Q3 2022 Market Commentary

Produced by our Portfolio Management Team, Affinity Investment Advisors, LLC

Capital Markets Review

Since 1928 there have been 28 bear markets with an average U.S. equity market decline of -35.6% occurring over an average of 289 days. The current bear market began at the beginning of 2022 during which time the S&P 500 Index has declined just under 24%. The severity of bear markets varies with each economic and capital markets environment. The worst bear market occurred in the 1931-1932 timeframe when the equity market fell -61.8%. In the 1948-1949 period, the equity market fell -20.6% which represented the softest decline in history.

The cause of bear markets may vary, but often significant market retreats are accompanied by rising interest rates and slowing or negative GDP growth. According to the Bureau of Economic Analysis (BEA), U.S. real GDP declined in Q2 2022 by -0.6%, driven by weakness in construction and non-durable goods. This followed a decline of -1.6% in Q1 2022. The Atlanta Federal Reserve's GDPNow estimate calls for real GDP to rise just over 2% in Q3 2022. The question, however, that looms over the capital markets is just how far will the Federal Reserve will go in this tightening cycle to tame inflation.

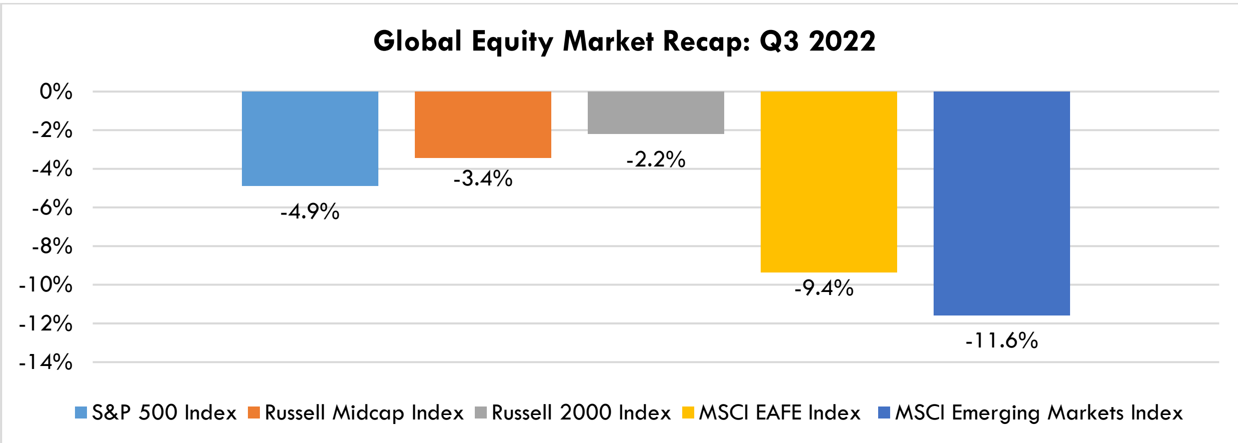
Inflation remains the elephant in the room. According to the U.S. Bureau of Labor Statistics, CPI rose 0.1% month over month in August and 8.3% year over year. Excluding food and energy, the CPI increased 0.6% in August and 6.3% year over year. As a result of stubborn price increases, the Federal Reserve lifted the Fed Funds Rate by an additional 75 basis points in September to a range of 3.0% to 3.25%, and estimates suggest that the rate may rise to 4.4% in 2023.

