TRIVANT

CUSTOM PORTFOLIO GROUP, LLC

January 2023

Quarterly Insights

EXECUTIVE SUMMARY

2022 - The S&P 500 Index Was Down 18.11%

In 2022, the domestic S&P 500 Index was down 18.11%. The US was in line with global performance - there was nowhere to hide. Our initial 2022 market prediction for the S&P (+8%) was way off. We did not foresee persistent close to double-digit inflation - so we did not expect the Fed to raise its target rate from zero to 4.25% over the year. "Aggressively restrictive" Fed policy hurt stocks and bonds. The Bloomberg Barclay's Aggregate Bond Index fell 13.01%, the worst year ever for bonds.

We Believe The S&P 500 Index Will Be Flat In 2023

We believe the S&P 500 Index will be flat in 2023, falling in the first half and rising in the second half. Conditions point to a "transition year" for stocks. Right now we have:

- More rate hikes expected in the first half of 2023
- Quantitative tightening (QT)
- Inflationary pressures
- Above-average market valuation
- Earnings expectations that may be too high

Fourth Quarter 2022

In This Issue

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Deliberate Investing

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Peace Of Mind

Stock Outlook: We Believe The S&P 500 Index Will Be Flat In 2023

We believe the S&P 500 Index will be flat in 2023, falling in the first half and rising in the second half. Conditions point to a "transition year" for stocks. On the positive side, the economy is resilient**,** unemployment is low, and the US is taking strong steps towards innovation (such as the CHIPS and Science Act of 2022). On the challenging side, high inflation persists and in order to cool the economy, the Fed is expected to continue to raise its target rate and "shrink the balance sheet" via quantitative tightening (tightening the monetary supply by reducing its securities holdings). Right now we have:

- More rate hikes expected in the first half of 2023 (in the range of 0.75% to 1.25%)
- Quantitative tightening (QT) - see discussion on page 3
- Continuing inflationary pressures - wages, the onshoring of industries, tariffs
- Above-average market valuation - the historical Price/Earnings ratio of the S&P 500 Index is 15.99 and the current P/E ratio is 19.69
- Earnings expectations that may be too high (must fully factor in recession risk, inflation, Fed rate hikes)

Follow The Fed

By far the biggest driver for our 2023 flat stock market outlook is the anticipated actions of the Fed. History has shown that the stock market out-performs in "Expansive Monetary Conditions" (when the Fed is lowering its target rate) and under-performs in "Restrictive Monetary Conditions" (when the Fed is raising its target rate).

US Stock Market Performance: January 1966 - December 2013

	All Monetary Conditions (576 Months)	Expansive Monetary Conditions (172 Months)	Indeterminate Monetary Conditions (209 Months)	Restrictive Monetary Conditions (195 Months)
S&P 500 Return (Annualized)	10.56%	**15.18%**	11.10%	**5.89%**

Source: Invest With The Fed

US Stock Market Performance: January 2014 - December 2022

	All Monetary Conditions (107 Months)	Expansive Monetary Conditions (21 Months)	Indeterminate Monetary Conditions (30 Months)	Restrictive Monetary Conditions (56 Months)
S&P 500 Return (Annualized)	11.28%	12.42%	21.56%	5.91%

Source: TriVant

The Fed anticipates further restrictive policy in 2023 in its effort to cool the economy and bring down inflation. Consequently, we will follow the Fed and anticipate a below-average year in the stock market.

Median Economic Projections of Federal Reserve Board From December 14, 2022 Meeting

Variable	2022	2023	2024	2025	Longer Run
Change in real GDP	0.5	0.5	1.6	1.8	1.8
Unemployment Rate	3.7	4.6	4.6	4.5	4.0
Inflation	5.6	3.1	2.5	2.1	2.0
Fed Funds Rate	**4.4**	**5.1**	4.1	3.1	2.5

The Stock Market Will Likely Be A Year Of Transition

We believe a realistic scenario in 2023 is a stock market that falls in the first half, rises in the second half, and nets out flat for the year. Here are three factors that could cause the market to fall in the first half:

1. **Further Fed Rate Hikes**

2. **Further Fed Quantitative Tightening (QT)**

The Fed has been shrinking its holdings of bonds since the summer as part of its broader effort to increase the cost of borrowing to help slow the economy and bring inflation down from its highest levels since the 1980s. There has been no end date given for QT. The total Fed balance sheet peaked at close to $9 trillion in April. Since QT started in September, the Fed said it would permit up to $60 billion a month in Treasurys and $35 billion a month in MBS (mortgage backed securities) to be reduced. As of December 14, the Fed holdings were $8.6 trillion. The Fed may aim to get this figure down to $7 trillion over time. Perhaps QT tails off by Q4.

