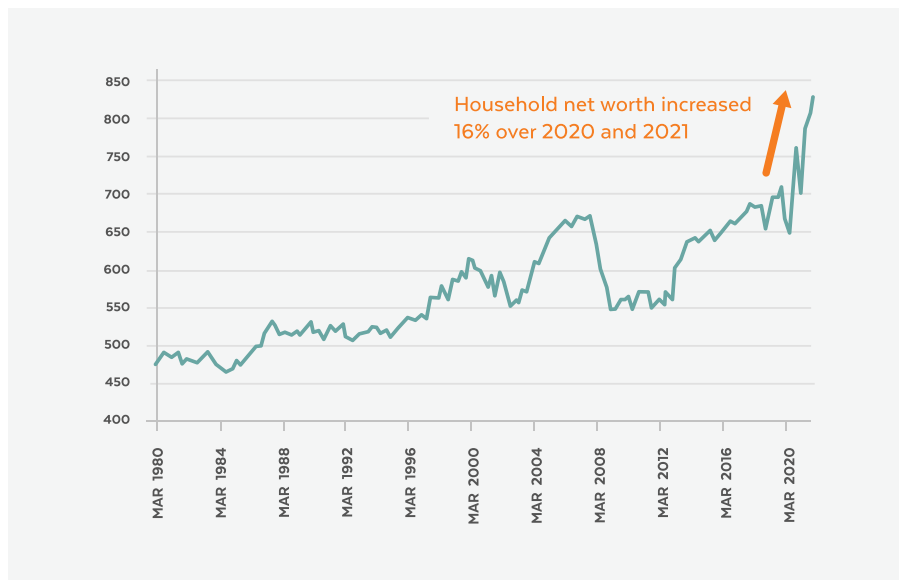


Dear Friend,

July 14, 2022

A flood of monetary and fiscal stimulus—coupled with historically high corporate profit margins—generated outsized gains in stocks from the bottom of the Covid-19 bear market through the end of last year. Low interest rates and a rapid shift to remote work also pushed U.S. housing prices up by 30+% over the same period. Reflecting back on the last three years, owning a home and staying invested in equity markets meant capturing a significant appreciation in overall wealth.

U.S. HOUSEHOLD NET WORTH AS A % OF DISPOSABLE PERSONAL INCOME, EOP %



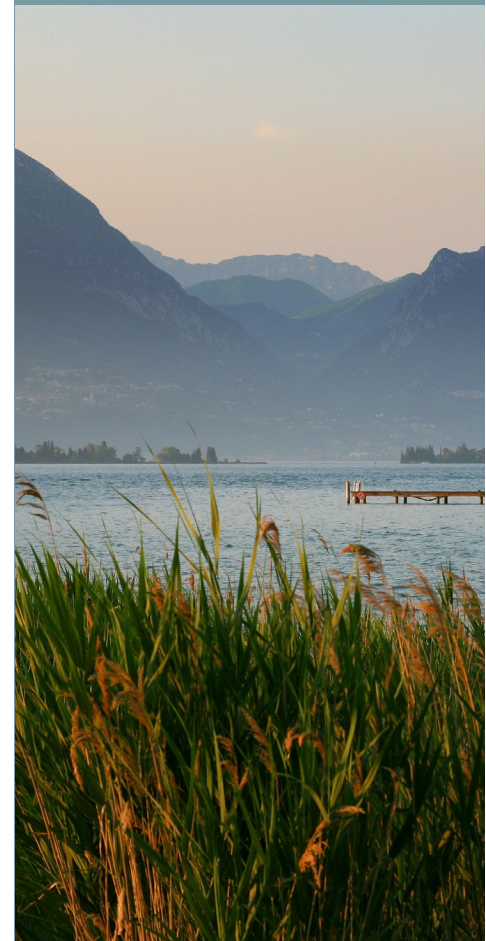
Source: KKR Global Institute

While equity markets have corrected sharply in the current calendar year, the current drawdown is still fractional relative to the 3-year 90%+ cumulative run-up in the S&P 500 index. And importantly, because earnings, dividends and corporate buybacks continue to increase on a long-term basis, the case for equities for the long-run remains firmly in place. As ever, Private Wealth Partners will continue to initiate/add to positions when valuations are compelling.

Though this period of wealth creation has been historic, the era of ‘easy money’ is fading for now. With the Federal Reserve shifting into hawkish monetary policy and fiscal stimulus long gone, stocks have undergone a rapid adjustment to the altered environment. In the housing market,

“Uncertainty actually is the friend of the buyer of long-term values.”

