CAPITAL ADVISORS

Key Points

- In a market commentary three weeks ago, we said we believed the odds of a recession in the U.S. may have risen above 50%, while the likelihood in Europe seems higher still.
- The primary drivers of this forecast include potentially acute inflationary pressures accelerated by the war in Ukraine, combined with tightening monetary policy that must catch up to reality following the Fed's errant forecast of "transitory" inflation last year.
- We believe the risk environment for investors looks unusually elevated today, but we also recognize important caveats for each of the major risk factors we identify.
- We believe the best investment approach in the current climate is to position for uncertainty, rather than a specific forecast for the future.
- This suggests an emphasis on balance and flexibility in the design of investment portfolios, with a bias to err on the side of caution.
- Later in this report we will describe certain measures we have taken in our investment strategies to improve their flexibility during this uncertain time.
- We will also discuss the bond market in greater detail than usual to provide context for the recent weakness in this asset class that investors typically rely upon for stability.

No Place for a One-Armed Economist

Harry Truman is said to have longed for a one-armed economist who couldn't say "on the other hand" when advising him. The discussion below would not please the former president due to its toggle between important risk factors and offsetting caveats that characterizes the current investment climate.

We believe the unfolding supply shock in global commodities in the face of tightening monetary policy from the Federal Reserve has the *potential* to be quite troubling for financial markets. We also recognize there is risk in being *too* careful with our investment strategies because there are important offsetting factors that might make it counter-productive to do so.

This uncertain environment is compounded by the fact that future events are highly dependent on the decisions of political actors rather than more traditional cause-and-effect relationships grounded in economics.

Our portfolio prescription for this environment is balance and flexibility with a bias toward caution. In the pages that follow we seek to describe our current interpretation of the current investment landscape and the actions we have taken in our investment strategies to address it.

Repercussions of Putin's War

On the morning of Russia's invasion of Ukraine on February 24th we advised readers to resist the temptation to buy-the-dip in the stock market, even though the historical record of geopolitical shocks shows it has typically been profitable to do so.[1]

Our primary concern that day was the risk of an inflationary shock due to disruptions in the supply of important commodities, most notably energy and agriculture. Since the invasion inflationary pressures have indeed intensified, as reflected in material price increases for multiple commodities, including energy, grains, vegetable oils, fertilizer, and industrial metals.

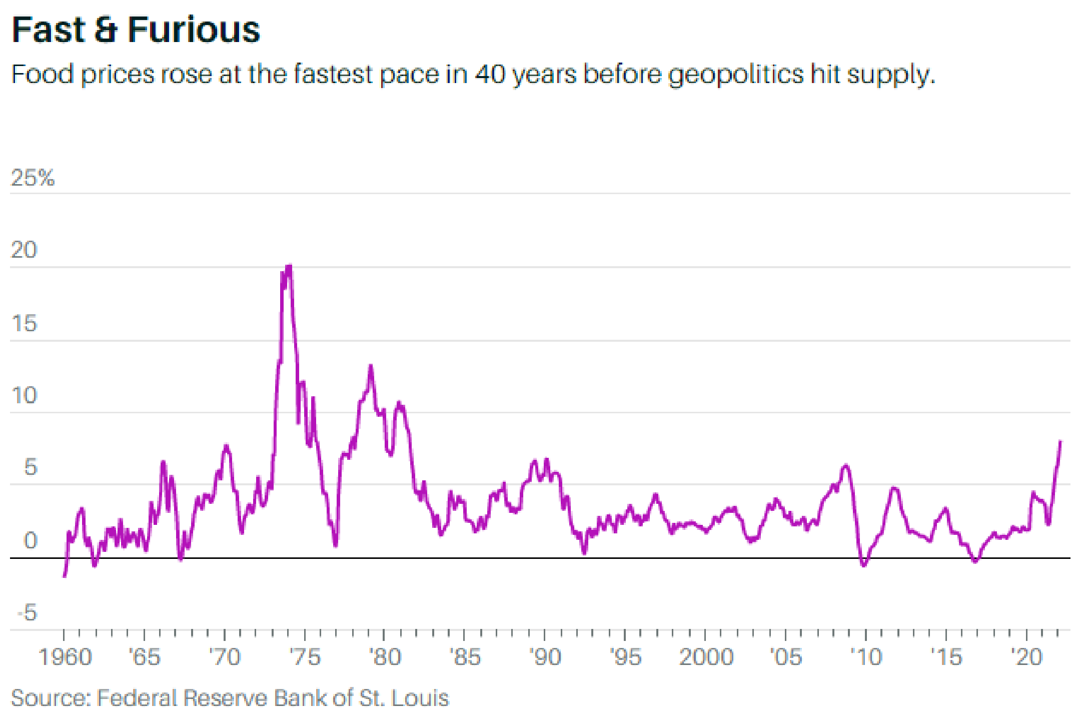
Inflation serves as the transmission mechanism between shortages and demand destruction that allows markets to clear at a new, lower level of output. Due to war related shortages, we expect a material hit to global economic growth, with some regions likely to experience outright contraction. The U.S. economy seems better positioned than most to avoid a contraction, but a material step-down in growth seems unavoidable in the near term.

