Capital Market Review

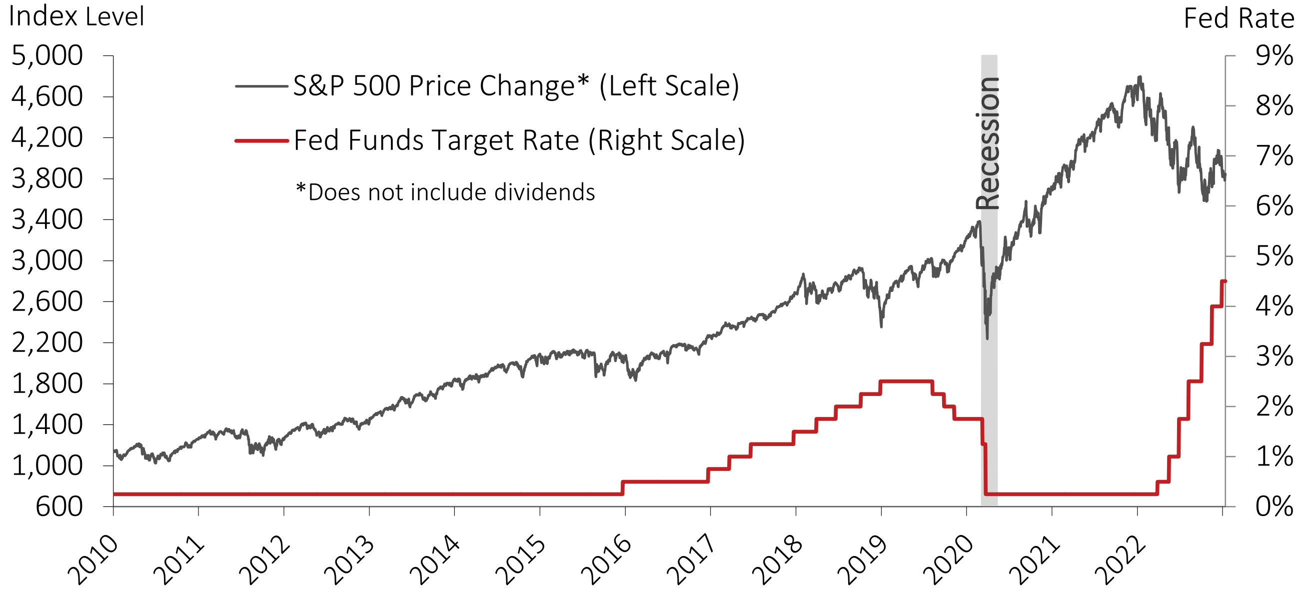
December 31, 2022

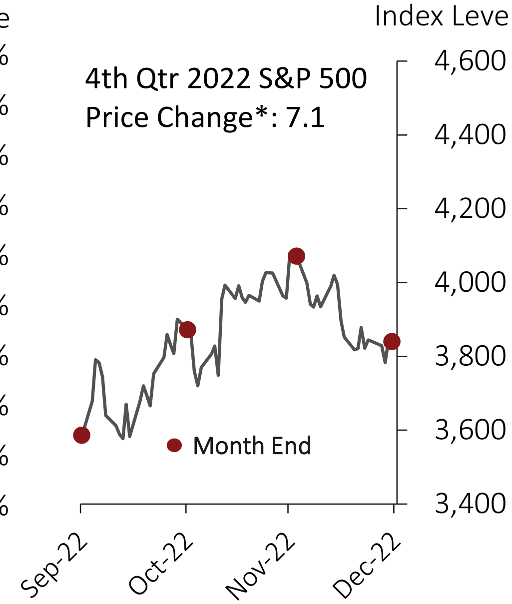



DeMarche

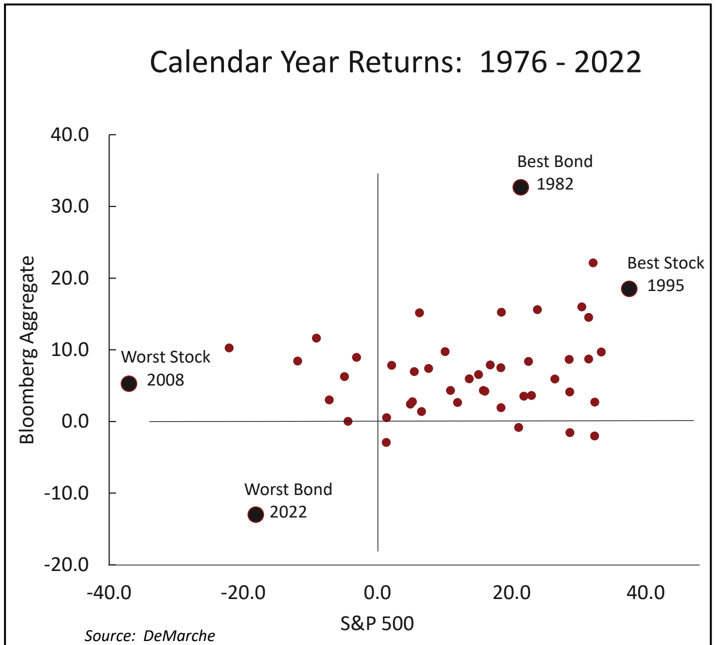
Watch the Capital Markets Review Key Takeaways Video

The Year of Living Dangerously

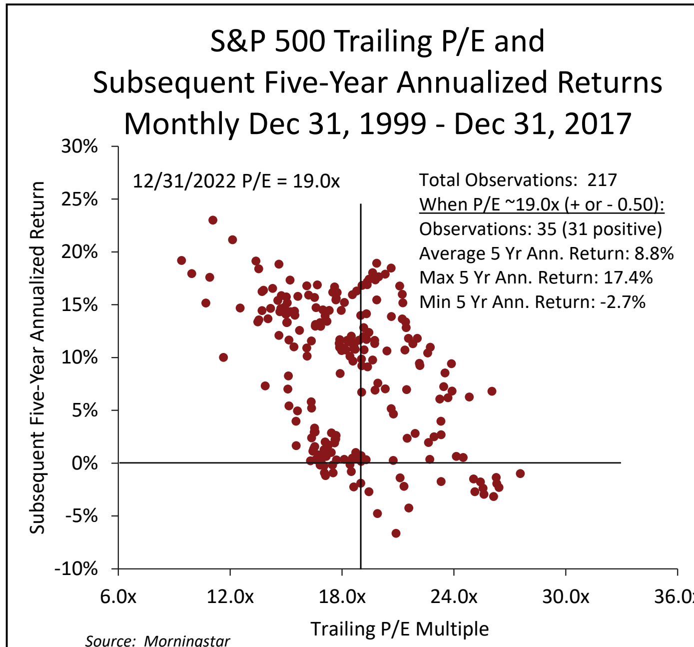




Source: Standard & Poor's, Federal Reserve



2022 was one for the ages. The chart to the left shows that it was the first time since 1976 (the bond index was assembled) that stocks and bonds both had negative returns for the same calendar year. Aggressive Fed interest rate tightening in the face of inflation put pressure on bond prices all along the maturity curve. In addition, higher borrowing costs put downward pressure on stock market multiples. In 2022, the Bloomberg Aggregate returned -13.0% and the S&P 500 returned -18.1%. The chart to the right shows that the 2022 contraction in the P/E ratio of the S&P 500 may bode well for the future returns. The P/E Ratio of the S&P 500 was 19x at the end of 2022; it was 25.2x at the end of 2021. Of the 35 five year return observations of the S&P 500, when stocks were priced near 19x, 31 were positive. The average return of the 35 observations is 8.8%.

