NEWSLETTER – APRIL 2022

MARKET TRENDS 3/31/22

Asset Class	3 Mo	1 Yr
Global Stocks		
MSCI World	-5.36%	9.96%
US Stocks		
S&P 500	-4.61%	15.61%
Large Cap Value	-0.80%	11.45%
Large Cap Growth	-9.08%	14.76%
Mid Cap	-4.89%	4.51%
Small Cap	-7.54%	-5.92%
International Stocks		
Developed Markets	-6.77%	0.21%
Emerging Markets	-7.80%	-13.03%
Fixed Income		
Taxable Bonds	-5.86%	-4.18%
International Bonds	-4.98%	-4.87%
Municipal Bonds	-5.60%	-3.86%
Alternatives		
Emerging Markets Bonds	-9.17%	-6.33%
Floating Rate	-0.23%	-0.08%
Preferred	-6.95%	-0.68%
Gold	6.60%	14.39%
Real Estate	-6.58%	20.26%

Source: Factset

Tim Vanech
tim@shorepointpartners.com

Luis M. Raposo, CFA
luis@shorepointpartners.com

John S. Barrett, CFA
john@shorepointpartners.com

Main 781 341 7250 | Fax 781 341 7246

220 Norwood Park South
Norwood, MA 02062

www.shorepointpartners.com

THIS IS HOW THE WORLD CHANGES

Midway through the first quarter of 2022, the world changed. Russia invaded Ukraine, igniting the first war in Europe since the Balkan conflicts of the 1990s. Prior to that, the last battles in Europe occurred during the conclusion of WWII.

Before getting into the details, we wanted to share our effort to make a small difference to those suffering from the invasion. We have donated to **Airlink**, an organization focused on logistics and transportation to make sure relief workers and supplies can reach those in need. We also contributed to the **World Central Kitchen**, which is providing much-needed meals to war-torn Ukrainian cities and to the many Ukrainian refugees.

PUTIN'S WAR

There is no doubt that this is Putin's War, a personal mission powered by a nation's military to grab land and resources and to rebuild the former Soviet Union piece by piece. Putin seems blindly focused on correcting what he sees as a horrible error committed 30 years ago by President Gorbachev when the Cold War ended and the USSR's Iron Curtain was lifted, allowing republics to go back to their own sovereignty.

PUTIN'S HUBRIS

Putin is known for tactics that are brutal, evil, and calculated. Upon first blush, Putin may have miscalculated his Ukraine siege on several fronts. First, the blitz that was expected to take a few days ending in the seizing of the capital city, Kyiv, never happened. Instead, the Russians have retreated to focus on the southern and eastern regions of Ukraine. Second, rather than weaken NATO, Russia's provocations have united the West (for the moment) in ways that haven't been witnessed in years. Third, NATO membership may actually increase as countries such as Sweden and Finland fear that Russia's ambitions threaten their way of life and sovereignty.

WHAT'S NEXT?

It would be difficult, if not impossible, to predict specific outcomes of this brutal invasion and its effects on the world order. We are watching in real time a battle between good and evil which will shape the simmering geopolitical tension between authoritarian and non-authoritarian governments around the globe. However, there are some hypotheses that we can make.

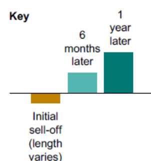
We do not expect the direct impact of the invasion on the markets to have lasting influence. Historically, geopolitical shocks to the market have been short-lived, and the market's swift recovery from its March lows suggests that this one will be no different in that regard.