[1] Source: Glenview Trust; Reuters

Bad Timing for a Supply Shock

The supply shock now unfolding from the war in Ukraine arrived at a time when markets were already tight for the two most important inputs for the global economy – food and energy. Note in the chart below that food prices were already rising at the fastest pace in 40 years *before* the Russian invasion.[2]

Jan. 1, 1960 – Jan. 31, 2022



The war is expected to make this situation worse in the near-term due to the immediate disruption to agricultural supplies from both countries. Ukraine managed to ship just 70% of its wheat harvest and 55% of its corn harvest before its ports closed, and the Ukrainian government subsequently banned the future export of all wheat to preserve supplies for its own population.[3]

Russia produces approximately 11% of the world's wheat, while Ukraine produces about 3%.[4] These countries make up a materially larger percentage of global wheat exports, and they are both significant exporters of corn. Neither country is a major producer of rice or soybeans, the other two major agricultural commodities in the world.

---

[2] Source: Barron's; Federal Reserve Bank of St. Louis
[3] Source: FHN Financial
[4] Source: FAOSTAT

Spare Capacity in the Oil Market?

As with agriculture, energy markets were tight before the war. In fact, some analysts believe global demand for oil was on pace to absorb all the world's spare production capacity as early as next year, and these forecasts were made *before* the outbreak of war.[5]

It is important to emphasize the potential significance of this viewpoint if it proves to be correct. Global consumption of oil has never reached the world's capacity to produce it in the history of the hydrocarbon age. There has always been a cushion of spare production capacity available to respond to supply disruptions that happen all the time in one place or another.

What this viewpoint is suggesting – again, *if* it proves to be correct – is that even *before* the war, the world was approaching the point where global demand for oil matched up with the *total pumping capacity* available to supply it, regardless of *willingness* on the part of OPEC (Organization of Petroleum Exporting Countries), or any other player in the system.

OPEC Spare Capacity

Estimates for 2022 *Before* the Ukraine Invasion

	IEA	Adj	G&R
Demand	101.6	--	101.6
2H22 Revisions		0.4	0.4
Total	**101.6**	**0.4**	**102.0**
Production			
US	18.4	(0.5)	17.9
Non-OPEC+ Ex US	30.6	(0.6)	30.0
OPEC+ NGLs	8.0	(0.3)	7.7
Total	**57.0**	**(1.4)**	**55.6**
Call on OPEC+ Crude	**44.6**		**46.4**
Current OPEC+	43.6	--	43.6
Spare Capacity	6.4	(3.6)	2.8
Pumping Capability	**50.0**		**46.4**

Source: Goehring & Rozenczwajg; IEA

Putin's war probably pulled the timing forward for this potential crossing of the lines between consumption and capacity. For instance, on March 16, the *International Energy Agency* (IEA) forecasted that Russian oil production would decline by 3 million barrels per day in April, effectively wiping out the spare capacity estimate of 2.8 million bpd in the table above.