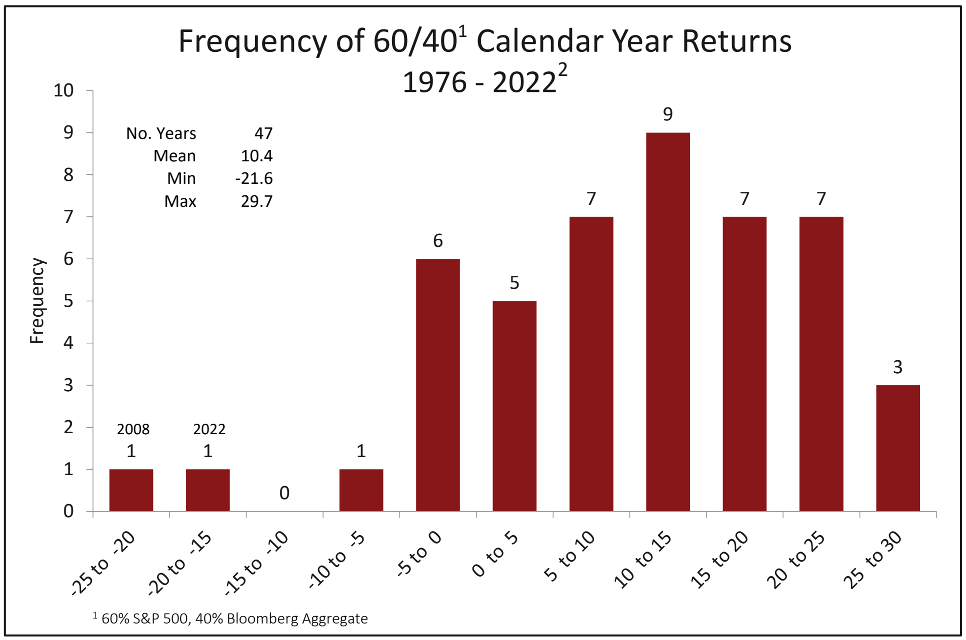


INDEX	4th Qtr	1-YEAR	3-YEAR	5-YEAR	10-YEAR
MSCI World	9.8	-18.1	4.9	6.1	8.9
Russell 3000	7.2	-19.2	7.1	8.8	12.1
S&P 500	7.6	-18.1	7.7	9.4	12.6
MSCI EAFE USD	17.3	-14.5	0.9	1.5	4.7
MSCI Emerging Markets USD	9.7	-20.1	-2.7	-1.4	1.4
Bloomberg Aggregate	1.9	-13.0	-2.7	0.0	1.1
Bloomberg Global Aggregate	4.5	-16.2	-4.5	-1.7	-0.4
FTSE Non-US Gov't Bond	6.5	-22.1	-8.0	-4.2	-2.3
NAREIT (Public RE)	4.5	-25.1	-0.5	3.9	6.9
Bloomberg Commodity	2.2	16.1	12.7	6.4	-1.3

Notes: Data are presented as percent returns. All 3-, 5-, and 10-year returns are annualized.

U.S. Indicators Yr Ending 12/31	2022	2021	2020	2019	50 Yr Average
GDP Annual Growth Rate*	1.7	5.7	-1.5	2.6	2.7
Unemployment	3.5	3.9	6.7	3.5	6.2
Inflation (CPI)	6.5	7.0	1.4	2.3	4.0
10-Year Interest Rates	3.9	1.5	0.9	1.9	6.0

**Note: Prior to the GDP quarterly release from BEA, we show the annual GDP Growth rate from OECD weekly tracker as the most recent year.*



[2]The Bloomberg Aggregate Bond Index had 10 years of backfilled historical data (1976 – 1985) when it was introduced in Jan 1986.

- Bonds, as measured by the Bloomberg Aggregate, posted a negative 13% return for 2022. This return is the worst annual bond return in 47 years of available index data[2]. To combat inflation, the Federal Reserve aggressively hiked interest rates during the year. The Fed Funds rate was 0 - 25 basis points at the beginning of the year and ended the year within the range of 425 - 450 basis points.

- Stocks also had a wild ride in 2022. The battle against inflation punished growth stocks primarily, but the decimation was wide ranging. Domestic large cap stocks, as measured by the S&P 500, experienced their first negative year since 2018 and its worst year since 2008. The index did rebound in the 4th quarter, gaining 7.6% from a negative 24% year-to-date at the end of the third quarter.

- International stocks also were pummeled in 2022. Developed and emerging market stocks were double whammied by a strong dollar and rising interest rates for the first three quarters of 2022. However, international markets did do better in the 4th quarter as the dollar weakened relative to other currencies. This stronger quarter helped pull the MSCI EAFE ahead of the S&P 500 for the year, -14.5% to -18.1%, respectively.

