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Jane Doe
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Dear Jane,

Greetings from your BLUEPRINT team at DA Davidson, where we are all hoping for a little friendlier new year. You won't find many investors feeling sad saying goodbye to 2022, one of the more challenging periods in memory. You know it's tough when one of the best performing asset classes was T-bills. It wasn't hard to name things that were down 50%, 60% and even 70% this past year, think Tesla and bitcoin! There were few places to hide, as even the average supposedly safe bond fund was down almost 15%[1]. For those of you who have been with us for a while, you likely noticed our normal pattern. We tend to lose some ground to the "averages" when markets are up strongly and tend to make up a little ground when markets are falling sharply. If it's excitement you are seeking from your investment portfolio, we are probably not your cup of tea. When you get your more detailed report shortly, you'll see that we certainly weren't unscathed, but we faired a little better than most. I suppose some of our less generous readers might remind us that "you can't eat relative performance".

So what's our best guess on the outlook from here? There's a well-regarded (seasoned) investor by the name of Howard Marks who recently wrote a long missive titled "sea change", where he detailed what he sees as a very substantial shift in the investment landscape. One that he believes will likely not reward investors at the same rate as the previous couple of decades. Over the last year or two, Susan has been steering down our return expectations in our meetings and conference calls with clients. For several decades, we have generally enjoyed a period of low inflation and falling interest rates. This came to an end in 2022 with a fairly significant inflation shock followed by a rather dramatic rise in interest rates. We think that the friendly tail winds that have been with us for some time now seem to have changed to more substantial head winds. As a result, we have been taking steps to inoculate ourselves from permanent loss of capital, by paying extra careful attention to the balance sheet of the companies we own or seek to own. Ryan tracks these things closely in an attempt to avoid nasty surprises. Of course, that doesn't mean that our holdings will be immune from declining in an economic slowdown, we simply have faith they can "weather a storm." In addition, we have been building up cash and putting much of it to work in shorter term CDs and T-Bills, currently yielding between 4 1/2%[2] and 5%[2]. We like having a little extra cash and short term bonds, as we diligently try to avoid having to be a forced seller of our stocks for withdrawals during market swoons. In addition we should have some "dry powder" to take advantage of opportunities as they arise. Of course, investing is far from a pure science and it's always difficult to know how much potential bad or good news is already baked into current stock/bond prices. I think it was some Nobel physicist who once said something like "imagine how hard our jobs would be if electrons had emotions". Welcome to our world!

During the financial crisis of 2008, the Federal Reserve dramatically lowered interest rates in an attempt to avoid an even more widespread crisis. Many debated the wisdom of this policy, but as some wise person pointed out, when your neighbor's house is burning down, you don't debate how his carelessness might have led to the fire, you simply work to put it out, because if you don't, your house is probably next. This Federal

Reserve playbook was pulled out again during the pandemic in 2020, when interest rates were essentially lowered to zero. Remarkably, the economy didn't fall off a cliff and the stock market, after a short lived decline, soared to new heights. I'm afraid all this monetary and fiscal stimulus, leading to rock-bottom interest rates, has conditioned people to become complacent about debt, both at the personal and government levels, and to forget that excess leverage always creates substantial risk. I suspect a little fear of the downside is probably healthy. Likely much better than FOMO (fear of missing out). And speaking of borrowing, interest on the government debt is estimated to reach 10%[3] of the total budget in the next several years. We don't know the actual effect that a possible doubling of this interest might have, but it's safe to say that it won't be good. We certainly aren't predicting Armageddon, but we are expecting a rather difficult transition, where those that have been taking on excess risk are reminded of the downside of such behavior. What's that great line, when the tide goes out, you see who's swimming naked?

In reading this over, we hope we aren't painting an overly negative picture and there are things such as inflation showing signs of easing that have us more hopeful for 2023. Living through volatile emotional markets can be a bit stressful, it can also be a time of great opportunity. While Napoleon is no one's favorite, he did know a little something about the emotional effects of fear, and perhaps greed. He defined a military genius as: "The man who can do the average thing when everyone else around him is losing his mind." Fortunately, we have a solid team, to support each other when one of us might be showing signs of panic!

Finally, a special thanks for those of you who included us in the mailing of your yearend "holiday letters". Some of them even included pictures! It's kind of fun for us to put faces on some of the people in your lives that you've often mentioned to us. This work can sometimes be quite challenging, humbling and a little stressful, but it can also be very rewarding. Especially when we feel like we might have a small positive impact on our client's lives. Please feel free to contact us if you have questions about any of this, or just want to check in and catch up.

Regards,

Russ and your Blueprint Team: Susan, Ryan, Jennifer, Sasha and Tien

1 www.morningstar.com/articles/1131213/just-how-bad-was-2022s-stock-and-bond-market-performance

2 https://www.wsj.com/market-data/bonds

3 https://www.thebalancemoney.com/interest-on-the-national-debt-4119024