3. **A Recession**

A recession is considered to be a prolonged economic downturn (reduction in GDP) that broadly affects the economy and typically lasts two quarters or more. Given the considerable Fed restrictive policies at this time, we anticipate a mild recession in 2023 where the initial headline news will hurt the stock market.

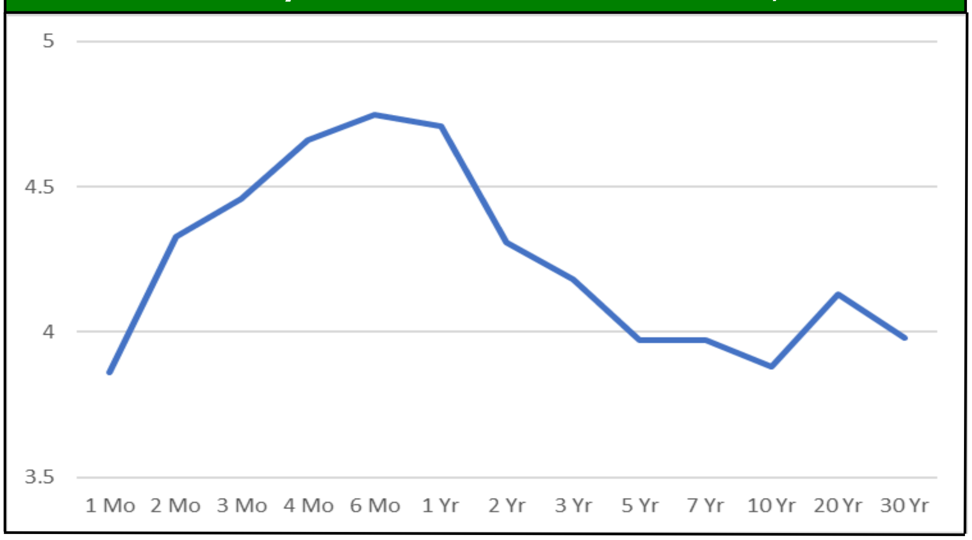
Here are three factors that could cause the market to rise in the second half:
1. **A Fed Rate Pause/Cut To Bolster The Economy** - the market would embrace an easing of Fed policy
2. **History** - since 1928, the S&P 500 Index has fallen for two straight years on only four occasions
3. **A Recession** - a recession is a positive forward market indicator (see Quarterly Insights, July 2022)

Stock Portfolio Considerations: Be Patient. Take Advantage Of Good Buying Opportunities.

The Bond Market Has Already Transitioned To Greater Investment Opportunities

With higher interest rates, the risk in the bond market has declined considerably and there are greater investment opportunities. Investors can now earn a safe 4%+ return with a short-term US Treasury bond (a year ago, a safe return was 1%). We are starting to see bond opportunities that exceed a 5% return with minimal investment risk. A balanced portfolio (a mix of stocks and bonds) now offers an increasingly attractive risk/return tradeoff.

The Treasury Yield Curve As At December 31, 2022



<u>The Yield Curve Is Inverted</u>

An inverted yield curve occurs when short-term debt instruments carry higher yields than long-term instruments of the same credit risk profile.

This suggests that the near-term is riskier than the long-term.

An inverted yield curve is one of the most reliable leading indicators of an impending recession.

