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BABY IT'S COLD OUTSIDE

2022 ended with a variety of surprises and "gifted" many Americans a very "Blue, Blue Christmas." Winter storm Elliot delivered a powerful dome of frigid weather that blanketed the country and colored weather maps in various shades of blue, violet, and indigo, highlighting temperatures that ranged from bitter cold to Ice Age like conditions. This abominable mega system was caused by a bomb cyclone; a storm created by a rapid drop in pressure resulting in a dramatic increase in winds. This inescapable "perfect storm" created a double threat to our already fragile energy grid. Just as demand was at its peak, catastrophic winds and flash freezes downed power lines and shut off thousands of homes across the country.

As people scrambled for coats, generators, and rock salt, markets tried to equate what this storm might mean for the important last few days of retail shopping and holiday travel, which are still recovering from the aftermaths of COVID. Despite the ability to order online, consumers may have been reluctant to make last minute purchases assuming their Christmas packages might get stuck on a semi-truck, jack-knifed in the middle of Kansas. The lackluster Santa Clause rally that never arrived (S&P 500 was down 18.1% for the year and 5.8% in December) along with higher interest rates on credit cards added additional downward pressure to the holiday cheer barometer. Whether you were on the naughty or nice list, I heard Santa gifted everyone a stocking of coal just to stay warm. My mistake, it was actually petrified reindeer droppings…it's the new "renewable" energy source powering the North Pole.

Speaking of naughty, a certain someone did not get to enjoy their traditional holiday festivities this year. Plucked from the beautiful, warm waters of the Bahamas, the disgraced Sam Bankman-Fried was extradited to New York and charged with eight federal criminal charges including securities fraud and money laundering. The fallen ex-CEO of FTX, a cryptocurrency exchange, allegedly lost some $8 billion of customer deposits. These depositors included high-powered executives, celebrities and even Wall Street moguls who seemingly trusted each other's due diligence on the investment opportunity. Bankman-Fried was released to his parents with an ankle monitor on a $250 million bond; the largest bail in history. Looks like he was skating on thin ice!

Sam Bankman-Fried is so notorious that he now goes by his initials "SBF", not to be confused with "BFF" (of which he now has none). It is traditional, especially around the holidays, to gift something tangible to people we care about. BFFs share matching silver necklaces, retirees receive a gold watch, and one's betrothed is presented a diamond ring on bended knee. Mr. Wonderful (aka famed businessman Kevin O'Leary) and several other well-known celebrities received something very different indeed. Now we are witnessing the fallout of trying to buy "friends" and influencers with ephemeral crypto coins "printed" out of thin air, as opposed to the real thing.

The unraveling of FTX not only took down its own token but roiled crypto markets in what has been deemed a crypto winter (Bitcoin is down 65% YTD and roughly $2 trillion in crypto market capitalization has disappeared). So much for COLD storage!

The bond market suffered from a case of the blues this year with the Bloomberg Aggregate tumbling 13% and wiping out 5 years of returns. Other economic factors were also feeling pretty low this holiday season. Existing home sales fell for the 10th straight month (down 7.7% month over month and 35.4% from the previous year) due to higher mortgage rates and lack of supply. In addition, leading economic indicators are down 3.7% over the last 6 months, consumer confidence is at an all-time low, and China's reopening has resulted in yet another wave of Omicron contagion. It's enough to make your teeth chatter.

One bright spot was that inflation continued to cool for the 3rd straight month (PCE dropped to 5.5% in November from 6.1% in October). Most of this decrease, however, has been categorized by goods inflation while service inflation is still a concern and a major focus for the Fed. With unemployment sitting stubbornly at 3.7% as of November, it's hard to forecast a Fed pause or pivot any time soon. Longer-term, these labor shortages and rising wage costs should drive innovation and force companies to adapt. Further investment in automation, robotics, and artificial intelligence will be necessary to control supply chains and will eventually provide deflationary forces through enhanced productivity.

Closing Thoughts

Yes, this winter of discontent has made me want to retreat to a sunny beach and bury my head in the sand. But as always, the frost will thaw, the grass will grow and the flowers will bloom again. There is a time for every season and as the world makes one more trip around the sun, we greet the 2023 new year with hope for the future. Investing is not a short-term game, and we continue to see opportunities to plant the seeds for a long-term, successful harvest for our clients.

