MONTH IN REVIEW

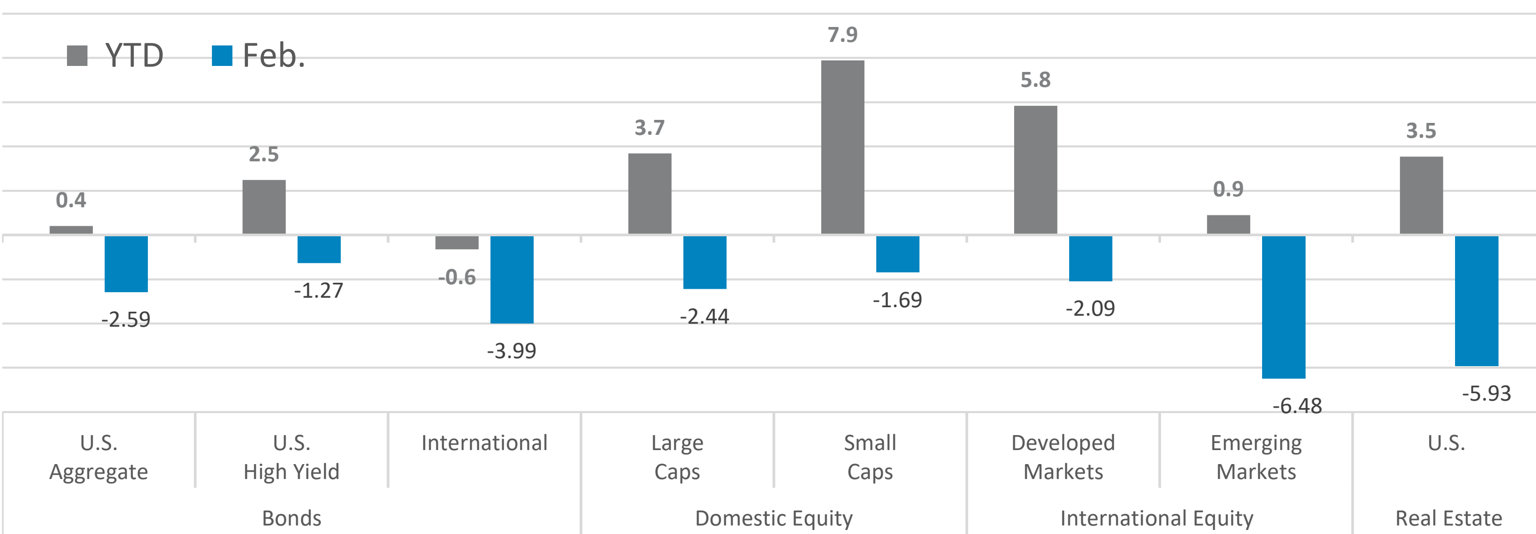
February 2023

Quick Takes

- **Risk Assets Stumble.** Risk assets lost steam in February with a majority posting a negative month, but most are still in positive territory for the year thus far.
- **Fed Raises Rates Again.** The Fed implemented yet another rate hike in the month of February, but they bucked their recent trend and only raised by 25bps. While the hike was more in line with historical raises, the rhetoric from members for the month hinted that further rate hikes will be necessary in the coming months and will likely keep rates “higher for longer”.
- **Greenback Resumes Grind Higher.** On the back of the increase in interest rates and maybe even more impactful, the Fed members’ rhetoric sent the dollar higher versus other major currencies, which negatively impacted international assets, especially emerging markets.
- **Labor Markets and Inflation.** For the February reading, Unemployment fell to a 53-year record low of 3.4% and several inflation metrics came in higher than expected, with previous readings being revised upward as well. This led to a downward revision in economic production from the final quarter of last year.

Asset Class Performance

Market participants went risk off on the back of the Fed’s increase in interest rates and guidance that more rate hikes will likely be necessary in the coming months. Most major asset classes were negative for the month with Emerging Market equities leading the drawdown on the back of a stronger dollar for the month.



Source: Bloomberg, as of December 31, 2021. Asset-class performance is presented by using total returns for an index proxy that best represents the respective broad asset class. U.S. Bonds (Barclays U.S. Aggregate Bond TR), U.S. High Yield (Barclays U.S. HY 2% Issuer-Capped TR), International Bonds (Barclays Global Aggregate ex USD TR), Large Caps (S&P 500 TR), Small Caps (Russell 2000 TR), Developed Markets (MSCI EAFE NR USD), Emerging Markets (MSCI EM NR USD), Real Estate (FTSE NAREIT All Equity REITS TR).