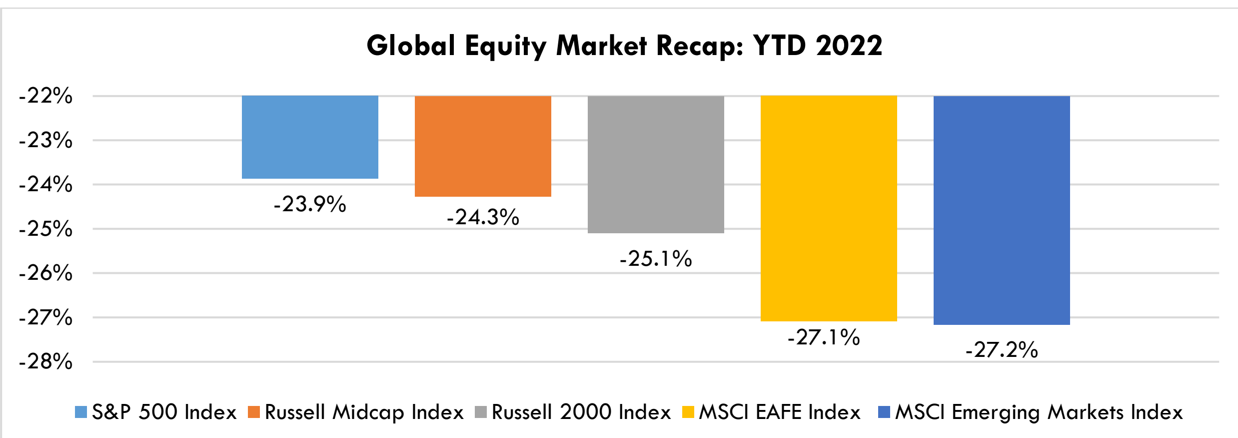
Equity Market Review

The 3rd quarter represented another disappointing period for global equities. The S&P 500 Index declined -4.88%, although U.S. stocks performed better than non-U.S. stocks where the MSCI EAFE Index cascaded -9.36% lower. Emerging market equities fared still worse, down -11.57% for the quarter. Not surprisingly, stocks within Eastern Europe were very weak, down more than -24% during the period. Equities in the Far East also produced strongly negative returns, declining -14.03%. The one bright spot was Latin America where stocks in that region rose 3.61% for the quarter. The strength in this region was likely due to its link to commodity products and exports. The tables below display Q3 and year-to-date performance for a variety of equity indices.

www.silverhawkfinancial.com
office: 480.296.0200 | fax: 480.296.0210
21090 N Pima Rd, Scottsdale, AZ 85255

Produced by our Portfolio Management Team, Affinity Investment Advisors, LLC





All data as of 9-30-2022; Source: Refinitiv

Large cap growth stocks performed better than value stocks in the 3rd quarter, a reversal of a trend that had persisted for many quarters. The prior trend – value stocks outperforming growth stocks – can be seen in the trailing one-year returns where the Russell 1000 Value Index demonstrated much better downside protection. Still, growth stocks have produced better results over the past 3-year, 5-year, and 10-year periods.

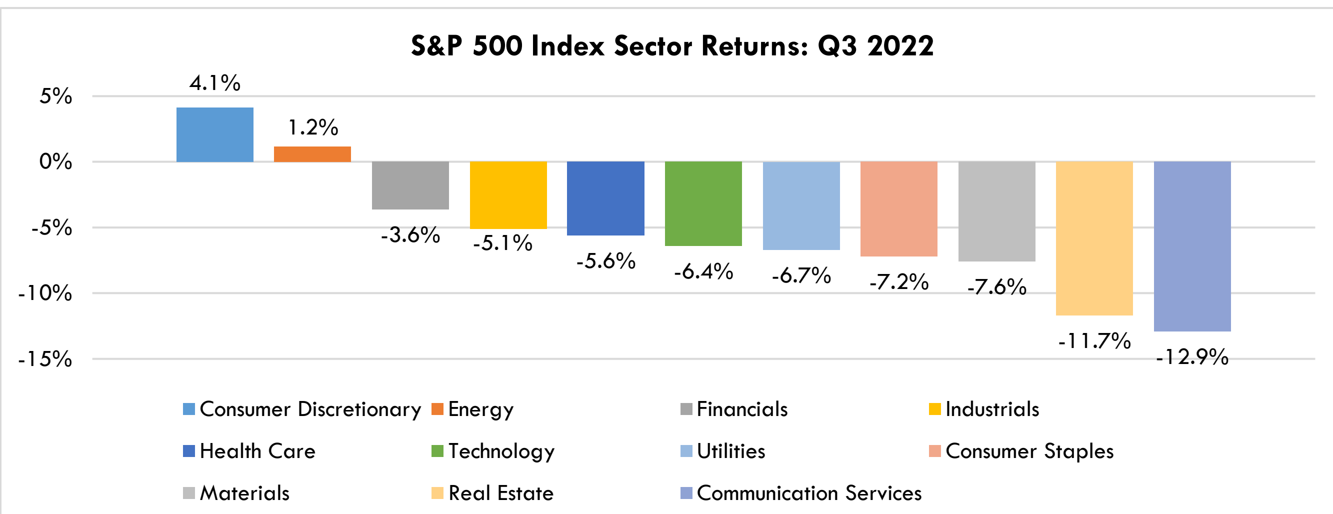
Performance Results	Q3 2022	1 Year	3 Years	5 Years	10 Years
Russell 1000 Growth Index	-3.60%	-22.59%	10.67%	12.17%	13.70%
Russell 1000 Value Index	-5.62%	-11.36%	4.36%	5.29%	9.17%

All data as of 9-30-2022; Source: FTSE Russell

www.silverhawkfinancial.com
office: 480.296.0200 | fax: 480.296.0210
21090 N Pima Rd, Scottsdale, AZ 85255

While growth stock returns declined slightly less than value stocks in the 3rd quarter, it was likely due to a strong rebound in Consumer Discretionary stocks (+4.1%) and a much more muted return from Energy stocks (+1.2%), despite the fact that they performed well relative to the market. Recall that Consumer Discretionary stocks, which represent a meaningful weight in the growth index versus the value index, declined -31.8% in the first half of 2022. Perhaps investors were looking for now more attractive valuations for stocks within this sector. Meanwhile Energy stocks, a larger weight in the value index, generated a return closer to the broad S&P 500 Index return during the quarter. During the first half of 2022, Energy stocks rose +31.1%. Overall, performance dispersion declined during the 3rd quarter relative to what was observed in the first half of the year.