Regards,

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President

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Equity Markets

U.S. stock indices posted positive returns in 4Q as investor sentiment improved, but the YTD results remained dismal with most indices posting double-digit declines. The S&P 500 Index rose 7.6% for the quarter, lowering its YTD loss to 18.1%. Returns were quite mixed across sectors with Energy (+22.8%) being the best and Consumer Discretionary (-10.2%) faring the worst. Value stocks trounced growth for the quarter (Russell 1000 Value: +12.4%; Russell 1000 Growth: +2.2%) and the year (Russell 1000 Value: -7.5%; Russell 1000 Growth: -29.1%). In 4Q, the Growth Index was hurt by relative underweights in Health Care, Financials, and Energy as well as significant underperformance from Tesla (-54%) and Amazon (-26%). Looking back three years, growth is only modestly ahead of value (Russell 1000 Value: +6.0%; Russell 1000 Growth: +7.8%). Small cap stocks exhibited the same pattern in 4Q (Russell 2000 Value: +8.4%; Russell 2000 Growth: +4.1%) but value's full year margin is smaller in the small cap space (Russell 2000 Value: -14.5%; Russell 2000 Growth: -26.4%).

Global ex-U.S. markets also participated in the 4Q rally, and currency appreciation vs. the U.S. dollar further bolstered returns. The MSCI ACWI ex USA Index gained 14.3% (Local: +7.8%), reducing its YTD loss to 16.0% (Local: -9.6%). Across developed market countries, gains were broad-based and value outpaced growth, but by a smaller margin than in the U.S. (MSCI ACWI ex USA Value: +15.7%; MSCI ACWI ex USA Growth: +12.9%). Unlike in the U.S., all sectors of the ACWI ex USA Index delivered a positive return in 4Q of 10% or more.

Emerging markets (MSCI Emerging Markets: +9.7%; Local: +6.6%) also rebounded in 4Q, but returns were mixed across countries. While many countries were up double-digits, India (+2.0%) and Brazil (+2.4%) weighed on broad market returns. China (MSCI China: +13.5%) outperformed. Quarterly returns were also mixed across regions: Latin America (+5.7%), Emerging Europe (+43.1%), and Emerging Asia (+10.8%). The 2022 return for the MSCI EM Index was -20.1%.

Fixed Income Markets

U.S. fixed income experienced its worst year—ever—in 2022, by a wide margin. The Bloomberg US Aggregate Bond Index sank 13.0%; the next worst calendar year was 1994 when the Aggregate fell 2.9%. The silver lining lies in the 4.68% yield-to-worst for the Index, up from 1.75% at the beginning of the year. The yield curve remained inverted at year-end; the 10-year Treasury yield was 3.88% and the 2-year yield was 4.41%. The inversion reflects investor expectations for the economy to slow and an eventual need for the Fed to lower rates. The fourth quarter brought some relief to bond investors as longer rates fell modestly and most "spread" sectors outperformed Treasuries. The Aggregate gained 1.9%. High yield corporates (Bloomberg High Yield Index: +4.2%) were star performers, but this Index was down 11.2% for the year.

The Bloomberg Municipal Bond Index rose 4.1% in 4Q, dampening the year's loss to 8.5%, the worst return in 20 years but ahead of most other fixed income sectors. The ratio of AAA municipal yields to the 10-year U.S. Treasury fell to 68%, below its 10-year average (88%). Outflows from municipal bond mutual funds were $122 billion in 2022, a record.

While rates across developed markets rose broadly in 2022, changes were mixed in 4Q. Rates fell in the U.K. but rose across most of Europe and in Japan. The Bloomberg Global Aggregate ex USD soared 6.8% (hedged: +0.2%) due largely to weakness in the U.S. dollar. Still, the YTD differential for hedged and unhedged investors is nearly 9% (unhedged: -18.7%; hedged: -9.8%). Emerging markets also had a good quarter with the JPM EMBI Global Diversified up 8.1% and the local currency JPM GBI-EM Global Diversified up 8.5%. For the year, the indices were down 17.8% and 11.7%, respectively.

Real Assets

Real assets as a group performed well in 4Q. The S&P GSCI Index rose 3.4%; Gold (S&P Gold Spot Price Index: +9.2%), REITs (MSCI US REIT: +5.2%), infrastructure (DJB Global Infrastructure: +9.6%), and TIPS (Bloomberg TIPS: +2.0%) all posted solid returns. Full year results remained poor, however, for most real assets outside of those related to energy. REITs posted the worst returns (MSCI US REIT: -24.5%) while MLPs (Alerian MLP Index: +30.9%) benefited from higher energy prices.

