PORTFOLIO REVIEW

Q4 2022

Rodney Sullivan, CFA, CAIA

EXECUTIVE SUMMARY

Investors will likely not soon forget 2022. Returns for both stocks and bonds declined, with global stocks finishing down -18% and bond returns falling -13% for the year. Declines in stock returns of course occur with some frequency, however bonds typically provide a safe haven from market downturns, but 2022 was the worst year on record for bonds.

A year ago we discussed with you our view that investors were at the time largely ignoring the risk of inflation and the Fed responding with dramatic tightening. This meant that both stocks and bonds would face headwinds. As our then minority viewpoint became a reality during Q1 of 2022, both stock and bond markets turned down rather abruptly and remained volatile throughout the year. Vesteer client portfolios fell between -12.0% and -12.6% in 2022, though still beating the 60/40 benchmark by 3.5% -4.0% after fees and expenses. Our tactical defensive portfolio positioning, combined with our strategic global diversified portfolio approach, helped to support Vesteer portfolios, providing at least some cushioning against the steep 2022 market downturn.

Although the outlook for 2023 is akin to seeing through a dense fog, our view is that risks to the downside for risk assets still dominate. As such our overall defensive market posture remains a key part of our portfolio strategy, at least for now.

The push of fiscal tightening in both the U.S. and Europe will be buttressed by the pull of China's economic reopening which will likely add to global growth (and inflation). Anticipating the outcome between these competing forces makes forecasting 2023 particularly challenging.

Finally, and importantly, we welcome two new Investment Advisor Reps to the Vesteer team! Frank Stalla, CFA, CAMS, joins us to support our business and clients in Omaha NE, while Alex Sullivan joins to support Vesteer clients from his home base in Springfield VA. We are thrilled to welcome the experience and expertise of both Frank and Alex to team Vesteer. We look forward to working together with our clients to provide our personalized approach to growing and preserving wealth across generations for many years to come!

OUTLOOK FOR 2023

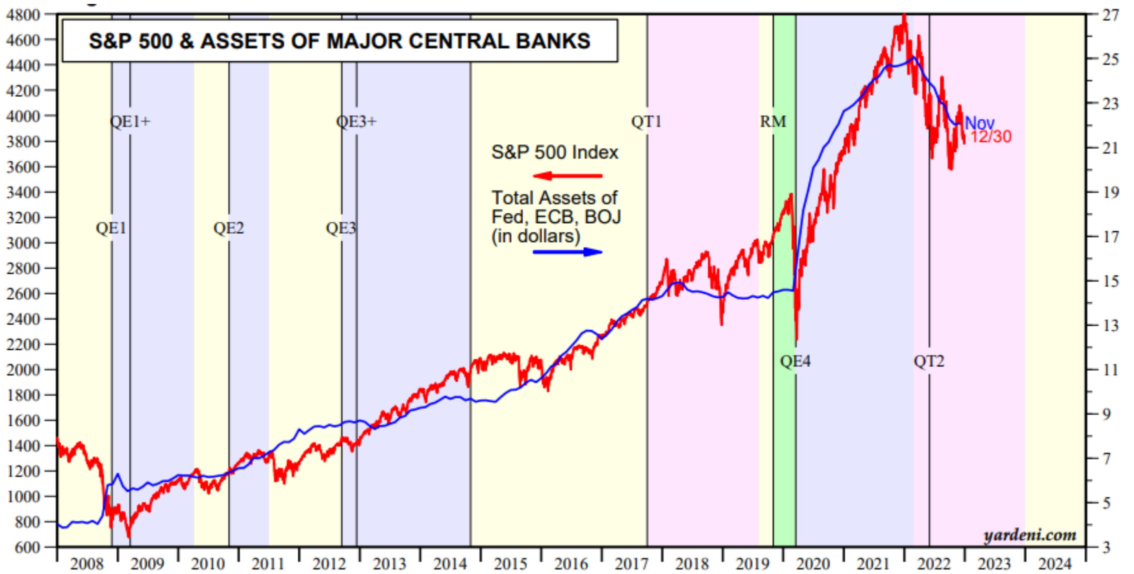
As we look ahead to 2023, the global economic outlook continues to be shaped by the aftermath of the global pandemic shock. As we've discussed over the course of the past year, Central bankers around the globe are facing an inflation surge to levels not seen in decades. Central banks continue to raise rates in a hurry. Our view remains that the Fed tightening (both higher rates and a reversing of quantitative easing) will continue to weigh on global economic activity in 2023, prompting global growth to cool down further.

