in Q1. If you felt nervous at times, you were not alone.



Don't Let Your Emotions Get The Best Of You

Amidst the high volatility, the S&P 500 Index fell over 12% from January 1 through March 8. We know that people get nervous when the market corrects by roughly 12%. That is when we start to get phone calls and emails. We also know that the worst long-range investing mistakes are made when people get nervous and act in a panic. Don't let your emotions get the best of you. As your portfolio manager, we are here to help by approaching investing with as little emotion as possible. Please contact us if you are feeling uncomfortable.

Remember The Baseline!

In the last 96 years, the US stock market has had an annual return of roughly 10% (the "baseline rate"). The century has endured two world wars, countless regional scuffles, assassinations of global leaders, nuclear detonations, recessions and depressions, impeachments, numerous scandals, asset bubbles, terrorism, and other external shocks. And yet the beat goes on: the baseline rate persists in a remarkably consistent fashion amidst countless times where it appears the world is falling apart.

We have faith in the market because we believe in capitalism: over the last century, companies have consistently adapted to new market conditions in a manner that has maximized profits. And we expect this trend to continue over the next century.

Periods Of Market Volatility Are Normal

While always unpleasant, market declines are regular events. They are normal. Don't fret when they happen.

A 70-Year History Of Market Declines (1951-2021) - Source: Capital Group			
Type of Decline	**Average Frequency**	**Average Length**	**Last Occurrence**
-5% or more	About 3 times a year	43 days	September 2021
-10% or more	About once a year	110 days	September 2020
-15% or more	About once every 3 years	251 days	March 2020
-20% or more	About once every 6 years	370 days	March 2020

Return Volatility Falls Over Longer Time Frames

It is interesting to note how consistent market returns have been from an historical standpoint (despite market corrections). The stock market has averaged an annualized 10.46% return since 1926. On a year by year basis, the market standard deviation from this average return is roughly 20%. However, the standard deviation drops dramatically the longer the investment time frame. Put another way, the stock returns become much more predictable the longer the investment time frame. Patience is key in successful investing.

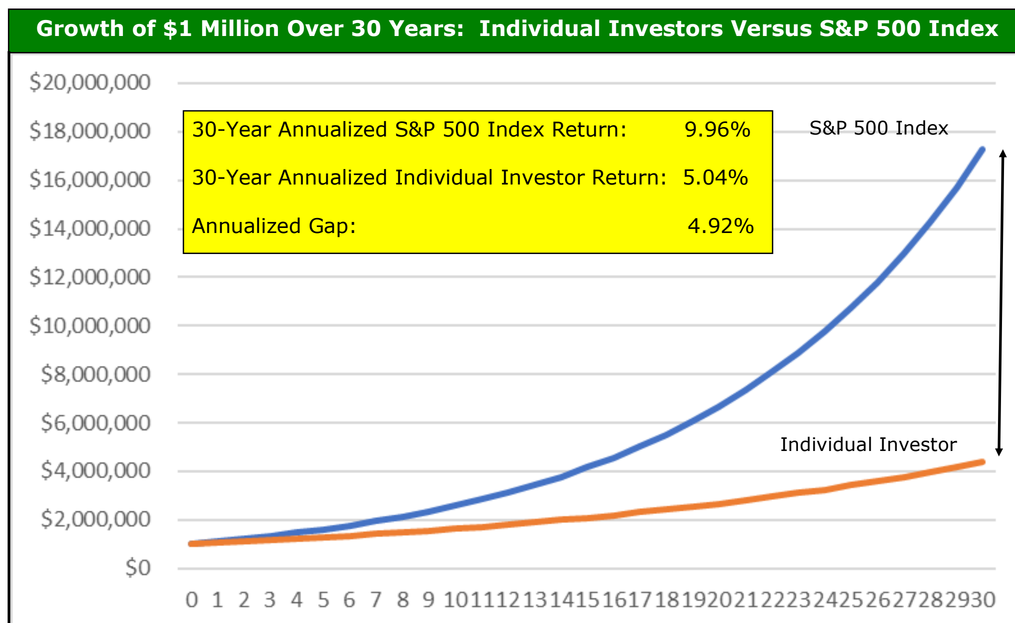
Return Volatility Falls Over Longer Time Frames				
	1 Year			
Average Return	10.46%			
		Trailing 10 Year	**Trailing 20 Year**	**Trailing 30 Year**
Standard Deviation	19.63%	5.51%	3.42%	1.30%

Source: Telemet

There Are Dire Consequences When Investors Act On Their Emotions

Dalbar Inc. publishes an annual study called the Quantitative Analysis of Investor Behavior (QAIB). Their research shows that the inability of individual investors to stay invested over time is a big detriment to their portfolio performance. Put another way, investors cannot time the market by jumping out every time they feel nervous and lose faith. They would be much better off being disciplined and sticking to their game plan.

