TRIVANT

CUSTOM PORTFOLIO GROUP, LLC

April 2023

Quarterly Insights

EXECUTIVE SUMMARY

Stocks And Bonds Up In Q1

In the First Quarter, the domestic S&P 500 Index was up 7.50% and out-performed all major regions except Europe. China was up 4.71%. Technology (+21.34%), Communication Services (+20.15%) and Consumer Discretionary (+15.44%) were the leading Q1 sectors. To combat high annual inflation (6.0% in February), the Fed raised its target rate by 0.25% on February 1 and a further 0.25% on March 22, bringing its current target rate to 4.75%. More rate hikes are possible. In Q1, the Bloomberg US Aggregate Bond Total Return USD Index (AGG) rose 3.72%.

Regional Bank Crisis & The Revenge Of The Laggards

We did not anticipate the two major market drivers in Q1: the regional bank crisis and “the revenge of the laggards”.

The regional bank crisis was a panic situation in early March where many depositors in the smaller “regional banks” rushed to move their money to larger banks. There was a fear that the smaller banks were in trouble due to large mark-to-market losses on their balance sheets stemming from bond losses (the AGG fell 13.01% in 2022).

We also witnessed “the revenge of the laggards”:

1. The three sectors that got beat up the most in 2022 rebounded the most in Q1.
2. Three significantly-weighted S&P 500 stocks that got hit the most in 2022 rose considerably in Q1 and were attributable to over half of the S&P 500 Index return.

First Quarter 2023

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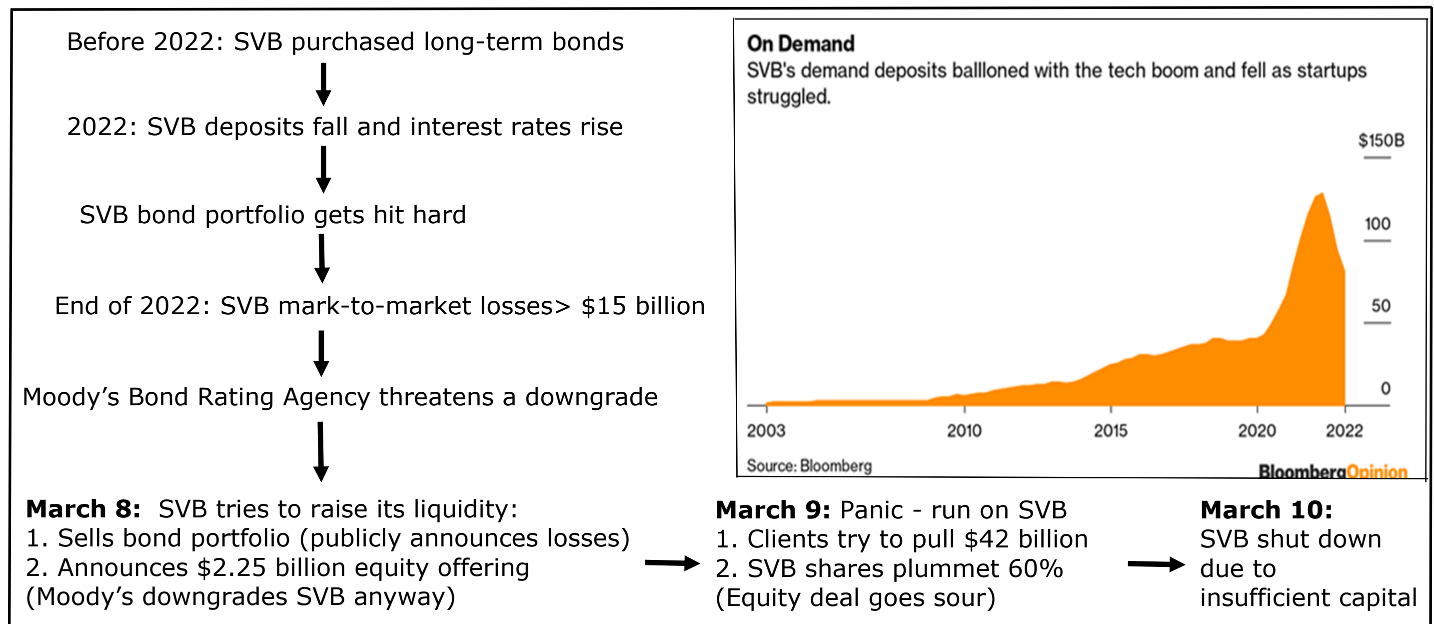
We Anticipated A Challenging Start To 2023, But Not For The Reasons That Played Out