Despite slightly better returns from growth stocks, global equity indices do not suggest that the "risk-off" environment has changed. This is based upon the outperformance of equities in developed markets relative to emerging markets as well as U.S. stocks relative to non-U.S. stocks. The table below shows the investment returns for the 3rd quarter for the eleven S&P sectors.

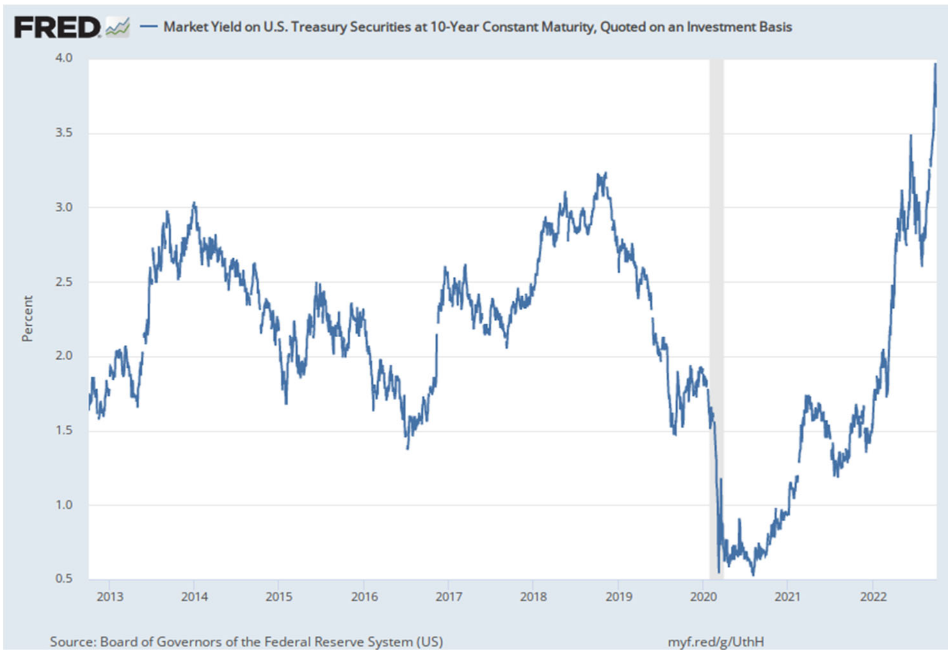


All data as of 9-30-2022; Source: Refinitiv

Fixed Income Markets Review

Interest rates continued to rise during the 3rd quarter, extending the bear market for bonds. The chart below shows the yield on the U.S. 10-Year Treasury over the past decade. The yield has surpassed the most recent high set in 2018. The Bloomberg U.S. Aggregate Bond Index has fallen -14.6% year-to-date (as of 9/30/2022), and the Bloomberg Global Aggregate Bond Index is down -19.9% so far this year. Bloomberg's U.S. Corporate Investment Grade Bond Index produced worse returns than Treasuries, falling -18.7% for the year (as of 9/30/2022).

www.silverhawkfinancial.com
office: 480.296.0200 | fax: 480.296.0210
21090 N Pima Rd, Scottsdale, AZ 85255



High yield bonds have held up better than some other fixed income categories, declining -14.7% so far this year (as of 9/30/2022). Interestingly, credit spreads, as displayed in the chart below, have remained somewhat contained given the uncertainty and discord in the financial markets. So far credit spreads have not broken out to a level that would demonstrate extreme conditions. The chart shows much more alarming levels being reached in 2016 and 2020.

www.silverhawkfinancial.com
office: 480.296.0200 | fax: 480.296.0210
21090 N Pima Rd, Scottsdale, AZ 85255