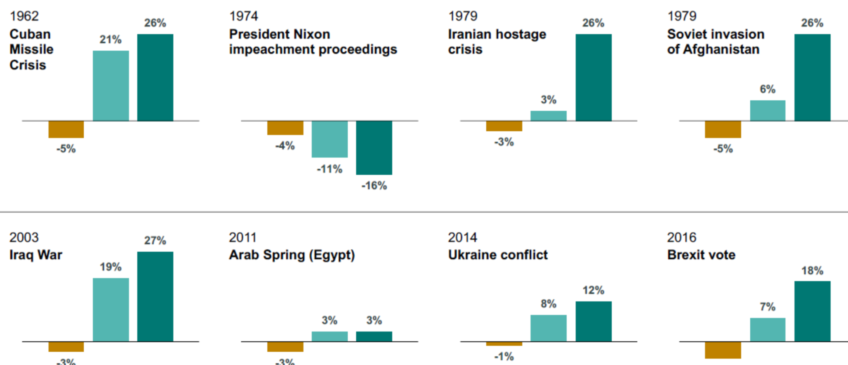
Vanguard

Geopolitical sell-offs are typically short-lived

5% Average total return **6 months** from event

9% Average total return **1 year** from event



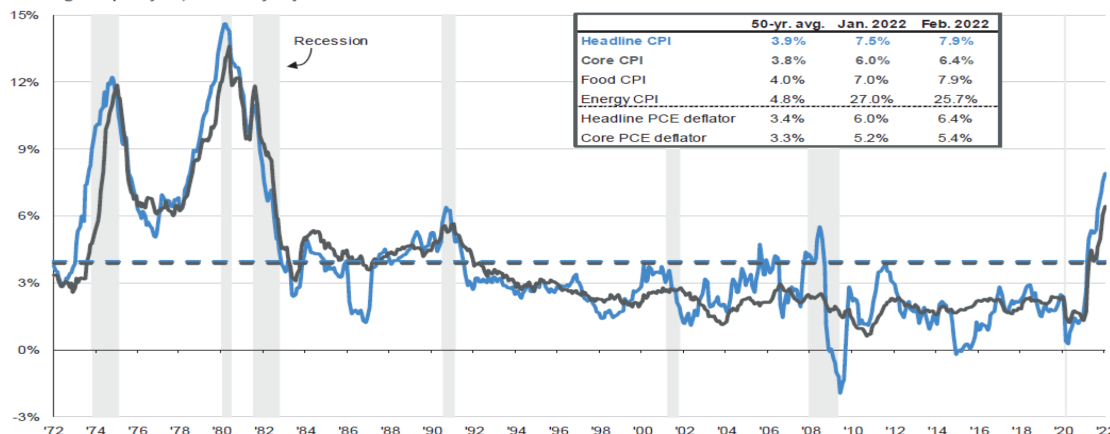


Unfortunately, the invasion of Ukraine does differ from many past geopolitical shocks in the number of knock-on effects it has had on the economy, with the impact of sanctions and the loss of Russian oil and gas being only the most obvious. Even if these secondary effects don't cause drops as dramatic as those seen at the start of the invasion, they may still cast a cloud on the market for the near future, especially as they continue to disrupt global supply chains.

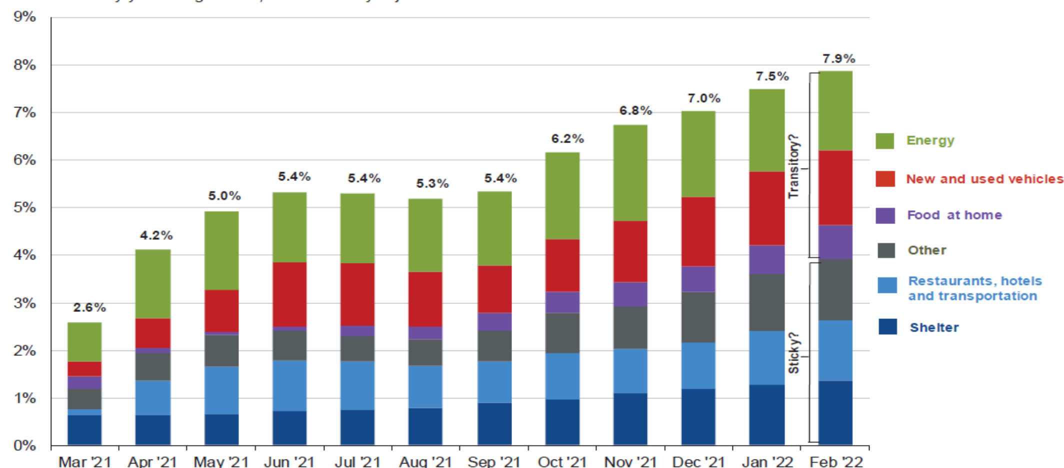
In a Covid world with an unprovoked bad actor in Russia, we expect countries to try to regionalize their supply chains more closely to their domestic operations. In addition, governments may want to diversify the production/manufacturing of their goods so as not to be overly reliant on any one trading partner – not only for Covid/disease risks, but also due to a lack of trust in existing trading alliances that might need to be re-examined. Europe, for example, and Germany in particular, will likely want to be less reliant on Russia for natural resources such as oil and natural gas.

It's hard to see these potential developments as anything but inflationary in the short term. We already see this in the increased price of oil and many commodities. Ukraine being taken offline as a farming resource could reduce the global availability of grains by as much as 10-15% this year.