Our 2022 Market Prediction Was Way Off

We predicted the S&P 500 Index would rise 8% in 2022 and the index fell 18.11%. These were our thoughts:

We believe the S&P 500 Index will rise 8% in 2022. Conditions point to a positive but below average year. Vaccines are here and being more readily adapted. The economy is strong, and both the Fed and federal government want to keep it that way. We have

- *A Fed that has signaled it will raise interest rates to combat inflation*
- *A mature US stock market where the S&P 500 Index has doubled in three years*
- *High market valuation (the Price/Earnings ratio of the S&P 500 Index is 28.65)*
- *A pandemic that continues to be a wild card despite higher vaccination rates*
- *Rising wages that may impact profits of labor intensive companies*

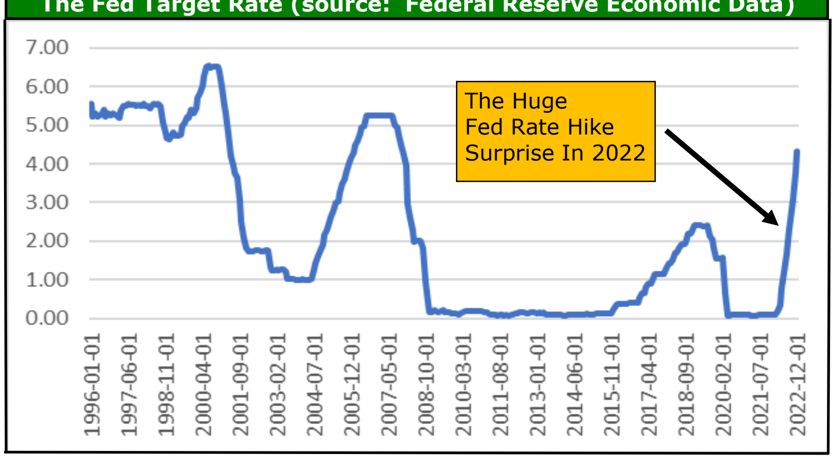
What Did We Miss?

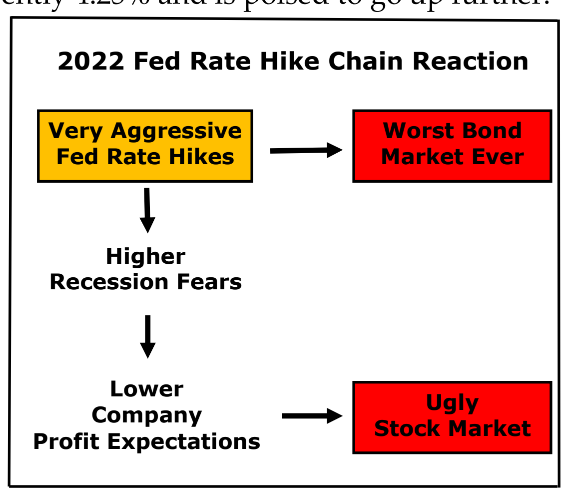
The inflation that was deemed "transitory" by the Fed in late 2021 did not subside. We did not foresee close to double-digit inflation throughout 2022 - so we missed how much (4.25%) the Fed would raise its target rate and its level of quantitative tightening. The Fed was "aggressively restrictive" to a level not seen since 1980. In its December 2021 meeting, the Fed signaled up to three quarter-point rate hikes for 2022 in response to a November inflation reading of 6.8% (at the time, a 39-year high). Presuming three rate hikes, the Fed target rate would have gone from zero to 0.75% by year-end. In our January 2022 Quarterly Insights, we cited 6-12 month time frames where the Fed hiked rates in the range of 0.50%-1.50% and the market was up 8%-10%. Hence our 2022 market prediction of +8%. This was not what ultimately happened - not even close.

In Q1, Russia invaded Ukraine (February 24), oil prices sky-rocketed, the COVID shutdown in China created supply chain issues, low US unemployment initiated rising wage pressures, and inflation rose further (7.9% in February). To combat high inflation, the Fed raised its target rate from zero to 0.25% on March 16, signaled six more quarter point rate hikes for the year and four more rate hikes in 2023, bringing its projected 2022 target rate to 2.8%. This was a surprise. Only three months earlier, the projected 2022 target rate was 0.75%.

In Q2, the Fed raised its target rate faster than earlier indicated as annual inflation reached 8.6% in May and 9.1% in June. There was a 0.50% rate hike on May 8 and another 0.75% hike on June 15. In Q3, high inflation persisted and the Fed initiated two more 0.75% rate hikes (July 27 and September 21). While inflation started to come down a little in Q4 (7.1% in November), it was still too high for the Fed. Rates were hiked 0.75% on November 7 and 0.50% on December 14. The Fed target rate is currently 4.25% and is poised to go up further.

