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Q2 2023 Newsletter | Jeff Griggs, CFA

Due to the wide range of risk tolerances of our clients, some topics or asset classes may have more, less, or no importance to your portfolio. For a detailed analysis, give us a call, or request a detailed performance review.

Big Picture

While the collapse of Silicon Valley Bank dominated headlines in the second half of the quarter, the market largely shrugged off the could-be crisis and rose 7% in the first quarter. Like the fourth quarter of 2022, the headline numbers were strong but the dispersion of returns between sectors and factors was massive. The Nasdaq rose 10.5% in January alone, for the best start to a year since 2001. Growth finished the quarter up 17.3% while Value fell -1.2%. Tech was up 22%, Communication Services 21%, and Consumer Discretionary 16%, while the next best sector was materials, up just 4% and Financials (-5.6%), Health Care (-4.3%), Energy (-4.7%), and Utilities (-3.25%) all fell.

The leading narrative throughout the quarter was disinflation, while we saw some positive macro surprises, soft landing expectations rose, and investors speculated that the Fed was close to pausing hikes and the timeline for rate cuts moved up. On March 8th, just two days before the SVB crisis hit headlines, the market was applying a 79% probability of a 50bps raise. That number plummeted to 0% by the following Tuesday. Ultimately, the Fed raised their target rate 25bps, but the futures market is now predicting a pause (54% probability) in May with rate cuts as early as July.

On the Fridge

Developed Market Stocks

Developed market stocks (excluding the US) led all asset classes for the second straight quarter, rising 8.2% vs. 7.7% from their US counterparts.

Information Technology

Tech stocks ended the first quarter up 22%, beating second place Comms. Services (+20.5%), and Consumer Discretionary (+16.1%) and was the top sector of only three that rose more than 4.5%. In fact, four sectors Financials, Healthcare, Energy, and Utilities fell during the quarter.

Looking Ahead

After a rebound in Growth stocks to start the year, and volatility surrounding the SVB bank failure, the market seems to have entered a holding pattern with no clear narrative or trend leading the way. Studying most relative and historical valuation metrics mostly show a stock market that is in the middle of extremes, with the exception of consumer sentiment. Despite reasonable valuations and growth expectations, consumer sentiment is just off a multi-decade low, implying upside potential. What we could be seeing is a proactive Fed Put keeping valuations from dropping to the levels typically associated with recession. Fed fund futures now place a 60% probability of a rate cut in July, a move that would likely be seen as positive for the stock market despite the likelihood that it would coincide with tighter financial conditions and poor economic growth.

While I expect Washington to continue to play political hot potato with the debt ceiling, I do not expect a default. Thus, I expect the drama to cause some volatility, but ultimately have little impact on capital markets. In the meantime, developed market stocks, which have traded below their typical discount to US stocks since 2016 have recently dropped 2 standard deviations below the average suggesting a very rare valuation situation and implying further outperformance potential. Elsewhere, short-term bonds and even money markets are offering yields far beyond what we have seen in over a decade and may present an attractive place to park cash until a more substantial trend has developed in the overall market.

In the Dog House

Floating Rate Bonds

With interest rate expectations reaching peaks, floating rate bonds matched cash, returning just 1.1% in the quarter. That puts the asset class in last place among those we track.

Financials

In the wake of the Silicon Valley Bank failure, financials were understandably the worst performing sector in the first quarter, as they fell –5.6% while the overall US stock market was up 7.7%.

Links and Articles

The False Promise of ChatGPT
Noam Chomsky throws a bit of cold water on the current hype surrounding ChatGPT and AI.

Value: Why Now?
AQR makes a compelling case for further outperformance from the value factor.

Worry About the Right Things
Michael Batnick on the psychology of loss aversion among other behavioral finance lessons.

Stock Pickers Failed to Take Part in Q1 Rally
Vicky Ge Huang of the WSJ illustrates the difficulties stockpickers faced in the first quarter.

