



## OSBORNE PARTNERS

Capital Management, LLC

# Quarterly Wealth Report

April 2023, Issue 91

New San Francisco Address:

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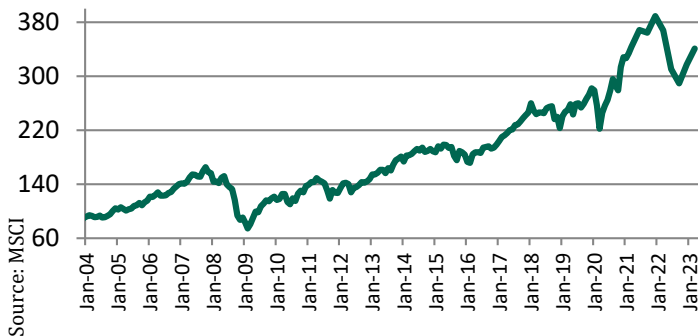
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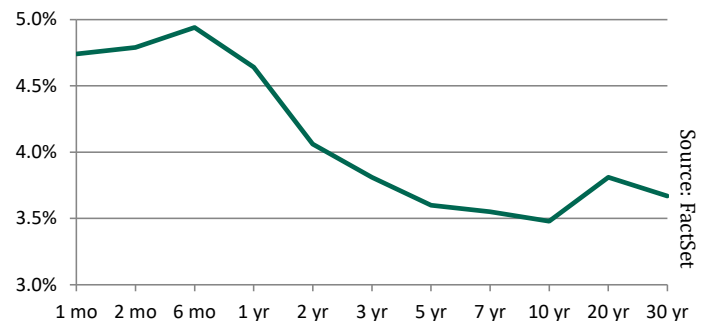
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MSCI World

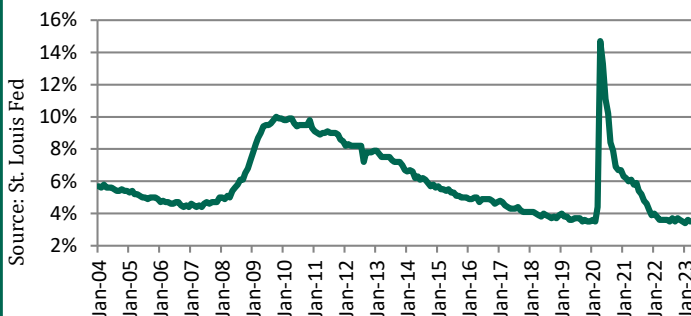


Treasury Yield Curve

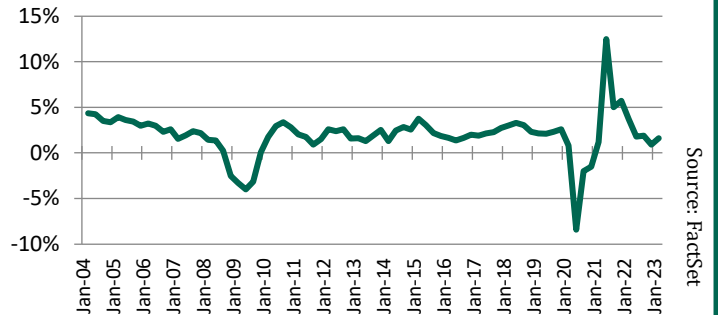


Global equities posted a positive return in the first quarter, while interest rates appear to be peaking.

Unemployment Rate



Real Gross Domestic Product (GDP)



Both unemployment and economic growth are low.

# Quarterly Wealth Report



## Now What?

By: Justin W. McNichols, CFA

*As the Fed approaches the end of the inflation fight, now what?*

In 2022, equity markets faced a major dilemma. Inflation had launched from core CPI of barely 1% to a level quickly approaching 7%. The economy was growing at a fast pace and corporate earnings estimates were seemingly ratcheting higher every week. Equity valuations were coming off of their 2021 peak at forward P/Es of 23.5x and 31.5x for the S&P 500 and Nasdaq 100 respectively. To fight the 30+ year high inflation and the overheating economy, the Federal Reserve Board was aggressively raising interest rates at a pace of 0.75% per **meeting** – nearly unprecedented.

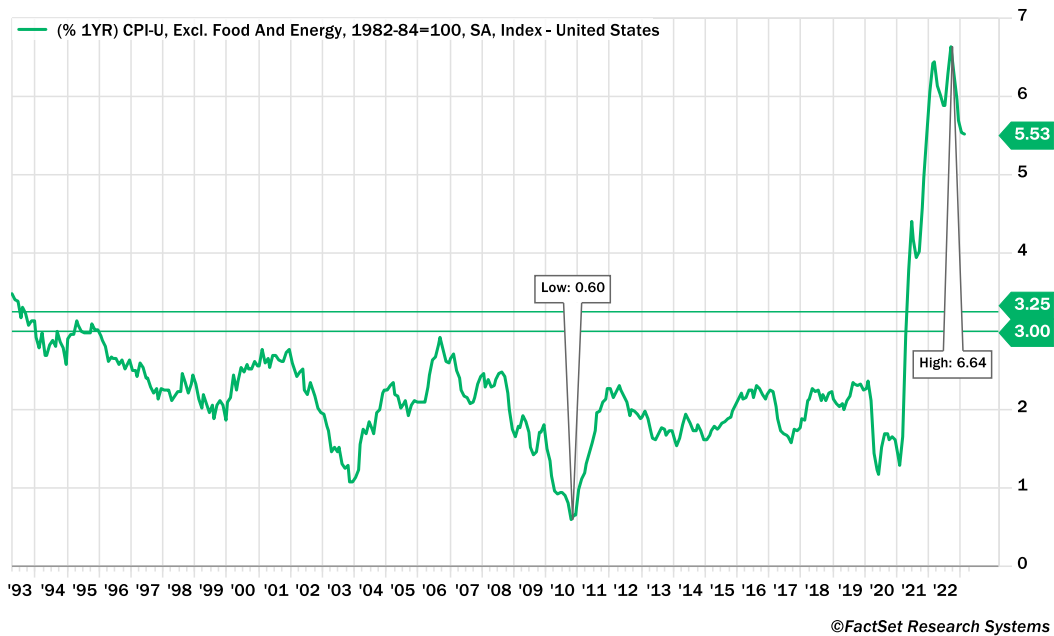
By the fall of 2022, the Fed had raised short-term interest rates from basically zero in the spring to 4.00%, including four increases of 0.75% in a row. The equity market response was decidedly negative, falling more than 20% and posting one of the worst returns in six decades. The Fed's goal through this environment? To achieve their stated mandates of full employment and price stability (low inflation)...with the additional goal of not torpedoing the economy into a recession.

Today the Fed Funds Rate stands at 5.00%. How is the Fed progressing on its goals and mandates?