- The trusty 60/40 portfolio of equities and bonds had a negative return for the first time since 2008. And only in 2008 did the portfolio perform this poorly. An event this extreme is a rare occurrence. The histogram to the left shows that the blend of S&P 500 and the Bloomberg Aggregate has only been negative 9 times since the inception of the bond index and six of the nine times the portfolio was negative, it was between -5% and 0%.

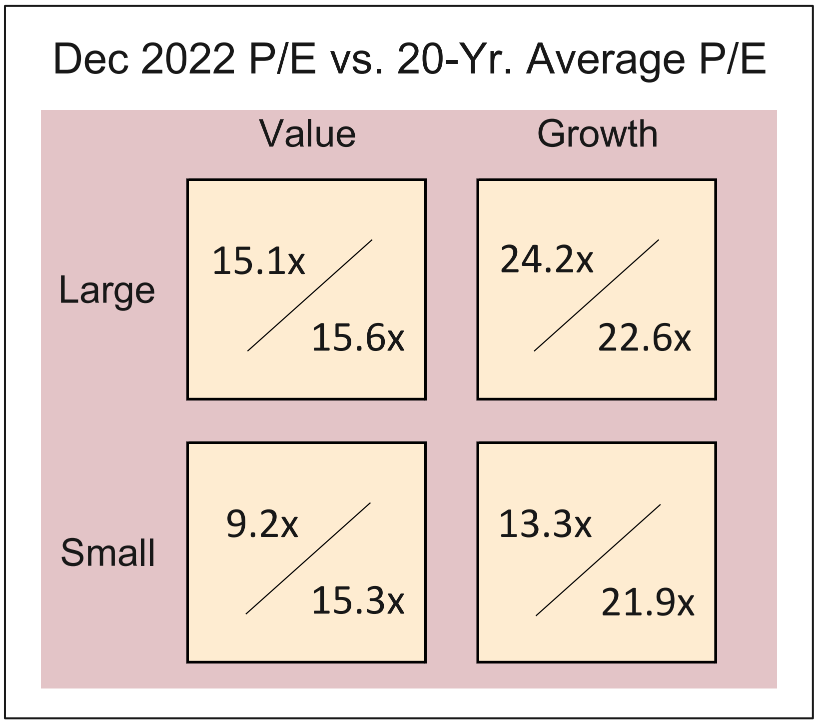
DeFact

By the end of 2022, global inflation had wiped out the last negative yielding bond with a maturity date of more than one year. The Japanese 2-year government peaked just above zero. There are now no negative yielding bonds for the first time since 2014. The amount of negative yielding bonds peaked at $18.4 trillion in December 2020. ~Bloomberg, MarketWatch

Domestic Equities

INDEX	4th Qtr	1-YEAR	3-YEAR	5-YEAR	10-YEAR
S&P 500	7.6	-18.1	7.7	9.4	12.6
S&P Mid-Cap 400	10.8	-13.1	7.2	6.7	10.8
S&P Small-Cap 600	9.2	-16.1	5.8	5.9	10.8
Russell 1000	7.2	-19.1	7.3	9.1	12.4
Russell 1000 Growth	2.2	-29.1	7.8	11.0	14.1
Russell 1000 Value	12.4	-7.5	6.0	6.7	10.3
Russell 2000	6.2	-20.4	3.1	4.1	9.0
Russell 2000 Growth	4.1	-26.4	0.6	3.5	9.2
Russell 2000 Value	8.4	-14.5	4.7	4.1	8.5

Notes: Data are presented as percent returns. All 3-, 5-, and 10-year returns are annualized.



Source: Morningstar – Russell 1000 and Russell 2000 quarterly P/E history

- Growth stocks were the primary recipient of the pain of increasing interest rates in 2022. Large cap growth stocks are dominated by tech and the other mega cap stocks that had been winners for the past decade. Google was down over 38%; Amazon was down over 50%; Meta was down over 65%: Tesla was down over 65%. Tech made up 46.1% of the growth index at year end 2021; it has now decreased to 43.2% of the index.