Perhaps the Fed will accomplish their goal of an economic "soft landing." However, risks clearly remain to the downside. As such, Vesteer portfolios remain defensively positioned overall meaning less exposure to risky assets versus our typical 60/40 portfolio benchmark. Having said that, we recently made some adjustments in our portfolios to add bonds (lengthen duration) and also to increase our equity weight from the relatively expensive US markets towards the relatively inexpensive international developed and emerging market stocks.[1]

The Fed has stated numerous times that bringing down inflation is their top priority and that "some pain" will result. Furthermore, they are quite willing to "risk a recession." The Fed's efforts will bring inflation down, but will also slow the economy, perhaps more so than expected, possibly leading to a recession in both the global economy and corporate profitability. Figure 1 updates one of our favorite graphs to help paint the picture.

[1] Source: JP Morgan Guide to the Markets, Jan 2, 2023. As of 12/31/2022, ACWI ex-US was trading at a 28% discount to the US based on P/E ratios.

Figure 1
Don't Fight the Fed



* Averages of daily figures for weeks ending Wednesday. Securities held by Fed include US Treasuries, Agency debt, and mortgage-backed securities. Note: QE1 (11/25/08-3/31/10) = $1.24tn in mortgage securities; expanded (3/16/09-3/31/10) = $300bn in Treasuries. QE2 (11/3/10-6/30/11) = $600bn in Treasuries. QE3 (9/13/12-10/29/14) = $40bn/month in mortgage securities (open ended); expanded (12/12/12-10/1/14) = $45bn/month in Treasuries. QT1 (10/1/17-7/31/19) = balance sheet pared by $675bn. RM (11/1/19-3/15/20) = reserve management, $60bn/month in Treasury bills. QE4 (3/16/20-infinity). QT2 = balance sheet pared by $95 billion per month. Source: Federal Reserve Board.

Source: Yardeni.com, https://www.yardeni.com/pub/peacockfedecbassets.pdf

The blue line shows the quantitative easing path of global monetary authorities following the global pandemic, while the red line tracks the S&P 500 index. Notice how closely the Fed easing/tightening paths are traced by the S&P 500 index. As the old market adage goes, "don't fight the Fed." We anticipate a continued Fed tightening and the negative result on the economy and corporate profits. In short, we should expect both economic growth and inflation to slow in 2023.