Capital Markets Outlook

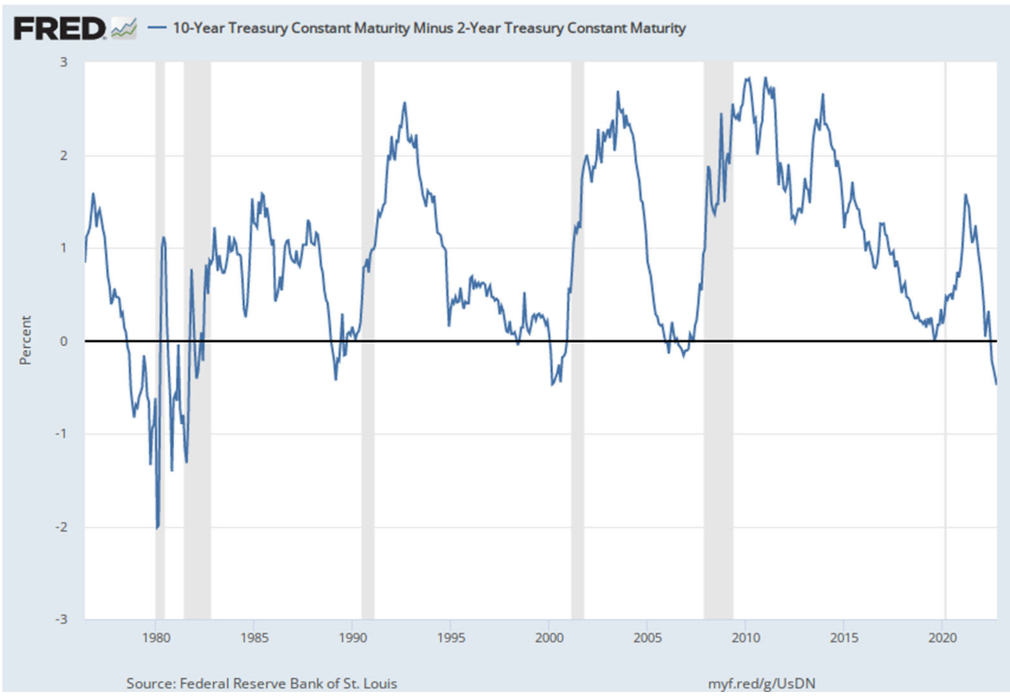
We now know that the U.S. experienced a recession in the first half of 2022. However, investors are looking ahead to ascertain the future path of interest rates (particularly the Fed Funds Rate), GDP growth, and the rate of earnings growth. As noted in the beginning of this commentary, estimates call for the Fed Funds Rate to rise to 4.4% in 2023, and, hence, headwinds remain for investors as we turn the corner towards a new year. Higher interest rates typically impact the ability of corporations to grow and expand. As a result, real GDP forecasts for 2023 are quite muted. The Conference Board expects U.S. real GDP to measure 1.4% in 2022 (year over year) and 0.3% in 2023 (year over year).

Decelerating economic growth from 2022 into 2023 would likely equate to softer earnings growth for U.S. companies. That said, at the end of September analysts' consensus earnings estimates stood at 8.2% for calendar year 2023. This may suggest a better market for U.S. equities, but with muted returns. It is also possible that there will be dispersion across industries and individual companies based upon the unique ability to drive above average growth and manage expenses. In our view, actively managed investment strategies offer the ability to add value to client portfolios in this environment.

Despite expectations for slightly positive growth in 2023, forecasts have been and remain volatile. Many respected economists and investment firms believe a recession is becoming more and more imminent, as a soft landing scenario evaporates. Key to the direction of the economy and capital market returns in the coming year is the ability of the Federal Reserve to reverse inflationary trends. Month over month inflation data suggests that perhaps inflation has peaked. Time will tell. But the chart below, which shows

www.silverhawkfinancial.com
office: 480.296.0200 | fax: 480.296.0210
21090 N Pima Rd, Scottsdale, AZ 85255

the spread between U.S. 10-Year and 2-Year Treasury yields, acknowledges that the relationship has inverted. Historically, this often portends a coming recession (the shaded bars represent recessions).



As long as the Federal Reserve is forced to continue its aggressive posture in order to slow the economy, interest rates will continue to rise. This has historically led to dampened or negative GDP growth, and the impact on equity and fixed income prices is generally negative. The extent to which the Federal Reserve must act will depend upon a variety of factors, many of which will materialize in the coming quarters. While investors are currently facing challenges and a great deal of discomfort in a negative return environment, bear markets are followed by bull markets. And it is important to recall that investors anticipate modest changes in financial and economic data. When positive changes begin to emerge, the markets will find their footing once again.

Sources: Federal Reserve Bank of St. Louis; Federal Reserve Bank of Atlanta; FTSE Russell; MSCI; S&P Global; Dow Jones; Bureau of Labor Statistics; the Conference Board; and Refinitiv.

www.silverhawkfinancial.com
office: 480.296.0200 | fax: 480.296.0210
21090 N Pima Rd, Scottsdale, AZ 85255