The Fed Target Rate (source: Federal Reserve Economic Data)





2022 - An Ugly Year All Around

We reflect on 2022 as a year where both the S&P 500 Index and US bonds gave way to restrictive Fed policy, and foreign and emerging markets gave way to their own restrictive central bank policies. Higher interest rates, recession fears and future earnings concerns were hard barriers for stocks to overcome.

S&P 500 Index At A Glance	
Q1 2022:	- 4.60%
Q2 2022:	- 16.10%
Q3 2022:	- 4.88%
Q4 2022:	+ 7.56%
2022 Total:	- 18.11%

1. There Was Nowhere To Hide

High (over 90%) exposure to US stocks did not affect our results because the US was in line with global developed market performance. Our larger-cap focus slightly helped us as the small cap Russell 2000 Index (-21.56% for 2022) lagged the S&P 500 Index. There was no relief with emerging markets emphasis. While China was +13.52% in Q4, it was down 21.93% for the year.

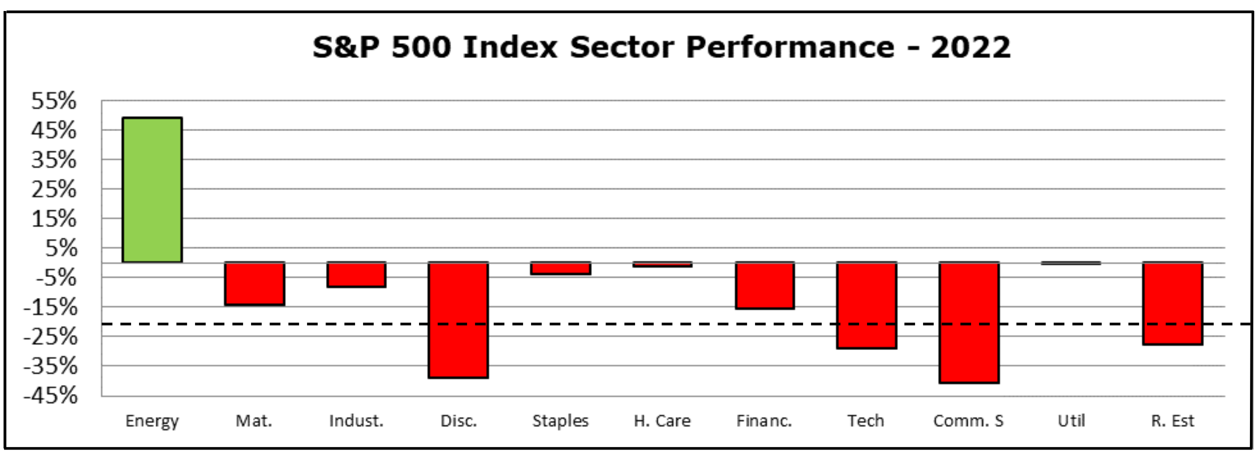
Equity Index Performance

Index	Q4 2022	2022
S&P 500 (Domestic)	**7.56%**	**(18.11%)**
MSCI EAFE (Foreign) *	**17.34%**	**(14.45%)**
MSCI Emerging Markets	**9.70%**	**(20.09%)**
MSCI EMU (European Monetary Union)	**22.80%**	**(17.86%)**
MSCI Japan	**13.23%**	**(16.55%)**

