Investment Tally & Perspective

MAJOR ASSET CLASS RETURNS	4th Qtr. 2022	1-Year	3-Year	5-Year
Equities				
S&P 500	7.6%	-18.1%	7.7%	9.4%
MSCI EAFE	17.3%	-14.5%	0.9%	1.5%
MSCI Emerging Markets	9.7%	-20.1%	-2.7%	-1.4%
Fixed Income				
Bloomberg US Aggregate	1.9%	-13.0%	-2.7%	0.0%
Bloomberg US Corp. Inv. Grade	3.6%	-15.8%	-2.9%	0.5%
Bloomberg Emerging Market	6.6%	-15.3%	-3.9%	-0.4%
Other Assets				
MSCI US Reit Index	5.2%	-24.5%	-0.1%	3.7%
S&P GSCI	3.4%	26.0%	10.5%	6.5%
ICE WTI Crude Oil	2.0%	6.7%	9.5%	5.8%
Comex Gold	9.2%	-0.1%	6.3%	6.8%

Source: Capital IQ — All returns greater than one year are annualized

Market Activity - The S&P 500 was able to post gains in the fourth quarter, as equities reacted favorably to signs of easing inflation. For the full year, the index declined 18.1% on a total return basis, posting its worst performance since 2008. International equities performed similarly for the full year, while outperforming in the fourth quarter mainly due to a softening U.S. Dollar.

The positive correlation seen between bond prices and stock prices, an anomaly for the post dot com era, persisted in Q4. Falling inflation expectations and weaker expected growth caused longer dated yields to drop as bond prices rose.

Economic Activity - The U.S. economy, as measured by GDP, continues to perform well. In fact, after slowing in the first half of 2022, the third and fourth quarters exhibited acceleration. When stripping out volatile net exports and changes in private inventories, GDP should be exiting the fourth quarter above 2% (per the Atlanta Fed GDP Now model). This is being driven by growth in personal consumption expenditures, which represents the bulk of the U.S. economy. Importantly, these figures are all adjusted for inflation.

GDP is a lagging indicator, which limits its usefulness as a real-time read on the economy. Many consider the Institute for Supply Management's purchasing managers index to be a better real-time barometer. Here, the picture is not as bright. The services index dropped into contraction territory in December for the first time in 30 months, while the manufacturing index also registered a contraction during the month.

In addition to the weak ISM surveys, other coincident or leading indicators

LINCOLN CAPITAL

Volume 32, Issue 1 January 2023

Our 33rd Year as a Registered Investment Advisor (RIA) Providing Fiduciary Asset Management and Financial Planning Services

Ronald E. Albert, CFP

Brittany A. Moran, CFP

Sean McGuirk, CFA

Alexander Albert, CFP

Nina Walsh

Karen Jones Ariosta

Lincoln Capital Corp.
620 Main Street, CU 2
East Greenwich
Rhode Island, 02818
401.454.3040 (phone)
info@lincolncapitalcorp.com
lincolncapitalcorp.com

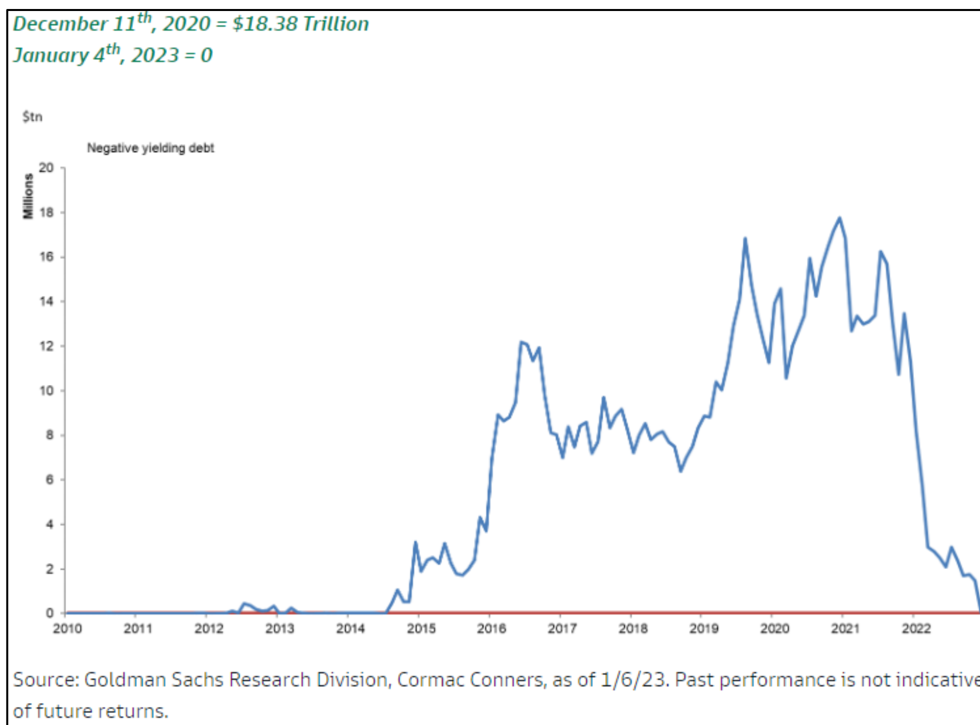
like the Conference Board Leading Economic Index and the shape of the yield curve continue to point to an impending growth slowdown.

While the most important variable in 2022 was inflation, we believe changes in the labor market should be the center of attention for 2023. Major components of core inflation – goods and housing – are, or soon will be, exhibiting low price increases or even declines. Inflation in these categories should continue to improve as we move through 2023. The last remaining piece of the inflation puzzle is services inflation, and here, work remains.

