Waterfront Balanced Composite
1Q 2023 Commentary

WATERFRONT
ASSET MANAGEMENT

The new year has started with an optimistic tone as both equity and fixed income markets posted solid advances despite pervasive pessimism and a growing chorus of recession forecasts. The global economy has proven surprisingly resilient in the face of both familiar as well as several nascent headwinds. Elevated inflation readings, hawkish commentary from Federal Reserve Board members, ongoing geopolitical tensions and pandemic impacts feel like 'yesterday's news' and yet they continue to dampen economic outlooks. Inflation measures have been easing from historical highs though the level remains far above the Federal Reserve's stated target. As a result, the Federal Reserve raised short-term interest rates by a cumulative 50 basis points (bps) during the quarter but have indicated in speeches and interviews that the pace of hikes will slow with growing anticipation of a pause. As is commonly recited by Fed officials, monetary policy works with long and variable lags. The current rate hike cycle, one of the most precipitous in history, is leaving an expanding wake of financial 'casualties' to include so-called 'meme stocks'; speculative growth investments in public and private markets; crypto currencies; and most recently, several regional banks in the U.S. and Credit Suisse in Switzerland. The specter of tighter global monetary policy casts a pall over global economic growth estimates for 2023 with a corresponding negative impact on corporate earnings growth. In addition, the consumer savings built up during the pandemic are dwindling as consumption patterns normalize and inflation erodes purchasing power. And yet, in the face of these headwinds and concerns, equity markets advanced with the S&P 500 rising 7.5% during the first quarter. Fixed Income markets also rose with equities as interest rates declined. The Bloomberg U.S. Aggregate Government / Credit Index advanced 3.2% for the quarter. To summarize markets over the last six months in a word: indefatigable.

	Q1 Total Return
Waterfront Balanced Composite	**4.2%**
S&P 500 Index	**7.5%**
Bloomberg U.S. Agg Gov't/Credit Index	**3.2%**
60% S&P 500 / 40% BBG U.S. Agg Gov't/Credit (benchmark)	**5.7%**
Morningstar Moderate Allocation category (median return)	**3.8%**

The Waterfront Balanced strategy advanced 4.2% in the first quarter, underperforming the funds benchmark (blended benchmark consisting of 60% S&P 500 & 40% Bloomberg U.S. Aggregate Govt/Credit) but outperforming peers in the Morningstar Moderate Allocation category. During the quarter and relative to the benchmark, performance was hindered by a conservative asset allocation and defensive risk posture in both the equity and fixed income sleeves of the portfolio. At quarter end, the strategy's allocation to equity was 56%; fixed income represented ~41% with the balance in cash.

The equity sleeve advanced 5.5% during the quarter, underperforming the benchmark as our quality bias hurt relative performance. In addition, poor stock selection in the Consumer Discretionary, Technology and Communication Services sectors were meaningful detractors to relative performance.

The fixed income sleeve advanced 3.0% during the quarter, slightly underperforming the benchmark. Late in the quarter, short-term rates collapsed and credit spreads widened as concerns over the health of the banking industry were sparked by the sudden collapse of two regional banks. The fixed income sleeve has over two-thirds of its exposure to Treasury's with the balance in Investment Grade rated bonds which acted as a buffer to the volatility. During the quarter, Investment Grade credit spreads widened modestly to 145 bps, below the 25yr average of ~150bps.

The quarter's top contributors to performance were diverse but were generally economically sensitive with several simply rebounding from declines in previous periods. As mentioned previously, mid- and long-term interest rates declined significantly during the quarter which benefited the strategies mid-duration posture. Investment-grade credit spreads widened modestly with the duration benefit overwhelming the negative impact of spread widening. Microsoft, Infineon Technologies and Alphabet rebounded from punishing declines last year as investors attitude toward cyclicality improved. In each case, the fundamental outlook is difficult in the near-term but adequately reflected in the equity valuation supporting my continued conviction.

TOP CONTRIBUTORS	AVG. WEIGHT	RETURN	CONTRIB-UTION
United States Treasuries (VGIT)	22.6%	2.9%	0.70%
Microsoft Corp. (MSFT)	3.4%	20.5%	0.67%
Infineon Technologies (IFNNY)	1.6%	37.1%	0.50%
Investment Grade Bonds (VCIT)	11.8%	4.1%	0.50%
Alphabet Inc. (GOOGL)	2.4%	17.6%	0.40%

Positions in PNC Financial Services, VF Corporation, Jazz Pharmaceuticals, UnitedHealth Group and Emerson Electric were notable detractors during the quarter. PNC Financial declined in sympathy with other regional banks as concerns over systemic risk from the collapse of Silicon Valley Bank and Signature Bank spread throughout the industry. I believe PNC Financial is well-capitalized with a conservative Balance Sheet that will help sustain it through this period of turmoil. VF Corporation has been a disappointing investment for the strategy but I believe in the power of the North Face brand and anticipate a revival of the Vans franchise. Jazz Pharmaceuticals and UnitedHealth Group have been strong performers over recent periods and investor preferences shifted during the quarter to more cyclically sensitive assets with greater EPS leverage to an economic recovery. Emerson Electric is a late-cycle industrial that is pursuing an expensive acquisition which soured investor attitudes toward management and the equity. I believe the speculated acquisition of NATI will prove accretive over time and expect management to continue to deliver on its transformation agenda to a more stable, highly profitable industrial company.

TOP DETRACTORS	AVG. WEIGHT	RETURN	CONTRIB-UTION
PNC Financial Services (PNC)	0.9%	<18.8%>	<0.18%>
VF Corporation (VFC)	0.8%	<15.9%>	<0.13%>
Jazz Pharmaceuticals (JAZZ)	1.4%	<8.2%>	<0.13%>
UnitedHealth Group (UNH)	1.0%	<10.5%>	<0.12%>
Emerson Electric (EMR)	1.1%	<8.7%>	<0.11%>

As I look forward, the backdrop for risk assets has deteriorated meaningfully over the last fifteen months. The inflation dynamic is troubling and a meaningful risk to the outlook for asset values. The war in Ukraine is, first and foremost, a human tragedy, but also an unhelpful catalyst for higher prices as the region is rich in energy, agriculture, metals and industrial goods. While I am encouraged by the consensus view that inflation rates will cool in the months ahead, the pace of interest rate increases (both completed and contemplated) by global central banks has become extreme. The impacts from tighter monetary policy occur with a lag and will likely drive a meaningful reset in consumer and corporate spending and investment in the months ahead. As a result, your account is conservatively positioned in terms of asset allocation, sector weights and credit exposure. We anticipate attractive investment opportunities in the year ahead and are positioned to respond quickly to capitalize on them when they come.

While the outlook has deteriorated, my focus is unchanged. Across economic cycles and irrespective of market moods, I seek to maintain an emphasis on finding high quality, growing companies whose securities are trading at a reasonable valuation with visible catalysts to drive relative performance over the next twelve months. This approach has served investors well over time, and my confidence in it has not waned.

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