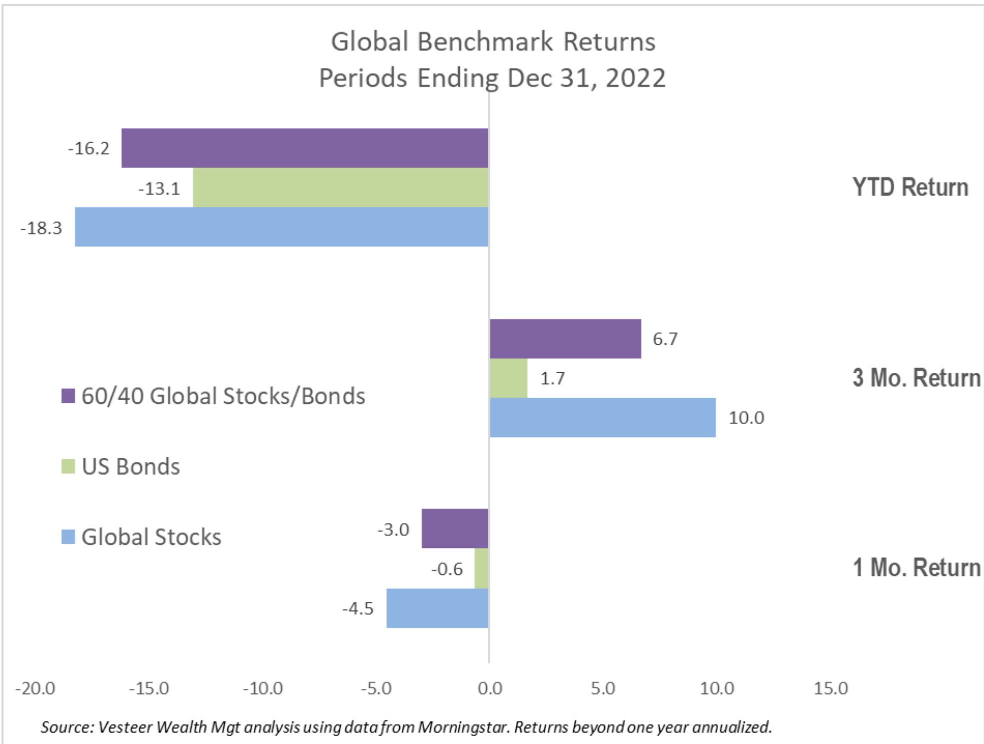
Pulling the global economy in the other direction, China's economy is finally reopening following a long shutdown. We shouldn't expect the China playbook to look very different from the U.S. reopening—the releasing of pent-up demand will be supportive for global nominal growth and also inflation. The push of fiscal tightening in the U.S. and Europe will be buttressed by the pull of China reopening. Anticipating the result of these push and pull forces makes forecasting 2023 once again like seeing through a thick fog.

VESTEER PORTFOLIOS

As readers are aware, we positioned portfolios defensively over the past year by tilting towards lower risk, higher quality stocks, shortening our bond duration, and adding commodities to protect against rising inflation.

This worked out well as total 2022 returns were negative for both stocks and bonds as shown in Figure 2. In fact, all of the major global asset classes, with the one exception being commodities (up 24% in 2022), report negative year-to-date returns with the most-risky asset classes being down the most. More specifically, for the year 2022, global stocks declined -18.4% as measured by the MSCI ACWI (All Countries World Index) and the Bloomberg Barclays Bond Index fell -13.0%. The combined stock/bond portfolio as measured by the standard 60/40 stock/bond benchmark portfolio was down -16.2%.

Figure 2: Global Benchmark Returns



The portfolios shown are hypothetical portfolios and do not necessarily represent any actual Vesteer portfolio or strategy. The results are hypothetical and are not an indicator of future results and do not represent returns that any investor might actually achieve. Indexes are unmanaged, do not reflect management or trading fees, and one cannot invest directly in an index. Purchases are subject to suitability. This requires a review of an investor's objective, risk tolerance, and time horizons. Investing always involves risk, whenever you invest you are at risk of loss of principal as the market fluctuates. Past performance is not indicative of future results.

Vesteer client portfolios also fell for the year, but fortunately less so than the 60/40 stock/bond benchmark. Vesteer client portfolios fell between -12.0% and -12.6% over the year, resulting in outperformance of between 3.5%-4% versus the 60/40 benchmark after subtracting advisory fees and fund expenses.

It's important to further note that those client portfolios with similar risk to a 60/40 stock-bond portfolio outperformed both stocks and bonds individually. Again, this comes from our defensive posturing over the year as well as the benefits of our global approach which invests in an array of asset classes including gold and commodities.