### **Inflation:**

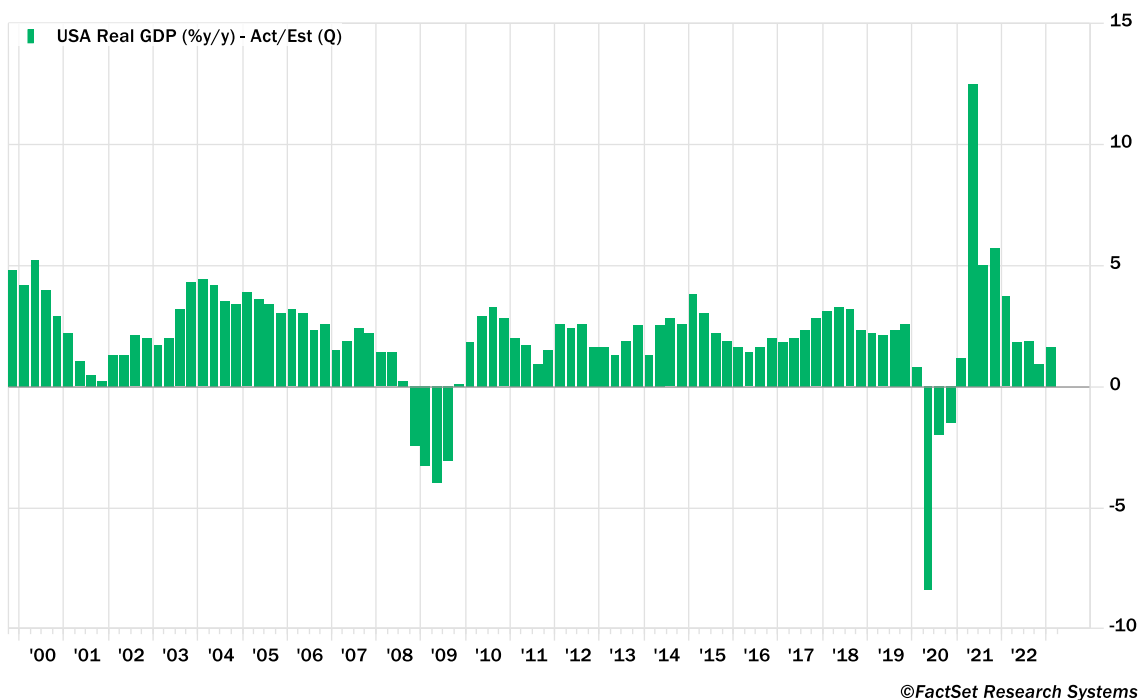
In early 2021, core CPI was slightly over 1%. By mid-2022, CPI was closing in on 7%. Inflation has recently started to normalize, dropping over 1% from the peak. It appears inflation is poised to fall further toward the sub-4% area. Longer-term, pricing for Treasury Inflation-Protected Securities (TIPS) points to an inflation expectation of mid-2% over the next 5 and 10 years. The Fed appears well on its way to achieving price stability.

## Now What?



## Growth:

In 2021, due to pent up demand from the global pandemic, GDP shot higher, piercing the 20-year record of 5% GDP growth. Growth was stubbornly high at the end of 2021 when the Fed started to raise interest rates. By the fourth quarter of 2022, GDP growth was under 1%. The first quarter of 2023 may print a growth rate just above 1%. The Fed has certainly slowed the economy, but the question remains if the Fed has merely slowed growth or if its rate increases are beginning to cause a recession.

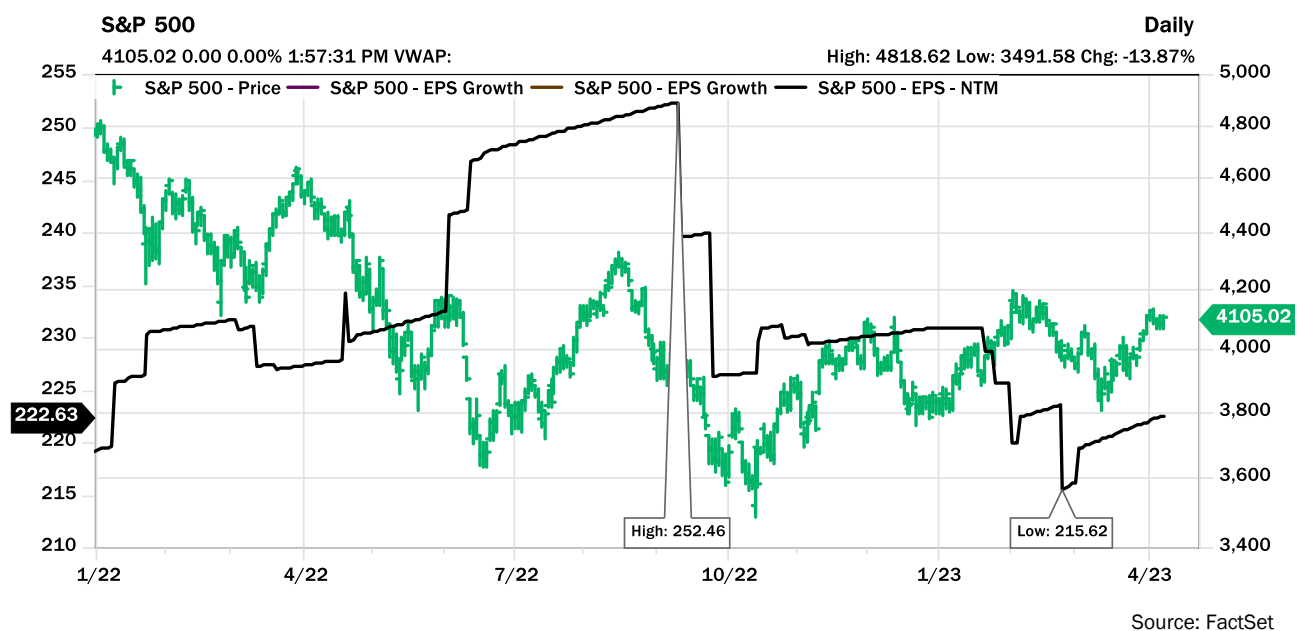


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## Now What?

