nVEST nSIGHTS

March 31, 2023

IN THIS ISSUE:

Delivering financial peace of mind.

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WHO'S DRIVING?

Bill Henderly, CFA, Nvest Wealth Strategies, Inc.

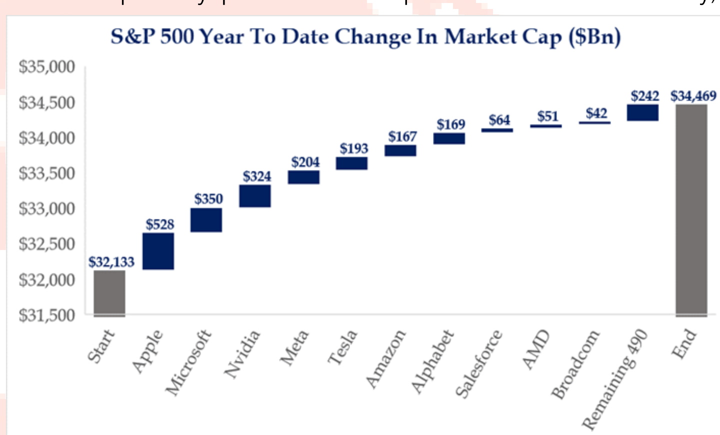
Interest rates and bonds are driving the financial markets; stocks are along for the ride. As the Federal Reserve continues to battle high inflation by raising rates and tightening money supply, its actions are driving bond market action. Rate hikes increase the cost of borrowing for both businesses and consumers. Thus, stocks are being "carried along" because policy change is significant and creating uncertainty. The greatest items of investor uncertainty relate to *when* will the Fed conclude tightening actions, and *how much* economic damage will their actions cause (ie: recession). This translates into volatility – up/down market action that also amplifies investor worry, on full display during 1Q2023.

Let's briefly review the sequence and events of the first quarter. The US economy started out 2023 with momentum despite the Fed's aggressive tightening during 2022. Market participants were hopeful these Fed actions would be enough to curb inflation. January financial market performance was exciting and strong, and investors were encouraged. As February arrived, economic news was too good (unemployment at all-time lows); "good news" was deemed "bad news" on the belief the Fed would be forced to continue raising rates even as bonds/stocks struggled. In general, the end of tightening was uncertain. As March arrived with signs of economic slowing, bonds and stocks attempted to rebound, until… two banks failed as many large tech-sector and startup-company depositors quickly pulled money (bank run). These bank failures elevated public worry that even short term money may not be safe. Stocks managed to recover by the end of March following the Treasury boosting cash reserves in the banking system. Volatility creates investor uncertainty, particularly when the Fed is raising interest rates aggressively to battle high inflation.

Recall, monetary policy affects the economy with a 6 to 9 month lag. Peak inflation likely occurred last summer at over +9%. Recent stats show it improved at 6% annualized, but it will likely take longer for inflation to recede toward a level of 2-3% as full employment (wages) will keep inflation sticky. Monetary policy often reveals "weak links in the chain" as a key business sector struggles (ie: two bank failures in March). Whenever the Fed embarks on tightening its policy, financial risk increases because excessive debt levels become a burden to repay. At some point, weak entities get exposed and fail (default); the "weak link" breaks.

Despite banking system strains in March, the Fed again raised interest rates by 0.25%; but that was its smallest rate increase since beginning this hiking campaign last year. Was this rate hike to 4.75-5.0% the last? Could the shock to the banking system in March from two bank failures (SVB and Signature Bank) cause the Fed to stop or pause, or be very close to the last hike?

Both stocks and bonds concluded 1Q with gains albeit much reduced from the strong returns enjoyed in January. Client portfolios trailed market indexes as focus shifted to newly defined "safe" assets. The recent definition of "safe": includes money market funds and a few big technology stocks (10 names accounted for 90% of the gains – a top-heavy performance experience that is unhealthy). These stocks were beat up in 2022, but are currently viewed as "defensive havens" if a recession occurs. The markets often amaze investors as they shift this way and that – value and dividend-paying stocks worked well during the bear market slide, but now pause as old leaders (viewed as "safe havens") are rebooted during 1Q. Be careful because the financial markets still reside in the bear trend; there is not robust broad participation to predict the beginning of a new bull market.