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May 2023 Q2 Newsletter

Performance

Developed markets outperformed US equities once again, but the outperformance was far less dramatic than in Q4 with developed markets up 8.2% vs. 7.7% from US equities. When comparing international and domestic investments, the foreign exchange rate can often play a bigger impact than some realize. From the start of Q4 2022, through January of this year, the ICE US dollar index fell –9%, while developed market stocks outperformed US stocks by about 14%. Meaning the currency fluctuation alone accounted for about 65% of the outperformance. Bonds returned 3% in the quarter, with each sub-class performing generally in line with expectations. Emerging markets underperformed their equity peers rising 4% in the quarter, while the strength or lack thereof in the China COVID reopening received quite a bit of chatter. The vast dispersion between sector returns continues to make active investments difficult. The winners and losers from 2022 largely swapped spots to begin the new year, and we're not talking about a small difference. Consumer discretionary is the worst performing sector over the last twelve months (-19.6%), but was up 16% in Q1, more than doubling the overall market. Tech is down -4.6% LTM and rose 22% in Q1. These are drastic swings and show very low correlation between sectors, meaning any deviation from market allocation has the potential to cause a dramatic deviation from market returns.

	Benchmark Index	2023 Q1	YTD	LTM	3yr	5yr	10yr
Cash	**Bloomberg US Treasury Bill 1-3 M TR USD**	1.1%	1.1%	2.6%	2.0%	1.4%	0.8%
Fixed Income	**Bloomberg Global Aggregate TR USD**	3.0%	3.0%	-8.1%	-3.4%	-1.3%	0.1%
Fixed Income Blend	Bloomberg Global Aggregate TR USD	3.0%	3.0%	-8.1%	-3.4%	-1.3%	0.1%
Government	Bloomberg US Government TR USD	3.0%	3.0%	-4.4%	-4.1%	0.8%	0.9%
Inflation Protected	Bloomberg US Treasury US TIPS TR USD	3.3%	3.3%	-6.1%	1.8%	2.9%	1.5%
Municipal	Bloomberg Municipal TR USD	2.8%	2.8%	0.3%	0.4%	2.0%	2.4%
Floating Rate	Bloomberg US Trsy Floating Rate TR USD	1.1%	1.1%	3.1%	1.2%	1.5%	0.0%
Corporate	Bloomberg US Corp Bond TR USD	3.5%	3.5%	-5.6%	-0.5%	1.6%	2.3%
High Yield	Bloomberg US Corporate High Yield TR USD	3.6%	3.6%	-3.3%	5.9%	3.2%	4.1%
International Bond	Bloomberg Gbl Agg Ex USD TR USD	3.1%	3.1%	-10.7%	-4.1%	-3.2%	-1.0%
Equity	**MSCI ACWI GR USD**	7.4%	7.4%	-7.0%	15.9%	7.5%	8.6%
Equity Blend	MSCI ACWI GR USD	7.4%	7.4%	-7.0%	15.9%	7.5%	8.6%
US Equity	MSCI USA GR USD	7.7%	7.7%	-8.5%	18.5%	11.1%	12.2%
Developed Markets	MSCI World ex USA GR USD	8.2%	8.2%	-2.2%	14.1%	4.3%	5.4%
Emerging/Frontier	MSCI EM GR USD	4.0%	4.0%	-10.3%	8.2%	-0.5%	2.4%
Alternatives	**Wilshire Liquid Alternative TR USD**	1.2%	1.2%	-2.7%	4.1%	1.3%	1.3%
Alternatives Blend	Wilshire Liquid Alternative TR USD	1.2%	1.2%	-2.7%	4.1%	1.3%	1.3%

Sector	2023 Q1	6mo	YTD	1yr	3yr	5yr	10yr
Information Technology	21.8%	27.6%	21.8%	-4.6%	24.4%	19.6%	20.1%
Financials	-5.6%	7.3%	-5.6%	-14.2%	18.1%	5.4%	10.3%
Health Care	-4.3%	7.9%	-4.3%	-3.7%	15.4%	11.8%	12.9%
Consumer Discretionary	16.1%	4.3%	16.1%	-19.6%	14.6%	8.7%	12.1%
Consumer Staples	0.8%	13.6%	0.8%	1.2%	14.7%	10.6%	9.6%
Industrials	3.5%	23.4%	3.5%	0.2%	21.7%	8.4%	11.2%
Energy	-4.7%	17.1%	-4.7%	13.6%	48.5%	9.5%	4.4%
Utilities	-3.2%	5.1%	-3.2%	-6.2%	10.3%	9.6%	9.4%
Materials	4.3%	20.0%	4.3%	-6.3%	23.9%	9.6%	9.7%
Communication Services	20.5%	18.8%	20.5%	-17.8%	9.4%	6.4%	5.3%
Real Estate	1.9%	5.8%	1.9%	-19.7%	10.1%	7.4%	7.4%

Source: Morningstar; The 1,3,5, and 10 year performance is annualized.