At the beginning of the year, we stated "we believe the S&P 500 Index will be flat in 2023, falling in the first half and rising in the second half". We cited conditions pointing to a "transition year" for stocks that included more rate hikes, quantitative tightening (QT), inflationary pressures, above-average market valuation, and earnings expectations that may be too high. While these conditions remain relevant in a positive market year-to-date (the S&P 500 Index was +7.50% in Q1), we did not anticipate the two major market drivers in Q1: the regional bank crisis and "the revenge of the laggards".

1. Regional Bank Crisis

The regional bank crisis was a panic situation in early March where many depositors in the smaller "regional banks" rushed to move their money to larger banks. There was a fear that the smaller banks were in trouble and that any bank deposits over the $250,000 threshold for Federal Deposit Insurance Corporation (FDIC) protection were at risk. To understand the crisis, let's briefly recap of what happened to interest rates in 2022. The inflation that was deemed "transitory" by the Fed in late 2021 did not subside. With close to double-digit inflation throughout 2022, the Fed raised its target rate from zero to 4.25% by year-end through a series of rate hikes - an "aggressively restrictive" policy not seen since 1981. When interest rates rise, bond prices fall. The Bloomberg Barclay's Aggregate Bond Index fell 13.01% in 2022, the worst year ever for bonds.

The "poster-child" for the regional bank crisis was Silicon Valley Bank (SVB), the go-to bank for tech startups where 93% of its demand deposits exceeded the $250,000 threshold for FDIC protection. SVB had rapid deposit growth as startups thrived during the pandemic in a zero interest rate environment. SVB purchased long-term bonds with the deposits. Here is a synopsis of the downfall of SVB caused by a run on its deposits.



The downfall of SVB prompted the regional bank crisis. The Financials sector got hit very hard as investors worried whether there would be additional runs on banks. SVB was the second biggest bank failure in US history (only exceeded by Washington Mutual in 2008). We didn't see this coming because of limited SVB financial disclosures. Additionally, things unraveled very quickly. SVB fell apart in 44 hours.