### Earnings:

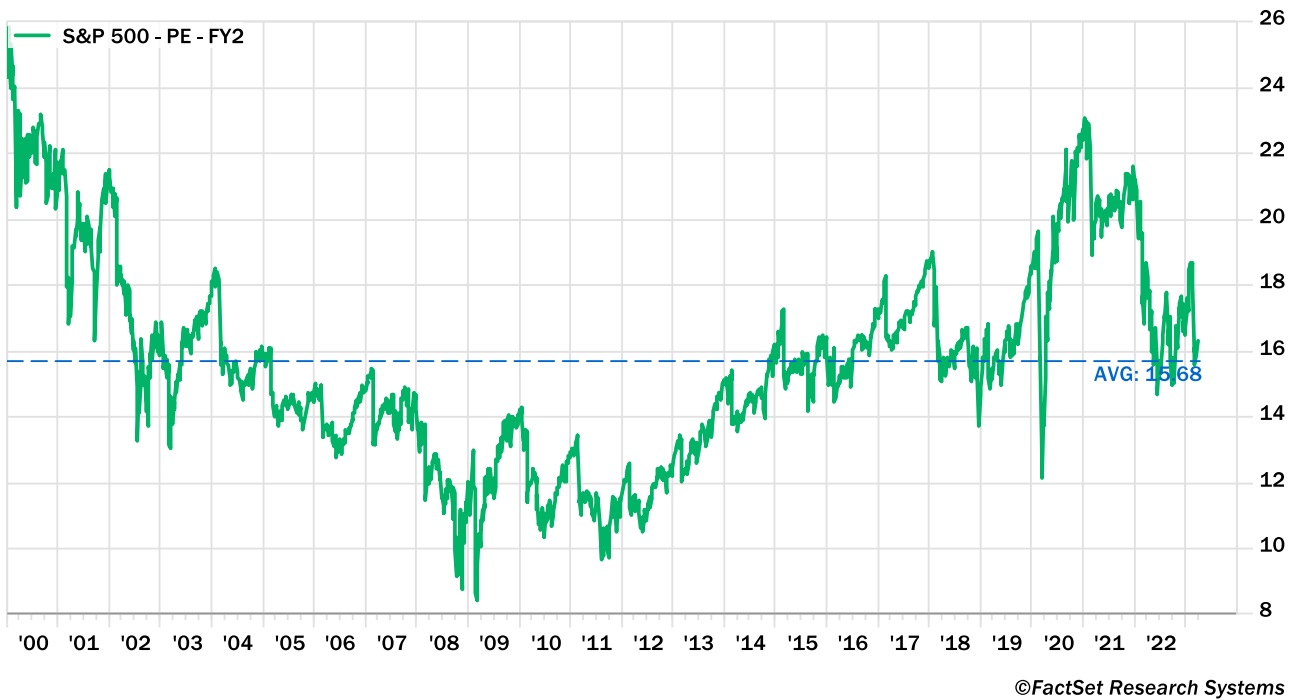
By the summer of 2022, earnings growth estimates for the next year-out had risen by over 15% from the start of the year. As the economy started to slow and the interest rate increases began affecting corporate fundamentals, earnings estimates began a downward revision cycle. Last month, future earnings estimates that once were \$252 per share for the S&P 500, hit \$215 per share, a negative revision of 15%. The interest rate increases have worked to slow corporate earnings growth.



### Valuation:

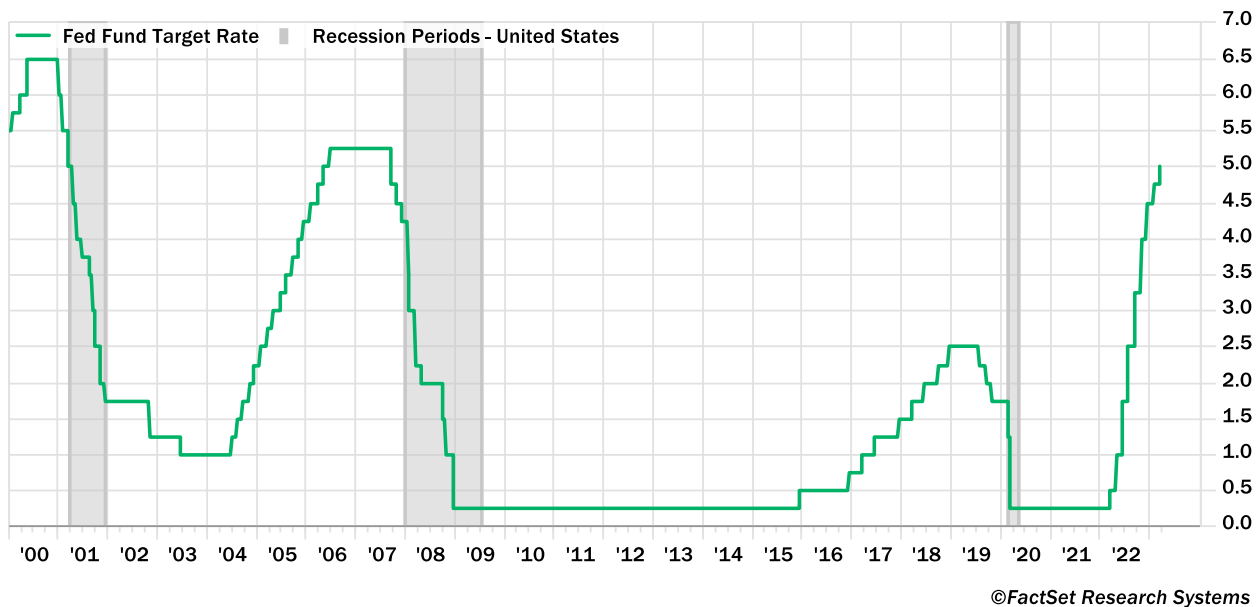
After reaching a high not seen since 2000, the S&P 500 two-year forward price to earnings ratio (P/E FY2) has normalized due to the 2022 bear market which reduced equity prices by over 20%. The S&P 500 is within 5% of the 20-year valuation average. Major valuation headwinds, seen just a year ago, have disappeared.

## Now What?



## Interest rates:

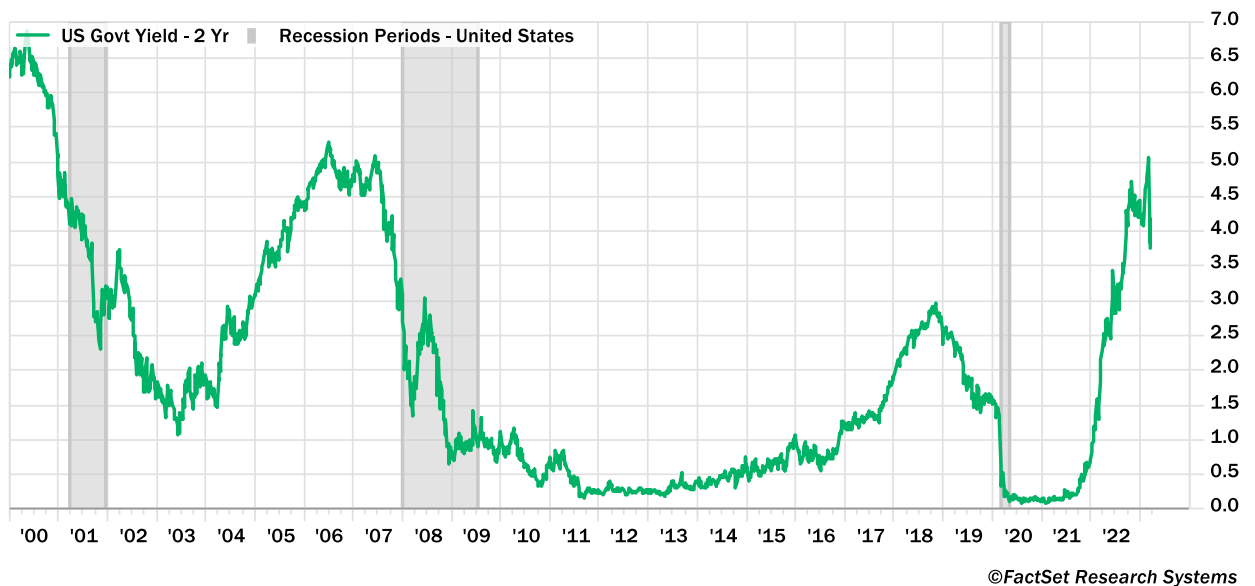
If the Fed raises the Fed Funds rate one more time, the rate will equal the 2006/2007 high of 5.25%. The Fed would have achieved this level in record time. Will this level be enough to tame inflation?



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## Now What?