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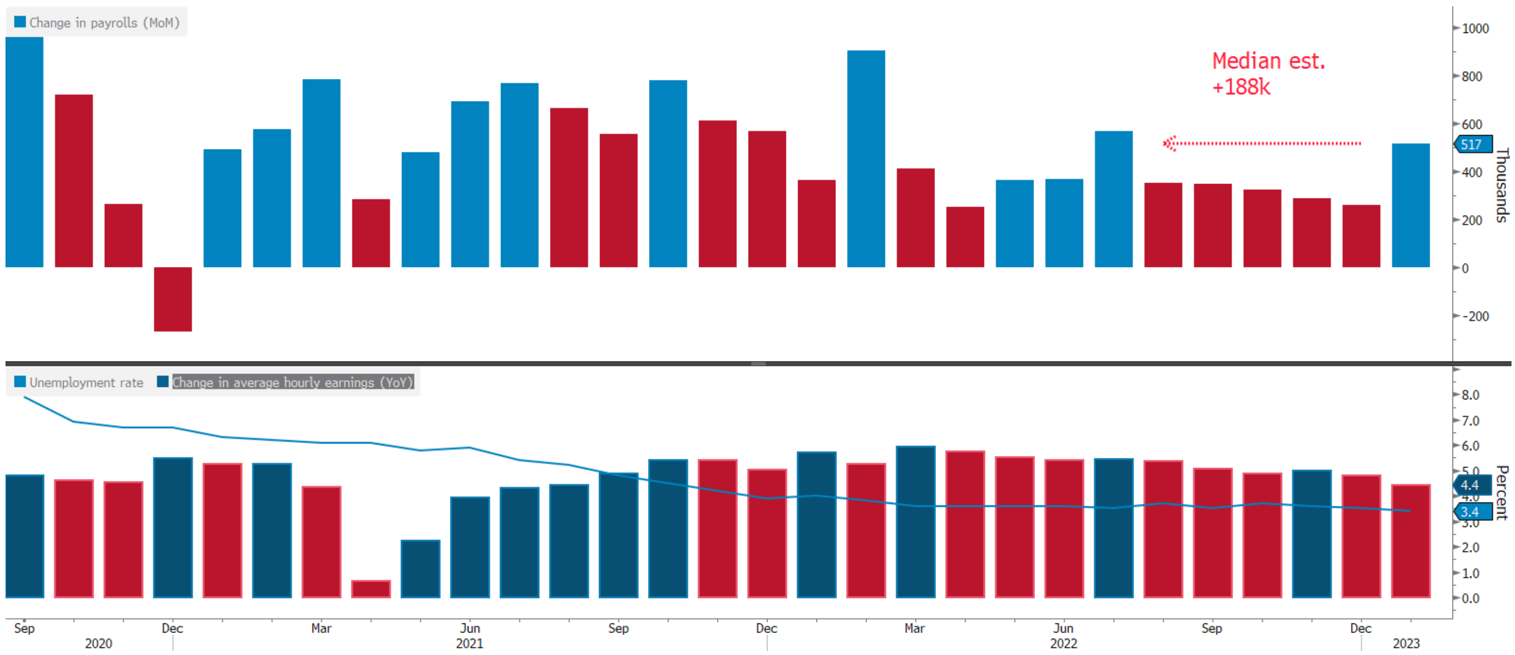
Markets & Macroeconomics

Labor Markets Remain Robust Despite the Fed

Unemployment Hits 5 Decade Low, Wages Remain Stable

Change in Payrolls MoM (top), Unemployment Rate and Change in Avg. Hourly Earnings (bottom)



Source: Bureau of Labor statistics, Bloomberg

Yet again, the Unemployment Rate in the US dropped for the month of February, coming in at 3.4%. This represents the lowest level since May of 1969. In January, the US added +517,000 jobs, well above economists' estimates of +223,000. This surprise in jobs comes on the back of a multitude of corporations announcing layoffs, especially those in the manufacturing and technology sectors. Putting the surprise together with the layoff announcements illustrates just how tight the demand for labor remains, despite several industries showing signs of slowdown. Additionally, wage growth has remained fairly stable with Average Hourly Earnings coming in at +0.3% for the month of December and +4.4% on the year-over-year metric. The strong labor market and wage growth comes on the back of the Fed's rigorous monetary tightening campaign to reign inflation in and has thus far defied the conventional playbook. Typically, when the Fed tightens monetary policy, the unemployment rate will begin to tick up as economic production begins to taper off and eventually, this should help to decrease upward pressure on prices, i.e., inflation. This time around, labor markets are retaining their tightness despite an unprecedented Fed tightening policy and inflation has remained persistently sticky, while economic production has held up but is starting to show signs of softening. It is likely that the Fed will continue to tighten monetary conditions until inflation shows substantial signs of softening, which could lead to the US economy entering a recessionary period to tame inflation. Strong labor markets and wages could act as lifeline for the US economy and keep, or at least soften the blow of a recession.

