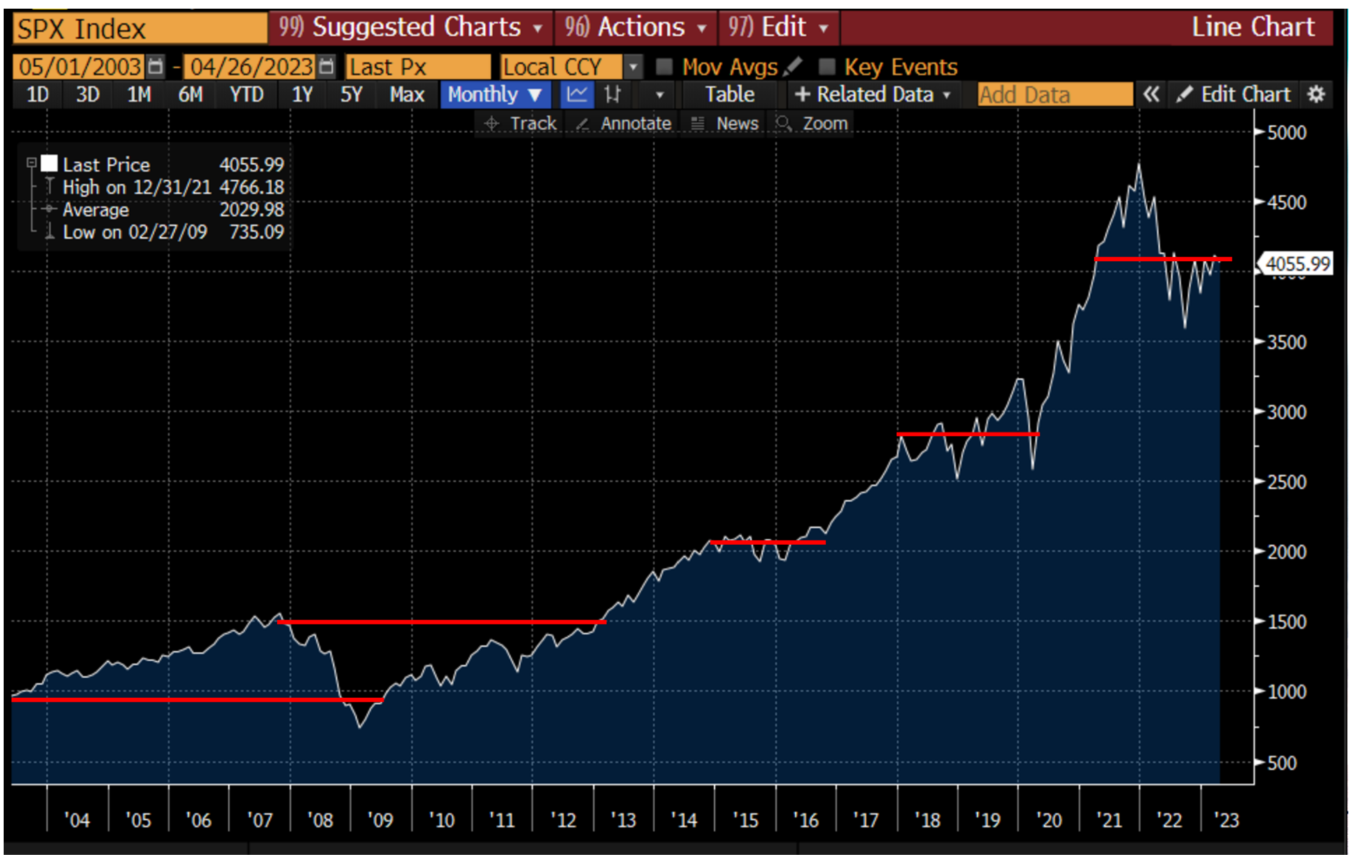
# Staying the Course

While we would prefer otherwise, financial markets don't always go up in straight lines. During the last two years through April 26, the S&P 500 is down 3%.[1] We've endured a lot of volatility to go essentially nowhere. This can be frustrating and test the patience of many investors. To help frame recent performance, we wanted to put provide some longer-term context. Below is a chart of the S&P 500 over the last 20 years. As you can see, there have been several multi-year periods where returns essentially flatlined (marked by the red lines). The good news is that periods of outperformance tend to come in bunches after these longer periods of consolidation.