[5] Source: Goehring & Rozenczwajg

No Relief in Sight from the Fed

Most observers now agree the U.S. central bank fell way behind its inflation mandate last year by assuming price pressures would be “transitory.” Having persisted with zero-percent interest rates and aggressive quantitative easing (QE) until March of 2022(!!), the Fed seems to have no alternative now but to tighten monetary policy – possibly aggressively – despite the extraordinary uncertainties emanating from Putin’s war.

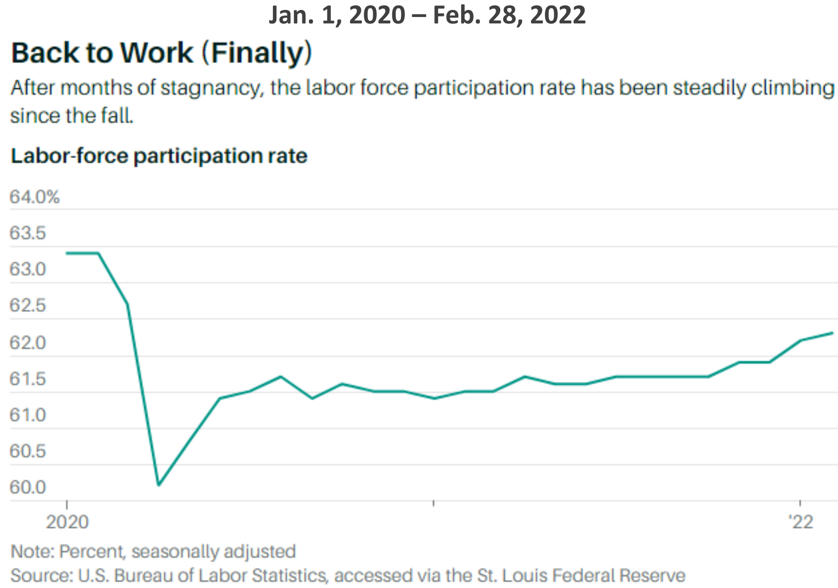
Investors fear monetary tightening cycles because most of them end badly for the stock market. Out of 16 monetary tightening cycles since the late 1970s in the U.S., U.K., and the eurozone, 13 ended in recession.[6] Moreover, the track record of central bankers achieving a so called “soft landing” after a tightening campaign is even worse when the policy is objective is to *reduce* the rate of inflation – like now – rather than merely preventing it from rising.

No Reason to Panic Yet

Fortunately, there are important caveats for each of the risk factors described above, particularly for the domestic economy. For example, many analysts argue that rising food and energy costs can be absorbed by U.S. consumers due to accelerating wage growth, strong labor markets, excess savings from the pandemic, and a massive boost to household wealth following a multi-year surge in the value of peoples’ homes and investment portfolios.

The domestic labor market is also responding to higher wages and the rising cost of living. The labor force participation rate has been ticking higher for six months, while the percentage of workers who quit their jobs has been declining.[7]