CPI and core CPI
% change vs. prior year, seasonally adjusted



	50-yr. avg.	Jan. 2022	Feb. 2022
Headline CPI	3.9%	7.5%	7.9%
Core CPI	3.8%	6.0%	6.4%
Food CPI	4.0%	7.0%	7.9%
Energy CPI	4.8%	27.0%	25.7%
Headline PCE deflator	3.4%	6.0%	6.4%
Core PCE deflator	3.3%	5.2%	5.4%



Overall, inflation is the highest it has been in decades, and we expect at least some of it to persist. And that will lead the Federal Reserve ("Fed") to continue jawboning rates, raising rates, and running off its massive balance sheet. Fortunately, higher interest rates should eventually increase bond returns, giving them a more prominent place in portfolios.

INFLATION'S MAGIC BULLET?

Inflation-protected bond funds are a common way to hedge against inflation, but while they've held up better than their non-inflation-protected peers, the same interest-rate risks which have dragged down the rest of the market have hurt their performance this year.

One potential to capitalize on higher inflation is to purchase **Series I bonds**. These are a type of savings bonds issued by the U.S. Treasury to protect your money from losing value due to inflation. The interest rate is made up of a fixed rate and an inflation-adjusted rate, which is adjusted semi-annually to keep pace with rising prices. **Series I bonds** are exempt from state and local income tax and lack the market volatility of bond funds. The current rate is 7.12% but will reset come May, and there is talk it will go above 9%.

However, these bonds can only be purchased directly from the U.S. Treasury. To do so, you need to create an account at TreasuryDirect.gov; while we can invest in funds tracking inflation-adjusted securities, we can't help with the direct purchase of **Series I bonds**. Individuals are limited to purchasing $10,000 per year or $20,000 for married couples, and an additional $5,000 can be purchased with your tax refund.

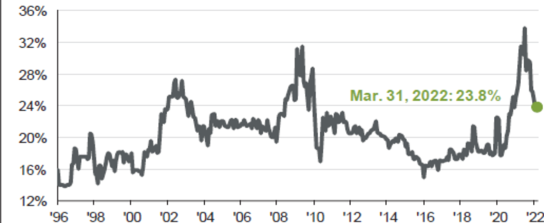
EXPECT LITTLE AND HOPE WE ARE WRONG

Shorepoint's advice in the face of all these points is to keep your expectations for making money in 2022 modest. The market's reaction to the dour news has been decidedly muted but the probability of a recession has increased. We are treating rallies thus far as bear market rallies. We have decreased our core bond exposure given the rising rate and inflation environment. In turn, we have added to income-producing assets that are more resilient to interest-rate risk, such as floating rate bond funds, short-term inflation-protected bond funds, and cash. In addition, we have been adding to stocks on weakness as we find pockets of value in stocks of great companies that are attractively valued in the broader market. Some areas that look especially attractive are in healthcare, communications, industrials, and finance.

P/E ratio of the top 10 and remaining stocks in the S&P 500
Next 12 months

Weight of the top 10 stocks in the S&P 500
% of market capitalization of the S&P 500

Earnings contribution of the top 10 in the S&P 500
Based on last 12 months' earnings



Although the short-term shifts that are occurring are certainly inflationary, it doesn't mean that adjustments being made won't be helpful to the economy in the future. We are Americans. We push everything too far - from outsourcing almost all of our manufacturing to China to printing money assiduously to quell the first hints of recession fears. However, we are also flexible and our quick twitch muscles and short attention spans can be a strength, especially compared to the slow boat of central planning in an authoritarian regime like China. Note their current approach to Covid with draconian shutdowns and the use of less effective locally manufactured vaccines.

We may be better off long term to have a more diverse set of manufacturing partners and perhaps to bring some of that work back home. It could be a more stable, more shock resistant approach to have a more diversified bench of trading partners and less dependence on certain countries.

We believe in the resilience of capitalism and the ability for well-run companies to adjust and manage through times like this. So, we look at the next 6-8 months as a time to be picky, to diversify, and to avoid big calls or undue risks, especially after the powerful multiyear run we have enjoyed in the equity markets. Hopefully things turn out better AND sooner, but let's not expect that. This year will be one to build portfolios for the next leg in the economic cycle.

Shorepoint's process is thoughtful, disciplined, and flexible. Please know that our team is working diligently to manage risk and returns as well as position your portfolio for the long term. There are always reasons not to invest, but staying the course usually wins out. We believe that appropriate portfolio diversification amongst asset classes can help buffer your portfolio from the ups and downs of market volatility. We will continue to monitor the risk/rewards of both asset classes and sectors to rebalance appropriately.

Team Shorepoint