In theory this makes sense, as investors often over-extrapolate trends in the short term, driving markets to levels perhaps not justified by underlying economic and company fundamentals. Company operating performance then takes some time to catch up to valuations. Also, unexpected financial or geopolitical events can at times throw everything off course. The important thing to note is that the multi-century history of markets is one in which things consistently get back on course.

Right now, we think we are in one of these consolidation periods. That doesn't mean we don't see opportunities (such as firms driving artificial intelligence progress, which we covered in our January correspondence). And the volatility – even though frustrating – can provide chances to enter quality firms at compelling valuations. Quality, in our view, is defined as: reasonable valuations, sound management, stable financials, history of revenue, earnings and free cash flow growth, and – most critical - a competitive edge in business.

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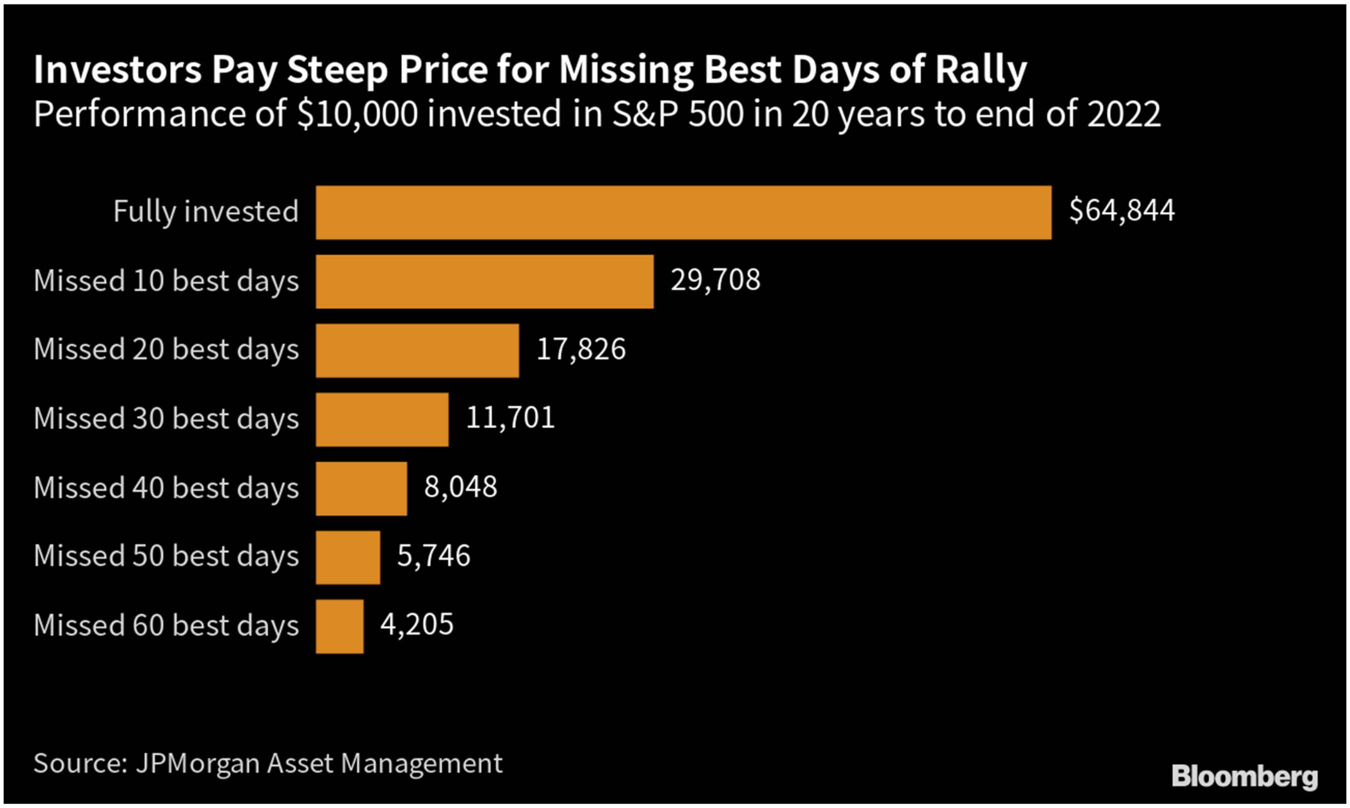
We understand the natural tendency to get impatient during such periods, or nervous during bouts of volatility, however, we think the important thing for investors is to stay invested in quality holdings – even if the returns are currently choppy. The data proves this out. While it can be tempting to trade in and out of the market, mistiming can really set one back. Below is a Bloomberg graphic (based on a JPMorgan study) showing the performance of $10,000 invested from 2002-2022 full-time vs. missing out on just a handful of the best days for returns (which often come at unexpected points after periods of negative performance). Missing out on just the best 10 days cut returns by more than 50%. Missing the best 60 days resulted in a more than 90% gap. The message is clear. Buy good companies and hold, unless you need liquidity. There's a reason Warren Buffet has had more success than day traders.

