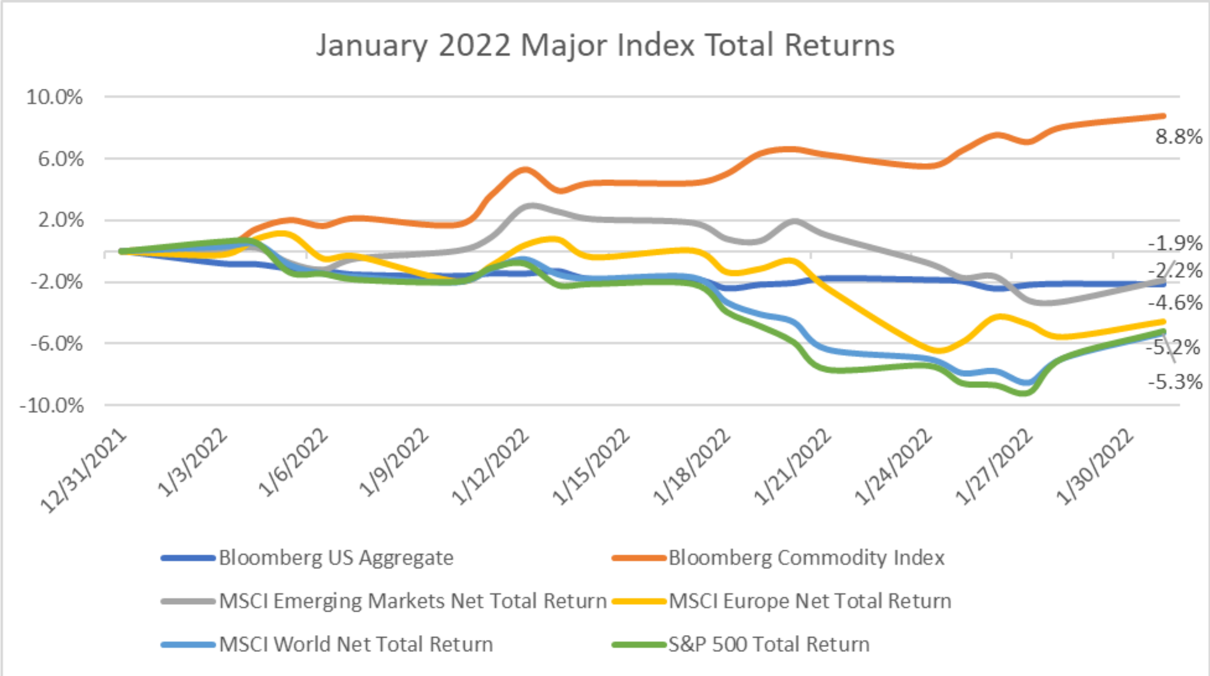
ENCORE INVESTMENT ADVISORS

JANUARY 2022 MARKET REVIEW

Market Recap: Following a strong fourth quarter to end 2021, global markets struggled in January as investors grappled with the reality of higher interest rates and a reemergence of geopolitical tensions. Global equities fell 5% in January, dragged down by US companies, as markets swung wildly, not just daily but also on an hourly basis. Equity market corrections, like we have recently experienced, occur on average every 18 months, far more often than conventional thinking. Typically, market corrections, while nerve racking in the moment, can provide a healthy dose of reality and rein in pockets of frothy investor behavior. We suspect that the main drivers of this volatility are the increase in treasury yields, persistent virus uncertainties, and what appears to be impending military action in Ukraine and Russia. We will focus the conversation on higher rates and the subsequent impact on our client portfolios.

Since the end of 2021, treasury yields have jumped higher throughout the yield curve – shorter maturities have actually seen larger increases in rates relative to longer maturities. So far this year, the five-year treasury has increased 36 basis points and the 10-year treasury has increased 27 basis points, while the 30-year treasury has only increased 21 basis points. The market seems to be frontrunning any central bank action, pricing in a series of rate hikes in 2022. Several weeks ago, Fed Chairman Powell discussed aggressive plans to increase short term rates and reduce the size of the central bank's balance sheet. While some market participants were surprised by the hawkish tone in the face of equity market volatility, the bond market has not shown the same nervousness as equities have. Calming the equity market volatility is not a part of the Fed's dual mandate (maximum employment and stable inflation), even if it has appeared to factor into the Fed's thinking over recent years.

How does this impact our perspective? Higher yields most directly hurt bond prices, but they also have an impact on equity valuations. For portfolios that hold bonds, we have protected capital by holding more shorter duration securities than the benchmark, which has proven to work well. On the equity side, higher interest rates hurt hyper-growth companies with expected earnings projected far out into the future. As such, our portfolios are tilted towards more value or cyclical based companies. This has also continued to push us into international markets, given the sector composition relative to the US. The recent bout of equity volatility has brought about select opportunities that we are taking advantage of. We are not necessarily trying to time market troughs, but we have put excess cash to work over the past several weeks for certain clients. Finally, one of the indicators that we are watching closely is the flattening yield curve, discussed above. The shape of the US yield curve has been a solid indicator of whether there will be trouble on the horizon; our alarms are not sounding yet, but we continue to closely monitor this.



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