The Fed is intent on slowing the economy enough to restore balance in the labor market—meaning lower demand for labor. While not getting tighter, the labor market has yet to see material relief. Unemployment claims, net payroll growth and job openings, while showing some progress from the early months of 2022, are still pointing to large imbalances.

Monetary Policy – As mentioned in the section above, we do not expect the Fed to relent on slowing demand until the labor market shows balance. Today, the Fed's policy is in restrictive territory, meaning they are actively slowing the economy by increasing the cost of money. The Federal Open Market Committee expects long-run Fed Funds equilibrium to be close to 2.5%. The real (inflation adjusted) Fed Funds rate, as measured using 1-year breakeven inflation in the TIPs market, is now at 2.55%. These measures of restrictiveness suggest that the current Fed Funds rate target of 4.25% – 4.50% is actively slowing the economy.

Going forward, the market still anticipates the Fed will raise rates to about 5% by April, and then to begin cutting rates as Fall approaches. The Fed, according to their own projections, sees the Fed Funds rate rising above 5% and staying at that level through the end of the year.



Source: Goldman Sachs Research Division, Cormac Conners, as of 1/6/23. Past performance is not indicative of future returns.

Globally, central banks are still tightening, though, like the Fed, some are slowing down their pace. Fighting inflation and depreciating currencies will likely drive non-U.S. central bank decisions in 2023, though deteriorating growth will likely gain prominence in their calculations throughout the year.

Today's central bank policies have closed the chapter on negative yielding debt (seen to the right). Whether that chapter stays closed will likely depend on the severity of the impending slowdown.

Valuation & Sentiment – The S&P 500's price-to-forward earnings ratio stands at 16.7x, which is in line with its 10- year average. Current consensus expectations are for earnings to grow just under 5% in 2023, which is a marked improvement from the expected decline in Q4 2022 earnings. Many believe that 2023 estimates will continue to decline and potentially exhibit negative growth if we enter a recession. So, while the P/E multiple's level typically would indicate reasonable equity valuations, it is less informative today given the uncertain earnings outlook.

LINCOLN CAPITAL – INVESTMENT OUTLOOK & STRATEGY

Before delving into our views and expectations, a brief primer addresses the question, "What are the Fed mandates"? From a Fed publication: **"The Federal Reserve Act mandates that the Federal Reserve conduct monetary policy "so as to promote effectively the goals of maximum employment, stable prices, and moderate long-term interest rates." Even though the act lists three distinct goals of monetary policy, the Fed's mandate for monetary policy is commonly known as the dual mandate."**

In 2022, declining values in virtually all asset classes – bonds, stocks, and real estate – were primarily caused by the Fed and other central banks. After previously viewing inflationary pressures as "temporary", the Fed took its foot off the gas pedal and slammed on the brakes when it became evident that inflationary pressures were not abating as expected. The pandemic and supply disruptions caused prices to rise and labor participation to decline, then more fuel was added to the fire by energy prices surging (pun intended) in response to the Russian-Ukraine developments.

While the above facts and history are of interest, the main question is, "Where do we go from here?" Though we cannot accurately predict the future, our knowledge and experience lead us to the following observations and expectations.

We sense inflationary pressures will reach the target levels of the Fed by the end of the year, yet we do not know if the Fed will make a mistake by being overly restrictive, which would put the economy in recession. If a recession develops, then it is likely to be relatively mild as the imbalances evident in past recessions are not currently present.

Assets repricing to higher interest rates was discomforting and painful, yet it was necessary and inevitable if we want a healthy economy. While it was laudable that the Fed and federal government supplied trillions of dollars to the economy and financial markets in response to the pandemic, excessive stimulus has a way of inflating asset values and causing bubbles. The demise of cryptocurrencies (FTX), SPACs, and deflated values of stocks without earnings are healthy developments as they purge speculation and correct the misallocation of investment capital.

We welcome higher interest rates as they are a vivid indication that things are normalizing. Now savers and investors can earn meaningful returns on bonds and bank CD's. Interest rates that were near zero or negative were manifestations of economies on life support—not a desirable situation.

Stocks now trade at reasonable and attractive valuations providing buying opportunities for long-term, patient investors. Importantly, our view is that the environment has changed from being a "Stock Market" to a "Market of Stocks". Stated differently, we envision a sea change that favors individual security selection over market indices (index funds).

Whether we experience a recession or not, whether the stock market rises or declines in the next few weeks or months, from current levels fixed income securities and common stocks are priced to provide competitive returns in the years ahead.

DISCLOSURES - This presentation is not an offer or a solicitation to buy or sell securities. The information contained in this presentation has been compiled from third party sources and is believed to be dependable; however, its accuracy is not guaranteed and should not be relied upon in any way, whatsoever. This presentation may not be construed as investment advice and does not give investment recommendations. Any opinion included in this report constitutes the judgment of Lincoln Capital Corporation as of the date of this report and are subject to change without notice. Additional information, including management fees and expenses, is provided on Lincoln Capital Corporation's Form ADV Part 2. As with any investment strategy, there is potential for profit as well as the possibility of loss. Lincoln Capital Corporation does not guarantee any minimum level of investment performance or the success of any portfolio or investment strategy. All investments involve risk (the amount of which may vary significantly) and investment recommendations will not always be profitable. The investment return and principal value of an investment will fluctuate so that an investor's portfolio may be worth more or less than its original cost at any given time. The underlying holdings of any presented portfolio are not federally or FDIC-insured and are not deposits or obligations of, or guaranteed by, any financial institution. Past performance is not a guarantee of future results. Lincoln Capital Corporation prepare presentation, 401.454.3040, www.lincolncapitalcorp.com Copyright © 2023, by Lincoln Capital Corporation.