- Value stocks, unloved for a decade, proved to be resilient in 2022 and had a positive 4th quarter return of 12.4%. Over the year, large cap value stocks fell 7.5%. Energy stocks were up over 65% for the calendar year and now make up 8.4% (up from 5.1% at year-end 2021) of the value index. Energy was the primary driver of value outperformance to growth stocks for the year.

- Small cap stocks traditionally bear the brunt of a slowing economy and rising rates; this year was no exception. Small cap stocks, as measured by the Russell 2000 index, fell 20.4% for the year. We did see a rebound in October and November 2022 for small cap stocks which propelled small caps to a positive return for the quarter.

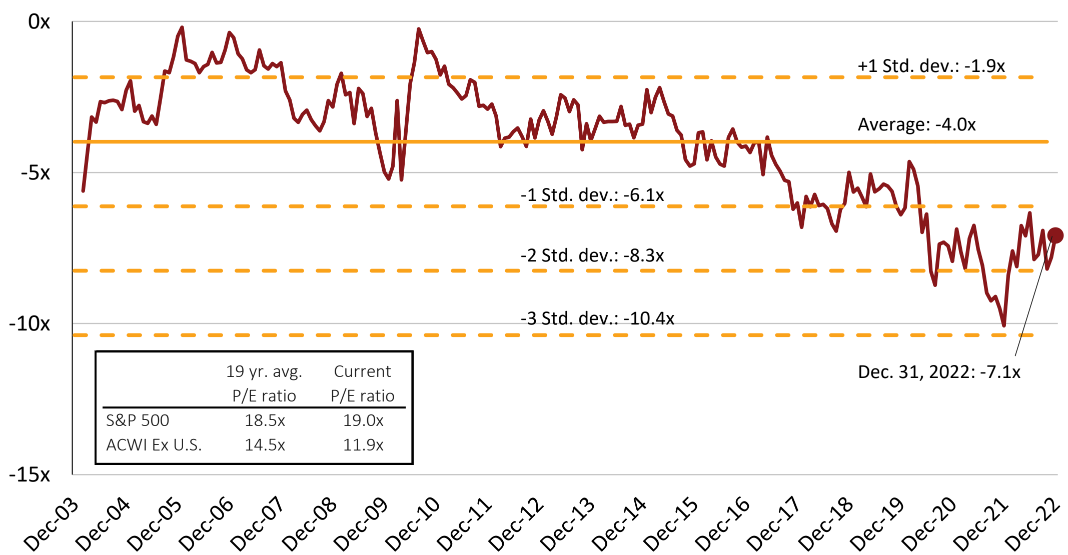
- Despite the pullback in stock prices in the face of inflation and higher rates, it appears stocks have not become extremely "cheap" but under-to-fairly valued relative to history depending on the cap size. It seems large growth stocks may still have some repricing to do as the chart to the left shows that they still have a higher P/E multiple than their 20 year average. Small cap sectors appear inexpensive.

DeFact

With stocks taking it on the chin in 2022, it is not surprising that IPO activity dried up. IPO deal proceeds plummeted 94% in 2022 from $155.8 billion to $8.6 billion according to a mid-December report by Ernst and Young. No single tech deal raised $1 billion in 2022 after 15 IPOs raised at least that much in 2021. ~CNBC

INDEX	4th Qtr	1-YEAR	3-YEAR	5-YEAR	10-YEAR
MSCI EAFE Local	8.7	-7.0	3.6	3.8	7.6
MSCI EAFE USD	17.3	-14.5	0.9	1.5	4.7
Growth	15.0	-22.9	0.5	2.5	5.6
Value	19.6	-5.6	0.6	0.2	3.5
MSCI All Country-ex US	14.3	-16.0	0.1	0.9	3.8
MSCI AC Asia-ex Japan	11.4	-19.7	-1.5	-0.6	3.6
MSCI Emerging Markets	9.7	-20.1	-2.7	-1.4	1.4
MSCI EAFE Small Cap	15.8	-21.4	-0.9	0.0	6.2
MSCI Japan	13.2	-16.6	-1.0	0.2	5.6
MSCI China	13.5	-21.9	-7.5	-4.5	2.4
MSCI Germany	24.6	-22.3	-3.0	-3.0	2.7
MSCI France	22.2	-13.3	2.5	3.4	6.1
MSCI UK	17.0	-4.8	0.3	1.0	3.1

Notes: Data are presented as percent returns. All 3-, 5-, and 10-year returns are annualized.