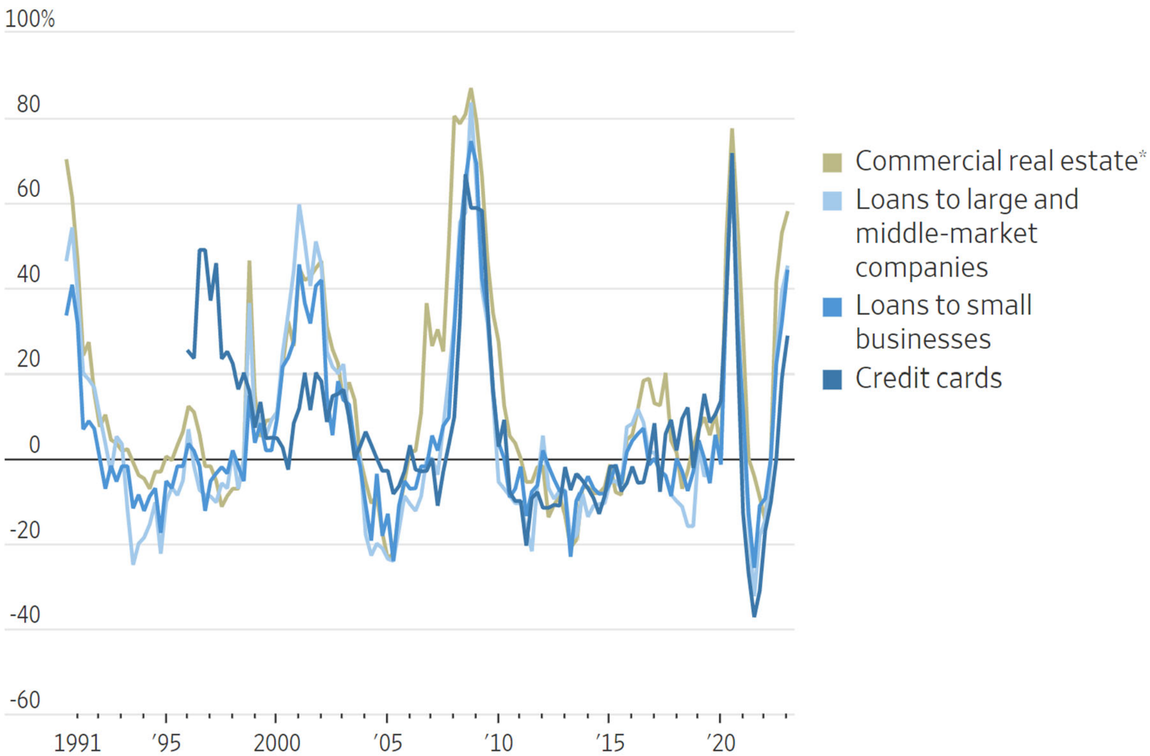



In terms of where to focus new capital right now, we still find short-term Treasuries attractive (despite the debt ceiling worries). And we still think money market funds yielding approximately 4.5% are a superior alternative to bank deposits yielding closer to 0%. As for stocks, we favor large cap firms that are not dependent on external financing. As seen in the graphic from the Wall Street Journal below, lending standards are tightening significantly in the wake of the recent banking system stress – particularly amongst smaller lenders.[2] There are certainly opportunities in smaller cap firms (and the Russell 2000 Index has been flat over the last five years compared to the two-year stretch for the S&P 500), however, those come with a greater degree of risk. As always, we'd be happy to discuss specific opportunities.

April 27, 2023

**Stingier Standards**

Net percentage of U.S. banks reporting tighter lending terms




*Note: Beginning in Q4 2013, commercial real estate includes only loans secured by nonresidential structures
Source: Federal Reserve

We hope you are well. Please let us know if you would like to discuss or review your portfolio with us.

Sincerely,

Peter Karmin
Managing Member

Stuart Loren
Director

**Citations and Disclosures**

[1] Bloomberg (as of April 26, 2023). All data herein sourced from Bloomberg unless otherwise cited.
[2] The Wall Street Journal, *Why the Banking Mess Isn't Over* (April 23, 2023).

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