# NEWSLETTER – APRIL 2023

## MARKET TRENDS 3.31.23

| Asset Class | 3 Mo | 1 Yr |
|---|---|---|
| **Global Stocks** | | |
| MSCI World | 7.8% | -6.5% |
| **US Stocks** | | |
| S&P 500 | 7.5% | -7.8% |
| Large Cap Value | 1.0% | -6.1% |
| Large Cap Growth | 14.3% | -11.1% |
| Mid Cap | 3.8% | -5.1% |
| Small Cap | 2.8% | -11.6% |
| **International Stocks** | | |
| Developed Markets | 8.6% | -0.2% |
| Emerging Markets | 4.1% | -10.3% |
| **Fixed Income** | | |
| Taxable Bonds | 3.1% | -4.7% |
| Municipal Bonds | 2.6% | 0.5% |
| **Alternatives** | | |
| EM Bonds | 1.9% | -8.0% |
| Floating Rate | 1.4% | 2.9% |
| Preferred | 3.8% | -9.0% |
| Gold | 9.1% | 1.5% |
| Real Estate | 1.5% | -19.0% |

Source: Factset


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## Consensus v. Reality: Never the Twain Shall Meet

Equity markets rallied for the first six weeks of 2023, unsurprisingly, since pundits across the investment industry had called for the opposite to happen. After a dour 2022 in both stocks **(S&P 500 Index -18%)** and bonds **(Bloomberg Aggregate Index -13%)**, it became "common knowledge" that investors would continue to suffer through the beginning of 2023 until a Fed pivot occurred later in the year.

At Shorepoint, we are skeptical, if not cynical, about these short-term predictions, and you should be too. It's fruitless to invest based on market timing, hype, and mania. As the great contrarian Humphrey B. Neil wrote, and we paraphrase: when everyone thinks alike, they are likely to be wrong. The violent, albeit short-lived rally of early 2023 exemplifies how you can hurt yourself financially if you make dramatic asset allocation moves based on fashion and consensus.

The longer we work in the financial industry, the more we channel ourselves into the wise, philosophical broker, Lou Mannheim, played perfectly by Hal Holbrook, from Oliver Stone's *Wall Street* (1987), looking into the abyss, and searching for character. Google "Lou Mannheim quotes Wall Street" for some of the best, straightforward advice on life and investing.

There are no shortcuts, no easy ways to make fast money consistently in the markets, but a sound, long-term approach combined with rigor and discipline almost always does; it's just challenging because it cuts against the short-term instincts of being a living creature, a sentient (and anxious) being who needs food and shelter and wants to protect oneself and one's tribe. Hit us with a 24-hour news cycle of breaking news dinging on our devices and the constant buzz of the next threat thrumming in the airwaves, and you might wonder how the world isn't even crazier than it seems now. But we ***can*** manage all of this ***together***!

## Don't Call it a Comeback; the 60/40 Portfolio Has Been Here for Years!

One of the key ways in which Shorepoint manages risk for clients is by taking a balanced approach to asset allocation. By combining stocks, bonds, cash, and alternative assets, we can reduce volatility and maximize what clients earn in their portfolios over time. Traditionally investors could rely on a portfolio that was allocated roughly 60% to stocks with 40% in bonds to produce lower volatility returns that were quite fair based on the amount of risk taken. You can imagine how well this works in conventional times when a 10-year Treasury bond yields 4%+!