* Europe, Australia and the Far East

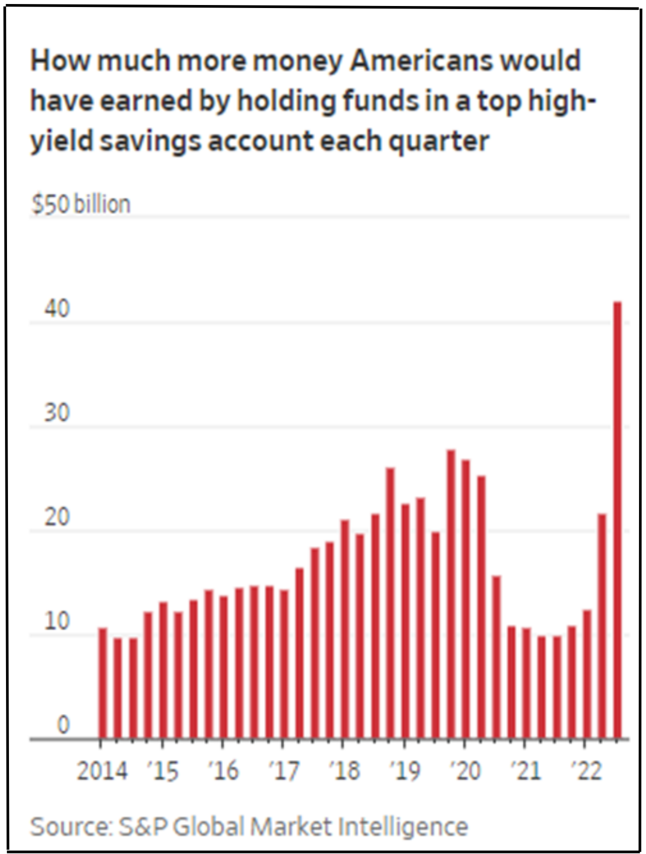
2. Energy Was The Lone Sector Star

Energy was the lone sector star and the only sector "in the green". In a year where the benchmark S&P 500 Index was down a lot, four other sectors fared relatively well: Staples, Health Care, Utilities and Industrials. The big sector laggards were Communication Services, Consumer Discretionary, Technology and Real Estate. We benefited from over-weights to Staples and Industrials, and under-weights to Tech and Communications.

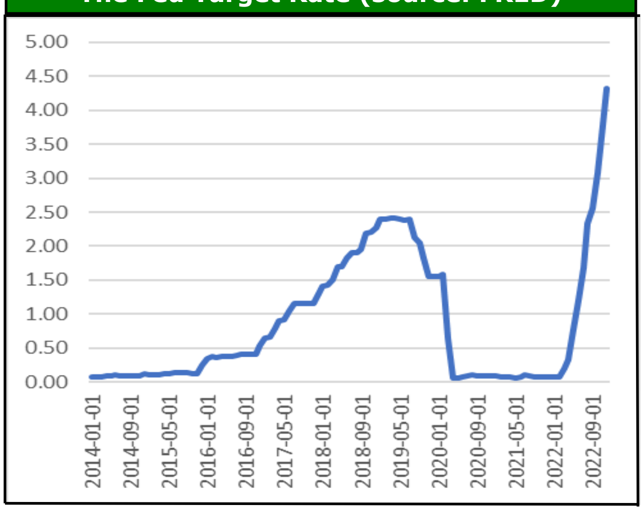


Do You Have Too Much Cash At Your Bank?

Higher interest rates provide better investment opportunities. Recent data shows that savers could have earned $42 billion more in interest during the Third Quarter if they had moved their cash deposits out of the five largest US banks - the largest gap recorded to date. Do you have too much cash at your bank?



The Fed Target Rate (source: FRED)



Is Your Bank Watching Out For You?

The five largest US banks - Bank of America, Citigroup, JP Morgan Chase, US Bancorp and Wells Fargo - paid an average of 0.4% interest on cash deposits in Q3. This was at a time where the highest-yielding savings accounts averaged 2.14%, the Fed Target Rate reached 3.00% and a "risk-free" 1 Year US Treasury bond yielded over 4.00%.

Are You Losing Out As Rates Rise?

There is a direct correlation between "lost interest" and the Fed target rate. As the target rate increases, so does the amount of "lost interest" to savers. This is easy to see by comparing the two charts on the left. They are literally mirror images of each other. As the Fed Target Rate reached 4.25% in Q4, the upcoming Q4 "lost interest" calculation will far exceed the $42 billion calculated for Q3!

We Are Here To Help

Let's take the data one step further. The Q3 $42 billion interest gap assumes the savers moved their cash to the "top yielding savings accounts" at the banks. The interest gap should be much higher because there are probably better investment options than what is available at the large banks - CDs (certificates of deposit) at Charles Schwab and risk-free US Treasury bills to name a couple.

If you are holding more cash at your bank than you need, talk to us. We will be pleased to assess your investment options.

