Good morning. As you may have noticed, I have been a bit radio silent lately as my travel schedule has kept me busy which concluded with an investor conference in Charleston, SC. Yes, coming back to rainy Boston was tough but I am happy to be back home.

The topic I would like to dig a little deeper on this week is nothing that usually excites people: Bonds. Yes, fixed income investing hasn't looked this interesting in years. With bonds, there are two main risk factors to consider: RISK & DURATION. Coming into this year, the goal for many investors, including us, was to limit your duration risk because the longer-to-maturity your bonds were, the worse they would perform in an increasing interest rate environment. What a rising rate environment we got, with rates going from ZERO to almost 5% on the Fed Funds rate. For the 20 Year U.S. Treasury Bond, that has resulted in a decline of principal of 25% as of 12/8/22 according to FactSet. For a Treasury bond, that is an enormous number. The good news is that is in the past. What lies ahead in the future could actually be an opportunity.

According to the oft-quoted Tom Essaye at The Sevens Report, the 10 Year Treasury peaked out at 4.24% in late October to 3.42% where it sits coming in to today, 12/8/22. The primary reasons for that drop:

1. A drop in the "fear trade" regarding the U.K. fiscal scare
2. Inflation showing signs of peaking
3. Fears of an economic slowdown.

Going forward, given a continued slowdown in the economy and a decline in inflation, the macro environment for parts of the bond market should be favorable. When we say parts, we are specifically referring to higher quality corporate bonds (companies with fortress balance sheets), U.S. Treasuries and Investment Grade Municipal Bonds. Although credit quality has not been a concern for the bond market this year, as the performance of that sector has shown in 2022, in a slowing economy it will begin to get more attention.

Finally, as it relates to duration, we could be looking at a situation where 2023 is the opposite of 2022 where the place to be was in shorter term maturities and instead for 2023 you want to be in longer dated maturities. Why? Because the sooner you can lock in longer duration rates, the better. When the economy slows down, the Fed will eventually cut rates and that will bring down the yield on short term investments like Money Markets and CD's and possibly at a faster pace than investors expect. **Given that scenario, if the economy is going to contract (or materially slow) and inflation is going to decelerate, then bonds and especially higher-quality bonds (investment grade and treasuries) and longer-duration bonds should be poised to bounce back in 2023.** Thank you again to Tom Essaye for that quote.

We are taking these things in to consideration as it relates to our allocation to fixed income. Thank you for your time and attention to this email.

<u>This paragraph for prospects only:</u>

If you would like to discuss how this impacts your portfolio, please let us know and we would be happy to have that discussion along with an overall year-end review of how you are positioned going in to 2023. We believe the market will continue to be challenged in places but at the same time, there are some opportunities we have not seen in a very long time. Reach out to us to find out where the best opportunities may be for you.

Regards,

Tim

See Our Latest Thoughts on the Markets:
https://davis.stewardpartners.com/.6.htm

https://calendly.com/timdaviscfp

Timothy Davis, CFP®
Executive Managing Director – Wealth Manager
Partner
Davis Executive Wealth Management Group

Steward Partners Global Advisory
One International Place, Suite 3210
Boston, MA 02110
(Direct) 617-377-4418
(Office) 617-377-4422
(Toll Free) 888-371-0086
(Fax) 857-233-2966

t.davis@stewardpartners.com
http://www.davis.stewardpartners.com/
https://www.linkedin.com/company/timothy-davis-executive-wealth-management

***2019, 2020, 2021, 2022 Forbes Best-In-State Wealth Advisor**
https://www.forbes.com/profile/timothy-davis

All recognition award information can be found on Steward Partners' website at http://www.stewardpartners.com/recognition.34.html

https://www.forbes.com/best-in-state-wealth-advisors

Past performance is no guarantee of future results.

Bonds are subject to interest rate risk. When interest rates rise, bond prices fall; generally the longer a bond's maturity, the more sensitive it is to this risk. Bonds may also be subject to call risk, which is the risk that the issuer will redeem the debt at its option, fully or partially, before the scheduled maturity date. The market value of debt instruments may fluctuate, and proceeds from sales prior to maturity may be more or less than the amount originally invested or the maturity value due to changes in market conditions or changes in the credit quality of the issuer. Bonds are subject to the credit risk of the issuer. This is the risk that the issuer might be unable to make interest and/or principal payments on a timely basis. Bonds are also subject to reinvestment risk, which is the risk that principal and/or interest payments from a given investment may be reinvested at a lower interest rate.

Interest on municipal bonds is generally exempt from federal income tax. However, some bonds may be subject to the alternative minimum tax (AMT). Typically, state tax-exemption applies if securities are issued within one's state of residence and, local tax-exemption typically applies if securities are issued within one's city of residence. The tax exempt status of municipal securities may be changed by legislative process, which could affect their value and marketability.

Bonds are affected by a number of risks, including fluctuations in interest rates, credit risk and prepayment risk. In general, as prevailing interest rates rise, fixed income securities prices will fall. Bonds face credit risk if a decline in an issuer's credit rating, or creditworthiness, causes a bond's price to decline. Finally, bonds can be subject to prepayment risk. When interest rates fall, an issuer may choose to borrow money at a lower interest rate, while paying off its previously issued bonds. As a consequence, underlying bonds will lose the interest payments from the investment and will be forced to reinvest in a market where prevailing interest rates are lower than when the initial investment was made. **NOTE:** High yield bonds are subject to additional risks such as increased risk of default and greater volatility because of the lower credit quality of the issues.

CDs are insured by the FDIC, an independent agency of the U.S. Government, up to a maximum of $250,000 (including principal and accrued interest) for all deposits held in the same insurable capacity (e.g. individual account, joint account, IRA etc.) per CD depository. Investors are responsible for monitoring the total amount held with each CD depository. All deposits at a single depository held in the same insurable capacity will be aggregated for the purposes of the applicable FDIC insurance limit, including deposits (such as bank accounts) maintained directly with the depository and CDs of the depository.

For more information visit the FDIC website at www.fdic.gov.

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