	19 yr. avg. P/E ratio	Current P/E ratio
S&P 500	18.5x	19.0x
ACWI Ex U.S.	14.5x	11.9x

Source: Morningstar, DeMarche

- International stocks also were battered during the year. However, since overseas stocks have underperformed domestic stocks over the past decade due to slower economic growth, a strong dollar, war and higher energy prices, the indexes had already priced in a fair amount of bad news. In the 4th quarter, the dollar reversed itself and weakened, providing a tailwind to international stocks in the 4th quarter.
- Emerging markets were primarily held down by the China stock market (32.6% weight in the index). Chinese stocks did better in the 4th quarter as COVID restrictions eased. The response to COVID by the Chinese government, and its crackdown on certain industries has weighed on economic growth and created uncertainty. Chinese stocks were down about 22% for the year. Commodity based emerging market countries, such as Brazil (up 14.2%) and Mexico (down 2.0%), performed relatively well for the year.
- The chart to the left suggest that international and emerging market stocks are still "cheap" relative to the US stocks despite some outperformance of developed international stocks in 2022. ACWI xUS index (all country world minus US) is posting a P/E ratio (11.9 times) below its long term average (14.5 times). There are a few reasons for this long term underperformance; primarily slower economic growth, less vibrant technology sector, a stronger dollar and war. Lastly China's COVID response significantly curtailed economic growth in that country.

DeFact

The US dollar index appreciated over 12% in 2022, hitting a two decade high in September 2022 versus a trade weighted basket of currencies. In response central banks around the world conducted rate hikes and foreign exchange interventions to boost local currencies. When the dollar strengthens to other currencies, goods denominated in dollars become more expensive for foreign consumers to purchase, for example, oil. ~DeMarche

INDEX	4th Qtr	1-YEAR	3-YEAR	5-YEAR	10-YEAR
Bloomberg Aggregate	1.9	-13.0	-2.7	0.0	1.1
Bloomberg 1-3 Gov Credit	0.9	-3.7	-0.3	0.9	0.9
Bloomberg Gov Credit Long	2.6	-27.1	-6.2	-1.2	1.6
Bloomberg US TIPS	2.0	-11.8	1.2	2.1	1.1
ICE BofA Merrill Lynch High Yield	4.1	-11.1	-0.2	2.1	3.9
CSFB Leveraged Loan (bank loans)	2.3	-1.1	2.3	3.2	3.8
Bloomberg Global Aggregate	4.5	-16.2	-4.5	-1.7	-0.4
JPM EmgMkt Bd Glbl Dvrsfd (hard)	8.1	-17.8	-5.3	-1.3	1.6

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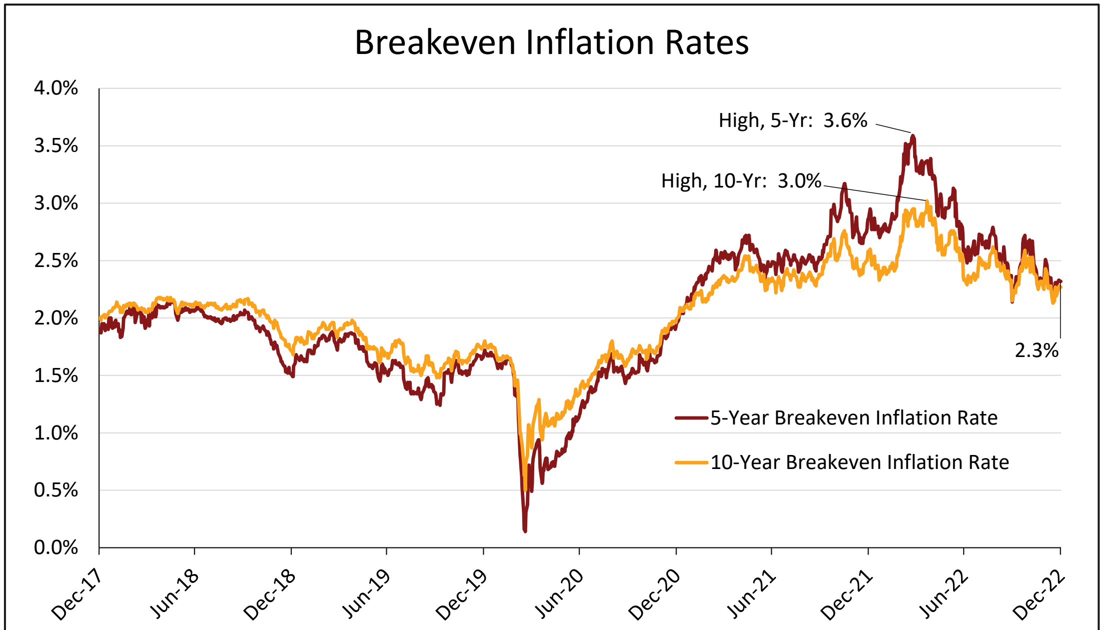