- WARREN BUFFETT



PRIVATE WEALTH
PARTNERS, LLC

591 Redwood Highway
Suite 3210
Mill Valley, CA 94941
Tel: 415. 461. 3850
<http://www.pwpart.com>

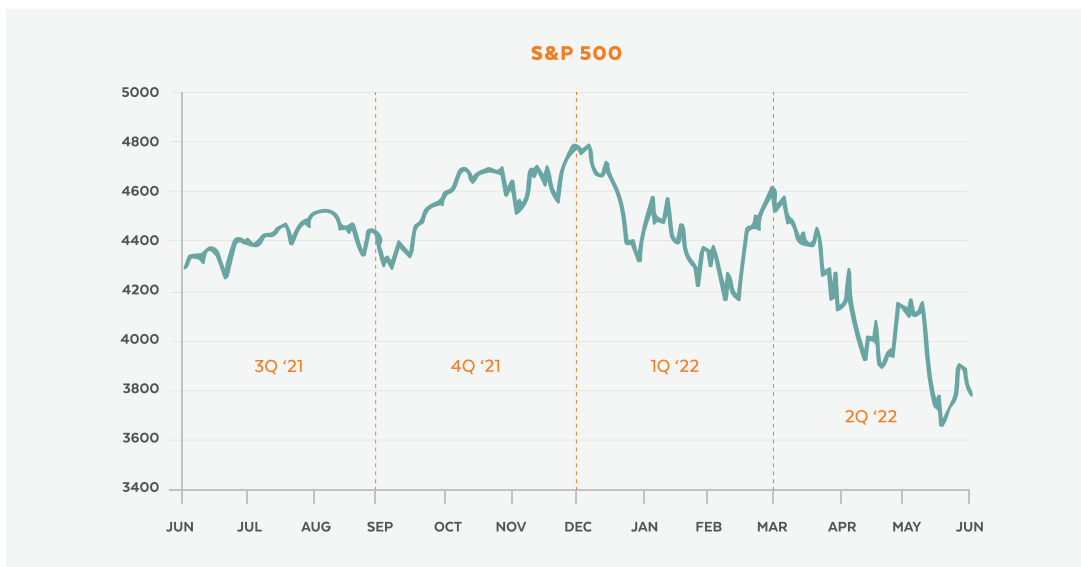


fundamentals remain strong as inventories are historically tight and millennials—many of which are first-time homebuyers—now comprise the largest demographic in the U.S. But rising mortgage rates have started to temper demand, and it seems likely that the pace of home price increases will almost certainly moderate.

Repricing in the stock market happened very quickly. U.S. stocks suffered their second worst start to a year in history, with the S&P 500 index declining by -20% and falling into bear market territory. A little perspective is needed here because the stock market formed its peak within a single trading day of the start of the new year, creating a year-to-date performance figure that looks worse than usual. Even with the sharp drawdown in the first 6 months, U.S. stocks are still +28.75% (price return) higher than they were on June 30, 2019—just 3 years ago.

The worst performing sector year-to-date has been Consumer Discretionary (-30.2%), likely in response to consumers slowly, but surely, pulling back on spending due to stubbornly high food, gas, and housing prices absorbing a growing percentage of disposable income.

THE S&P 500 INDEX OVER THE PAST 12 MONTHS



Source: Strategas Research

Bonds did not offer much respite in the first half of the year either. The yield on the 10-year U.S. Treasury more than doubled from 1.44% to 2.98% in the first six months, which ultimately meant that a 60% stocks/40% bonds portfolio did not perform much better than an all-equity portfolio. Such a tight correlation between bonds and stocks is rare.