Jan. 1, 2020 – Feb. 28, 2022



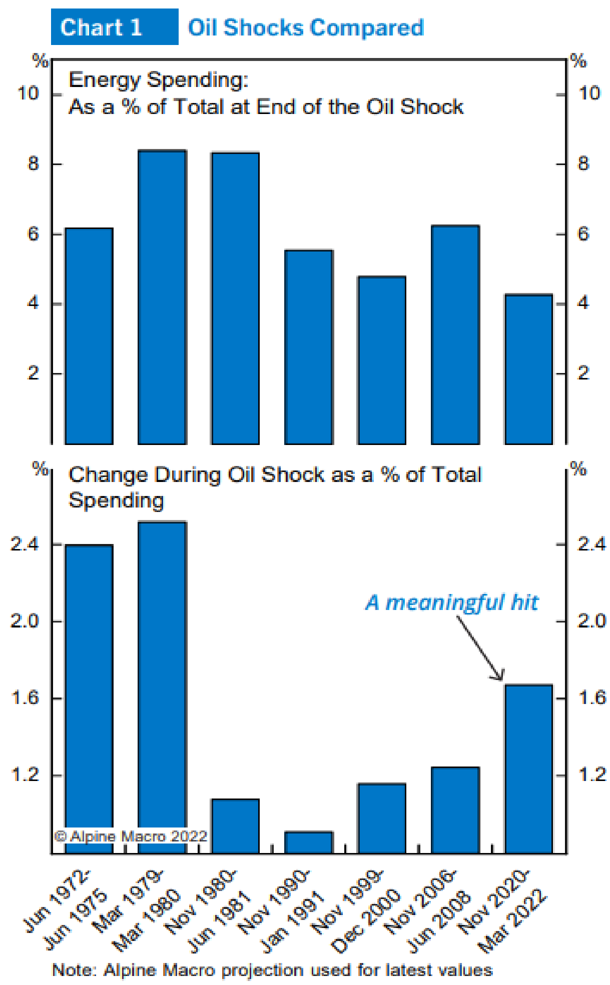
---

[6] Source: Capital Economics; Wall Street Journal

[7] Source: Bureau of Labor Statistics; Barron’s

It is also helpful that the domestic economy is far less energy-intensive than it used to be. As the table below reflects, even after the recent surge in the price of oil, domestic household spending on energy is expected to remain well below the levels reached during the oil price shocks of the 1970s, or the spike in 2008 that preceded the financial crisis (provided energy prices don't continue advancing substantially from here).

Jan. 1, 1972 – March 25, 2022



Source: Alpine Macro; IEA

Another potential offsetting factor is the reality that individuals, companies, and countries do not stand still. In the energy markets, China and India are working to increase their oil imports from Russia – at a steep price discount no less – which should free-up barrels for other buyers from elsewhere in the system.

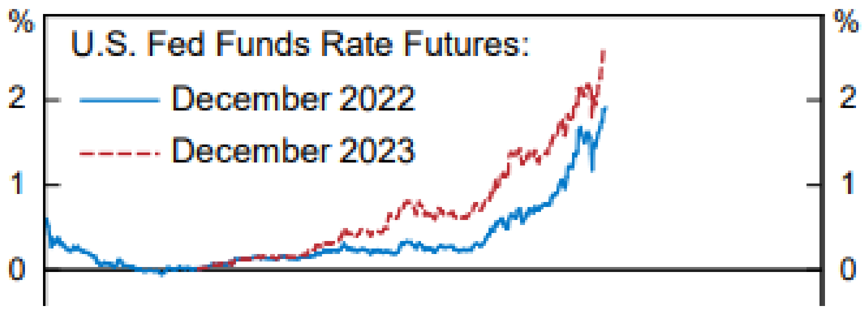
We might also expect a fiscal response to rising energy prices in many parts of the world. Taxes represent a meaningful percentage of the price of motor fuel in many countries, leaving room for price relief via temporary tax reductions. Several U.S. states have already proposed temporary reductions in their respective gasoline taxes.

In the grain markets, the U.S. Department of Agriculture recently increased its forecast for wheat output this year and next from Australia and India, partially offsetting expected losses from Ukraine and Russia.[8] The outlook for food prices also seems less daunting when the grain markets are measured in calories, rather than tons, or dollars. The combined exports of wheat and corn from Russia and Ukraine amount to less than 3% of total calories consumed globally from the four major grains.[9] At least for the developed nations of the world, this would seem to leave room for substitution with other foods to help offset expected shortages in wheat and corn.

Lastly as it relates to monetary policy, we believe much of the initial adjustment to tighter monetary policy may have already occurred in the U.S. credit markets. As the chart below reflects, markets are already pricing in up to seven one-quarter-point interest rate hikes in 2022, plus another two or three hikes next year. Unless the Fed eventually raises rates substantially *more* than what is already priced in, much of the adjustment in the bond market may be behind us.

We have more to say on this topic below where we describe recent weakness in the fixed income markets in greater detail.