Disclosures: We cannot offer guarantees or promises that your financial goals and objectives will be met. Past performance is no guarantee of future results. This newsletter is being provided for informational purposes only and should not be considered investment advice, a solicitation of advisory services, or a recommendation to buy or sell any types of securities. No investment decisions should be made solely based on the information in this newsletter. There is a risk of loss when investing in securities, including the risk of loss of principal. Different types of investments involve varying degrees of risk, and there can be no assurance that any specific investment will be profitable or suitable for a particular investor's financial situation or risk tolerance. Asset allocation and portfolio diversification cannot assure or guarantee better performance and cannot eliminate the risk of investment losses. The opinions contained herein reflect Spectrum Strategic Capital's views as of the date of this newsletter and are subject to change without notice. Spectrum Strategic Capital obtained most of the information from third party sources, which are believed to be reliable but are not guaranteed. The links and articles provided in this newsletter are for convenience only and does not imply that Spectrum Strategic endorses, sponsors, or approves the content of the links and articles.

Asset Class	Benchmark	Description
Cash	Bloomberg US Treasury Bill 1-3 M TR USD	Measures US dollar-denominated, fixed-rate, nominal debt issued by the US Treasury.
Fixed Income	Bloomberg Global Aggregate TR USD	The Bloomberg Global Aggregate Index is a flagship measure of global investment grade debt from twenty-four local currency markets. This multi-currency benchmark includes treasury, government-related, corporate and securitized fixed-rate bonds from both developed and emerging market issuers.
Government Bonds	Bloomberg US Government TR USD	The Bloomberg US Government Bond Index comprises the US Treasury and US Agency indices. The index includes US Dollar-denominated, fixed-rate, nominal US Treasuries and US agency debentures (securities issued by US government owned or government sponsored entities, and debt explicitly guaranteed by the US government).
Inflation Protected	Bloomberg US Treasury US TIPS TR USD	The Bloomberg US Treasury Inflation-Linked Bond Index (Series-L) measures the performance of the US Treasury Inflation Protected Securities (TIPS) market.
Municipal	Bloomberg Municipal TR USD	The Bloomberg U.S. Municipal Index covers the USD-denominated long-term tax exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds and prerefunded bonds.
Floating Rate	Bloomberg US Trsy Floating Rate TR USD	The Bloomberg US Treasury Floating Rate Index measures the performance of floating rate bonds issued by the US Treasury.
Corporate Bonds	Bloomberg US Corp Bond TR USD	The Bloomberg US Corporate Bond index measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD-denominated securities publicly issued by US and non-US industrial, utility and financial issuers.
High Yield Bonds	Bloomberg US Corporate High Yield TR USD	The Bloomberg US Corporate High Yield Bond Index measures the USD-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below.
International Bonds	Bloomberg Gbl Agg Ex USD TR USD	The Bloomberg Global Aggregate Index is a flagship measure of global investment grade debt from twenty-four local currency markets. This multi-currency benchmark includes treasury, government-related, corporate and securitized fixed-rate bonds from both developed and emerging market issuers. This version excludes USD-denominated debt.
Equity	MSCI ACWI GR USD	The MSCI ACWI captures large and mid cap representation across 23 Developed Markets and 23 Emerging Markets countries. With 2,477 constituents, the index covers approximately 85% of the global investable equity opportunity set.
US Equity	MSCI USA GR USD	Captures broad US equity coverage. The index includes 3,108 constituents across large, mid, small, and micro capitalizations, representing about 99% of the US equity universe.
Developed Market Equity	MSCI World ex USA GR USD	Captures large and mid cap representation across 22 of 23 Developed Market countries, excluding the United States. With 1,023 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.
Emerging Market Equity	MSCI EM GR USD	The MSCI Emerging Markets Index captures large and mid cap representation across 23 Emerging Markets (EM) countries. With 829 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.
Alternatives	Wilshire Liquid Alternatives TR USD	Measures the collective performance of the five Wilshire Liquid Alternative strategies that make up the Wilshire Liquid Alternative Universe, including the Wilshire Liquid Alternative Equity Hedge, Global Macro, Relative Value, Multi-Strategy, and Event Driven indices. This index is meant to provide a representative baseline for how the liquid alternative investment category performed as a whole. Constituents comprised of '40 Act mutual funds.
US Large Cap Equity	S&P 500	Widely regarded as the best gauge of large-cap US Equities. The S&P 500 is a market-weighted index that includes 500 leading companies and captures approximately 80% coverage of available market capitalization.