The Fed finds itself in a challenging spot – continuing its tightening policy to fight inflation while needing to ease and thereby improve public confidence in banks. Two recent bank failures create the challenge. Another new challenge is just arriving. OPEC+ (includes Russia with its economic sanctions resulting from its invasion of Ukraine), announced additional oil supply cuts. Supply cuts are inflationary; they will raise the price of energy and slow economic growth. This action by Russia (OPEC+) is economic warfare. It seems purposefully announced at a tough time for the USA, the Fed, and western allies.

(Continued on pg 2)

What does this suggest for investing client portfolios? Simply put, "go slow" but keep investing. The OPEC+ announcement suggests, to me, that dividend payers and short-duration assets should reclaim leadership and bounce back; old leaders (new "safe") that were recently "rebooted" will surrender their recent lead. Bear markets evaporate risk and reveal new market leaders. Further, "Experience teaches the best buying opportunity in long bonds presents itself when the yield curve is inverted" (from George Soros' book, "The Alchemy of Finance"). Current rates are attractive compared to the past 10+ years. Be careful though to invest in short to intermediate higher quality bonds that comply with your investment time horizon and purpose. Long maturity bonds are much more risky than short/intermediate bonds. Bonds and cash do not battle inflation well over time; they struggle to provide real return. Always focus on marketability, quality and time horizon when owning bonds. Both offer attractive diversification benefits again because current yields exist.

"dividend payers and short-duration assets should reclaim leadership and bounce back; old leaders that were recently 'rebooted' will surrender the recent lead"

KINDNESS OF STRANGERS

Twelve years of easy money and available credit are over; probably for quite some time. During that time, interest rates were nil to zero. "Anyone who could fog a mirror could get a loan" at an attractive rate. Risky ventures performed well because money was free. In the words of research group Strategas Partners, we might call this era "kindness of strangers." Following the huge stimulus programs by the government and Fed monetary policy to aid businesses, families, and workers during COVID's Great Lockdown, the economic and financial market backdrop changed. Huge money supply created inflation; huge inflation spikes were everywhere. Now, the Fed finds itself in a rather odd position where it needs to tighten policy to control inflation and boost money supply to comfort public perspective regarding financial conditions at banks.

nvest WEALTH STRATEGIES

We anticipate interest rates will remain elevated for longer, or stickier than expected. That's because inflation, while off its peak, will stay elevated and persist for longer. Did kindness shift to investors who now earn higher interest rates on money market savings and bonds? Current interest rates are a massive difference or "sticker shock" for owning MMFs and bonds compared to 0% at the start of the current rate hike process (see chart MMF yields on pg 3). Investors worried about the economic outlook now see money market funds (paying 4.5%+) and short-maturity bonds attractive vehicles and provide comfort. They are not however, a long-term investment solution because inflation is their key enemy. Diversifier - yes; inflation fighter - no. [If inflation is 6%, MMF paying 4.5% lose purchasing power by the inflation rate; real after inflation rates are still negative.] In the short-term, they offer attractive current yield and safety while stock market clouds exist.

"This market backdrop warrants investment caution. Caution does not mean stop investing or altering investment objectives - the bond/stock mix."

Yield curves and yield spreads are often viewed as a predictive tool about future rates. The current yield curve provides a unique predictive message. Currently, Treasury securities of all maturities (3-month T-Bills, the 2-year Treasury, 5-year, 10-year and all the way to the 30-year Treasury Bonds) offer yields that are lower than the Fed Funds (FF) rate at 4.75% which the Fed started raising in 2022. The yield curve is inverted (short maturity bond rates are higher than those maturing further in the future; abnormal); a trait existing for the past 11 months. This means a government policy mistake. This is a rare experience. The 2-year calls the shots in bond world, often leading Fed policy on the way up *and* the way down. The 2-year is currently 110 basis points below FF. History reveals that Fed policy hikes were done when 2-year yields were below FF. Unfortunately, a recession followed. Between 1978-1982, the 2-year was regularly below FF and accompanied a very volatile stock market (sounds like recent experiences). If the 2-year gets its way, the Fed is done raising interest rates; just not sure the Fed is listening yet.