Bottom Line: Curiously, Labor Markets remain extremely tight despite the Fed's campaign to tighten monetary conditions in their combat against persistently high inflation. The strong Labor Markets and stable wage growth could help to offset some of the negative impacts of monetary tightening and help to soften the blow to economic production. On the flip side, continued wage growth could also apply upward pressure on prices.

February 2023

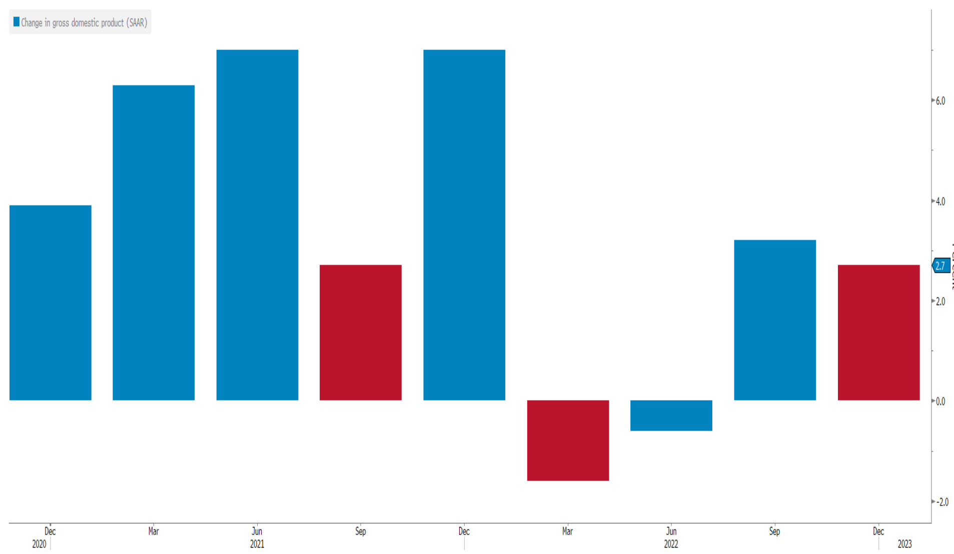
What's Ahead

Inflation Revised Higher, Economic Growth Revised Lower

As shown in the chart to the right, GDP for the final quarter of 2022 was revised lower, coming in below market expectations of +2.9%, at +2.7%. The downward revision was mostly due to Personal Spending figures being lowered. As shown in the chart at the bottom, Core PCE Price Index, one of the Fed's preferred metrics of inflation, was revised higher. Combined with lower personal spending, this paints a concerning picture where consumers are spending less but prices are still increasing. With the Fed conducting a +25bps increase in interest rates during the FOMC meeting in February and the rhetoric from Fed speakers throughout the month, it appears that the Fed will continue to remain in tightening mode for the next several months and there were a plethora of hints that the FOMC members expect rates to remain "higher for longer". This adds to the conundrum where inflation is remaining persistently sticky despite the Fed's already rigorous monetary tightening policy enacted over the past 12 months.

GDP for Q4 of Last Year Misses The Mark After Revisions

GDP QoQ (top)