Credit Markets Anticipate Aggressive Fed Tightening
Jan 1. 2020 – March 20, 2022



Source: Alpine Macro; Bloomberg

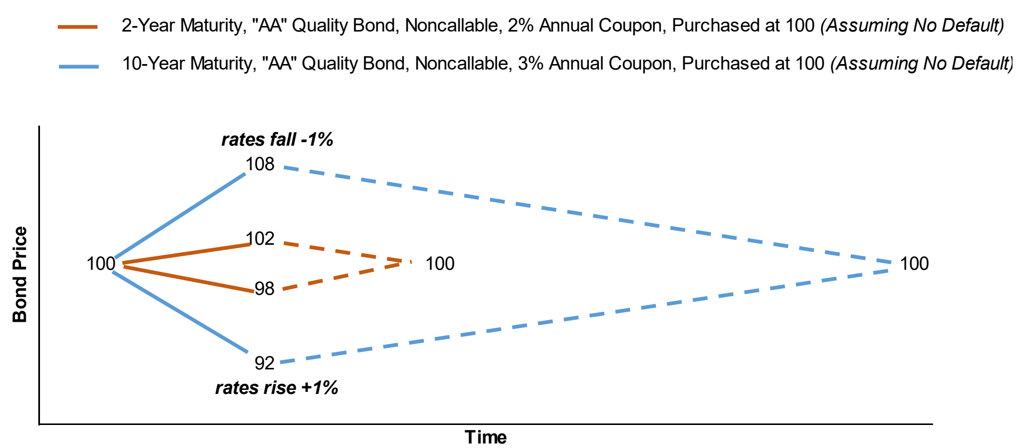
[8] Source: FHN Financial; Department of Agriculture
[9] Source: FAOSTAT

A Brief Review of Bond Math

Assuming a given bond does not default, its expected return to maturity is measurable within a narrow margin *at the time of purchase*. However, the price of the bond can take a varied path between the purchase date and maturity. The range of these interim price swings is a function of the bond's time to maturity, and the magnitude of the interest rate move.

The graphic below illustrates the impact of a hypothetical one percentage point change in interest rates on the price of a 2-year bond versus a 10-year bond. It is important to note that in both cases, the interim price move has no effect on the outcome at maturity.

Bond Pricing Illustration



	Year 0	Year 1	Year 2	....	Year 10
2- Year Cash Flow		2%	100% + 2%	.... Subject to Reinvestment Risk	
10-Year Cash Flow		3%	3%	.... 3% Each Year	100% + 3%

