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Dear Clients & Friends,

After a minor rally in recent weeks, stock markets have resumed a downward trajectory, falling approximately 9% in the last three trading days and officially pushing the S&P 500 index into a "bear market" – defined as a decline of 20% or more. As we noted in our last update in May, many technology stocks have fallen more sharply than this, with the popular NASDAQ index now more than 30% off its highs. Meanwhile, interest rates have risen sharply: the 10 year Treasury yield now stands above 3.30% and the Bloomberg Aggregate Bond index has fallen 12% for the year.

The catalyst for this renewed selling was Friday's disappointing inflation report. May's Consumer Price Index (CPI) rose to a 40 year high of 8.6%, well above expectations and dashing some observers' hopes that inflation may have peaked. Significant gains in gasoline, groceries, and housing costs helped fuel the increase, and also served as a warning that inflationary pressures are becoming more broad based.

For investors, the persistence in inflation has increased concerns that the Federal Reserve will be forced to more aggressively tighten monetary policy. This is something we have written about extensively in our recent communications: after years of "easy money" policies, our central bank is reversing course by hiking short term interest rates and shrinking its balance sheet. The explicit purpose of these actions is to slow economic growth and undermine rising consumer prices. However, a continuation of reports like the one we saw Friday will require a much more significant policy response that could tip us into a recession. There is now a real chance that the Fed surprises this week with a larger than expected interest rate hike of 0.75%.

How we escape this negative cycle in the short term is, unfortunately, difficult to forecast. Many of the world's current inflationary pressures can be traced to supply chain disruptions caused by the war in Ukraine and the China's Covid-19 lockdowns. Some elements of the CPI figure should recede on its own. Durable goods prices, for example, have fallen three months in a row after surging earlier in the pandemic. The methodology for measuring inflation – comparing today's prices to year ago levels – should also dampen reported figures as we start to measure against higher base prices. However, the longer inflation persists, the more difficult it will be to eradicate as consumer expectations shift.

Markets will likely remain volatile around inflation rhetoric for the foreseeable future. At this stage, we believe the best course of action is to remain patient as we wait for better valuations or for inflation data to stabilize. Stock market valuations are improved, but not yet cheap. At a 16.3x forward price-to-earnings multiple, the S&P 500's valuation is now slightly below its 25 year average of 16.9x. However, those are predicated upon earnings that are more uncertain in the face of a broader economic slowdown. Credit spreads for high yield bonds – one of the primary measures of market sentiment that we follow – have also remained stubbornly low (i.e.,

expensive). We don't believe they have reached levels that signal a significant buying opportunity is here, despite the volatility we have seen thus far this year.

In the interim, we encourage you to maintain a long-term perspective regarding your investments. Your portfolio is diversified and constructed to achieve your objectives commensurate with your time horizon. Our inclusion of non-traditional assets like private credit and private real estate has helped mitigate the impact of stock and bond market volatility, though we acknowledge that has not been enough to prevent overall portfolio losses this year. History is also on your side: stocks have experienced 14 bear markets since World War II; in all but three instances, stock markets were higher one year after surpassing a 20% decline. Ultimately, we believe investors will be rewarded for maintaining discipline and taking advantage of the opportunities that emerge in the quarters ahead.

We are here to speak with your further about your portfolio and financial markets. Please don't hesitate to contact us at your convenience.

Sincerely,

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