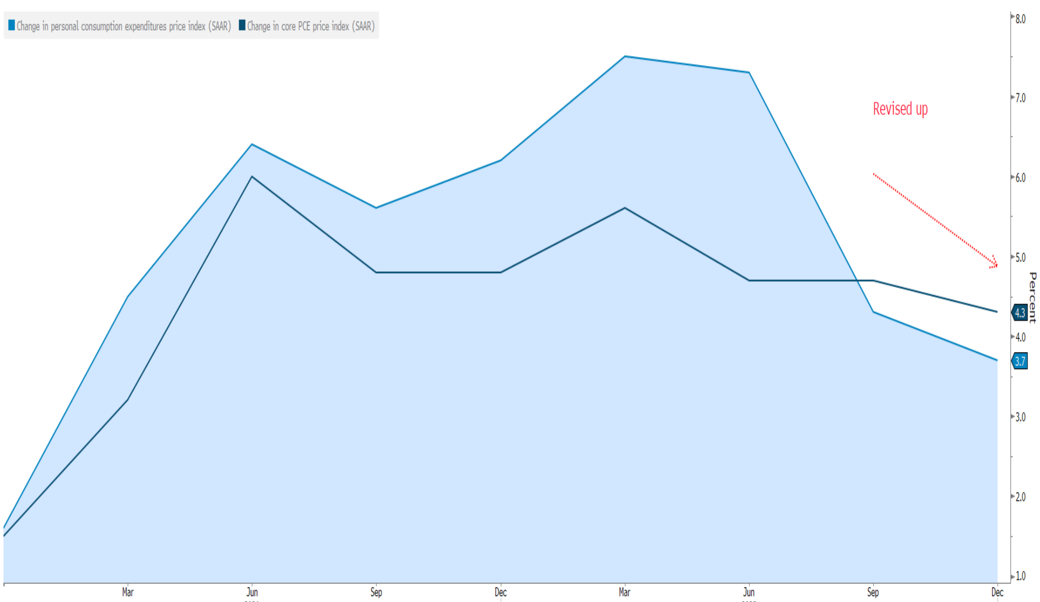


Source: Bureau of Economic Analysis, Bloomberg

The consumer was assumed to be the one saving grace for the US economy throughout the Fed's tightening, where consumer balance sheets exited the pandemic in the best shape that they have ever been in, with the hope that the excess on consumer balance sheets would be adequate to absorb the tightening of monetary conditions and ultimately keep the economy from stumbling into a Fed induced recession. As mentioned in the previous section, the labor markets remain very tight and wages are at least stable, which could act to help offset some of the higher prices felt by consumers, however this could also end up keeping inflation persistently higher as well. Market participants will likely keep a close eye on consumer spending trends and the labor markets in the coming months.

Inflation Revised Up, Personal Consumption Lower

Change in PCE Price Index and Change in Core PCE Price Index



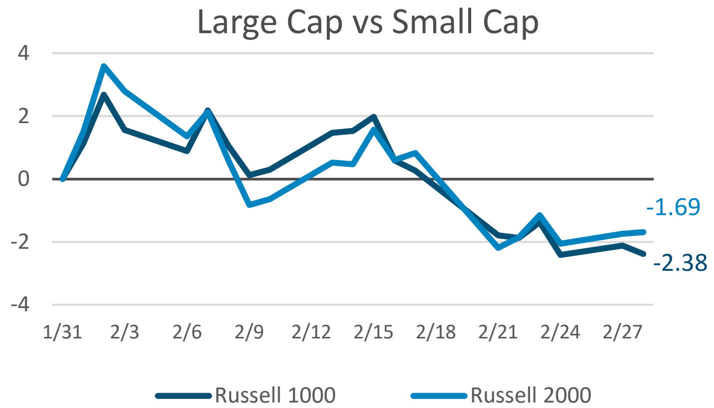
Source: Bureau of Economic Analysis, Bloomberg

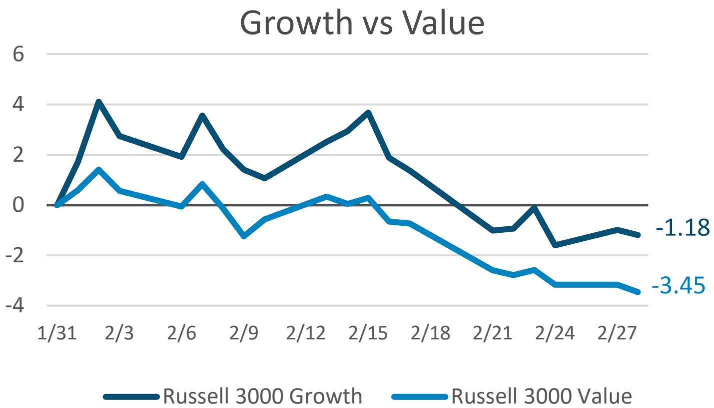
<u>Bottom Line</u>: Economic growth is starting to show signs of losing steam, while inflation remains persistently higher on the back of softening consumer spending. Labor markets and wages remain robust and could help to soften the blow that consumers are experiencing with increased pricing pressures from inflation, but this could also continue to impact inflation to the upside, despite all the tightening conducted by the Fed thus far. Ultimately, the Fed and market participants alike will be keeping a close eye on these metrics in the coming months.