Source: Federal Reserve of St. Louis (FRED)

- As we already stated, the increase in interest rates puts downward pressure on bond prices. The Aggregate posted the worst annual return since the creation of the index. It could have been worse, but rates at the longer end of the maturity curve fell slightly in the quarter. In this new interest rate regime, it is possible for an investment grade bond allocation to provide a coupon return of anywhere between 4% and 5.5% depending on the credit rating of the issuer of the bond.

- High yield bonds also had negative annual returns but outperformed the higher quality Aggregate index. This outperformance is due to two factors; a shorter duration for the High Yield index and a higher starting coupon. Coupon income provides positive attribution to total return and helps cushion price volatility. In this current environment, current coupon on the high yield index can approximate 9%.

- Back in March, just as the Fed starting raising rates, the five- and ten-year implied inflation rates were either at their peak or near their peaks. As the Fed became more aggressive during 2022, the market expectation for future inflation continued to fall. That aggressive rate increase was the driver of historically bad bond market performance.

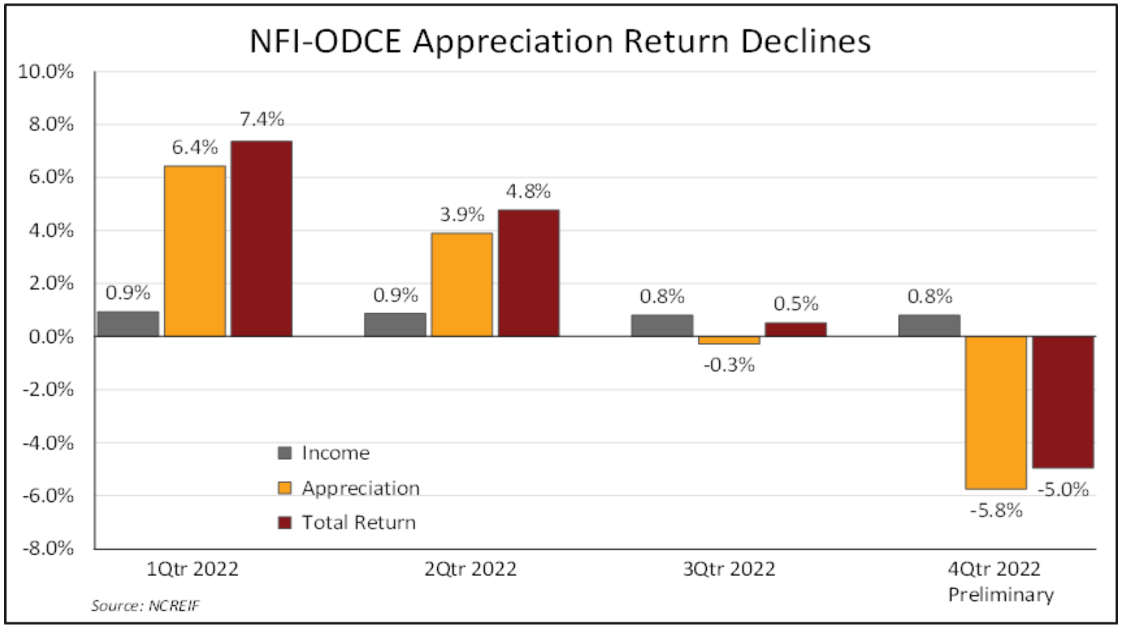
DeFact

Bonds have not been this attractive since 2008, in terms of current yield. We have talked about how strange this year was for the bond market. Here is another bit of trivia: 2021 and 2022 were the first back to back years of negative Bloomberg Aggregate total return performance in the history of the index. So not only was 2022 historically bad, it followed a bad 2021. The Bloomberg Aggregate index was created in 1986 with data backfilled to January 1976.