Fed Funds Rate vs. U.S. Treasury Curve

Maturity	Yield	Bps Below FF
Fed Funds	5.00%	--
3-Month	4.58%	-42
6-Month	4.73%	-27
12-Month	4.40%	-60
2-Year	3.90%	-110
5-Year	3.50%	-150
7-Year	3.50%	-150
10-Year	3.45%	-155
20-Year	3.81%	-119
30-Year	3.66%	-134

Further, history shares that recession followed 7 of the last 9 tightening campaigns by the Fed, and today's inversion is more than any since 1981 when US interest rates peaked. The inversion this cycle started 11 months ago. Since 1978, recessions started 14 months after the first inversion. Recent bank failures are likely to cause savers (consumers) to pull back spending. That can help lower inflation, but also slow the pace of the economy.

This market backdrop warrants investment caution. Caution does not mean stop investing or altering investment objectives (bond/stock mix). Those types of investor actions may provide

ANNOUNCEMENTS:

- Early April - 2Q 2023 fees collected and performance reports sent.
- April 7 - Good Friday; stock market closed, bond market and banks open.
- April 18 - Tax Filing Day! Also last day to make contributions to IRA/Roth accounts for 2022.
- May 29 - Memorial Day; markets, banks, and Schwab closed.
- June 30 - End of 2Q. Quarterly Reports sent early July.
- Our ADV Part 2A & B as required by the SEC & Ohio (and other states) is available to you anytime upon request.

short-term comfort but will lead to missing the next bull market which no one knows its beginning. Miss the beginning and miss a lot. Charlie Munger (co-key Berkshire partner with Warren Buffett) stated "The world is full of foolish gamblers, and they will not do as well as the patient investor." Berkshire's individual stockholders are largely "once-a-saver, always-a-saver" variety. We too encourage clients to find investment amazement through the magic of compound interest in the growth of portfolio values which only occurs by remaining a long-term investor. In other words, timing generates poor experiences.

For such a time as this…Expect investing in the near term to be a grind. Stocks and bonds will rally and retreat, rally, and retreat. This is part of the process of wringing out risk which was high when money access was virtually "free" and unlimited. Know too that bear markets ultimately reveal new leaders. That is likely to include dividend paying stocks (short duration) because interest rates stay high, longer; they offer better values. Seek higher quality companies with high return on capital/equity to shareholders. Technology stocks remain the most overvalued relative the S&P500 index (since October 2007 – chart-tech/energy), while energy and traditional banks are the cheapest sectors… most investors dislike both; that's contrarian opportunity. And we already discussed the "kindness" of owning short-maturity bonds and MMFs – something we can be comfortable with in the short term, but MMFs are not a long-term investment solution.

S&P 500 Current and Historical Valuations

Sector	NTM P/E	15-Year Avg	Ratio	Relative P/E	15-Year Avg	Ratio (sorted)
Technology	23.5x	17.1x	1.37	1.32	1.07	1.24
Discretionary	23.4x	20.0x	1.17	1.33	1.24	1.07
Health Care	16.8x	14.5x	1.15	0.95	0.92	1.03
Staples	19.7x	17.6x	1.12	1.12	1.11	1.01
S&P 500	17.6x	15.9x	1.11	1.00	1.00	1.00
Industrials	17.6x	16.2x	1.09	1.00	1.02	0.98
Utilities	17.4x	16.1x	1.08	0.99	1.02	0.97
Communications	16.1x	15.5x	1.04	0.92	0.99	0.93
Materials	16.1x	15.8x	1.02	0.91	1.00	0.91
Financials	11.2x	12.8x	0.87	0.63	0.82	0.77
Real Estate	34.0x	42.6x	0.80	1.93	2.31	0.84
Energy	9.2x	19.2x	0.48	0.52	1.16	0.45

ARE MY ASSETS SAFE?

Steve Henderly | Nvest Wealth Strategies, Inc.