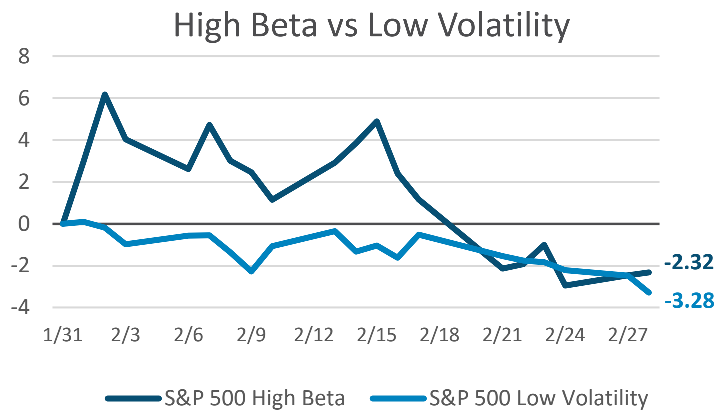
Equity Themes

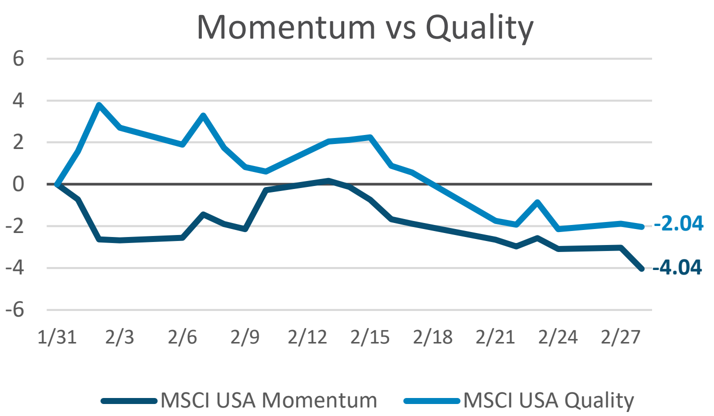
What Worked, What Didn't

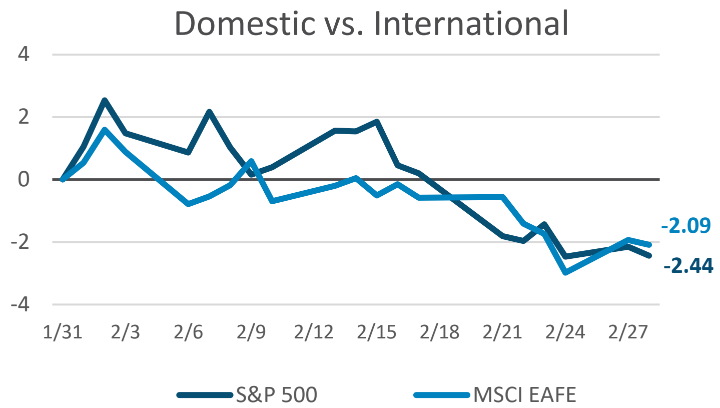
- **Small over Large and Growth over Value.** Closely tracking each other throughout the month of February, Small Cap equities bested Large Cap equities, but both were in the red. Growth protected to the downside versus Value styled equities, but both were negative for February.
- **High Beta Beats Low Vol, Quality beats Momentum.** High Beta equities offered some downside protection for the month, but both High Beta and Low Volatility equities were down for the month. Similarly, Quality factor equities outperformed Momentum factor equities but both were in the red for February.
- **International over Domestic, Developed over Emerging.** International equities outperformed Domestic equities for the month, but the margin of outperformance was small. Emerging Markets struggled for the second month of the year with Developed posting a strong margin of outperformance versus Emerging Markets.

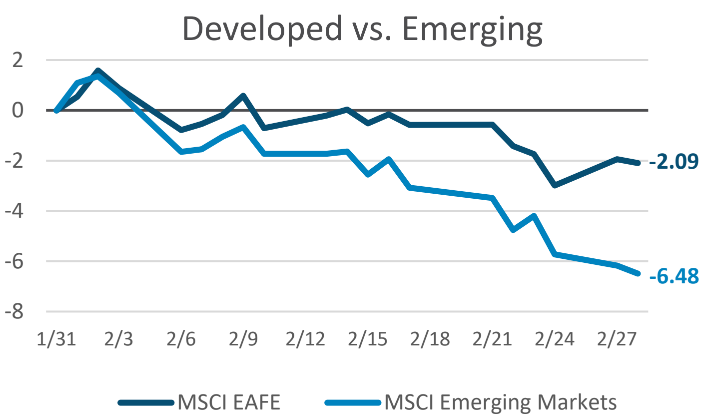












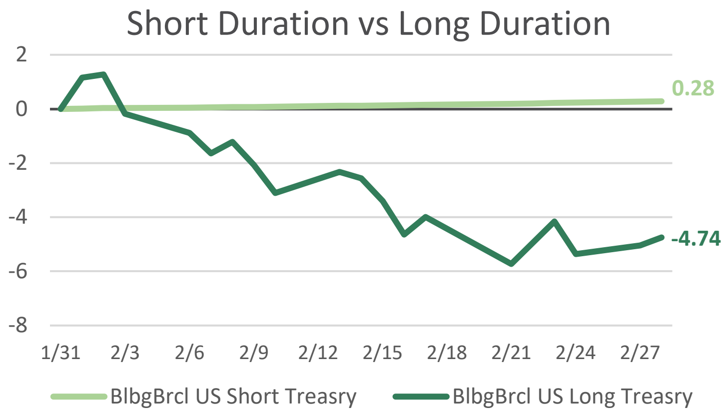
Source: Bloomberg.