Less Liquid Strategies – Lagged One Qtr

INDEX	Qtr	1-YEAR	3-YEAR	5-YEAR	10-YEAR
NCREIF ODCE	4.8	29.5	12.7	10.5	11.2
NCREIF Property (Private RE)	3.2	21.5	10.2	8.9	9.7
Apartment	3.9	24.4	11.1	9.1	9.4
Industrial	5.9	47.7	26.0	21.1	16.9
Office	0.6	5.8	4.4	5.3	7.4
Retail	1.7	7.9	0.2	1.4	6.4
NCREIF Timberland	1.9	12.0	5.0	4.3	5.7
NCREIF Farmland	1.5	9.7	6.1	6.1	9.5
HFR FOF Composite	-3.9	-5.5	3.9	3.6	3.7
Conservative	-1.7	0.1	4.6	4.0	3.8
Diversified	-3.1	-3.3	4.4	4.1	3.9
Strategic	-6.8	-11.9	3.1	3.0	3.8
Preqin Private Equity	-2.5	3.5	20.6	17.4	15.7
Preqin Private Debt	-1.0	4.5	9.4	8.0	8.8
Preqin Infrastructure	4.9	20.0	13.2	12.2	11.2

Notes: Data are presented as percent returns. All 3-, 5-, and 10-year returns are annualized.
All data in the table above are as of 9/30



- Commodity price movements often foreshadow inflation as commodities are inputs into the price of goods and services. Commodity prices fell in the past two quarters, primarily due to relief in crude oil and industrial metals prices. Over the past years, energy (oil and natural gas) were major contributors to the increase in commodity prices as together, they make up about 28% of the Bloomberg Commodity index.

- Real estate continues to be a diversifier to portfolios this year and is proving to be a good inflation hedge. As we continue to see, the industrial sector of real estate has posted strong one year and longer term returns.

- Hedge funds over the past year have provided downside protection to stock and bond portfolios. Hedge funds with a strategic bias performed the worst due to the directional aspect of the investment strategies they employ. The most conservative oriented strategies performed the best.

- The chart to the left shows a 2022 preliminary estimate from NCREIF for real estate returns (ODCE). The graph tells us that the increase in interest rates have had a negative impact upon the appreciation of real estate. After three great quarters of real estate returns providing a boost to portfolios, the Fed’s rate raises have finally caught up.

DeFact

Private real estate has seen a divergence in returns across different sector types. One of the sectors, office space, a driver of longer term returns pre-pandemic, has seen vacancy rates in 2022 reach a record 19.1% across the country. While some office workers are back in the office, attendance is below pre-pandemic levels due to the work from home trend. Additionally, weakness in the tech sector has led to layoffs. ~NYT, JLL

Upcoming DeMarche Events

Top Golf with DeMarche *Register at:* https://cvent.me/x8D333

January 26, 12:00 - 3:00 PM
Topgolf Houston - Spring

March 16,12:00 - 3:00 PM
Topgolf Nashville

April 26, 12:00 - 3:00 PM
Topgolf Dallas – The Colony

May 3, 12:00 - 3:00 PM
Topgolf Omaha

May 10, 12:00 - 3:00 PM
Topgolf St. Louis - Chesterfield

Market Outlook Luncheons *Register at:* https://cvent.me/kKbdyQ

Feb. 15, 11:30 AM - 1:00 PM
Del Frisco's Grille

Feb. 16, 11:30 AM - 1:00 PM
The Capital Grille

Feb. 22, 11:30 AM - 1:00 PM
Smith & Wollensky

International Women's Day Luncheon *Register at:* https://cvent.me/NvNBBv

March 8, 11:30 AM - 1:00 PM
Seasons 52