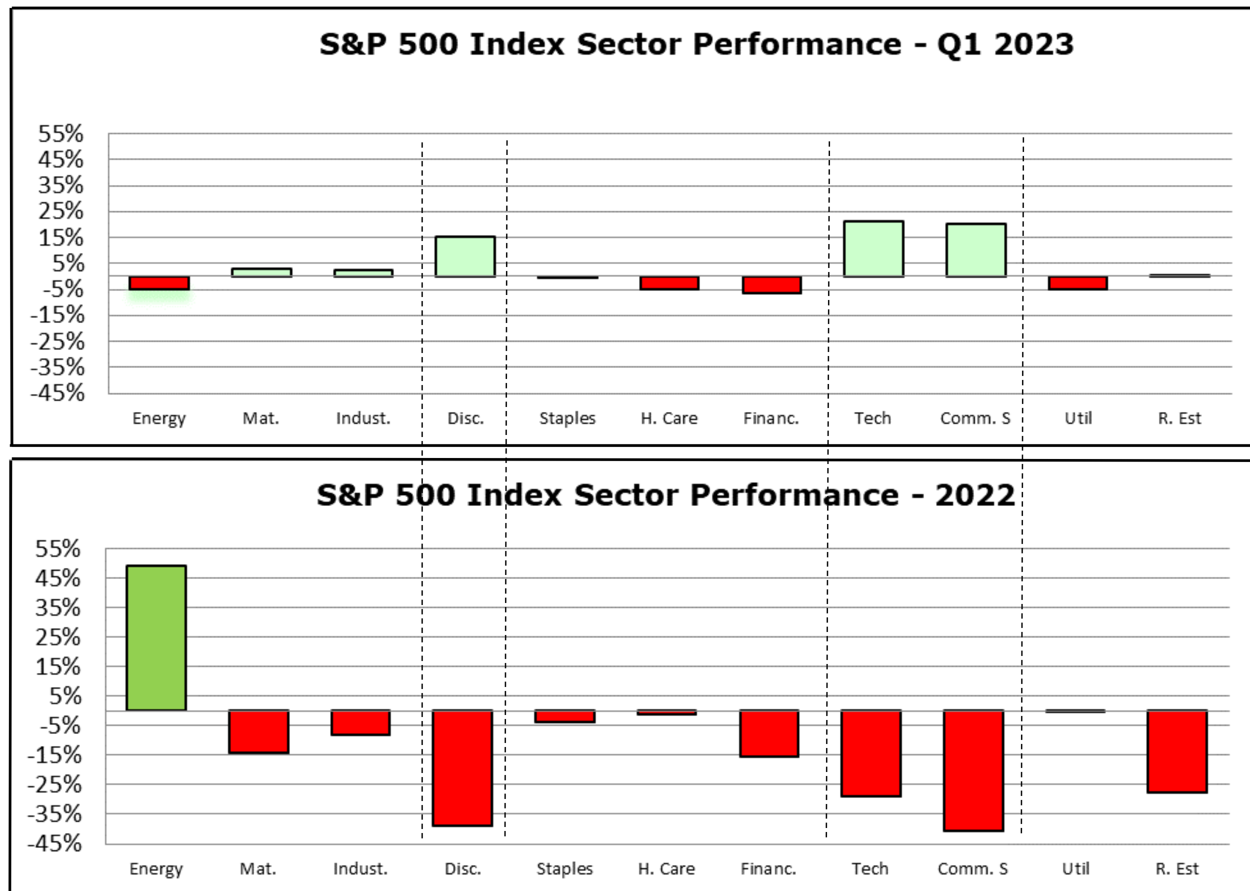
It is hard to conceive how badly SVB managed their bond risk. The Fed gave very clear signals leading up to and during 2022 that interest rates were going to rise as long as inflation exceeded the Fed's 2% target level.

"You Can't Fix Stupid."
Ron White, American Comedian

2. The Revenge Of The Laggards

A. Sectors

In January, the three sectors that got beat up the most in 2022 (Technology, Telecommunication Services and Consumer Discretionary) rebounded the most. Movement to these sectors was further intensified by the regional bank crisis in early March as investors fled Financials.



B. Individual Stocks

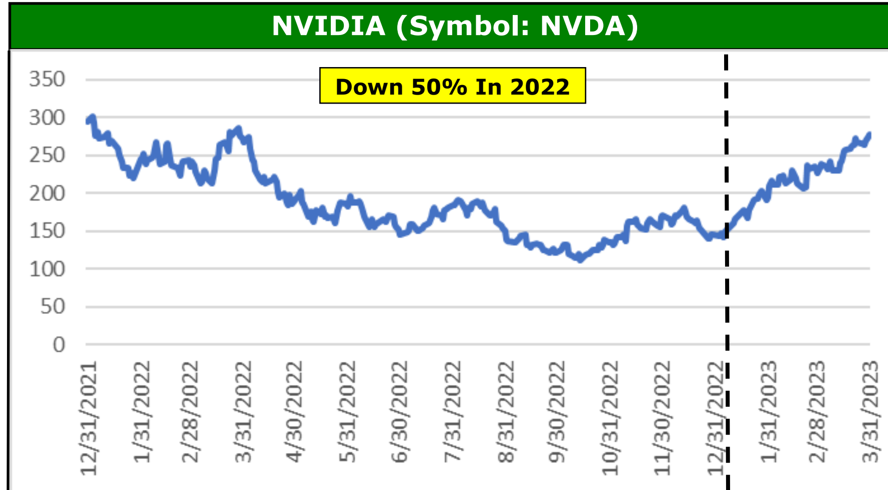
The "Revenge Of The Laggards" extended further to individual stocks. Just three S&P 500 Index stocks, one in each of the highest-rebound sectors, were attributable to 57% of the S&P 500 Index Q1 performance.