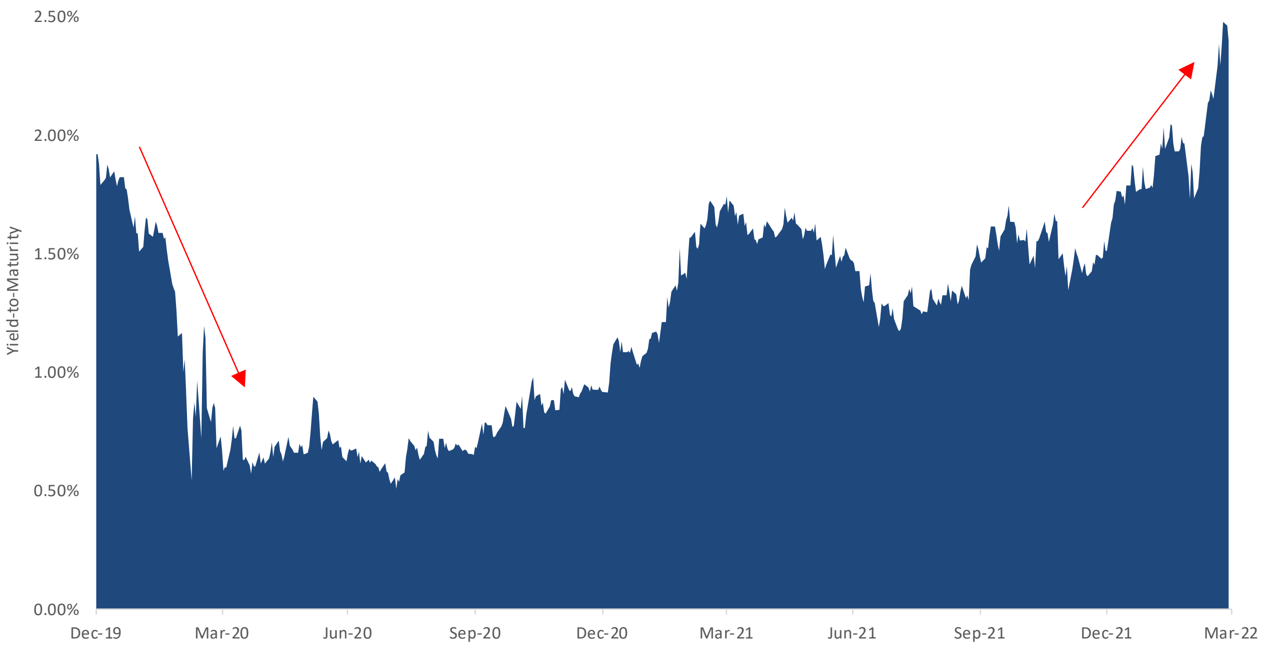
Source: Capital Advisors

Recent Bond Market History Revisited....

This reminder of how bond prices work is helpful for interpreting recent behavior in the fixed income markets. The bond market has experienced a roundtrip in the level of interest rates since the end of 2019, characterized by a rapid drop in yields at the outset of the Covid-19 pandemic in early 2020, followed by a recovery to higher yields by the end of March 2022.

The initial drop in yields in 2020 drove interest rates to all-time lows in conjunction with the extreme measures taken by the Federal Reserve to cut rates and increase ownership of market securities on its own balance sheet. Per the graphic above, a drop in interest rates leads to a corresponding increase in the price of bonds *in the short-term*. However, as the world grew confident the pandemic would slowly subside in late 2020 and early 2021, bond market prices began to reflect the inevitable reversal of the Fed's extreme liquidity measures, resulting in higher interest rates and a *decline* in bond prices.

10-Year U.S. Treasury Yield-to-Maturity
December 31, 2019, to March 29, 2022



Source: Bloomberg

The recovery in yields accelerated sharply in the first quarter of this year when the Fed put the market on notice they were serious about attacking inflation, signaling multiple future rate hikes over the coming 12-24 months. Since year-end, 5-year Treasury yields nearly doubled from 1.3% to 2.5%, while 10-year yields rose nearly 0.90%.[10]

To put the recent rise in interest rates (and drop in bond prices) into perspective, the *Bloomberg U.S. Intermediate Government/Credit Bond Index* just experienced its largest negative total return over a three-month period since the first quarter of 1980, falling -4.7% in Q1 2022. (For what it's worth, this index finished positive for the full year 1980).[11]

On a brighter note, recall from the previous illustration of bond math that short-term movements in the price of a bond have little impact on its total return to maturity. If an investor purchases a (hypothetical) bond with a 2.0% yield-to-maturity, and then holds the bond until it matures at par value, the investor can expect a total return on that investment of approximately 2.0% annualized, regardless of the path it takes to get there.

[10] Source: Bloomberg 3/29/22
[11] Source: Bloomberg; The Bloomberg U.S. Intermediate Government/Credit Bond Index measures the yield and return of a diversified basket of U.S. investment grade corporate and government securities with maturities less than 10 years.

The dynamic of bond math is reflected in the table below showing a tight correlation between the yield-to-maturity of an intermediate bond index relative to its subsequent 3-year total return. For each starting point in the table with a full 3-year holding period beyond it, the relationship between starting yield and subsequent return is consistent.

Bloomberg Intermediate Government/Credit Bond Index
3-year annualized return (%) vs. starting yields
Dec. 31, 1990 – March 29, 2022

Dates	Index End of Year Yield (%)*	Index Subsequent 3-year annualized return (%)
12/31/1990	7.94	10.15
12/29/1995	5.50	6.77
12/29/2000	6.07	7.67
12/30/2005	4.75	5.50
12/31/2010	2.05	2.91
12/31/2015	2.06	1.70
12/31/2018	2.99	3.86
12/31/2019	1.93	-0.02*
12/31/2020	0.59	
12/31/2021	1.30	
3/29/2022	**2.74**	

** annualized through 3/29/22*

It is not possible to invest directly in an index.