Our work points to the 2-year U.S. Treasury yield as a strong indicator of the future path of the Fed Funds rate. Historically, we have found the 2-year yield rises with the Fed Funds rate and starts to roll over, or begins to fall, just prior to Fed Funds peaking. Recessions generally emerge when the 2-year yield falls steeply and continuously. Recently the 2-year yield touched 5%, matching the 2006/2007 peak area, then fell to around 3.7%. Seeing the 2-year normalize at lower levels would be welcome.



To summarize, the Fed raised short-term interest rates from nearly zero a year ago to 5.00% today to combat inflation which has now started to fall and is potentially headed toward sub-4%. Economic growth has slowed to a level of 1% year-over-year, below the long-term average of over 2%. The slowing economic growth has caused corporate earnings estimates to contract by 15% while last year's bear market reduced high valuations toward the long-term average. At the same time, interest rates overall may have peaked for this cycle.

## Now what?

The Fed certainly knows inflation overall is slowing but remains concerned that services inflation remains elevated. If both inflation measures continue to normalize, the Fed may cease the tightening cycle with one more increase to 5.25% on May 3<sup>rd</sup>. The result

## Now What?

of this tightening cycle may be a mild recession or an earnings recession where earnings growth is negative, but the economy does not contract meaningfully.

This scenario would affect our portfolio asset classes in varying ways. For example: For U.S. equities, corporate earnings estimates could bottom and start to rise over time. If interest rates gently glide lower, valuation upside would increase, especially in growth equities that tend to be valued on future earnings discounted (via the level of interest rates) to the present. Lower interest rates generally equate to higher valuation multiples.

In Fixed Income, the Investment Team purchased a large number of individual bonds on the interest rates spikes from late 2022 through 2023. Although lower interest rates in the future make bond yields less enticing versus other asset classes, we could see above average appreciation from the bonds purchased in 2022 and 2023.

In Natural Resources, while blindly buying a commodities index may not deliver outsized returns in the future, there continue to be sub-segments in natural resources where supply is scarce and demand is increasing. Finally, watch Foreign Equities closely. As much of the world exits the slowdown before the U.S. and the U.S. dollar may have peaked for the cycle in the fourth quarter of 2022, Foreign Equities, trading at over 30% discounts to the U.S., have quietly outperformed the U.S. since the October equity market lows. The ingredients could be assembled for a more extended period of Foreign Equities outperformance, just as most managers and individual investors are majorly underweight.

Thus far the Fed has achieved the goal of reducing inflation and slowing an overheating economy. Regardless of the policy path the Fed follows from here and the policy's lagged impact on inflation and growth, the Investment Team will use our style-agnostic approach within a diverse, robust asset allocation framework to guide your portfolio through all potential future environments. ■

## Quarterly Wealth Report



### The Banking Crisis: The Impact Beyond the Initial Failures

By: Jason Rodnick, CFA

*Rising interest rates and deposit outflows trigger a banking crisis. Explore the implications on credit growth, the tightening cycle, and the economy.*

The recent banking crisis, starting with Silicon Valley Bank's collapse in early March, could have widespread impacts on the markets and economy. The Federal Reserve's efforts to combat inflation through monetary tightening over the past year have fueled the crisis. The Fed has raised short-term rates from 0% to 5% since March 2022. Simultaneously, it has engaged in quantitative tightening, reducing its balance sheet size by selling bonds acquired during the pandemic, which has led to an increase in long-term interest rates as well. The rapid rise in interest rates has created a dual crisis for many banks, with significant unrealized losses on investments and funding challenges as depositors move their cash to larger banks or higher-yielding money market funds.

While the crisis' immediate consequences include Silicon Valley Bank's collapse and First Republic Bank's turmoil, its longer-term economic effects could be more widespread. We believe three key aspects help understand this crisis and its broader implications: the dual crisis affecting regional and smaller banks, the impact on credit growth and the economy, and the implications for the monetary tightening cycle, interest rates, and equity markets.

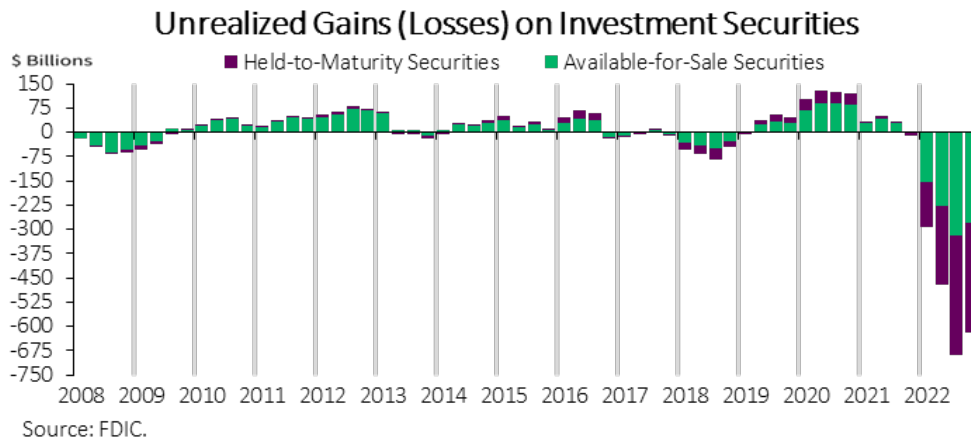
### The Dual Crisis:

As interest rates have moved higher, unrealized losses on bank balance sheets have ballooned to over \$600 billion. When a bank classifies loans (e.g., mortgages or commercial loans) or bonds it has bought (e.g., Treasuries or agency mortgage-backed securities) as available-for-sale or held to maturity, the bank doesn't have to recognize losses as the value of the loans fluctuate with interest rates (loan values have an inverse relationship to interest rates). Concerns about unrealized losses initially sparked fears at Silicon Valley Bank and then First Republic Bank.<sup>1</sup>

<sup>1</sup> See our recent article "A Crisis of Confidence" for more detailed explanation of the origins of the banking crisis. <https://osbornepartners.com/a-crisis-of-confidence/>

<sup>2</sup> Federal Deposit Insurance Corporation, "FDIC Quarterly, 2023, Volume 17, Number 1," FDIC, March 16, 2023. <https://www.fdic.gov/analysis/quarterly-banking-profile/fdic-quarterly/2023-vol17-1/fdic-v17n1-4q2022.pdf>

## The Banking Crisis: The Impact Beyond the Initial Failures



Under normal circumstances, unrealized losses on securities that a bank intends to hold until maturity are not an overwhelming concern. Due, in part, to stricter banking regulations in the aftermath of the 2008-2009 financial crises, banks are generally well-capitalized and maintain sufficient cash reserves to meet normal withdrawal requests. However, in the current environment, small and regional banks face growing withdrawals, possibly necessitating the liquidation of these investments to fund withdrawals and forcing these banks to realize losses. The realized losses could significantly impact the banks' financial stability or even their solvency. Customers with deposits exceeding the Federal Deposit Insurance Corporation's (FDIC) \$250,000 insurance limit are understandably nervous and moving their funds into the larger banks that are deemed "too big to fail." There is over \$17 trillion on deposit at more than 4,700 U.S. banks, and only about \$10 trillion of the deposits are insured. Within the subset of regional and local banks supervised by the FDIC, up to \$2 trillion of the \$3.4 trillion of deposits are uninsured.<sup>2</sup> The migration of deposits from smaller to larger banks may persist, worsening liquidity pressures with no easy solution.