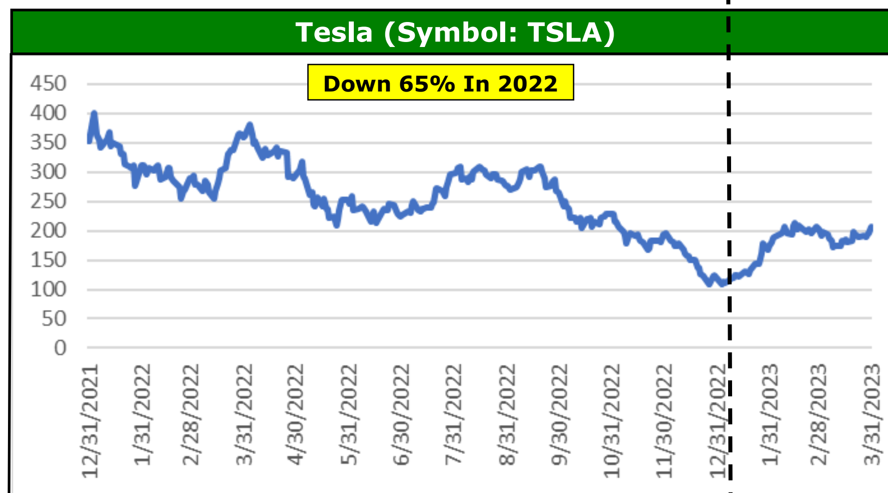
Symbol	Name	Sector	Market Cap ($ billions) 31-Mar-23	Total Return (%) Q1 2023	Index Weight (%) 31-Mar-23	Performance Impact (%) (see Note 1)	
NVDA	NVIDIA	Technology	$686	90.07%	1.99%	1.79%	
TSLA	Tesla	Discretionary	$656	68.42%	1.89%	1.29%	
META	Meta Platforms	Comm. Services	$549	76.12%	1.59%	1.21%	
					5.47%	**4.30%**	
		S&P 500 Index:	$34,472		Q1 S&P 500 Index:	7.50%	
				Impact:	3 Stocks	4.30%	0.57
					497 Stocks	3.20%	0.43
					500 Stocks	7.50%	1.00

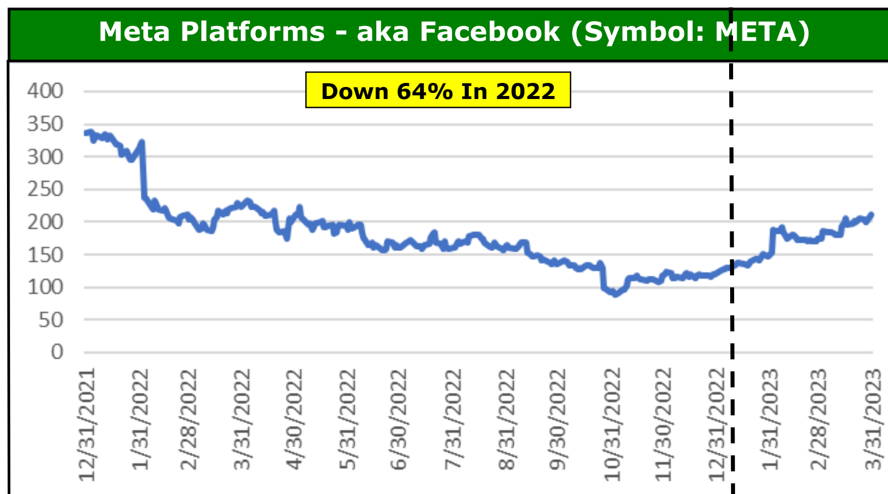
Note 1: Performance Impact Of An Individual Stock = (Total Return) * (Index Weight)