Nvest, since its inception, has utilized the brokerage and custody services of Charles Schwab & Co. We consider Schwab to be the industry leader based on its history, low fees, and industry leading technology; it is also long considered one of the most conservatively managed asset custodians in the industry. While the entire industry continues to undergo significant changes via consolidation and expanding access to investing via cost reductions (advocating for no-load mutual funds, elimination of trading commissions, account maintenance fees, and more), Schwab's commitment to client security and financial stability remains unchanged. For example, Schwab avoids underwriting new securities issuance, does not hold or permit direct investing in risky or highly speculative assets (such as cryptocurrency), and remains highly protective of client assets.

With that said, recent events in the financial sector over the last month and resulting impact to financial sector stock prices, can raise concern. Clients may be asking "***Are my assets safe at Schwab***"? Over the last month, Schwab is communicating regularly on the topic; included below are links to Schwab's website outlining the numerous protections to be mindful of and a couple highlights:

- Your investments (assets) held at Schwab are segregated at the broker/dealer level and are not available to Schwab to use or satisfy their own liabilities or creditors. Your assets are <u>your assets.</u>
- Investment assets are separate and not commingled with assets at Schwab Bank.
- For cash held at Schwab Bank, FDIC insurance applies up to $250,000, per depositor. Different, higher effective FDIC limits apply to cash held in brokerage accounts.
- Schwab continues to hold a safe and liquid balance sheet, but Schwab can also make use of recent programs made available by the Fed to shore up confidence in the general banking system that transpired in March.
- *Links for more detail: <u>Video From Schwab's CEO</u> <u>Schwab Asset Protection Details</u>*

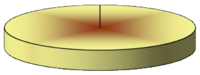
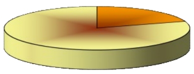
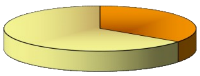
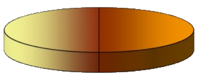
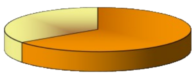
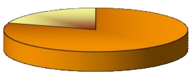
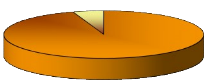
Beyond these protections, we are keenly aware that a number of clients are utilizing higher-yielding money market offerings managed by Schwab, often as an alternative to traditional bank savings accounts or pending longer-term investment. While these are not bank products nor FDIC insured, we are conducting ongoing due diligence on these funds. Schwab's core philosophy and priorities in the management of these offerings is focused on: 1) Stability of capital (stable NAV of $1.00/share); 2) Daily Liquidity; and 3) Attractive income that does not jeopardize the first two.

We trust this additional insight into the industry will help ease any concerns. Recall too, "we eat our own cooking". This phrase applies not only to how our own personal and retirement savings is invested, but also the custodian where those assets are held – we ourselves utilize Schwab exclusively. As always, we welcome the opportunity to discuss in more detail. Feel free to call or visit.

Closing thought: an article, "Ignorance Really is Bliss When it Comes to Investing", was recently published in the WSJ. Investors are hit daily with a fire hose of information (news, analysis, etc) and possess an ease of instant trading not available even 10 years ago. Studies are proving that this "access" is not improving long-term performance. Rather, it is leading to overconfidence, greater risk-taking, and impulsive behavior. We have long shared there are two types of investors: the mental accounter who checks and tracks his portfolio movement "daily"; by contrast the Rip Van Winkle is one who invests and then takes a long nap. The mental accounter experienced great stress and struggles to stay invested; Van Winkle awakens following his extended nap in great amazement of how his money grew… unaware of all the ups/downs that were part of the journey. We don't advocate burying your head in the sand, but be careful not to let noise take you off track.

Benchmarking as of March 31, 2023

Summary of index portfolio returns compiled by Nvest Wealth Strategies, Inc.