Compounding the issue is that banks are also losing deposits to money market funds at an accelerating rate. Due to the rapid rise in interest rates, many banks don't have the ability to offer meaningful deposit rates. These banks are holding loans and investments acquired when rates were low, which are now paying interest well below current market rates. During previous rate hike cycles, the slower pace of Fed increases allowed banks to adjust their balance sheet assets as interest rates continued to rise. They could invest in higher-yielding investments as lower-yielding ones matured. During this

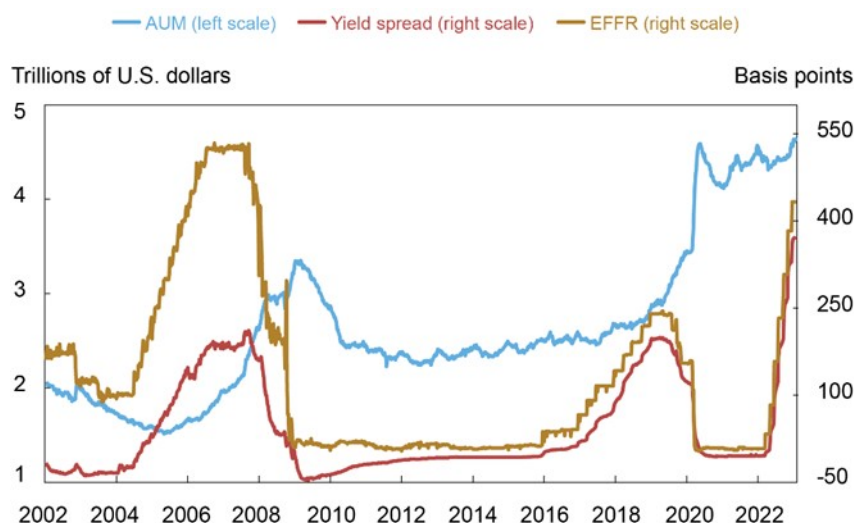
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## The Banking Crisis: The Impact Beyond the Initial Failures

cycle, such readjustment has not been possible. Banks are struggling to attract or retain deposits with higher yields, as a significantly large portion of their assets remain locked into low-yielding loans and investments.

Fundamentally, bank earnings come from the difference between the interest rate the bank pays depositors and the one it earns on its loans and investments – banks can not offer deposit rates higher than what they are themselves earning. This situation risks creating a negative feedback loop, threatening bank solvency: low deposit rates lead to slow, or negative, deposit flows, which then result in fewer or no new loans at current rates; banks, lacking higher-yielding assets, keep deposit rates low, and the cycle repeats. While different than Silicon Valley Bank's 24-hour bank run, this slow and persistent deposit outflow creates a major headwind for many smaller and regional banks.

The following chart vividly illustrates this dynamic. Assets invested in money market funds (blue line) have reached record highs as the spread, or difference, between the interest rates banks are offering and what is available in money market funds (red line) is at multi-decade highs. Money market funds invest in short-term bonds and Treasuries that pay yields close to the current effective Fed Funds Rate (EFFR – orange line).



Source: Sources: Federal Reserve Bank of St. Louis FRED database; RateWatch; iMoneyNet.

## Credit Growth:

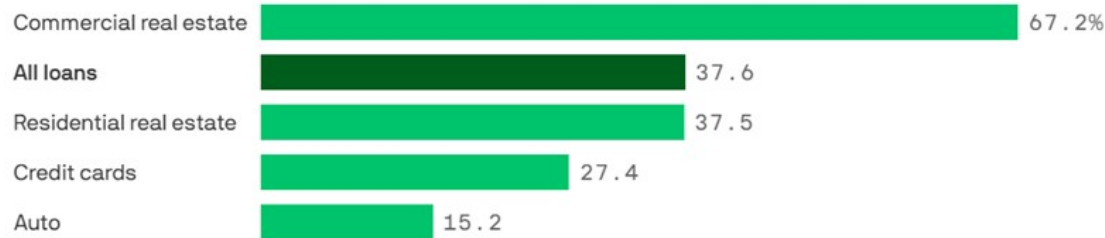
Small banks are the lifeblood of credit in several important areas of the economy, fueling the commercial real estate market (2/3 market share) and having a significant role

## The Banking Crisis: The Impact Beyond the Initial Failures

in the residential real estate and credit card markets. Deposits fund loans, so when deposits migrate out of small banks, these banks will fund fewer loans.

### Share of loans held by small domestic banks, by select sectors

Banks not in the top 25, by assets; As of March 8, 2023



Data: Federal Reserve; Chart: Axios Visuals

When banks extend credit, they provide households and businesses with the necessary funds to invest in new projects, acquire capital goods, or finance consumption. This, in turn, drives economic activity and creates jobs. For example, a business may borrow money from a bank to purchase new machinery, which increases its production capacity and allows it to hire more workers. Similarly, a consumer may borrow money to buy a house or car, which stimulates demand in those industries. If small and regional banks keep experiencing deposit outflows, they will have fewer funds to lend. This could result in tighter credit conditions, with less lending by banks, and create ripple effects throughout the economy.

### The Tightening Cycle:

The Fed's response to this crisis has been two-fold. On one hand, the Fed has introduced additional bank lending programs to reduce the stress on the banking system, such as allowing banks to borrow against some held-to-maturity securities without realizing losses. On the other hand, it now must contemplate how the crisis will impact its fight against inflation. In many ways, tightening credit conditions have a similar impact on the economy as the Fed raising interest rates. Federal Reserve Chairman Powell remarked at a recent press conference, "The events [banking crisis] of the last two weeks are likely to result in some tightening credit conditions for households and businesses and thereby weigh on demand, on the labor market, and on inflation. Such a tightening in financial conditions would work in the same direction as rate tightening."<sup>3</sup>

<sup>3</sup> Jerome Powell, FOMC press conference, Federal Reserve, Washington, D.C., March 22, 2023, <https://www.federalreserve.gov/mediacenter/files/FOMCpresconf20230322.pdf>

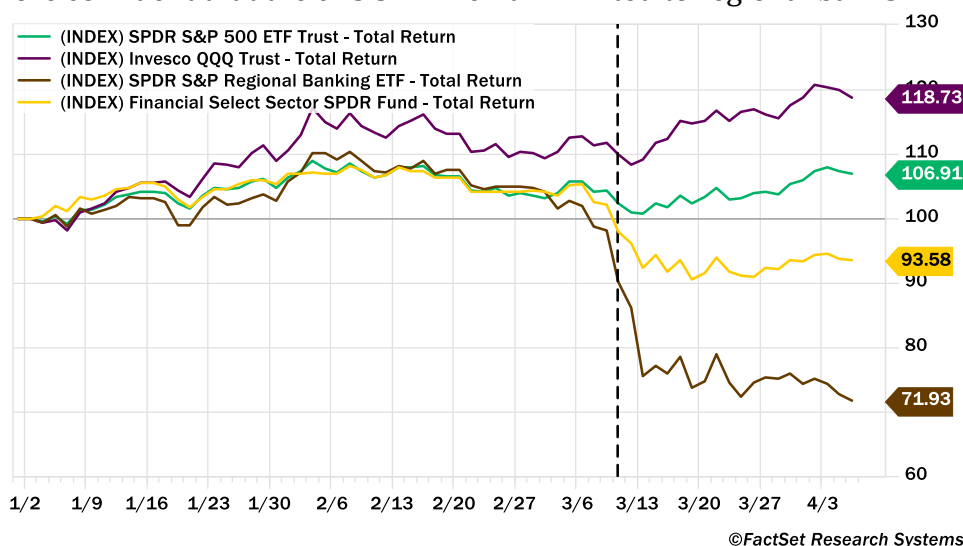
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## The Banking Crisis: The Impact Beyond the Initial Failures

The market concurs with Chairman Powell's view and anticipates the imminent end of monetary tightening. Before the failure of Silicon Valley Bank, market implied probabilities indicated that the Fed would continue raising rates through the second quarter and hold them above 5% through year-end. However, the market now expects the Fed to begin cutting rates as early as the third quarter and finish the year with short-term rates at 4% – 1% below current levels.