This Q1 impact was unexpected and arguably unjustified as these stocks were horrible throughout 2022! NVDA fell 50%, TSLA fell 65%, and META (Facebook) fell 64%. We avoided all of these stocks in 2022. NVDA concerned us because of its uncertain exposure to the "mining of crypto". TSLA had an excessively high valuation (a total market cap nearly double that of Ford, General Motors and Toyota combined) and was crazily tied to an unraveling Twitter. META had internal challenges and advertising revenue pressures.

2022 Performance Hall of Shame







Stocks Rise In Q1

In the First Quarter, the domestic S&P 500 Index was up 7.50% and out-performed all major regions except Europe. All global regions were positive. China was up 4.71%. Technology (+21.34%), Communication Services (+20.15%) and Consumer Discretionary (+15.44%) were the leading Q1 sectors.

Equity Index Performance

Index	Q1 2023	2022
S&P 500 (Domestic)	**7.50%**	**(18.11%)**
MSCI EAFE (Foreign) *	**8.47%**	**(14.45%)**
MSCI Emerging Markets	**3.96%**	**(20.09%)**
MSCI EMU (European Monetary Union)	**14.23%**	**(17.86%)**
MSCI Japan	**6.19%**	**(16.55%)**

* Europe, Australia and the Far East

We Remain Cautious

While the market rose in Q1, it was not a broad rally - just three stocks were attributable to over half of the S&P 500 Index return and only five out of the 11 sectors were positive. We remain cautious for these reasons:

1. It is likely there will be at least one more Fed rate hike. Inflation rose 6.0% in February 2023, down from 6.5% in December and a 9.1% peak in June. However, that is still three times the Fed's preferred 2% target.

2. Financial conditions have tightened since the March regional banking crisis (source: Chicago Fed National Financial Conditions Credit Subindex). Tougher loan access could slow the economy.

3. There is a reasonable chance of a mild recession. The 10-year Treasury yield has been trading below the 2-year rate since early July 2022. An inverted yield curve is an indicator of a recession.

4. 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 21.64.

5. Earnings expectations that may be too high (must fully factor in recession risk, inflation, Fed rate hikes).

Portfolio Strategy Considerations

We anticipate keeping the stock portfolio in a defensive position. In our view, this is not the right time to be aggressive. That time will come.

For now, we will likely raise the average market cap of the portfolio (favor the less-volatile large cap versus small cap stocks) as well as rotate towards defensive sectors such as Health Care.

Stay tuned for updates.

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

Bonds Rise In Q1

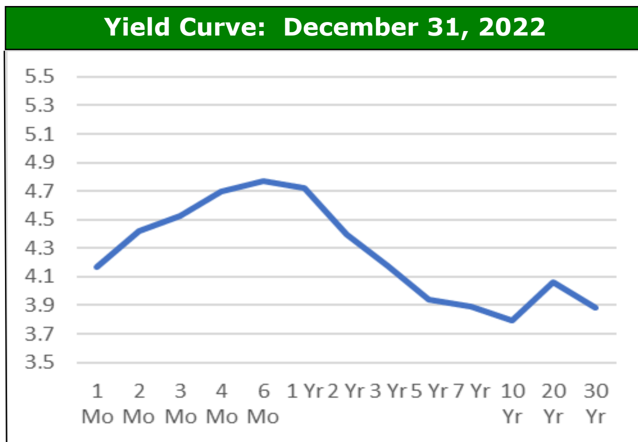
The Bloomberg US Aggregate Bond Total Return USD Index (AGG), a broad-based representation of bond performance, rose 3.72% in the First Quarter. This was a welcome relief from 2022, where bonds fell 13.01% (the largest bond decline in history). To combat high inflation, the Fed further raised its target rate by 0.25% on February 1 and another 0.25% on March 22. More rate hikes are possible.

