Arbor Capital Management

A Pure Asset Manager

Fourth Quarter 2022 Investment Overview

The global economy is in transition. Growth is slowing while the prices of food and energy have sparked inflation. The financial markets are trying to adjust to the dislocations this has created. The consensus of economists are leaning heavily toward a recession occurring in 2023. We think market returns in stocks and bonds have already discounted a lot of potential bad news. Markets tend to be forward-looking, so by the time an official recession is "called," stocks and bonds could be already on the road to recovery. We believe our strategies are well-positioned for the environment we think will unfold over the next few years.

Economy / Monetary Policy – The current relationship between the macro-economy and monetary policy is similar to that of a chicken and egg. Inflation is proving to be much stronger than previously hoped. In response, the Fed has raised short-term rates very aggressively. Since the recent rate increases have not had the desired effect on inflation, more rate hikes are expected. The Fed is resolute that the 2% inflation target be re-established. To do so will come at the cost of significantly increased unemployment. We think the slowdown that would occur as a result may not be sufficient to curb inflation in the desired manner. Nevertheless, it will take clear evidence of weak jobs data before the Fed considers relaxing its position. We think that the unusually aggressive Fed tightening results from being slow in its initial reaction. Playing catch-up runs the risk of overshooting the mark. Based on what we know today, the trough in economic activity should occur sometime next summer. We generally have a healthy skepticism when it comes to economic forecasts. However, Bloomberg is predicting a 100% probability of recession in 2023. Whether or not this forecast is accurate remains to be seen.

The surge in inflation has been led by Food and Energy prices. Although each has moderated, we think fundamentals will keep price pressures relatively elevated in a slowdown due mainly to the war in Ukraine. Ukraine is one of the World's largest food suppliers and will unlikely be able to restore full production for several growing seasons. This past summer's pullback in oil prices was largely artificial. The Government sold nearly 1/3 of the US Strategic Petroleum Reserve (SPR) to drive oil prices downward. Engineered supply shocks are temporary. Reduced global supply and a resurgent OPEC will likely keep prices higher than they would otherwise be. A price resurgence seems probable after the mid-terms, all other things being equal. In our view, all the rate increases in the World won't have much impact on either Food or Energy. Therefore, we think the stage is being set for a possible return to stagflation similar to what the World experienced in the 1970s. We will keep you posted.

Fed rate increases have helped lift 30-Year Mortgage rates to 7%, which has reduced new home demand. After a price increase of nearly 50% over the past three years, a 10-15% decline is not unusual.

We don't know how high rates will go, but from a historical perspective, they are still relatively low. In the big picture, we could make the case that bond yields could stabilize around 5% without any long-term adverse business effects. If businesses cannot compete with a 5% cost of capital, then they should reallocate their resources.

Fixed Income. Our strategy of laddering maturities is ideally suited to this environment. As bonds mature, we can capture the higher yields currently available. The Fed rate increases and accelerated inflation will probably continue to drive yields higher until inflation breaks, and the Fed takes a more relaxed posture. As always, we emphasize strong creditworthiness in each of our purchases.

Equities. In the face of a major change in the economy, the equity markets have discounted a lot of bad news. Bearish sentiment is widespread. At least one more rate increase of 0.75% is already baked in. On a tactical basis, stocks are deeply oversold and may have a sharp rally from here that could carry through the end of the year. Strategically, there remain a number of dislocations that need resolution before a new bull market can resume. This sort of dichotomy persisted throughout the 1970s and early 1980s. Money can be made, but selectivity will be essential.

While the macro-economy is a mess, and geopolitical risks are rising, earnings are holding up well. The companies we hold were selected because of their relative earnings stability. Moreover, we are focused on buying businesses. We focus on companies whose products remain in high demand regardless of economic circumstances. We like companies that can use their cash flows to compound their invested capital and grow organically. These aren't always glamorous, just steady performers with staying power.

Clients with taxable accounts will find your Realized Gain and Loss Statement through the first three quarters of 2022 enclosed. You may wish to share this information with your accountant and advise us of any tax planning as soon as possible.

Also, we would like to remind our IRA clients if you need or require a distribution from your IRA, please notify us prior to December 1, 2022 in order that processing is accomplished in a timely manner.

We appreciate the opportunity to be of service to you. Please call us anytime to discuss your account, particularly if you have any changes in your goals or lifestyle. Also, you should be receiving custodial statements directly from your qualified custodian at least quarterly. If you are not receiving these statements, please contact us so that we may assist you in resolving this matter.

We extend a special welcome to the many new clients to 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 **October 25, 2022**

Chief Investment Officer

Lawrence T. McGowan

100 Corporate Pkwy, Suite 308

Amherst, NY 14226

(716) 446-9111

ltmcgowan@arborcapitalmgt.com

Daniel M. Toole

100 Corporate Pkwy, Suite 308

Amherst, NY 14226

(716) 446-9111

dmtoole@arborcapitalmgt.com

Leo Mesa, CFP

790 Juno Ocean Walk, Suite 600

Juno Beach, FL 33408

(786) 202-0602

lmesa@arborcapitalmgt.com