### Market and Economic Impact:

So far, it seems that the crisis is primarily affecting regional banks. The chart below shows the year-to-date performance of the S&P 500 (green line), the Nasdaq 100 Index (purple), the S&P 500 Financial Sector Index (yellow), and the S&P Regional Banking ETF (brown). After an initial decline at the beginning of the crisis (black dotted line), the S&P 500 and Nasdaq 100 have rallied as the market factors in the end of the tightening cycle and becomes more confident that the crisis will remain limited to regional banks.



The economic impact will require more time to unravel. With the potential for tighter credit conditions, the Federal Reserve now faces another complication in its fight against inflation. If the Fed overtightens by continuing to raise rates, it could exacerbate problems within the banking sector, potentially leading to contagion in the broader economy. However, if the Fed eases monetary conditions too soon, inflation may again begin to increase. The Osborne Partners Investment Team will continue to monitor the evolving situation, ready to adjust to changing market conditions, with our style-agnostic, flexible investment strategy focused on risk vs reward. ■



## Déjà Vu All Over Again

By: Karen McMillan, CFP®

*Declining confidence in banks and increasing interest rates: what can we do about it?*

It has been a while since investors have had to review the rules around FDIC and SIPC insurance, but that is not because of an absence of bank failures, but rather an absence of spectacular failure. While 2021 and 2022 both recorded zero bank failures, that was not the case for 2019 and 2020 - both years recorded four bank failures each. 2018 passed without any bank failures, but before that, consecutively from 2007 to 2017 there were bank failures each year. The scariest were the 325 bank failures in 2007 through 2010 when our whole economy was imploding.

Back in 2008, investors learned that FDIC insurance is critical, and furthermore, how quickly FDIC insurance pays out. People who had deposits protected by FDIC insurance were made whole in about four days after a bank failure.

**The Federal Deposit Insurance Corporation (FDIC)** is an independent U.S. government agency that provides insurance to depositors in case their bank fails. FDIC insurance covers up to \$250,000 per depositor, per ownership category, at each FDIC-insured bank. There are several ownership categories, the most common being an individual account, a joint account, certain retirement accounts, and beneficiaries of trust accounts. A person could be insured for well over \$250,000 in cash deposits at the same bank using these separate ownership categories.

To forestall the risk of a larger bank crisis, on March 12, 2023, the Secretary of the Treasury Janet Yellen, Federal Reserve Board Chair Jerome Powell, and FDIC Chairman Martin Gruenberg announced that all depositors at Signature Bank and Silicon Valley Bank would have access to all of their money, even amounts in excess of the FDIC insurance amount. That was an extraordinary action, and I would not expect it to be applied again in the future. Far better to review bank accounts and maintain balances below the FDIC insured amounts. The FDIC website calculator can be used to enter the bank name, the account titles and balances to obtain the applicable FDIC insurance amount.

<https://edie.fdic.gov/calculator.html>

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## Déjà Vu All Over Again

While FDIC insurance covers cash on deposit in banks, what about cash and securities at brokerage firms? Brokerage firms (such as Charles Schwab, TD Ameritrade and Pershing to name a few) are covered by **Securities Investor Protection Corporation insurance (SIPC)**. SIPC is a non-profit membership organization created by Congress in 1970 to protect investors from the loss of cash and securities that are held by brokerages in the event of failure or insolvency of the firm. SIPC insurance coverage generally extends to stocks, bonds, options, mutual funds and other securities. The maximum amount of protection provided by SIPC for each separate account is \$500,000, with a cash limit of \$250,000. Most brokerage firms maintain excess SIPC policies for investors with over the \$500,000 limit.

Unlike banks, it is exceedingly rare for brokerage firms to be unable to meet their financial obligations, and when they do, a buyer is generally found for the brokerage firm. However, in the Great Recession of 2008 – 2010 collapsing brokerage firms were not so exceedingly rare. Lehman Brothers went bankrupt, JP Morgan bought Bear Stearns when it collapsed, Bank of America bought Merrill Lynch forestalling a collapse, and Wachovia was purchased by Wells Fargo. But even with all of that turbulence, there were no losses of the various securities held in individual brokerage accounts, and no loss of cash covered under SIPC. Stocks and bonds held in brokerage accounts are not the property of the brokerage firm and remain the property of the account owner, even in the case of a brokerage firm bankruptcy.

### **So cash and brokerage accounts are safe; should any changes be made?**

As Jason Rodnick and Jack Fagan detailed in their articles this quarter, the bankruptcy of Silicon Valley Bank and the weakness in bank stocks were caused in part by the actions taken by the Federal Reserve to fight inflation. When interest rates start to rise it becomes more expensive for businesses and consumers to borrow money, which generally leads to lower spending and lower profits for companies. This slow-down should result in a reduction of inflation, and, as we saw throughout 2022, many sectors in the stock market are negatively affected when interest rates rise.

On the other hand, as interest rates have increased, it has become steadily more attractive to purchase bonds and other Fixed Income securities. Bonds purchased now carry

## Déjà Vu All Over Again

higher interest rates than they have for several years, and those higher rates will continue through the maturity of the purchased bonds. Finally, it is even possible to get interest on the three to six months of living expenses that are recommended to be tucked away as a cash reserve.

**Inflation and rising interest rates suggest a review** not only of the amounts and locations of cash deposits, but also a review of the cost of any debt. Low fixed-rate debt is generally advantageous to continue to carry, while prioritizing paying off high-interest debt such as credit card balances and other floating rate loans, such as home equity lines of credit.

**The most important rule when it comes to investing in a rising interest rate environment is the same as investing in other economic market conditions: be *diversified*.** Your well-diversified Osborne Partners managed investment portfolio can help to mitigate the risks associated with rising interest rates by being invested in a variety of asset classes, including alternative investments, real estate and natural resources, making your portfolio well-positioned to participate in stock market gains when interest rates peak and ultimately begin to decline.