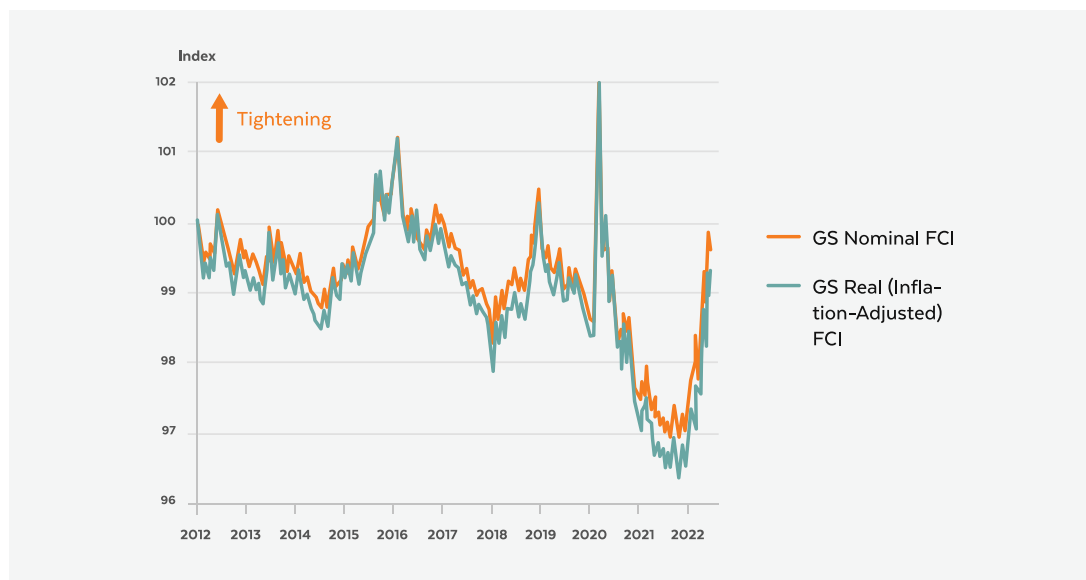
All told, it has been a very strange two-year period for asset prices, the global economy, and life in general. Demand for goods and services has been distorted by a flood of easy money and pandemic-related restrictions, while the supply of goods and services has been mired by



lockdowns, rising costs of labor and raw materials, snarled supply chains, and geopolitical crises. Unsurprisingly, U.S. and global monetary/fiscal policy has not been effective at re-establishing a supply/demand equilibrium, and the end result has been soaring inflation.

The Federal Reserve is now trying to address the issue. Since the central bank has no control over the supply of goods and services, they are aggressively targeting the demand side of the equation by raising interest rates and shrinking their balance sheet at a rapid clip. As seen on the chart, a key feature of 2022 has been sharply tightening financial conditions, which helps explain the concurrent downdraft in equity markets.

GS U.S. FINANCIAL CONDITIONS INDICES



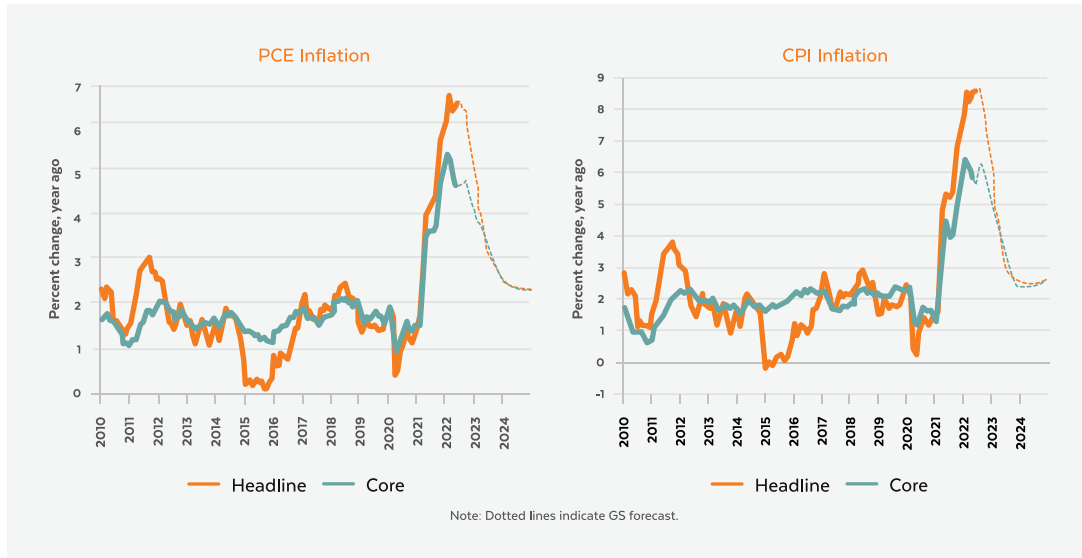
Source: Goldman Sachs

Whether or not inflation starts to moderate in future months is a key question not only for policymakers but also for equity market investors. If inflation pressures begin to subside in the second half of the year, it could remove pressure from the Federal Reserve to tighten monetary policy so aggressively, which could provide some relief to equity markets. This outcome would seem highly likely were it not for the ongoing war in Ukraine combined with China's unpredictability when it comes to "zero-Covid" and lockdowns—both of which add substantial uncertainty to supply/demand dynamics in the global economy.