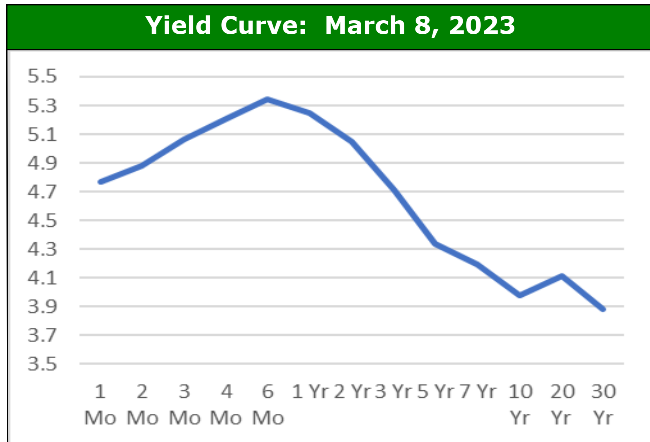
Key US Interest Rates	March 31, 2023	December 31, 2022	Change
Federal Reserve Board Funds Target Rate	4.75% - 5.00%	4.25% - 4.50%	+ 50 basis points
2-Year Treasury (Constant Maturity)	4.06%	4.41%	- 35 basis points
5-Year Treasury (Constant Maturity)	3.60%	3.99%	- 39 basis points
10-Year Treasury (Constant Maturity)	3.48%	3.88%	- 40 basis points

While Bond Yields Fell Due To The Regional Bank Crisis, Yields Remain Attractive

A) December 31, 2022 To March 8, 2023

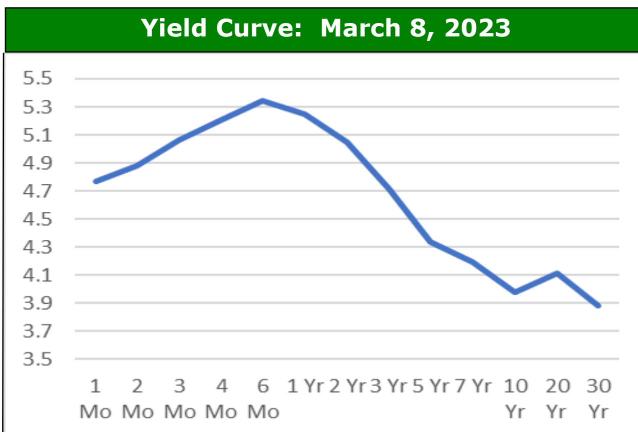
From the beginning of the year through March 8, bond yields rose (bond prices fell) as investors moved from bonds to stocks. On March 8 (when yields peaked in Q1), a 1-year Treasury yielded 5.25%.

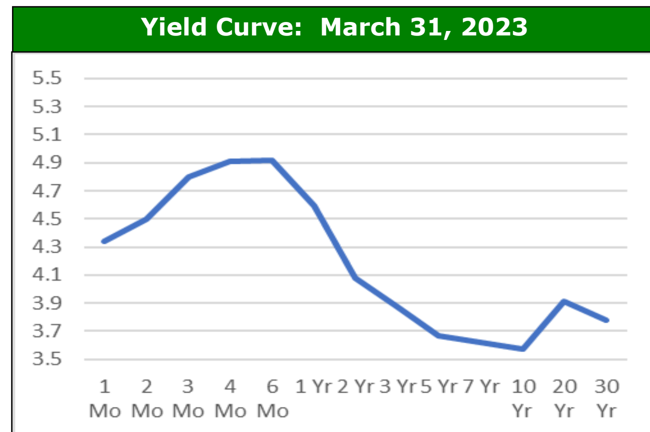




B) March 8, 2023 To March 31, 2023

The regional bank crisis started on March 8 with the subsequent 44-hour collapse of Silicon Valley Bank. Investors moved to bonds for safety. Bond yields fell (bond prices rose). On March 31, a 1-year Treasury yielded 4.64%. While Treasury yields fell during Q1, we still view no-risk Treasury yields as attractive.