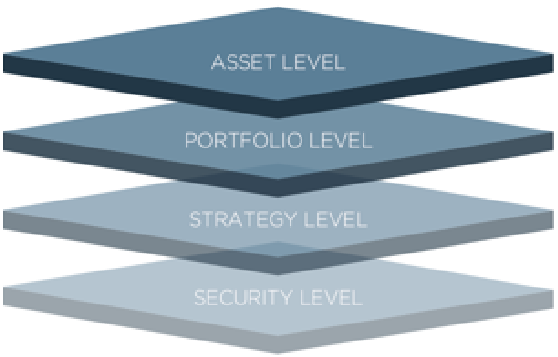
This data leads to an important silver lining from the recent poor performance of the bond market. Specifically, the ability to generate *future* returns in fixed income improves with each tick higher in the general level of interest rates.

The yield-to-maturity for the *Bloomberg U.S. Intermediate Credit Bond Index* recently hit 3.40%, while the tax equivalent yield-to-maturity for the *Barclays Municipal Bond 10-Year Index* reached 4.00%[12] (for investors in the top income tax bracket). With rates having moved substantially higher over the past two quarters anticipating multiple Fed rate hikes, we are finding significantly better opportunities across the yield curve to invest, and we believe much of the adjustment to tightening monetary policy may be priced in.

[12] Source: Bloomberg; The Bloomberg U.S. Intermediate Credit Index measures the yield and return of a diversified basket of investment grade corporate bonds with maturities in the 1-to-10-year range; The Barclays Municipal Bond 10-Year Index measures the yield and return of a diversified basket of investment grade municipal bonds with an average maturity of 10 years.

Current Design of Our Investment Strategies[13]

The remainder of this report addresses the current positioning of each of our investment strategies under current macro conditions. The specific design of *your* portfolio is customized to match your return objectives and risk tolerance. For a refresher on how your portfolio is designed, and why, please reach out to your Wealth Advisor any time.



ASSET LEVEL	Based on your investment objectives and risk tolerance, we set parameters for an optimal stock/bond mix. Instead of keeping your portfolio at a stagnant allocation, we have the ability to change the stock-to-bond-to-cash ratios as market conditions change.
PORTFOLIO LEVEL	By understanding the types of portfolios/accounts we're managing, we structure each portfolio to fit its stage in the investment life cycle (accumulation vs. distribution). We also take into account legacy positions and/or outside assets.
STRATEGY LEVEL	By understanding your optimal asset allocation range and the types of portfolios being managed, we determine how our specific strategies should be combined. We utilize both fundamental and tactical strategies to help take diversification one step further.
SECURITY LEVEL	Our team of CFA charter holders performs deep research behind each security selected and provides rationale for trades. We strive to position your portfolio for prevailing market conditions to participate in long-term trends.

<u>Managed Equity Strategies</u>

The first thing to keep in mind is that stock market groups do not move in the same direction all at once. "Factor diversity" has certainly been prevalent in recent quarters. Through March 14, the Russell Growth Index was down more than 19% year-to-date, while the S&P 500 Index was down more than 12%, and the Capital Advisors *Managed Equity Dividend* strategy was roughly flat.[14]

In many ways the level of volatility happening beneath the surface of the stock market among different sectors and factors has been greater than the volatility on the surface of the market. Since the low on March 14 referenced above, the S&P 500 has recovered approximately 11%, while the Russell Growth Index is up roughly 16% (through March 29).[15]

We believe one of the reasons for this volatility is that there remains unprecedented liquidity (money) in the global economic system. In a time of high geopolitical uncertainty, we believe the United States remains a relatively attractive safe haven. Corporate balance sheets remain strong and flush with cash; corporate profits also remain solid. Share buyback activity was one of the major sources of US stock market liquidity last year, and we believe it is likely to remain so this year, quite possibly even more so.

---

[13] The portfolio strategy discussions in this section are supplemental to a compliant presentation. A complete list of Capital Advisors' portfolio models and compliant presentations are available by contacting Capital Advisors.
[14] Source: Bloomberg, Orion
[15] Source: Bloomberg

The potential for a meaningful recession, and high degrees of uncertainty regarding proposed tax and financial market regulation policies, have the potential to counter those factors in ways that may cause systemic liquidity to decline.

