

Portfolio Manager



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Senior Portfolio Manager

Top Contributors as of March 31, 2022

Company Name	Avg. Weight (%)	Contribution to Return (%)
JPMorgan Ultra-Short Income ETF	4.02	-0.02
iShares Short Treasury Bond ETF	12.76	-0.01
SPDR Bloomberg 1-3 Month T-Bill ETF	12.09	-0.00

Top Detractors as of March 31, 2022

Company Name	Avg. Weight (%)	Contribution to Return (%)
SPDR Portfolio S&P 500 ETF	33.53	-2.42
iShares Core S&P Small Cap ETF	14.03	-1.34
iShares Core MSCI Total International Stock ETF	12.53	-0.89

Source: Factset. For illustrative purposes only. Past performance does not guarantee future results. The holdings identified do not represent all of the securities purchased, sold or recommended for advisory clients. In the chart above, "weight" is the average percentage weight of the holding during the period, and "contribution" is the contribution to overall performance during the period. To obtain the calculation methodology and a list showing every holding's contribution to the overall composite during the period, contact: PortfolioAnalytics@ccmg.com.

Inflation and Rising Rates Provide Opportunities in 2022, but Risks in 2023 and 2024

Market Review

U.S. large and small-caps, international stocks, and particularly bonds, took on major losses throughout the first quarter, as inflation drove interest rates higher. The war in Ukraine exacerbated global stability and supply issues, providing further inflationary fuel. Commodities, for many years a derided and unprofitable asset class, proved to be the only safe haven. Energy and Material stocks, gold, oil, and agribusiness were some of the few areas investors could hide.

While the quarter began with markets declining amidst startling inflation data, things took a turn for the worse as the Ukraine invasion became a probability and then a tragic reality in late February. Oil prices soared above \$100 and peaked at \$123 per barrel by March 8th. By March 14th, the S&P 500 was down 12.2% on the year, and the NASDAQ 100 (QQQ) had fallen into a bear market, down over 20.0%. However, investor fear and pessimism had become extreme, and the S&P 500 staged an 8% relief rally to end the quarter down only 4.6%. Meanwhile, the Bloomberg U.S. Aggregate Bond Index suffered a 5.9% decline, its worst loss in 42 years.

First Quarter Performance Highlights

- Early January's dramatic Consumer Price Index (CPI) and Producer Price Index (PPI) inflation data and the subsequent spike higher in rates turned our credit-based models more cautious, and on January 31st, we moved from fully risk-on to a 50% equity and 50% cash position. The trade closed out a profitable 18 months long risk-on position in equities, during which we saw the S&P 500 (SPLG) gain 42.1% and small-caps (IJR) 52.7%. Broad international (IXUS) was up 26.4%, while international small-caps (VSS) gained 30.1%. In contrast, the 7-10 year Treasury (IEF) was down 7.2% over the same period.
- Notably, when we turned defensive, we introduced cash equivalents, and not U.S. Treasuries, into the portfolio. The 2-year Treasury yield began 2022 at 0.73%, but by the end of the quarter, it had reached 2.34%, indicating that markets have priced in nine 25 basis point Fed rate hikes over the next two years. While our models are modestly positive towards equities and risk, they decidedly recommend avoiding Treasuries and their duration and interest rate risk. Since our January 31st risk reduction, the S&P 500 (SPLG) is up 0.8%, while broad International stocks are down 3.4%. However, U.S. Treasuries are down even more, declining 4.4%. Cash, and its ability to preserve capital above all else, has proven to be an effective defensive vehicle.
- When our models favor risk-on and stocks, the portfolio allocates 70% to U.S.

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equity and 30% to international equity; for each region, it gives 70% weight to large-caps and 30% to small-caps.

Positioning and Outlook

The Global Tactical portfolio enters risk-on positions when its credit-driven models favor risky assets (equities); it sells equities and moves into Treasuries or cash when the models indicate negative broad credit trends. At the end of January, the portfolio moved to a more modestly defensive position in 50% equities and 50% cash, which reflects the mixed readings in our models and conflicting economic positive and negative factors towards equities. First among the negatives is the hawkish Fed. While interest rates have risen sharply, they remain fairly low in nominal terms, and negative in real terms. Markets perceive that the Fed is behind the curve regarding inflation, though that has begun to lessen as Fed members have become more vocal and hawkish.

Other negatives include consumer sentiment dampened by inflation, historically high valuations that despite having cooled off, present long-term risks, and poor market breadth during the rebound after the March 14th low. The biggest positive is the contrarian economic indicator of investor sentiment. In mid-March, market sentiment reached levels last seen in April 2020, and when those extremes are reached, forward returns 6-12 months out are typically positive.

Bond and interest rate sentiment have also become ex-

treme, and our research shows that when markets build future Fed rate hikes into interest rates, often those rate hikes never fully come to pass. If, as expected, inflation takes a bite out of economic growth, it also could slow expected Fed hawkishness, and we believe that would be a big boost to risk assets. Finally, from a seasonality perspective, while the first half of a mid-term election often brings weakness, the second half of the year is typically much more positive. Taken altogether, we anticipate a more positive factor environment for equities the further that we move into 2022.

The Global Tactical portfolio's philosophy is driven by the belief that we can add value to our clients' portfolios by wisely and opportunistically reducing risk, rather than taking on greater than market risk in order to maximize upside. While valuations have moderated somewhat, at the end of 2021, valuations were only exceeded by 1999 bubble highs. Corporate earnings appear solid for now, though their growth is slowing. At the same time, inversion along many points in the yield curve point have many screaming that a recession is imminent.

While we do not see any signs of a slowdown right now, inverted yield curves usually have a 12 to 18 month lead time before potential trouble. We are somewhere in the later innings of the economic cycle, but we believe 2023 or 2024 will present greater risks of recession and major market declines. The Global Tactical portfolio has been constructed with risk management and capital preservation as primary goals – along with opportunistic risk taking. We remain 50% invested currently, and while the first half of 2022 could deliver more volatility, our forecast has the second half of the year providing more opportunities for gains.

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Non-investment-grade debt securities (high-yield/junk bonds) may be subject to greater market fluctuations, risk of default or loss of income and principal than higher-rated securities.

Foreign securities are more volatile, harder to price and less liquid than U.S. securities. They are subject to different accounting and regulatory standards, and political and economic risks. These risks are enhanced in emerging markets countries.

The Consumer Price Index (CPI) is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services.

The Bloomberg Aggregate Bond Index or "the Agg" is a broad-based fixed-income index used by bond traders and the managers of mutual funds and exchange-traded funds (ETFs) as a benchmark to measure their relative performance.

The Nasdaq-100 is a stock market index made up of 101 equity securities issued by 100 of the largest non-financial companies listed on the Nasdaq stock market.

The Producer Price Index (PPI) program measures the average change over time in the selling prices received by domestic producers for their output.

The S&P 500 measures the performance of the 500 leading companies in leading industries of the U.S. economy, capturing 80% of U.S. equities.

The 2 Year Treasury Rate is the yield received for investing in a US government issued treasury security that has a maturity of 2 years.

The volatility (beta) of a client's portfolio may be greater or less than its respective benchmark. It is not possible to invest in these indices. Index returns include the reinvestment of income and dividends. The returns for these unmanaged indexes do not include any transaction costs, management fees or other costs. It is not possible to make an investment directly in any index.

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