As mentioned before, while we remain pleased with the relative outperformance of our global diversified portfolio strategy, we fully appreciate that this has been a difficult environment in which to preserve wealth and that negative absolute performance is still painful!

As we've discussed before, our portfolio approach adjusts our strategic global diversified portfolio by tilting towards areas of the market we view as potentially offering the best return for the risk taken. Most often, these tilts take the form of medium to long-term themes, like protecting portfolios against inflation and its attendant effects, or avoiding overpriced market sectors (like the hot "COIVD stocks" of 2020-21) in which market prices for securities exceed reasonable valuations in our view. As an aside, I teach a course at UVA Darden School of Business on security valuation. We have had some vigorous class discussions in our efforts to anticipate markets and the best opportunities to add value— quite challenging in today's highly uncertain environment!

Yes, markets are volatile. A harsh reality of investing that is too often forgotten by our industry, especially following a long bull run. My experience in managing investments during past turbulent periods gives rise to our portfolio philosophy – in short, slow and steady (with lower costs) wins over the long haul. We hope that our approach better enables you to stick with your chosen portfolio mix over the long haul, through the tough times as well as the good.[2]

For now, we are maintaining our defensive posture in the face of continued heightened economic uncertainty. Our approach will hopefully continue to provide some downside protection until markets eventually turn positive. We take seriously our responsibility to help our clients grow and preserve their wealth over the long term.

Though we spend a majority of our quarterly updates on a market review and outlook, it is important to note that we also seek to add value by going beyond managing your investment portfolio to fully support all of your financial planning needs. Please reach out to us if we can ever be of service to your long-term financial success.

[2] Research shows that as a group, investors tend to underperform the market over the long-term due to their buying after the market has gone up and selling after it has gone down. The result of the poor "market timing" behavior, investors underperform the market by a whopping 3.7% per year over the long term.

WELCOME NEW VESTEER TEAM MEMBERS!

As we complete our third year since forming Vesteer, it has been quite rewarding to see the positive response to our unique approach to growing and preserving wealth for families and small businesses! To support our growing business, we are thrilled to welcome two new Investment Advisor Reps to the Vesteer team! Frank Stalla, CFA, CAMS, joins to support our business and clients in Omaha NE, while Alex Sullivan joins to support Vesteer clients in Northern VA from his home base in Springfield VA. We are thrilled to be joined by Frank and Alex and look forward to working together for many years to come to deliver our personalized approach to growing and preserving wealth across generations!

FRANK STALLA, CFA, CAMS

Frank is an investment advisor representative with Vesteer Wealth Management serving clients in Omaha, Nebraska. He has a passion for making complex financial concepts accessible by simplifying them into their basic core elements. Frank's investment experience includes training financial analysts and portfolio managers for over 15 years as an author, editor, and instructor. Working with several professional training companies, he led public and in-house corporate seminars in major financial center cities throughout the U.S. and Europe. His work has helped prepare thousands of candidates for the rigors of the Chartered Financial Analyst exams, the most widely respected and difficult to attain professional credential in finance. Frank's other professional experience includes senior management positions in the insurance and banking industries. He holds an MBA from Case Western Reserve University and a bachelor's degree in Finance from Miami University. Frank is a chartered financial analyst (CFA) and a certified anti-money laundering specialist (CAMS). Frank resides in Omaha, NE with his family.

ALEX SULLIVAN

Alex is an investment advisor representative with Vesteer Wealth Management serving clients in the northern VA region. He got his first taste of investing with his interest in blockchain technology which offers digital assets in exchange for raw computation resources. His love for technology is expressed through his work to deliver advanced IT solutions for businesses and the Federal Government. Alex also enjoys fine wine and has completed the Introductory Sommelier certification. Alex's other professional accomplishments include the FINRA Series 65 and the VCP-DCV6.5 VMware. Alex resides in Springfield VA with his family.

As always, thank you for your trust. We wish everyone a happy and prosperous 2023!

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