It can be challenging to remain confident of your overall financial situation in the face of the worrisome economic and geopolitical news that we are bombarded with on almost a daily basis. Your Osborne Partners Wealth Counselors are available to review your portfolio and especially your long-term financial plan with you. Financial plans anticipate that some years will be good and others bad, and it is generally reassuring to see that even with the stock market volatility, rising interest rates, inflation and war, **most financial plans continue to be on-track, providing for targeted goals and objectives.** ■

## Quarterly Wealth Report



### Fixed Income and Credit: Never a Dull Moment at the End of a Cycle

By: Jack Fagan, CFA

*The next phase of the Fed's monetary policy campaign must make room for an unexpected running mate: financial stability concerns. In the background, inflation remains at large.*

After a forgettable 2022, a year that accomplished the worst 12-month performance on record, U.S. Fixed Income markets were set to return to something of a more placid environment in 2023. The Federal Reserve was still clearly in hiking mode, yes, but there was light at the end of the tunnel. Entering 2023, the Federal Funds Rate stood at 4.50% and the December 'Dot Plot' indicated a peak Fed Funds rate of 5.25%, implying just 0.75% more tightening before the cycle would be complete. Treasury yields were the highest they have been in many years with the 2-year yield (4.42%) the highest since 2007 and the 10-year yield (3.88%) since 2008. Of course, the reason for the Fed's rapid tightening cycle was to rein in the uncomfortably high levels of inflation experienced across the economy. Core CPI (consumer price index) reached a 40-year high in September 2022 and the data continued to post elevated, yet moderating, inflation rates through the end of the year.

As we moved into the first quarter of 2023, the focus was on two related questions: 1) how fast would the pace of inflation decelerate, also termed *disinflation*, and 2) how high would the Fed Funds rate need to go before the Fed paused hiking? Straight forward enough, right? Faster disinflation would mean fewer hikes and/or a shorter period until pause. Slower disinflation or reacceleration – perish the thought – would mean a prolonged hiking cycle.

Turns out, it wasn't quite that simple.

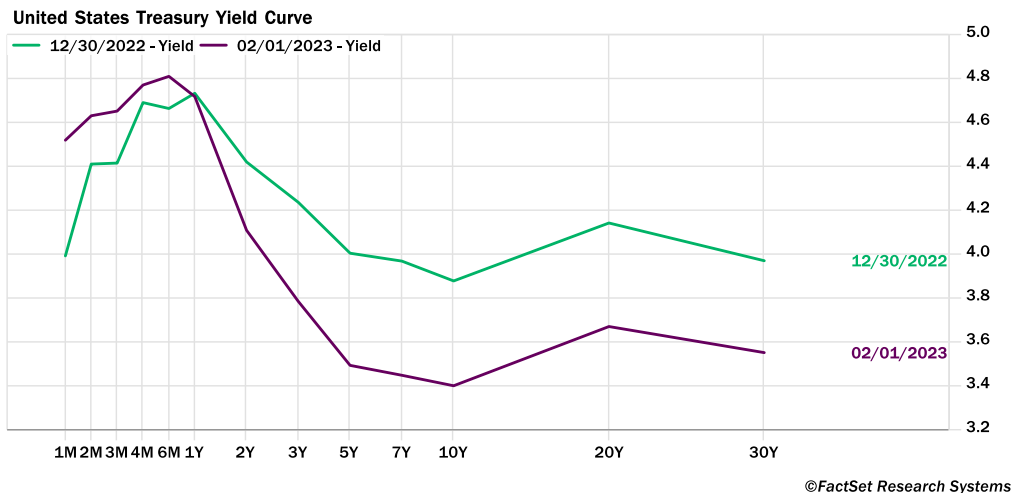
While we may in fact have reached the end of the hike cycle, as hoped for, it was not for the conventional reasons expected at the start of the year. To take a closer look we can view Q1 through the lens of two distinct periods, before and after the Silicon Valley Bank saga.

### Pre-Silicon Valley Bank Failure

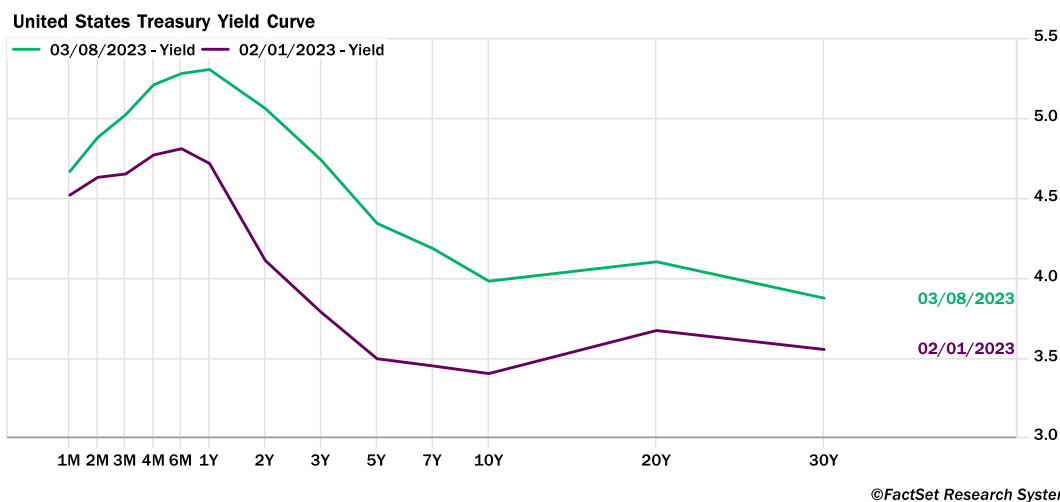
After three months of sequentially improving data, core PCE (personal consumption expenditures), one of the Fed's preferred inflation measures, hit 4.6% in January, the lowest in 15 months. Five days later the Fed hiked rates again but notably decelerated the hike to

## Fixed Income and Credit: Never a Dull Moment at the End of a Cycle

just 0.25%. It seemed as though the disinflation process was in full swing. The immediate aftermath saw equity and interest rate markets rally in unison with U.S. yields entering February lower for the year between ~0.35%-0.50% across the curve.



Then, entering February, strong economic data continued to roll in upending the simple disinflation narrative. An outstanding jobs report in early February triggered a rebound in yields. Later in the month, inflation data broke the three-month streak of lower readings, disrupting the hope for a gradual path toward the Fed's 2.0% inflation target. Rates steadily marched higher over the month of February with 2-year yields reinflating a full 1.00% (100bps!), highlighting the market's capitulation that the Fed would pause then cut rates in short order. In the first week of March, attempting to demonstrate his determination to defeat inflation, Chairman Powell even indicated the possibility of returning to 0.50% rate hikes. Other Fed Presidents reiterated their preference for a terminal rate as high as 5.75% or even 6%. The March 8th yield curve reflects accordingly.



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As it turned out, the first week of March would be the year-to-date high for rates with the 10-year Treasury peaking at ~4.10% and the 2-year just above 5%.

Enter the Silicon Valley Bank debacle.