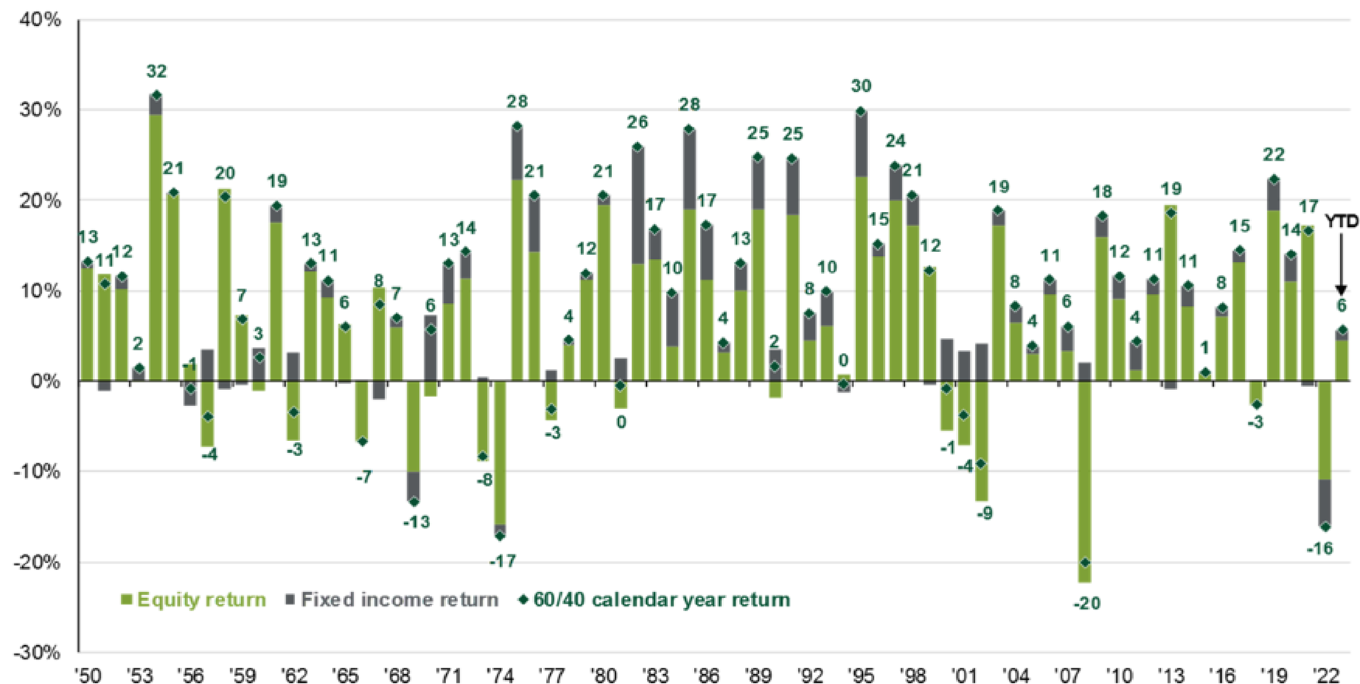


*Figure 1- JPM Guide to The Markets*

Over the last 10-15 years, the 60/40 truism was challenged as the Federal Reserve ("Fed") lowered interest rates so much that a 10-year Treasury bond yielded just 1% as recently as 2021. When such a significant side of a portfolio yields less than half its usual rate, investors have choices to make. One can accept the lower rate. One could decrease bond exposure and up the equity risk by holding more stocks. Private equity (and other alternative investments) can replace lost yield, especially for larger, more sophisticated investors. Or you could do what Shorepoint did successfully for many years: increase yield by going to longer maturity-dated bonds and sacrificing some quality with lower credit bonds or floating-rate bank loans, for example.

At this time in history, the financial press, ever humble (not), long-term in its view (nope), and nuanced (0 for 3), pronounced the 60/40 portfolio as DEAD! Well, it turns out it was just resting. After a brutal 2022 for bonds in which the Fed raised rates aggressively (from 0% to a Fed Funds target of 4.25% to 4.5%), there has been a reset in fixed income. With 10-year Treasuries yielding about 3.6%, we have restored higher-quality bonds with shorter maturities to client portfolios!

While stocks remain volatile, at least we can begin rebalancing portfolios for the long haul with higher-yielding bonds and lower risk to investors. Savers will also be rewarded with higher-yielding money markets, savings accounts, and CDs. So don't believe the hype. And don't call it a comeback. The 60/40 portfolio never really went away, and as a basic foundation for constructing a portfolio, it will make even more sense now for years to come. Since 1950, the 60/40 portfolio has produced positive calendar year returns 81% of the time!

# Oxymorons and Orderly Bank Runs

Do you remember when we learned what oxymorons were in middle school and/or high school? The example I remember most was the character Tiresias from the *Odyssey*. He was a mythological Greek character known for the accuracy and the truth of his prophecies. He could "see" the future but was physically blind. Hence, the *blind seer* oxymoron.

On the news lately, you may have heard about these worrisome runs on banks, especially on local or regional ones like *First Republic*. Clients of these banks became concerned about the safety of their deposits and started to withdraw cash from them immediately AND simultaneously. *Silicon Valley Bank* failed in an astonishingly short period - only a few days.

Government officials and bank analysts tried calming these fears with their modern own oxymoron. They said that ***orderly bank runs*** wouldn't threaten our financial system. Well, it's nice to see a liberal arts education come to our aid here. Here's a newsflash: **there are no orderly bank runs**. We don't go down the street to the Bailey family's savings and loan bank and haggle with George for a few bucks. Technology has enabled us to move vast sums of money to other financial institutions instantaneously.

In our view, the government did the right thing when it stepped in to guarantee deposits (insured - under $250k per registration as well as implying the backing of uninsured monies over $250k) for bank clients in the U.S. to avoid the lightning contagion of what could have been a massive bank panic. After all, there are major questions about the Fed's ability to regulate these banks, so how can we be expected to know better? Shorepoint continues to recommend clients keep less than $250k in bank accounts per registration regardless of the perceived strength of the bank – just a prudent practice!