Growth of $1 Million Over 30 Years: Individual Investors Versus S&P 500 Index



Source: DALBAR QAIB 2020

SAD BUT TRUE

Starting with an investment of $1 million, an individual investor lagged the S&P 500 Index by roughly

$1 million over 10 years

$4 million over 20 years

$13 million over 30 years

due to

Emotional Behavior.

Radical Shifts In Asset Allocation Are Dangerous

During the quarter, some clients asked whether we should consider a major shift from stock exposure to bond/cash exposure. In theory, this is an easy move to make. In reality, this is a dangerous move to make. The motivation to move away from stock exposure is to
- Avoid a portfolio market decline
- Re-enter the market just in time for its recovery

Short-term market direction is unpredictable, as evidenced by the late rebound to end Q1. The odds against a perfect portfolio move (exiting the market just when it begins to move down and subsequently re-entering the market just when it begins to move up) are staggering. One of the most important aspects of portfolio management is risk control. An ill-timed radical shift in asset allocation can have tremendous downside.

CASE STUDY

Suppose a retired 65 year old client has a target 75% stock exposure (25% bonds / cash), and that the portfolio is comprised of taxable and tax-deferred accounts. The target asset allocation allows for a 90% "Probability of Success". Shifting the portfolio to a 100% exposure in low-yielding bonds / cash will automatically bring the "Probability of Success" significantly below the 90% target. This is not a sustainable long term strategy.

Let us assume that we rid the portfolio of stocks with the intent of re-entering the stock market at a later point in time. Regardless of the subsequent direction of the market, there will most likely be significant realized capital gains in the taxable account (the S&P 500 Index doubled in the last three years alone). If the market exit proves to be wrong (the market subsequently goes up over time and the portfolio has no stock exposure), the client loses. If the market re-entry proves to be wrong (the market subsequently goes down over time and the portfolio has repurchased stocks), the client loses.

In a worst-case scenario of market timing, there are two rounds of losses as well as taxes owed for realized capital gains. The client may never be able to recover a satisfactory "Probability of Success". **This is the chance (whatever the odds) that we cannot take.** The prospect of "staying in the market" (75% stocks) and "weathering the storm" will not likely deter a long-term satisfactory "Probability of Success". After all, we have incorporated the odds of a "down market" (down 20% or more) into our financial planning model.

The Payoff Matrix

Strategic Action	Costs Incurred	Subsequent Direction Of The Market	
		Market Goes Up	Market Goes Down
Exit the Market	Taxes on gains (non-IRAs)	LOSE	GAIN
Re-Enter the Market	-	GAIN	LOSE
Stay in the Market	-	GAIN	LOSE

Conclusion: Maintain Discipline In Asset Allocation Strategies

Market corrections in the range of 15% - 20% are unpleasant but not unusual. In any historical longer-term time interval, stocks have out-performed bonds and cash due to what is called an "Equity Risk Premium (ERP)". Stocks are riskier than bonds and cash, and must reward investors for assuming this extra risk. We expect the ERP will persist going forward.

It is a poor bet to anticipate the ERP will not apply in the long-term. It is also a dangerous bet to try and "time the market" in the short-term (the market is positive in 75% of calendar years). The combination of these bets, in our opinion, would likely be disastrous. We have maintained portfolio equity exposure where warranted.

All Major Regions Down In Q1

In the First Quarter, the domestic S&P 500 Index was down 4.60% but out-performed all major regions. Europe was negatively impacted by the Russia/Ukraine crisis. Energy (+38.00%) was positively impacted as oil prices soared and was by far the star sector performer - only two sectors were positive in Q1.