Returns for Various Periods - December 31, 2022

	Last Quarter	Year to Date	Last Year	Last 3 Years	Last 5 Years	Last 10 Years	Last 15 Years
MSCI:ACWI	9.76	(18.36)	(18.36)	**4.00**	5.23	7.98	**4.84**
Russell:3000 Index	7.18	(19.21)	(19.21)	**7.07**	8.79	12.13	**8.66**
Russell:3000 Growth Index	2.31	(28.97)	(28.97)	**7.32**	10.45	13.75	**10.10**
Russell:3000 Value Index	12.18	(7.98)	(7.98)	**5.88**	6.50	10.16	**6.96**
MegaCap							
Russell:Top 50	3.22	(24.05)	(24.05)	**7.82**	10.07	12.67	**8.65**
Russell:Top 200	6.56	(19.77)	(19.77)	**7.89**	9.90	12.92	**8.90**
Russell:Top 200 Growth	1.14	(29.74)	(29.74)	**8.72**	11.77	14.90	**10.84**
Russell:Top 200 Value	13.42	(5.11)	(5.11)	**5.99**	7.13	10.40	**6.59**
Large Cap							
S&P:500	7.56	(18.11)	(18.11)	**7.66**	9.42	12.56	**8.81**
Russell:1000 Index	7.24	(19.13)	(19.13)	**7.35**	9.13	12.37	**8.77**
Russell:1000 Growth	2.20	(29.14)	(29.14)	**7.79**	10.96	14.10	**10.32**
Russell:1000 Value	12.42	(7.54)	(7.54)	**5.96**	6.67	10.29	**6.96**
MidCap							
S&P:400 Mid Cap	10.78	(13.06)	(13.06)	**7.23**	6.71	10.78	**8.87**
Russell:Midcap Index	9.18	(17.32)	(17.32)	**5.88**	7.10	10.96	**8.44**
Russell:Midcap Growth	6.90	(26.72)	(26.72)	**3.85**	7.64	11.41	**8.61**
Russell:Midcap Value	10.45	(12.03)	(12.03)	**5.82**	5.72	10.11	**7.96**
Small Cap							
S&P:600 Small Cap	9.19	(16.10)	(16.10)	**5.80**	5.88	10.82	**8.89**
Russell:2000 Index	6.23	(20.44)	(20.44)	**3.10**	4.13	9.01	**7.16**
Russell:2000 Growth	4.13	(26.36)	(26.36)	**0.65**	3.51	9.20	**7.26**
Russell:2000 Value	8.42	(14.48)	(14.48)	**4.70**	4.13	8.48	**6.81**
Russell:Microcap	4.72	(21.96)	(21.96)	**4.05**	3.69	8.86	**6.34**
Non-US Equity							
MSCI:ACWI xUS	14.28	(16.00)	(16.00)	**0.07**	0.88	3.80	**1.52**
MSCI:EAFE	17.34	(14.45)	(14.45)	**0.87**	1.54	4.67	**1.81**
MSCI:EAFE Growth	15.05	(22.95)	(22.95)	**0.47**	2.49	5.59	**2.61**
MSCI:EAFE Value	19.64	(5.58)	(5.58)	**0.65**	0.17	3.51	**0.82**
MSCI:EAFE Small	15.79	(21.39)	(21.39)	**(0.93)**	(0.05)	6.21	**3.80**
MSCI:EM	9.70	(20.09)	(20.09)	**(2.69)**	(1.39)	1.44	**0.65**
Fixed Income							
Blmbg:Aggregate	1.87	(13.01)	(13.01)	**(2.71)**	0.02	1.06	**2.66**
Blmbg:TIPS	2.04	(11.85)	(11.85)	**1.21**	2.11	1.12	**3.05**
Blmbg:Long Gov/Credit	2.61	(27.09)	(27.09)	**(6.20)**	(1.21)	1.57	**4.36**
Blmbg:Long Credit A	4.96	(25.65)	(25.65)	**(6.09)**	(1.33)	1.90	**4.35**
Blmbg:HY Corp Cash Pay	4.22	(11.15)	(11.15)	**0.08**	2.33	4.04	**6.10**
Blmbg:Muni 1-10 Yr	3.12	(4.84)	(4.84)	**(0.10)**	1.37	1.69	**2.83**
Blmbg:Glb Agg xUSD	6.81	(18.70)	(18.70)	**(5.94)**	(3.07)	(1.64)	**0.54**
Blmbg:Glb Agg xUSD Hdg	0.18	(9.76)	(9.76)	**(2.57)**	0.52	2.10	**2.98**
JPM:EMBI Plus	8.70	(24.67)	(24.67)	**(8.34)**	(3.87)	(0.35)	**3.11**
Other Assets							
Blmbg:Commodity TR Idx	--	--	--	**--**	--	--	**--**
S&P GSCI	3.44	25.99	25.99	**10.49**	6.46	(3.30)	**(4.93)**
S&P:Gold Spot Price Ix	9.22	(0.13)	(0.13)	**6.24**	6.88	0.86	**5.33**
FTSE:NAREIT Equity Index	5.24	(24.37)	(24.37)	**(0.11)**	3.68	6.53	**6.17**
Alerian:MLP Index	10.11	30.92	30.92	**9.38**	4.08	1.99	**5.39**

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