As the regional bank crisis unfolded, Charles Schwab got dragged into the mess. The company is not a regional bank yet the market punished it as if it was a regional bank. There were numerous headlines insinuating that Charles Schwab was in a lot of trouble along the lines of Silicon Valley Bank. Some clients saw the news and out of concern called us. We want to assure you that we regard Charles Schwab as an excellent company and the best custodian for your assets.

Charles Schwab is the largest public broker-dealer in the U.S., serving over 34 million clients with $7 trillion in assets. The company protects its clients. There is capital availability well in excess of regulatory requirements, a high-quality and relatively small loan portfolio, and a conservative investment portfolio of securities backed by the U.S. Treasury and various government agencies. More than 80% of client cash is below the $250,000 threshold for FDIC insurance, and hence is insured dollar-for-dollar by the FDIC. As the custodian, client assets are segregated from the Schwab bank division and are completely secure.

In the week ending March 17 (the week after the crisis started), Schwab had an asset inflow of over $16 billion. This was not a pattern of panic cash outflows characteristic of the regional banks. Year-to-date, core new assets have exceeded $116 billion. In the past two years, new assets have totaled over $2 trillion.

Focusing attention on the “unrealized losses” in Charles Schwab’s held-to-maturity (HTM) bond portfolio can be misleading. Given the company’s significant access to sources of liquidity, most of these losses will not be realized. Rather, the vast majority of the bonds will be held to maturity and redeemed at par (no realized losses). The unrealized “paper losses” will decrease over time as the bonds get closer to maturity.

It is upsetting to see the stock price of Charles Schwab falter. To some degree, we believe Charles Schwab has been “guilty by association” amidst the regional bank crisis. As the dust settles, we anticipate the stock will recover. We did not want to sell the stock in a panic.

On a personal note, we have custodied 100% of our accounts at Charles Schwab since our 2003 inception. Prior to starting TriVant, we worked with other firms and were able to observe all of the major custodians and how they worked with clients. Charles Schwab was, in our view, far and above the best company out there. Twenty years later, our view has not changed.

Sincerely,

Dan Laimon	John Barber, CFA	Michael Harris, CFA, CFP®
Managing Member	Chief Investment Officer	Research Director

We made only two portfolio adjustments in Q1 and anticipate further adjustments in Q2. More often than not, it is best to "wait out" unusual short momentum events such as the regional bank crisis and "the revenge of the laggards" before executing a longer term strategy. Otherwise there is a tendency to get duped into poor decisions on raw emotion. We don't want to get whipsawed. Patience is a virtue.

We bought Sempra Energy (symbol: SRE; $47 billion market cap), one of North America's premier energy infrastructure companies. SRE is a California-based holding company with its business activities organized under four reportable segments:

1. SDG&E – San Diego Gas & Electric, a regulated public utility in California
2. SoCalGas – Southern California Gas, another California regulated public utility
3. Sempra Texas Utilities
4. Sempra Infrastructure – includes investments in US and Mexico with focus on liquified natural gas (LNG) and clean power

We sold Southern Co (symbol: SO; $68 billion market cap), the third-largest utility in the US by revenue. It distributes electricity and natural gas to approximately 9 million customers in 7 states. There were two reasons why we felt it was time to make a switch from SO:

1. Cost overruns at two project locations (Vogtle and Kemper) have added uncertainty to SO's excellent regulatory relationships and frameworks in Georgia and Mississippi
2. SO has assumed an increasingly high level of debt in a rising interest rate environment

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

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.