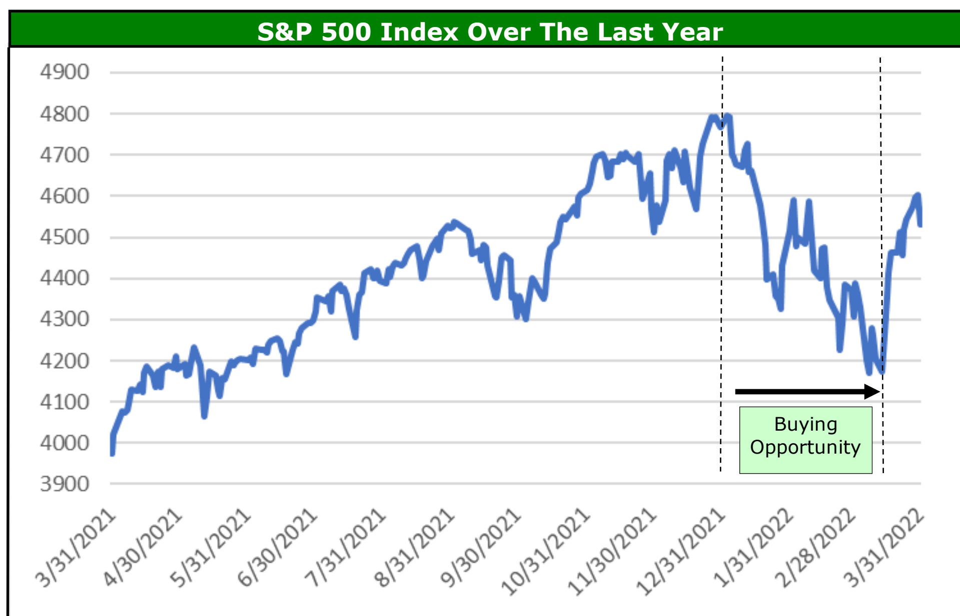
Equity Index Performance

Index	Q1 2022	2021
S&P 500 (Domestic)	**(4.60%)**	**28.71%**
MSCI EAFE (Foreign) *	**(5.91%)**	**11.26%**
MSCI Emerging Markets	**(6.97%)**	**(2.54%)**
MSCI EMU (European Monetary Union)	**(11.14%)**	**13.54%**
MSCI Japan	**(6.61%)**	**1.71%**

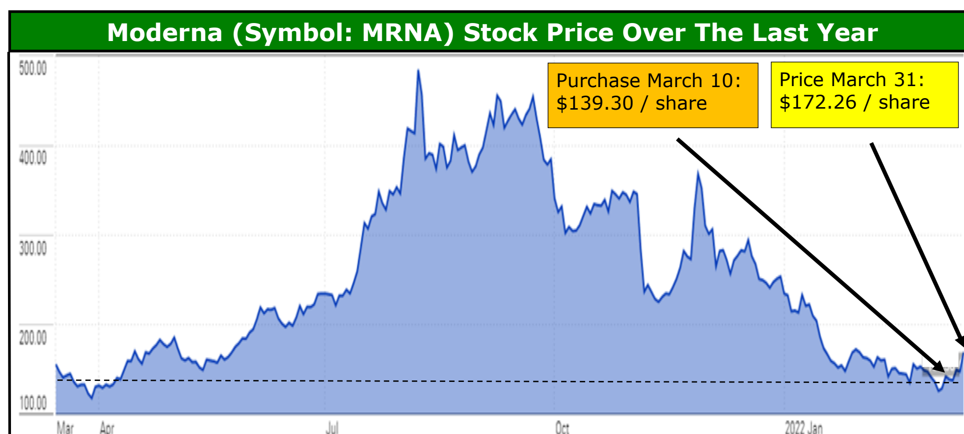
* Europe, Australia and the Far East

Anatomy Of A Buying Opportunity In A Down Market: Moderna Inc (Symbol: MRNA)

The S&P 500 Index steadily rose in 2021 (+28.71%) but fell 12.48% from January 1 through March 8. This decline technically qualified as a correction, and was a magnitude of which we know our clients start to get nervous. As discussed, investment discipline is key when managing through the tougher times. We have a game plan if the market goes up or down, and we looked at the market decline as a buying opportunity for the right stock(s).



Moderna (symbol: MRNA) had its COVID-19 vaccine approved in early 2021, validating its mRNA technology. The stock price exploded through mid-summer. Then covid settled down, investors took profits, and the stock price retreated to its level a year ago. We saw this as a buying opportunity. MRNA has significant upside potential.



After we purchased MRNA on March 10, it rose 23.66% in 21 days.

Bonds Fall A Lot In Q1

The Bloomberg US Aggregate Bond Total Return USD Index (AGG), a broad-based representation of bond performance, fell 5.93% in the First Quarter, following a 1.54% fall in 2021. The Q1 bond index decline was the largest quarterly decline since 1980. Many investors were likely shocked - normally they expect bonds to be the "safe" component of their portfolio.