SECURE Act 2.0 - A Push Towards Safer Retirement For Americans

The SECURE Act 2.0 was passed by Congress at year-end. Many provisions were made due to a concern that not enough Americans are adequately preparing for their retirement. Nearly half of working age Americans - 57 million people - do not have access to an employer-sponsored retirement savings plan (source: AARP). Those who do save are not saving enough. The median retirement account in 2019 was $65,000 and for older Americans was $134,000 (source: Federal Reserve's Survey of Consumer Finances).

Here are some highlights of the SECURE Act 2.0 we believe may be of interest to our clients.

1. Increased Age For RMDs

Before the SECURE Act, the age for RMDs (required minimum distributions) from tax-deferred accounts was 70.5. The SECURE Act increased that age to 72. The SECURE Act 2.0 further increases the age to 73, beginning on January 1, 2023. The RMD age will be increased to 75 beginning on January 1, 2033.

2. Mandatory Automatic Enrollment In Retirement Plans

Effective for plan years beginning after December 31, 2024, new 401(k) and 403(b) plans will have to automatically enroll participants upon eligibility. The automatic deferrals will start at between 3% and 10% of compensation, increasing by 1% each year to a maximum of at least 10% but no more than 15% of compensation. Automatic enrollment in retirement plans has been shown to increase participation.

3. Higher Catch-Up Contribution Limit

Workers who are younger than age 50 can contribute a maximum $22,500 to a 401(k) in 2023. If you are age 50 and older, the catch-up contribution has been increased to $7,500, bringing your maximum 2023 401(k) contribution to $30,000. The SECURE Act 2.0 increases the catch-up limit, beginning in 2025, to the greater of $10,000 or 50% more than the regular catch-up amount if you are 60, 61, 62, or 63 years old. This would equate to a catch-up of $11,250 based on current 2023 limits. After 2025, those amounts will be indexed for inflation.

4. Tax-And-Penalty-Free Rollover From a 529 Plan To A Roth IRA

Right now, money in a 529 Plan that is distributed for non-education purposes may be subject to penalties and taxes. Under the new SECURE Act 2.0 provision, beneficiaries would be able to do a rollover of up to $35,000 aggregate in life from a 529 to a Roth IRA in their name. The rollovers would be subject to the Roth IRA annual contribution limits and the 529 would need to have been open for at least 15 years.

The main benefit of this provision is to remove the uncertainty that happens if you over-fund a 529 or if your kids ultimately don't need it. Now you can reposition up to $35,000 from a 529 to your own Roth IRA or to a Roth IRA for your child. Remember that a Roth IRA is the most tax-advantaged account.

We made several portfolio adjustments in Q4 because the market has some good buying opportunities. When presented, we want high quality companies that have been hit unduly hard and are "on sale". While we think market conditions will remain challenging in the short term, and know our timing will not be perfect, we have started to position the portfolio in anticipation of a future market bounce.

We bought Alphabet Inc Class A (symbol: GOOGL; $1.2 trillion market cap), the holding company for Internet media giant Google. GOOGL is the epitome of a high quality well-run dominant company. We also bought Salesforce Inc (symbol: CRM; $127 billion market cap). CRM provides enterprise cloud computing solutions and customer relationship management technology that brings companies and customers together. It is the clear front-runner in a category that increases the productivity of sales representatives. Finally, we bought Siemens Healthineers AG (symbol: SMMNY; $59 billion market cap), a Germany-based leading global health care provider of imaging, diagnostics, cancer care technologies and advanced therapies. We see significant market growth opportunities, especially in its cancer care segment and overall US-based sales.

In the bond portfolio, we bought a 20-year US Treasury. The bond market is much more attractive now than at the beginning of the year, so we are acquiring bonds that present a better risk/return tradeoff.

We sold PepsiCo Inc (symbol: PEP; $248 billion market cap), one of the largest global food and beverage companies. As we had hoped, PEP was an out-performer in a down market. It served its purpose and it was time to move to other positions. We also sold Medtronic PLC (symbol: MDT; $104 billion market cap), a medical device company headquartered in Ireland. MDT was a mediocre performer and we felt it was worthwhile to switch up MDT for SMMNY.

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