	Index Portfolio	Stock/Bond Allocation		Total Return Through 3/31/2023			
				1st Qtr	12 Mths	3 Years	5 Years
	Capital Preservation	0% / 100%	*Cumulative*	1.7%	-0.3%	2.8%	6.9%
			Annualized		-0.3%	0.9%	1.3%
	Income	20% / 80%	*Cumulative*	2.5%	-2.0%	12.4%	12.5%
			Annualized		-2.0%	4.0%	2.4%
	Balanced Conservative	35% / 65%	*Cumulative*	3.0%	-2.7%	17.6%	15.8%
			Annualized		-2.7%	5.6%	3.0%
	Balanced	50% / 50%	*Cumulative*	3.6%	-3.7%	25.6%	21.0%
			Annualized		-3.7%	7.9%	3.9%
	Balanced Growth	65% / 35%	*Cumulative*	4.3%	-4.6%	33.8%	25.5%
			Annualized		-4.6%	10.2%	4.7%
	Growth	80% / 20%	*Cumulative*	4.9%	-5.8%	42.9%	31.2%
			Annualized		-5.8%	12.6%	5.6%
	Aggressive Growth	95% / 5%	*Cumulative*	5.3%	-6.4%	49.1%	34.2%
			Annualized		-6.4%	14.2%	6.1%

The index returns reflect returns of various mutual fund averages compiled by Morningstar and allocated as follows: Capital Preservation: 90% Bond Average, 10% Treasury Bill Index; Income: 80% Bond, 10% Large Cap, 3% Mid Cap, 2% Small Cap, 5% International; Balanced Conservative: 65% Bond, 15% Large Cap, 5% Mid Cap, 3% Small Cap, 7% International; Balanced: 50% Bond, 24% Large Cap, 7% Mid Cap, 4% Small Cap, 10% International; Balanced Growth: 35% Bond, 30% Large Cap, 9% Mid Cap, 6% Small Cap, 15% International; Growth: 20% Bond, 38% Large Cap, 12% Mid Cap, 8% Small Cap, 17% International; Aggressive Growth: 10% Bond, 40% Large Cap, 15% Mid Cap, 10% Small Cap, 20% International. You cannot invest in these indexes or averages and all above indexes/averages include a 5% allocation to the Treasury Bill Index, reflecting a nominal level of cash. The level of diversification represented by these benchmark averages may be materially different than actual client accounts; therefore, clients may experienced different levels of performance volatility. Past performance is no guarantee of future results.

Money Market Yields

Many are amazed by the yields currently being paid on money market funds; rates not seen in at least 17 years. While these current yields *feel* great following an era being at or near 0%, we should recognize that they still trail inflation by roughly the same degree as when inflation was running between 2-3% annually. In other words, while we can take comfort in price stability and yield in the short-term, they still possess no opportunity to outpace inflation over the long-term and as inflation recedes, money market yields should drift lower as well.

Largest Money Market Funds 7-Day Yield

Today vs. Start of Current Fed Hiking Cycle vs. 10-Years Ago

Ticker	Fund Name	Today	Start of Hiking Cycle (3/16/22)	Mar-2013
FGTXX	Goldman Sachs Financial Square Government Fund	4.5%	0.1%	0.0%
SPAXX	Fidelity Government Money Market Fund	4.3%	0.0%	0.0%
VMFXX	Vanguard Federal Money Market Fund	4.6%	0.0%	0.0%
OGVXX	JPMorgan US Government Money Market Fund	4.5%	0.0%	0.0%
FDRXX	Fidelity Government Cash Reserves	4.3%	0.0%	0.0%
SWVXX	Schwab Value Advantage Money Fund	4.5%	0.0%	0.0%
GOSXX	Federated Hermes Government Obligations Fund	4.2%	0.0%	0.0%
FIGXX	Fidelity Government Portfolio	4.5%	0.0%	0.0%
MVRXX	MSILF Government Portfolio	4.5%	0.0%	0.1%
DGCXX	Dreyfus Government Cash Management	4.5%	0.0%	0.0%