Markets appear, for now, to be wagering that inflation pressures will ease in the coming quarters. Market-based measures of future inflation, like the 5-year and 10-year breakeven inflation rates, have come down in recent weeks, signaling that the bond market may be expecting lower growth and lower inflation looking ahead. Commodity and energy prices have also broadly declined over the last month, perhaps as the market resets expectations for global growth going forward. As seen on the chart on the next page, Goldman Sachs is forecasting that inflation's peak is likely not too far off, assuming it hasn't happened already.



GOLDMAN SACHS IS FORECASTING INFLATION TO PEAK SOON



Source: Goldman Sachs

It also now appears possible that the U.S. economy entered a recession in the first half of 2022, which if confirmed would mark a very shallow and atypical contraction. Recessions are most accurately characterized by declining output, rising unemployment, and some level of dislocation in credit markets where businesses and consumers fail to meet financial obligations. Essentially none of these conditions were met in the first half of 2022.

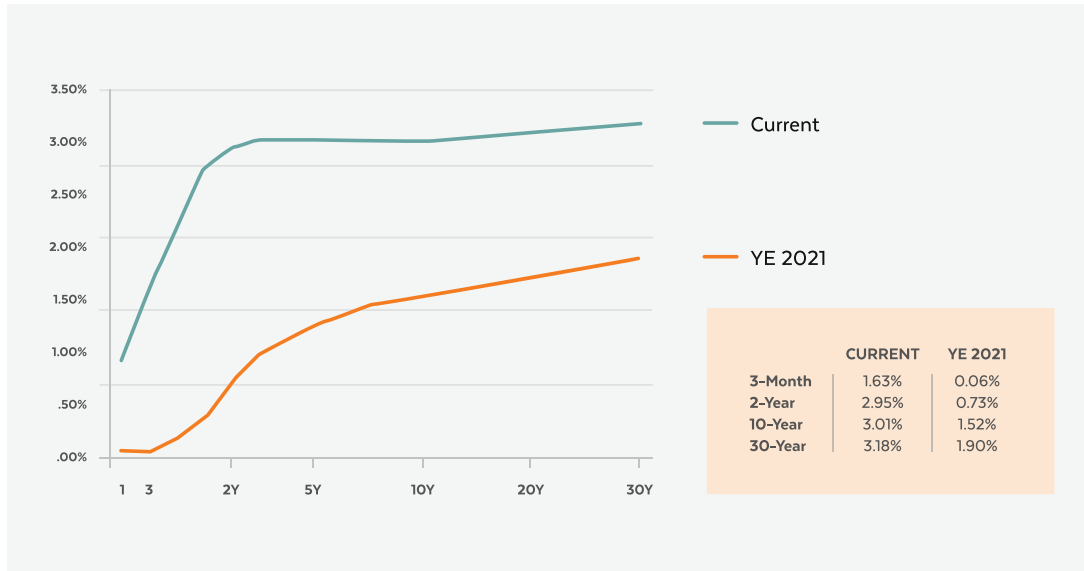
Economic growth is slowing, but Q1 GDP's negative print was largely the result of a big swing in inventories and a surge in imports, both of which detract from the GDP calculation but do not necessarily signal a sharp drop-off in activity. Manufacturing and services indices in the U.S. have yet to dip into contraction territory this year, and have been in expansion mode for 25 months straight.

The past 12 recessions have also all featured rising unemployment, which we have not seen in 2022. Over the past six months, the unemployment rate has fallen from 4% to 3.6%, and there have been over 10 million open jobs in the U.S. in every month of this year—nearly double the amount of typical job openings in years prior to the pandemic. There are also 'only' 1.3 million Americans collecting unemployment today, which is 400,000 fewer than before the pandemic. For context, there were over 6.5 million unemployed Americans receiving benefits during the 2008 Financial Crisis.

Banks are also not showing any signs of duress so far. The latest round of Fed 'stress tests' found that banks could easily handle the unemployment rate soaring to 10% and a collapse in stock market and commercial real estate that would wipe out over \$600 billion. Even with those unlikely shocks, banks would have capital ratios of 9.7%, which is over double the 4.5% required by law. An upward sloping yield curve also suggests that banks can still lend profitably in the current environment (see chart on next page).