Key US Interest Rates	December 31, 2021	March 31, 2022	Change
Federal Reserve Board Funds Target Rate	0 - 0.25%	0.25% - 0.50%	+ 25 basis points
2-Year Treasury (Constant Maturity)	0.73%	2.28%	+ 155 basis points
5-Year Treasury (Constant Maturity)	1.26%	2.42%	+ 116 basis points
10-Year Treasury (Constant Maturity)	1.52%	2.32%	+ 80 basis points

Why Did Bonds Fall So Much?

Put simply, bonds fell a lot in Q1 because interest rates rose. Remember the inverse relationship between interest rates and bond prices. As interest rates rise, bond prices fall. The Fed mandate is full employment and 2% inflation. We have full employment, but in February the Consumer Price Index increased 7.9% over the last 12 months (source: US Bureau of Labor Statistics). To combat this very high inflation, the Fed raised its target rate from zero to 0.25% on March 16, signaled six more quarter point rate hikes this year and four more hikes in 2023, bringing its projected target rate to 2.8% in 2023. The combination of current rising rates (see Q1 Yield Curve upward shift below) and the expectation of significant future rate hikes wreaked havoc on bond prices.

The Relationship Between Interest Rates and Bonds

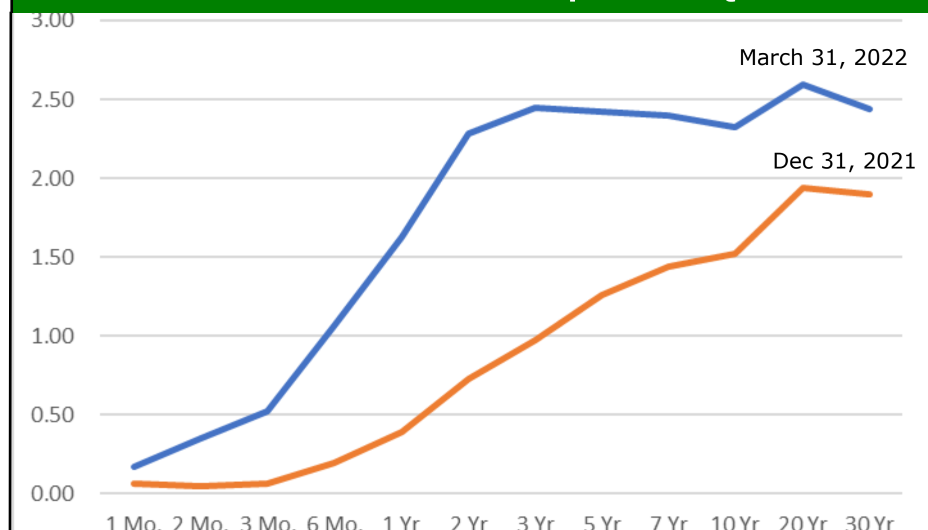
Interest Rates Rise

Bond Prices Fall

Bond Yields Rise

Ultimately we view rising bond yields as good news for investors who need income from their investment assets.

The Yield Curve Shifted Upward In Q1



Three Reasons Why Our Bond Portfolio Significantly Out-Performed The AGG

1. Our portfolio had less sensitivity to rising interest rates than the AGG.
2. 30% of our portfolio was in inflation-indexed bonds (TIPS), where principal and payments keep pace with inflation through semi-annual adjustments. There are no inflation-indexed bonds in the AGG.
3. Our SPDR Senior Loan ETF has floating rate interest protection that pays more when rates rise.

Avoid IRS Paperwork By Staying Within The Annual Gift Tax Exclusion Limit

Those who gift large sums of money to individuals are usually giving this money to their children. By giving these funds gradually over time rather than all at once, and staying within the annual gift tax exclusion limit, reporting the gifts to the IRS is avoided. There is the added benefit of reducing your estate and potentially sidestepping estate taxes. The annual gift tax exclusion to any one individual was $15,000 for the 2021 tax year and has been raised to $16,000 for 2022.

This means you can avoid IRS reporting by giving up to $16,000 to any one individual during a calendar year (starting in 2022). Your spouse (if applicable) can also gift the maximum to the same individual, effectively allowing a $32,000 annual gift without tax reporting. You (and your spouse) do not have to let the IRS know about the gift, and the gift recipient will not have to report or pay taxes on the gift.