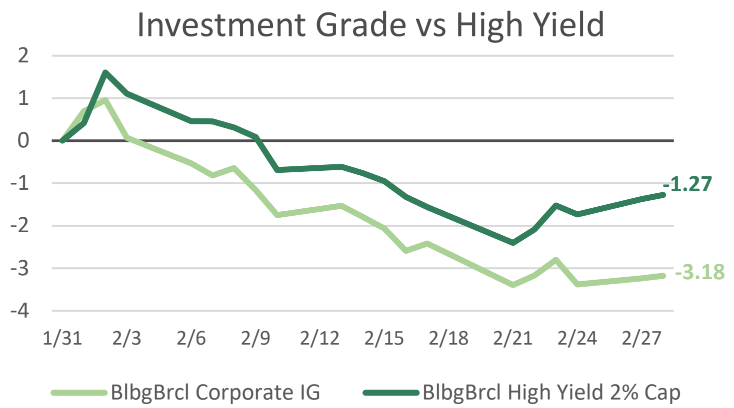
February 2023

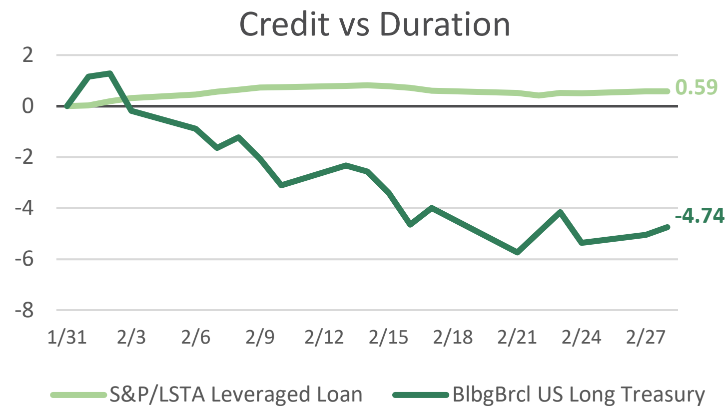
Bond Themes

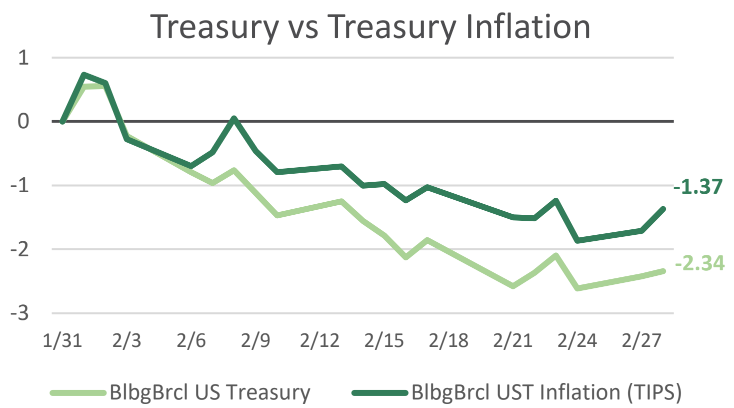
What Worked, What Didn't

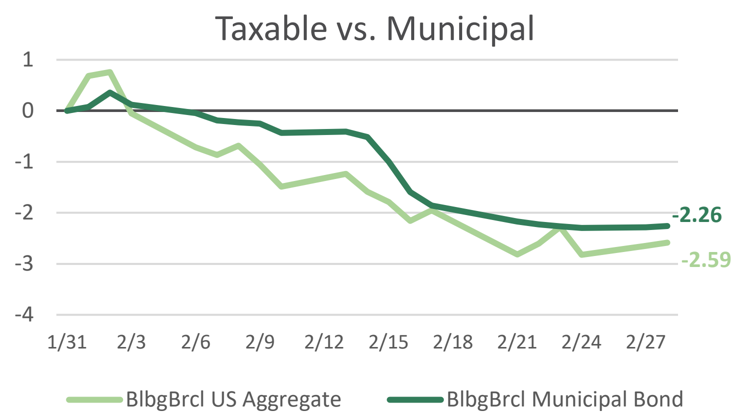
- **Short Duration and Low Quality Outperform.** With interest rates climbing back up, Long Duration had a difficult month versus their Short Duration peers. High Yield posted a decent margin of outperformance versus Investment Grade but was still in the negative for the month.
- **Inflation Adjusted Outperforms, Credit Beat Duration.** TIPS protected to the downside for February versus Treasuries and Credit posted a modest gain versus Long Duration's drawdown.
- **Munis Outperform Taxables and Domestic Outperforms International.** Munis posted a small margin of outperformance versus Taxables for February, but both were negative. Domestic Bonds posted a decent margin of outperformance versus International Bonds, but both were also negative.