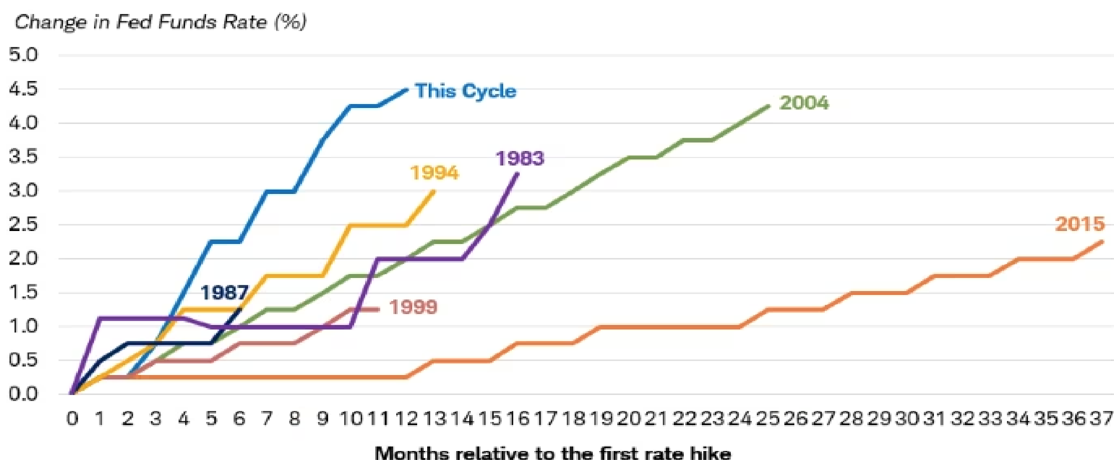


*Figure 2-Schwab Investment Management*

When driving on a new highway, we don't quality check the asphalt vendor's work and history. When we get on planes, we rely on the FAA to ensure our aircraft aren't shoddy-not ourselves. Making this bank situation particularly thorny was that many of these banks did NOT run into trouble based on risky loans and assets. The Fed being late to the party on raising interest rates and subsequently having to move more dramatically decreased the short and intermediate value of the…. wait for it…***TREASURIES***!!! that these banks owned, typically considered a very safe asset-more on this and the FED's conundrum in the next section.

## Looking Ahead

It was clear that the aggressive moves of the Fed to try to thwart inflation could lead to some unintended consequences. And in short order, the recent banking scare, albeit a marginally different beast than the financial crisis of 2008, has caused panic among investors and depositors. Only time will tell, but some type of recession (earnings and/or economic) is likely, while hope for a 'soft landing' seems to be fading.

And in terms of bank stocks, we hold a basket of what we perceive to be high-quality banks with strong capital positions and conservative lending practices. However, given the recent turmoil, we are re-examining our holdings to determine if there is any opportunity to upgrade our holdings ever more. Shorepoint exited 2022 with the highest cash position in twelve years (yielding over 4%), providing us with dry powder to take advantage of opportunities. We have shifted our bond position into higher quality bonds, taken our equity position down to a neutral position and added a gold miner stock/ETF to our alternatives as a hedge against higher inflation, weakness in the U.S. dollar, and general global turmoil. ***We also plan on launching the Shorepoint Income Fund II, LP, later in 2023 – we are available to discuss with you if this is appropriate for your situation.***

Our equity portfolios have focused on owning companies with a leading competitive position, well-respected management teams, solid balance sheets, and robust cash flow generation with the potential for capital appreciation. With volatility expected to continue, we will continue to add to high-quality companies, reposition the portfolio to capture upside without taking any undue risks, and perform tax harvesting throughout the year. As the Fed eventually pivots, history has informed us that high-quality companies tend to lead the pack.

**Quality readying to lead?**

Average returns after Fed hiking cycle ends, 1984-2021

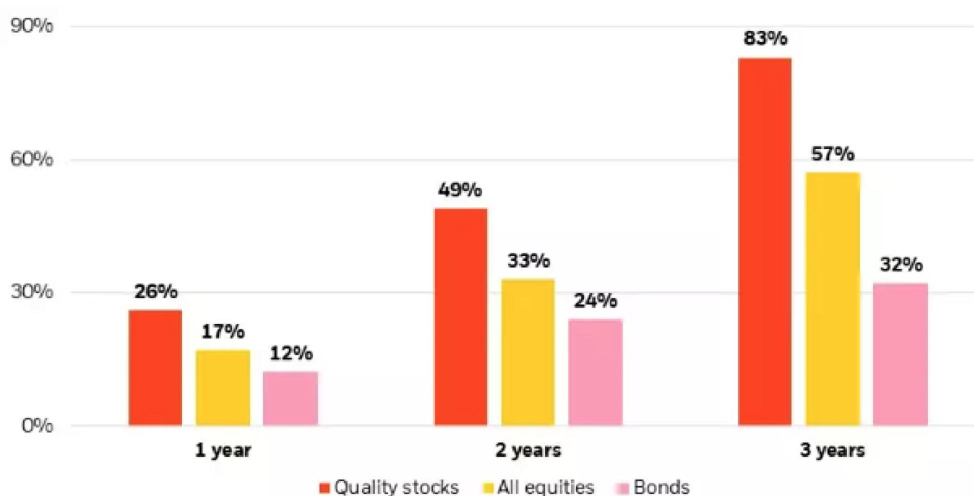


*Figure 3- Blackrock*