Reduce Your Estate By Staying Within The Annual Gift Tax Exclusion Limit

Under current law, a single person has a lifetime limit of gifts equal to $12,060,000. The federal state tax laws provide that a person can give up to that amount during their lifetime or die with an estate worth up to $12,060,000 and not pay any estate taxes (currently the estate tax is up to 40% for amounts above the lifetime exemption). Annual gifts that fall within the annual gift tax exclusion do not count against the lifetime limit of gifts - so a series of these annual gifts can add up over time and ultimately reduce your estate. Also bear in mind that the current lifetime limit of gifts is set to be cut in half at the start of 2026.

Annual and Lifetime Gift Limits	2021 Limit	2022 Limit
Annual Gift Tax Exclusion (for a Single Person)	$15,000	$16,000
Annual Gift Tax Exclusion (for a Married Couple)	$30,000	$32,000
Lifetime Limit of Gifts (for a Single Person)	$11,700,000	$12,060,000
Lifetime Limit of Gifts (for a Married Couple)	$23,400,000	$24,120,000

What Happens If You Exceed The Annual Gift Tax Exclusion Limit

You will need to submit Form 709 to the IRS if you give a gift of more than $16,000 to one individual in 2022 (for a single person) or more than $32,000 to one individual in 2022 (for a married couple). On this form, you'll notify the IRS of your gift. The IRS uses this form to track gift money you give in excess of the annual exclusion throughout your lifetime. Therefore, you'll be asked for the amount of the gift and the amount over the annual exclusion amount. If you ever go over the lifetime limit of gifts, you'll then need to start paying the gift tax. Form 709 is lengthy and complicated - try to avoid it if possible!

What Happens If Your Estate Exceeds The Lifetime Limit Of Gifts

If you’re lucky enough and generous enough to use up your exclusions, you may indeed have to pay the gift tax. The rates range from 18% to 40%, and the giver generally pays the tax. For those who anticipate their estate will exceed the lifetime limit of gifts, it may be opportune to consult with both a tax professional and a legal professional. We are neither tax nor legal professionals. Please let us know if we can facilitate an introduction.

We made several portfolio adjustments in Q1. The rationale for these moves included an increased defensive posture (Health Care, Staples and Industrials), geopolitical concerns, and selling/paring back some highly appreciated positions to take profits.

We bought Moderna Inc (symbol: MRNA; $68 billion market cap), whose mRNA technology was rapidly validated with its COVID-19 vaccine. With 44 mRNA development programs as of early 2022, we believe the company has tremendous upside potential. Also, we bought Boston Beer (symbol: SAM; $5 billion market cap), a leader in US high-end malt beverages. Finally, we bought Nutrien Ltd (symbol: NTR; $59 billion market cap), the world's largest fertilizer producer, in light of the Russia/Ukraine fertilizer supply shock. We increased our position in Abbott Laboratories (symbol: ABT; $213 billion market cap) a leader in Health Care, and in Northrup Grumman Corp (symbol: NOC; $67 billion market cap), a leading defense contractor.

We sold Chipotle Mexican Grill Inc (symbol: CMG; $43 billion market cap), the largest fast-casual restaurant chain in the US. Also, we sold Starbucks (symbol: SBUX; $100 billion market cap), the globally dominant player in specialty coffee. Both CMG and SBUX did exceptionally well during our many years of ownership, but we felt it was time to exit the companies. Additionally, we sold Taiwan Semiconductor Manufacturing Company (symbol: TSM; $540 billion market cap). TSM also did exceptionally well since initially purchased in November 2019, but we became concerned about rising political tensions between Taiwan and China. Finally, we pared back Lowe's Companies Inc (symbol: LOW; $174 billion market cap) to take profits.

We will continue to closely monitor the market and adjust your portfolio as needed. Please feel free to contact us anytime to discuss questions or comments you may have. We will keep you informed of portfolio progress.

Respectfully submitted,

TRIVANT

CUSTOM PORTFOLIO GROUP, LLC

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Disclaimer

The information presented herein is intended for informational purposes only. All views are subject to change based on updated indicators. The recommendations made in this publication are made without regard to individual suitability. Investors should consider their own needs and objectives before making any investment decision.

Commentary in this review reflects our portfolio strategy. Many of our clients have different objectives and circumstances which are reflected in unique portfolio considerations. Please note that accounts may not contain all elements of the strategy discussed here. Additionally, individual client customizations and start dates may preclude certain elements of this strategy from being implemented.

Past performance is no guarantee of future results. A risk of loss is involved with investments in stock markets.