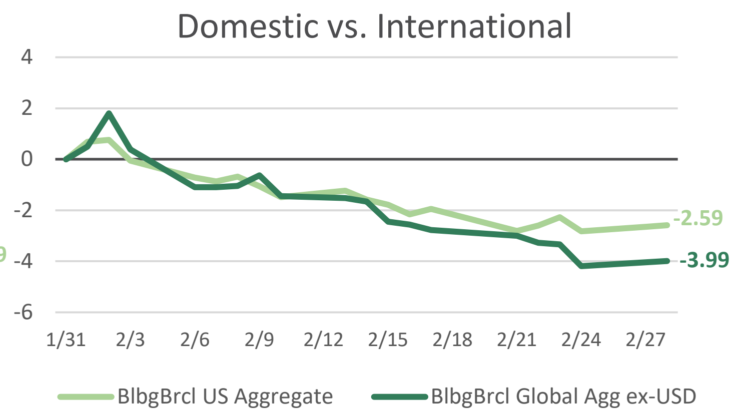












Source: Bloomberg.

February 2023

Asset Class Performance

The Importance of Diversification. From period to period there is no certainty what investment will be the best, or worst, performer. Diversification mitigates the risk of relying on any single investment and offers a host of long-term benefits, such as less portfolio volatility, improved risk-adjusted returns, and more effective compounding.

	Feb-01	Feb-02	Feb-03	Feb-06	Feb-07	Feb-08	Feb-09	Feb-10	Feb-13	Feb-14	Feb-15	Feb-16	Feb-17	Feb-21	Feb-22	Feb-23	Feb-24	Feb-27	Feb-28	Feb	YTD	
High	MCG 2.01	LCG 2.43	SCV -0.38	USB -0.55	LCG 1.65	USB 0.14	EM 0.47	LCV 0.67	LCG 1.43	MCG 0.68	MCG 1.50	EM 0.02	IBD 0.43	USB -0.94	HYB 0.65	HYB 0.99	USB -0.57	IEQ 1.19	SCG 0.04	MCG -1.02	SCG 8.64	High
	IBD 1.83	RE 2.20	LCV -0.84	LCV -0.60	MCG 1.32	IBD -0.09	IEQ 0.18	MCV 0.39	MCG 1.38	LCG 0.42	SCG 1.12	USB -0.42	HYB 0.39	IEQ -1.10	SCG 0.38	LCG 0.83	HYB -0.60	HYB 0.67	USB -0.01	LCG -1.19	MCG 7.61	
	LCG 1.75	SCG 2.06	IEQ -0.93	RE -0.61	SCG 0.98	EM -0.12	IBD 0.04	RE 0.32	SCG 1.29	IEQ 0.18	SCV 0.93	IBD -0.43	SCG 0.26	EM -1.26	USB 0.27	SCG 0.79	MCV -0.60	LCG 0.63	SCV -0.05	SCG -1.23	SCV 7.16	
	SCG 1.74	SCV 2.00	SCG -0.96	HYB -0.64	LCV 0.93	HYB -0.42	USB -0.39	SCV 0.27	SCV 1.15	SCG 0.16	LCG 0.71	IEQ -0.49	SCV 0.26	IBD -1.36	SCV 0.26	RE 0.61	LCV -0.62	EM 0.52	RE -0.10	HYB -1.89	LCG 7.04	
	EM 1.23	MCG 1.89	USB -0.96	MCV -0.72	IEQ 0.85	RE -0.42	60/40 -0.43	SCG 0.11	MCV 1.05	HYB 0.03	MCV 0.64	60/40 -0.71	IEQ 0.25	60/40 -1.49	MCG 0.11	MCG 0.52	SCG -0.89	MCG 0.51	HYB -0.19	SCV -2.28	IEQ 5.65	
	SCV 1.19	MCV 1.15	HYB -1.05	LCG -0.76	MCV 0.75	60/40 -0.46	HYB -0.65	60/40 -0.31	IEQ 1.00	60/40 -0.09	RE 0.44	SCV -0.77	USB 0.24	HYB -1.54	LCG 0.08	IEQ 0.52	IBD -0.94	SCG 0.47	MCG -0.21	USB -2.67	MCV 4.58	
	HYB 1.05	LCV 0.72	MCV -1.13	60/40 -0.82	SCV 0.53	IEQ -0.62	MCG -0.74	LCG -0.40	RE 0.95	IBD -0.14	LCV 0.24	HYB -0.80	60/40 -0.03	LCV -1.81	MCV -0.03	SCV 0.50	SCV -1.00	60/40 0.46	IBD -0.22	IEQ -3.07	RE 3.42	
	60/40 1.03	60/40 0.60	60/40 -1.13	MCG -0.98	60/40 0.50	LCV -0.88	LCG -0.75	USB -0.44	LCV 0.90	EM -0.17	60/40 0.01	RE -0.86	LCV -0.09	RE -1.99	60/40 -0.07	EM 0.49	60/40 -1.09	SCV 0.29	LCG -0.24	60/40 -3.09	60/40 3.03	
	MCV 0.93	HYB 0.57	LCG -1.37	IEQ -1.02	EM 0.40	MCV -0.90	LCV -1.09	IEQ -0.44	EM 0.82	SCV -0.27	HYB -0.16	MCV -0.95	MCV -0.18	LCG -2.29	LCV -0.23	60/40 0.47	MCG -1.23	RE 0.21	60/40 -0.28	MCV -3.24	HYB 1.71	
	IEQ 0.89	IBD 0.48	MCG -1.45	IBD -1.08	HYB 0.36	MCG -0.96	MCV -1.14	MCG -0.48	60/40 0.75	MCV -0.28	USB -0.19	LCV -0.99	RE -0.46	MCV -2.29	IBD -0.34	USB 0.36	LCG -1.55	USB 0.20	MCV -0.29	LCV -3.52	LCV 1.44	
	USB 0.70	USB 0.11	IBD -1.74	SCV -1.39	USB -0.17	LCG -1.27	RE -1.16	IBD -0.67	USB 0.30	LCV -0.31	IEQ -0.45	SCG -1.12	LCG -0.56	MCG -2.55	EM -0.48	MCV 0.24	IEQ -1.67	IBD 0.15	LCV -0.31	IBD -4.46	EM 0.87	
	RE 0.65	IEQ -0.14	EM -1.78	EM -1.47	RE -0.17	SCV -1.41	SCG -1.38	HYB -0.77	HYB 0.25	USB -0.35	IBD -0.46	MCG -1.46	MCG -0.75	SCV -2.77	IEQ -0.56	IBD 0.24	RE -1.71	MCV 0.15	EM -0.70	RE -5.96	USB 0.57	
Low	LCV 0.60	EM -0.60	RE -2.03	SCG -1.50	IBD -0.19	SCG -1.53	SCV -1.51	EM -0.96	IBD 0.00	RE -0.88	EM -0.84	LCG -1.78	EM -1.10	SCG -3.11	RE -1.02	LCV 0.21	EM -2.25	LCV -0.03	IEQ -0.73	EM -7.57	IBD -1.25	Low