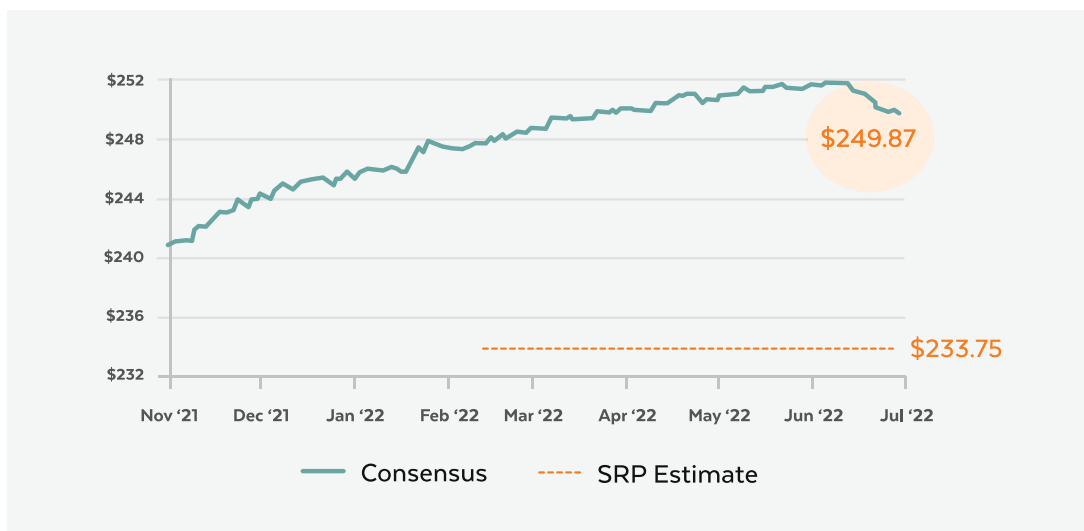
THE YIELD CURVE IS UPWARD SLOPED BUT FLATTENING



Source: Credit Suisse

These conditions could all change in the coming months, for better or for worse. But the upshot in the present moment is that the stock market has already declined -20% in 2022, meaning that a good portion of all the headwinds to growth may already be incorporated in current prices. What remains to be seen, in our view, is a potential reduction in earnings expectations as businesses grapple with slowing consumer spending and rising labor costs and input prices. We are starting to see early signs of shifting expectations with 2023 earnings-per-share projections (chart below). If the coming compression in profit margins comes as a negative surprise, there could be more selling pressure left in the bear market.

2023 S&P 500 EARNINGS-PER-SHARE PROGRESSION



Source: Strategas Research



CONCLUSION

The current inflation setup seems equally positioned for a positive or a negative surprise. A positive outcome would be slowing or declining inflation that removes pressure from the Fed to raise rates so aggressively. A negative outcome would be additional supply constraints, likely tied to China's Covid-19 policies and the war, that could continue to exacerbate shortages and push prices higher. The outcome is largely unknowable.

But even if we believe there could be more runway in this bear market, trying to forecast and time the exact bottom is difficult and risky. Bear market bottoms almost always happen when conditions feel terrible and pessimism reaches a peak, but we could see both of these factors for weeks or months to come. Americans, for instance, are more unhappy with the economy today than they were during the Great Recession when the unemployment rate was in double digits and millions of people lost their homes. A shift in inflation would likely reverse this dour mood, but it may take more than one or two quarters to see price stability in the US and abroad.

We think portfolios can be positioned more cautiously in the near-term, while holding on to core equity exposures with a longer-term time horizon. Tactically, we have taken our cash levels higher, while trying to remain tax-efficient for taxable accounts, and we continue owning great companies we think can deliver resilient earnings even in challenging economic conditions.

If you have any questions about this review or your portfolio strategy, please do not hesitate to reach out to us. We hope you enjoy the rest of your summer.

Sincerely,

Kenneth F. Siebel

Elyse Gottschalk

Jason M. Saxon

William F. Dagley

Richard G. Kuchen

Vickie Marinovich

Chris Greene

James Lenczowski

Katrina Sutherland



This letter has been prepared by Private Wealth Partners LLC, a registered investment adviser solely for informational purposes. This letter is not an offer of or a solicitation of offers to buy or sell security or investment. The opinions expressed herein represent the current, good faith views of the authors as of the date hereof and are provided for limited purposes, are not definitive investment advice, and should not be relied on as such. The information presented in this letter has been developed internally and/or obtained from sources believed to be reliable; however, Private Wealth Partners, LLC does not guarantee the accuracy, adequacy or completeness of such information. Predictions, opinions, and other information contained in this letter are subject to change continually and without notice of any kind and may no longer be true after the date indicated. Any forward-looking statements speak only as of the date they are made, and Private Wealth Partners, LLC assumes no duty to and does not undertake to update forward-looking statements. Forward-looking statements are subject to numerous assumptions, risks and uncertainties, which change over time. Actual results could differ materially from those anticipated in forward-looking statements. This material is directed exclusively at investment professionals. Any investments to which this material relates are available only to or will be engaged in only with investment professionals.