Selected Funds - Total Return Performance Summary

As of March 31, 2023

Bond Funds - Taxable	Style	1st Qtr	12 Mths	3 Years	5 Years
Taxable Short-Term Bond Average		*1.7%*	*-0.7%*	*0.9%*	*1.3%*
Taxable Intermediate Bond Average		*3.0%*	*-5.1%*	*-2.3%*	*0.8%*
Allspring (fka Wells Fargo) Ultra Short	AS	1.4%	1.8%	1.9%	1.6%
Vanguard Short Federal	HS	1.3%	-1.3%	-1.0%	1.0%
American Century Short Duration	HS	1.6%	0.0%	1.1%	1.5%
Pioneer Short-Term Income	HS	1.8%	0.4%	3.0%	1.2%
DoubleLine Low Duration	HS	1.8%	0.6%	1.9%	1.3%
Vanguard Short-Term Investment Grade	HS	1.9%	-0.3%	0.7%	1.5%
American Funds Bond Fund of America	HI	2.8%	-5.1%	-1.8%	1.5%
American Century GNMA Income	HI	2.7%	-5.0%	-3.3%	0.0%
BrandywineGlobal Corporate Credit (fka Diamond-Hill Corp Cred)	LI	2.3%	-2.9%	6.1%	3.7%
Miller Convertible	LI	0.8%	-8.6%	7.7%	3.3%
Bond Funds - Tax Exempt					
Tax-Free Intermediate Bond Average		*2.3%*	*-0.3%*	*0.4%*	*1.6%*
Vanguard Muni Limited Term	HS	2.4%	0.8%	0.6%	2.1%
T. Rowe Price Tax Free S/I	HS	1.6%	1.1%	0.5%	1.2%
Vanguard Muni Intermediate Term	HI	2.4%	0.8%	0.6%	2.1%
Vanguard Ohio Long-Term	HL	3.0%	-2.1%	-0.1%	2.1%
Stock Funds - Domestic					
S&P 500 Index		*7.5%*	*-7.7%*	*18.6%*	*11.2%*
Equity Fund Average (Morningstar Mgr Agg US Core EW)		*4.4%*	*-8.4%*	*18.3%*	*7.3%*
Schwab Large Cap Growth	LG	17.5%	-12.3%	18.5%	13.5%
Parnassus Value Equity (f.k.a. Endeavor Fd)	LG	1.4%	-7.3%	24.9%	11.6%
T.Rowe Price Dividend Growth	LV	2.0%	-3.8%	17.4%	11.4%
WisdomTree US Quality Dividend Growth	LV	3.8%	0.3%	19.5%	11.5%
American Century Equity Income	LV	0.5%	-3.2%	13.5%	7.1%
Hennessy Focus	MG	4.4%	-13.7%	15.9%	6.1%
John Hancock Multifactor Mid-Cap	MB	2.9%	-7.8%	20.2%	8.1%
John Hancock Disciplined Value Mid-Cap	MV	1.3%	-5.5%	21.6%	6.9%
SPDR S&P600 Small Cap Growth	SG	2.1%	-11.0%	17.9%	5.9%
Neuberger & Berman Genesis	SB	7.0%	-2.9%	17.3%	8.9%
American Centry Small Cap Value	SV	2.6%	-8.3%	25.6%	7.6%
Avantis US Small Cap Value	SV	-0.1%	-5.4%	35.7%	N/A
SPDR S&P600 Small Cap Value	SV	2.1%	-11.0%	17.9%	5.9%
Stock Funds - International					
Morgan Stanley EAFE Index (Foreign)		*8.5%*	*-1.4%*	*13.0%*	*3.5%*
Oakmark International	LV	13.9%	5.2%	21.1%	1.5%
Schwab Fundamental International Index	LV	7.5%	-0.7%	17.5%	4.2%
John Hancock International Growth	LG	7.1%	-9.3%	8.6%	2.6%
Thornburg Developing World	LG	4.6%	-13.3%	7.1%	0.3%
Harding Loevner International Small Company	SG	4.0%	-8.6%	12.5%	2.0%
Hennessy Japan	LB	7.1%	-8.9%	2.6%	-0.3%
Stock Funds - Specialty					
Invesco S&P500 Eq Wt Energy	MV	-5.1%	5.6%	55.7%	7.8%
Direxion Auspice Broad Commodity ETF	N/A	4.0%	-1.7%	19.7%	9.2%
Neuberger Berman Real Estate Securities	MV	2.3%	-20.5%	8.0%	6.5%

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