Legend

- 60/40 Allocation (60/40)
- Large Growth (LCG)
- Large Value (LCV)
- Mid Growth (MCG)
- Mid Value (MCV)
- Small Growth (SCG)
- Small Value (SCV)
- Intl Equity (IEQ)
- Emg Markets (EM)
- U.S. Bonds (USB)
- High Yield Bond (HYB)
- Intl Bonds (IBD)
- Real Estate (RE)

Source: Bloomberg. Asset-class performance is presented by using market returns from an exchange-traded fund (ETF) proxy that best represents its respective broad asset class. Returns shown are net of fund fees for and do not necessarily represent performance of specific mutual funds and/or exchange-traded funds recommended by the Prime Capital Investment Advisors. The performance of those funds June be substantially different than the performance of the broad asset classes and to proxy ETFs represented here. U.S. Bonds (iShares Core U.S. Aggregate Bond ETF); High-Yield Bond (iShares iBoxx $ High Yield Corporate Bond ETF); Intl Bonds (SPDR® Bloomberg Barclays International Corporate Bond ETF); Large Growth (iShares Russell 1000 Growth ETF); Large Value (iShares Russell 1000 Value ETF); Mid Growth (iShares Russell Mid-Cap Growth ETF); Mid Value (iShares Russell Mid-Cap Value ETF); Small Growth (iShares Russell 2000 Growth ETF); Small Value (iShares Russell 2000 Value ETF); Intl Equity (iShares MSCI EAFE ETF); Emg Markets (iShares MSCI Emerging Markets ETF); and Real Estate (iShares U.S. Real Estate ETF). The return displayed as “Allocation” is a weighted average of the ETF proxies shown as represented by: 30% U.S. Bonds, 5% International Bonds, 5% High Yield Bonds, 10% Large Growth, 10% Large Value, 4% Mid Growth, 4% Mid Value, 2% Small Growth, 2% Small Value, 18% International Stock, 7% Emerging Markets, 3% Real Estate. 030623014 MKS