### Post-Silicon Valley Bank Failure

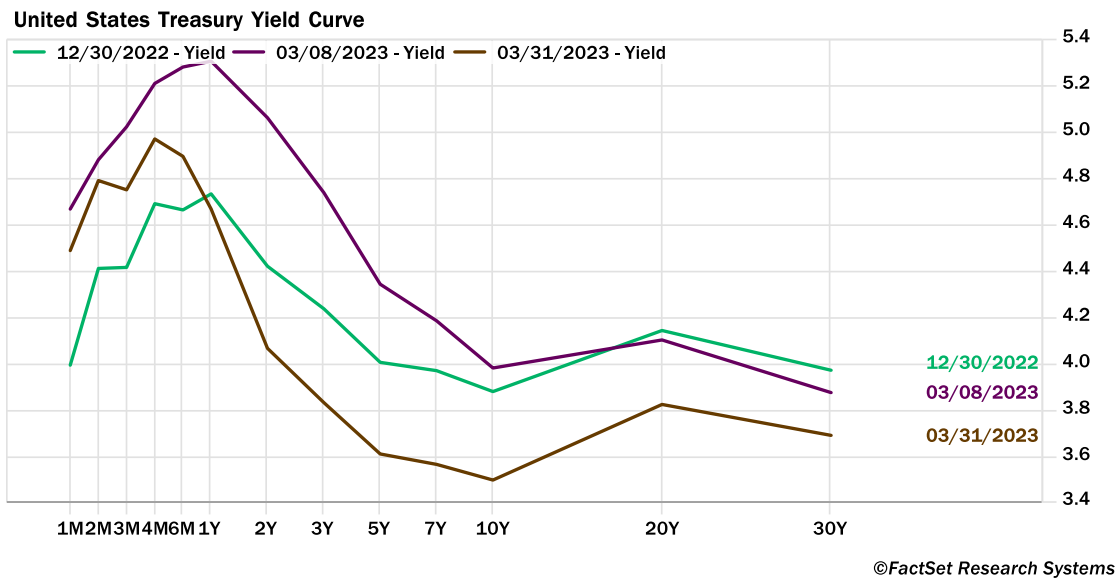
Skipping over the details of the first bank run of the social media era, a subject further investigated by Jason Rodnick in this Wealth Report, the impact on rates and monetary policy is considerable. In a matter of days, the banking panic sparked a flight to quality and Treasury yields plummeted in response. Yields on the 10-year fell as much as 0.70% over the course of a few weeks, with most of the rally occurring in the immediate aftermath of the collapse of SVB.

Of the many impacts of the situation, some highlights include:

- Fixed Income volatility spiked to the highest since 2009 (measured by the ICE MOVE Index).
- High Yield spreads widened over 1% in a week, from ~4% to as high as 5.2% in late March.
- The 2-year Treasury yield experienced the greatest drop, falling ~1.30% from over 5% to ~3.75% in three weeks, indicative of the market expectations for impending rate cuts.

The aftermath of the Silicon Valley Bank saga culminated with the FOMC meeting on March 28th. At that meeting, against many calls for a pause to avoid further stress to the banking system, the Fed chose a 'dovish hike' of 0.25%. Hiking the Fed Funds rate, to an upper bound of 5.00%, in the face of such a challenging environment signaled a willingness to continue the fight against inflation although softer language invited a new sense of caution, and perhaps patience, as the stresses of the rapid hike cycle come to bear. Powell and the Fed could no longer take a whatever-it-takes approach to beating inflation despite the fact that inflation remains several percentage points above target. The financial stability concerns of such a rapid rate hike campaign, although always in the 'conversation' in a hypothetical sense, have come to the forefront.

## Fixed Income and Credit: Never a Dull Moment at the End of a Cycle



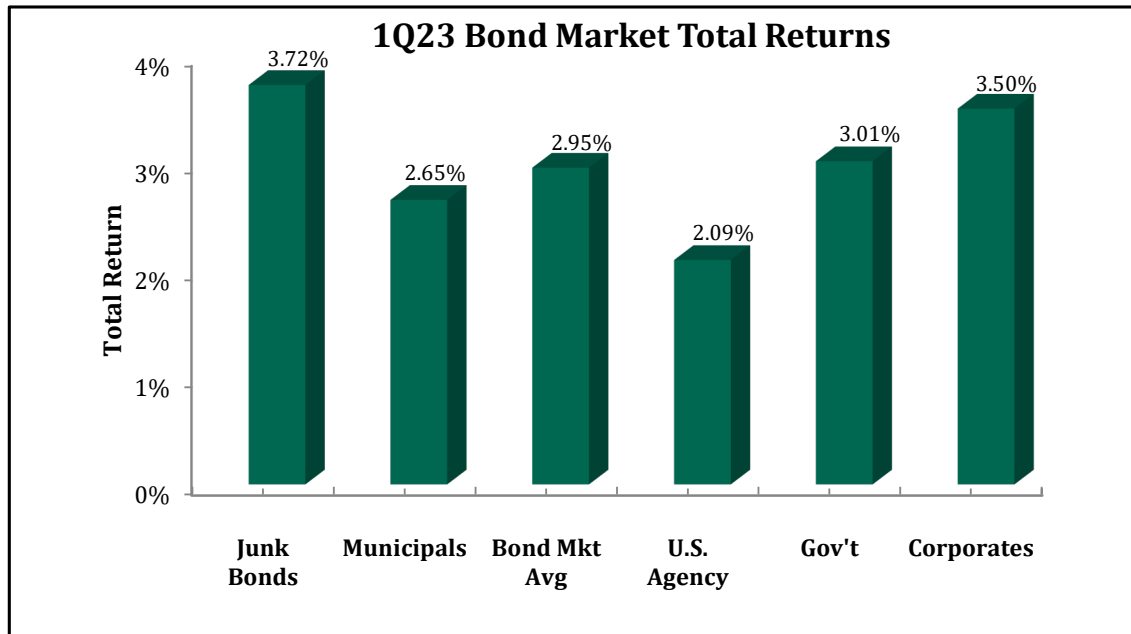
### Looking Ahead

Moving forward, uncertainty remains ever-present – although that’s nothing new. The duration of the hike cycle is again in question with the market pricing in as many as three rate cuts by year end, despite the Dot Plot reiterating a 5.125% median Fed Funds rate. The differential is uncomfortably wide. The market is currently split ~50/50 as to the outcome of the next FOMC meeting on May 3<sup>rd</sup>. A hike would demonstrate the fight against inflation remains paramount, while a pause would usher in the end of a remarkable, albeit short, era of monetary policy.

As the world tries to figure out the exact path of monetary policy, a fool’s errand to be sure, it’s important to remember the purpose of the Fixed Income asset class for long-term investors: Income and Capital Preservation. While this latest banking crisis episode did result in some losses and more credit downgrades, it is important to keep perspective. High quality, non-financial investment grade bonds remained very resilient through the quarter, as overall corporate credit spreads widened only modestly and already have recaptured some of the initial change. In fact, the fall in Treasury yields caused price *appreciation* for many bond issues. The Osborne Investment Team will continue our focus on buying and holding high quality bonds in the context of a well-rounded portfolio, and seek yield without compromising on credit quality. ■

# Quarterly Wealth Report

## Fixed Income and Credit: Never a Dull Moment at the End of a Cycle



| Bond Market Yields 3/31/2023         |       |   |       |
|--------------------------------------|-------|---|-------|
| Average Money Market Fund            | 0.23% | 10 Yr. AAA Muni Bond                    | 2.28% |
| 5 Yr. AAA Muni Bond                  | 2.23% | 10 Yr. AA Corporate Bond—Long Term      | 4.27% |
| 5 Yr. AA Corporate Bond—Intermediate | 4.13% | 10 Yr. U.S. Treasury                    | 3.47% |
|                                      |       | 30 Yr. Fixed Rate Mortgage (Conforming) | 6.88% |

Source: Bankrate.com

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