Stirling Bridge
Wealth Partners, LLC

MARKET COMMENTARY – March 1, 2022

… your Quest stands on the edge of a knife. Stray but a little and it will fail, to the ruin of all. Yet hope remains while all the Company is true.
~ J.R.R. Tolkien

As if we all have not had enough worries over the previous two years, the entire world is now forced to dance upon the narrow blade of a knife in response to Russia's invasion of Ukraine. Respond without sufficient force (economic or otherwise) and this type of behavior by totalitarians is encouraged and may spread. Respond with immediate, punishing force and we might truly find ourselves embroiled in a conflict with unspeakable implications.

Prior to these events, we had been diligent in conveying our thoughts on what was to be a continuation of the economic recovery, peaking of inflation, and a normalization of interest rate policy. As it was, the path for optimal monetary policy was narrow. This war will only complicate things. Some of our calls may still occur and our leadership may find the footing necessary to safely tread the fine edge. However, the risk (i.e. the range of possibilities) has widened substantially. What follow are updates based upon the framework in the geopolitical email sent out last week.

<u>Inflation</u>: For energy, food, metals, and a host of other goods, a broadening conflict could mean a negative feedback loop for inflation becomes embedded in pricing. Militaries demand goods. Supply lines get messed up further or diverted or halted. Prices increase to compensate.

But as we mentioned in last week's email, making predictions in this case is not so simple. A contained, though sustained, conflict could divert resources away from what was the recovery, slowing growth and therefore acting as a brake on additional inflation.

While we need more data, <u>we are now leaning toward the inflationary outcome</u>.

<u>Interest Rates</u>: Our Federal Reserve generally acts in prudent fashion. We expect that to continue. And so, with the backdrop of an improving domestic economy and the threat of sticky inflation, we foresee an interest rate increase of ¼ percent at the March meeting. This is different from what we suggested at the outbreak of war, mere days ago, when we considered the possibility of no rate change. Barring catastrophe, we then expect them to march rates higher at least until inflation is past its inflexion point.

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<u>Bonds</u>: We reiterate that bonds remain important holdings. They certainly provide an anchor for portfolios during troubled times. However, given our revised outlook for rates, we suggest steadily shortening bond duration. And while we generally invest in what should be considered a core bond portfolio anyway, a decided tilt toward quality may be in order in some cases as well.

<u>Commodities</u>: We aim to use them sparingly via ETFs. However, since commodities by themselves produce no cash flow (unlike businesses or bonds), they are exceptionally difficult to own for the long term. Some folks ask about commodity-oriented companies such as gold miners or oil drillers. We will use them. But we should know going in that these types of investments are far more correlated with other companies than with the underlying commodity they may produce.

<u>Stocks</u>: Owning a set of companies remains the best way to grow wealth – over the long haul. But there are times when it may not feel that way. At the end of last year and the beginning of this year, we projected that we might have to suffer through six months of difficult markets due to shifting rates. As this conflict looks to become entrenched, risk has increased.

Remember, as investors we look to optimize the risk we take for the return we expect. We do not expect to *eliminate* risk. To do so would mean eliminating the prospect of returns. Yet, in light of the unfolding situation, it is prudent to begin to get portfolios' equity allocations back down to their long run targets. To the extent accounts are heavy in stocks, expect us to make the shifts in opportunistic ways over the coming weeks.

To be clear, we are not eliminating stocks in any wholesale manner or making any suggestion like that. After several years of being overweighted to stocks, we are simply pulling in the risk to the long run targets.

In closing, let us then pray for this situation. And in the words of Tolkien above, let us carry hope that the company of nations of which we are members remains true.

Stirling Bridge Wealth Partners, LLC is fortunate to count many of you as clients. In the good times and bad, we remain committed to providing customized investment solutions and robust financial planning wrapped in a package of exceptional service. We thank each of you for your dedication to us and for your trust.

Sincerely
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