Arbor Capital Management

A Pure Asset Manager

Second Quarter 2022 Investment Overview

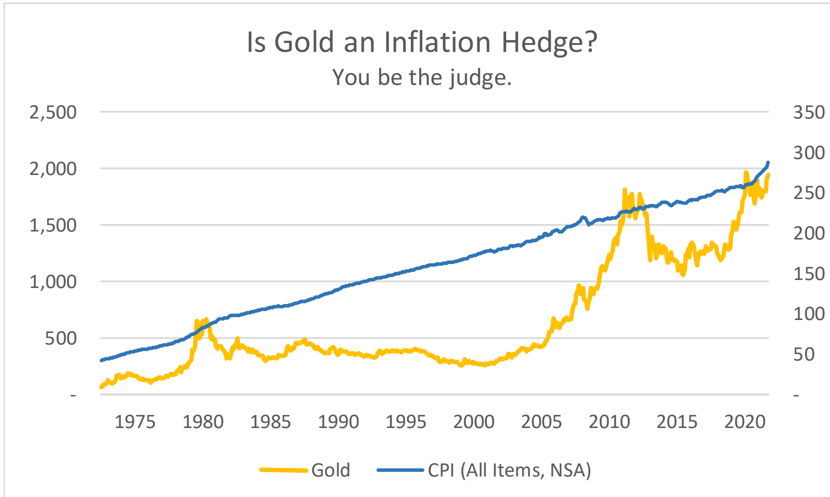
As 2022 progresses, it is becoming increasingly apparent that the global economy is transitioning to higher inflation and global uncertainty.

Economy. What a difference a year makes. A little over a year ago, the US enjoyed growth and relative price stability as it recovered from the COVID-induced economic shock. When we started the recovery from the COVID shock, we and many others felt the imbalances between supply and demand would be self-correcting by now. We were over-optimistic. There are still shortages of new vehicles, materials to build homes, energy, and consumer products. While we believe the Fed's sincerity when they tell us that they expect inflationary pressures to ease over the summer, our experience with the 1970s inflation cycles comes to mind. We think that there are several similarities to the early 70s. An oil price shock hit consumers the hardest in the gas tank and later in the increased cost of everyday products. Wage pressures seem to be on the rise, particularly at the entry levels. However, the structure of the labor force today is materially different. In the 1970s, baby boomers were entering the labor force. Today, that same demographic cohort is retiring. As the boomer generation's retirements accelerate, we think the labor force will experience a skill vacuum lasting a few years until the "echo generation" comes up to speed. Reduced productivity and higher wages will create persistent inflationary pressure, all other things being equal. The war in Ukraine has added a few wrinkles. Ukraine is traditionally one of the world's largest food producers. The reduction of Ukrainian harvests for at least this season pressures the global food supply. Russia is also the most significant energy supplier to Europe, which stalemates Europe's ability to apply many of its desired sanctions. OPEC has already stated that it cannot produce enough crude in the short term to meet a shortfall created by boycotting Russian oil and natural gas production. Combining these factors leads us to conclude that inflation will probably trend higher and last longer than the consensus anticipates.

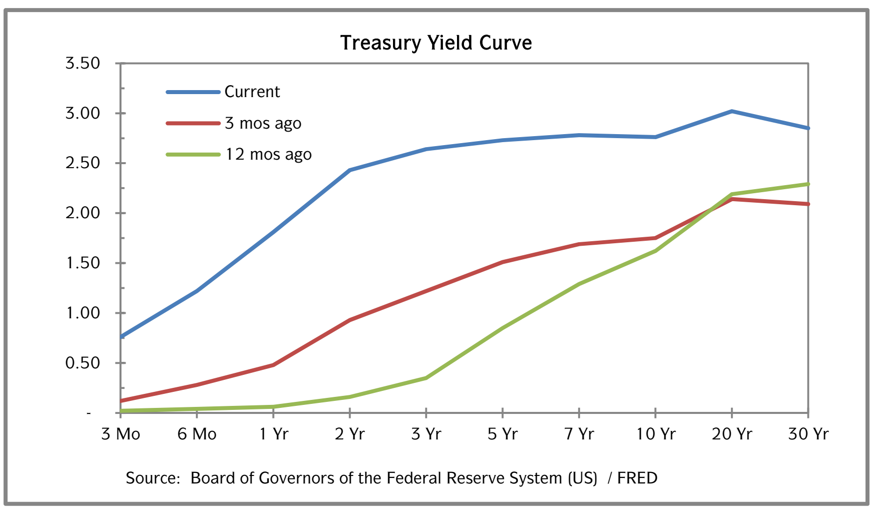
Gold. When inflation accelerates, many investors look toward gold or other precious metals as an inflation hedge. We have studied gold prices vs. inflation in some depth over the years. In our view, there are three primary sources of gold demand:

1. Commercial uses such as jewelry and electronics;
2. Speculation / Investment such as bullion, coins, mining shares, and etf's;
3. Replacement of paper currency.

The disparate drivers of gold demand make forecasting its future price nearly impossible. The commercial use category is the most stable but is still subject to business cycles and fashion trends. For the most part, Investment and speculation come and go with expectations for future changes in inflation and trend-following. The currency replacement component is mostly influenced by wars, trust (or lack of trust) in one's government, and perceptions of central bank stability. During high periods of uncertainty, people often turn to coins as a means of exchange not subject to government seizure, as may be the case in highly conflicted areas around the world. The sources of demand are a bit unique because they are almost totally unrelated. So when people ask: "Is gold an inflation hedge?" an accurate answer is: "It depends."



Monetary Policy and Fixed Income Strategy. It has been widely reported that the Fed intends to tighten money supply by stopping its bond purchases and increasing short-term interest rates. As the Treasury yield curve shows, interest rates over the full range of maturities have risen markedly over the



past three months. The shape of the yield curve tells a story. To achieve the highest yield available, one only has to extend maturity to a little over two years. From 2 years to 10 years term to maturity, there is vey little yield pick up. The market is telling us that it expects a brief run of moderate inflation over the next few years and stabilizing later.

In contrast, we anticipate a longer period of inflation at rates that may also be higher than consensus estimates. If our analysis proves correct, long maturity fixed income will perform poorly relative to shorter bonds. Hence our overall fixed income strategy is both defensive and opportunistic. We are keeping average maturities short, but at the same time, we may be able to take advantage of the relative steepness of the curve inside of three years to pick up a little extra income.

Stocks. A rise in inflation is not the end of the world for equities by any stretch. The selections need to be more focused on fundamentals and return on invested capital. Buying stocks in trendy areas because there seems to be a hot story is always a dangerous game, more so when the cost of capital (interest rates) rises. Currently, we have been focused heavily on solid fundamentals. Going forward, we will keep that as an emphasis, but we expect to season portfolios with specially situated companies who are executing their businesses particularly well and may possess a competitive advantage over their competition.

As a registered investment advisor, the SEC, under the Investment Advisors Act, requires that our disclosure brochures be delivered to each client and prospective client. We offer to send you our current Firm Brochure with additional information should you request it. If you would like to receive our current Firm Brochure, please call or write Sandy Dodson, or the undersigned or go to SEC.GOV.

We appreciate the opportunity to be of service to you. Please call us anytime to talk, particularly if you have any changes in your goals, lifestyle, or your health. We are the Arbor Capital family and we are here for you.

We extend a special welcome to the many new clients who have joined the Arbor family in the last quarter. If you know someone or any organization that you believe would benefit from our services, please mention our name. We would be honored to have more clients like you.

Sincerely

Gerald T. Cole, CFA **April 26, 2022**

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