While US and European central banks are tightening their monetary policies, Chinese authorities have recently loosened a bit. COVID remains a significant problem in China, slowing potential recoveries within the global supply chain that could have helped control inflation more quickly. Significant future progress within the supply chain (globally and in the U.S.) could make at least as much progress in controlling inflation as the Fed can with interest rate hikes, in our view. Any meaningful signs of supply chain improvement could therefore be factored into stock market trends over the next two-three quarters.

We expect "subsurface" factor volatility to remain high in 2022, impacting how we use cash in the *Managed Equity Growth* strategy and how we go about increasing the cash yield of the *Equity Dividend* strategy. This view further reinforces the importance of remaining engaged in the stock market, with a particularly flexible (and potentially more active) approach.

A quick note on the yield curve and equities

With much discussion of recession probabilities and potential yield curve inversions, it is a good time to look at what these mean in the current environment, and what implications they have for equity investors.

All else equal, when longer-term interest rates get close to shorter-term rates, it could be a sign that investors believe inflation (therefore economic activity) will slow in the future. The risk of tying up investment funds in fixed-return securities increases over time, therefore yields are typically higher for longer-dated securities to reflect this risk. When longer-term yields fall below short-term rates it is called a "yield curve inversion."[16]

Yield curve inversions can tell investors important things, but by themselves, do not directly link to stock market outcomes. Take the late 1970s/early 1980s, for instance. The curve initially inverted in August 1978, six months after the stock market had already bottomed.[17] The S&P 500 proceeded to rise 40% through November 1980. An economic recession did not happen until nearly a year-and-a-half after the initial inversion. At the time (pre-1980), typical economic cycles included recessions about every four years. That historically "normal" economic cycle largely broke after the U.S. policy actions in the early 1980's. The yield curve remained inverted into July of 1982, just before U.S. stocks embarked upon a multi-decade ascent. [18]

[16] We define a yield curve inversion as the 10-year U.S. Treasury yield falling below that of the 2-year Treasury.
[17] The S&P 500 Index bottomed at 86.9 on March 6, 1978 and has not closed a session at that level since. Source: Bloomberg
[18] During the post-war period from 1950 through 1980, the average period between recessions is approximately 4.3 years. Source: Bloomberg, National Bureau of Economic Research: List of recessions in the United States - Wikipedia

Following is a list of the subsequent times when the yield curve began to invert:[15]

- January 1989: The S&P rose 27% over the following 12 months.
- February 2000: The early stages of the dot.com bubble burst. Stocks had already started to buckle and were near the bubble top.
- December 2005: The S&P rose 14% over the next 12 months.
- August 2019: The curve inverted for eight days before steadily steepening (with longer-term rates going well above shorter-term ones) through the COVID-induced recession.

Every yield curve flattening, or inversion is different - that is the point. Curves hold important information, but do not all speak the same story. Their interpretation gets rather involved and goes well beyond the simple relationship between short- and long-term interest rates.

Similarly, economic weakness does not always mean investors should sell growth stocks or raise cash. It likely does mean enhanced volatility ahead, and that can translate into opportunity if investors remain flexible enough and interpret the information correctly.

Managed Equity Growth

The strategy remains invested in a diversified set of "growth" and "value" stocks. Given the heightened volatility that might continue in 2022, we remain focused on the strategy's "strong core." This core includes companies that have strong balance sheets, impressive cash flow structures, sustainable market leadership, and management teams that have proven they can gain share throughout market cycles and other challenges.

The investment process includes four clearly defined categories, each of which tends to behave somewhat uniquely in different market environments.

1. Emerging Franchises: Companies that are pioneering or leading what we believe could develop into very large markets. The gene editing stocks are examples.
2. Core Innovators: Companies that have the ability not only to lead large, attractive markets but also effectively target and penetrate new ones. **Amazon (AMZN ~$3380)** is an example.
3. Core Operators: Companies that lead large, attractive markets and continue innovating at the head of those markets, in our view. **Microsoft (MSFT ~$311)** is an example.
4. Tactical Opportunities: Companies in which we believe investors are missing something that is causing a temporary undervaluation.

This structure enables us to manage the weights in each segment depending upon our market outlook. It is also a key part of our risk management process. The strategy's (1-year) beta is currently 0.76, indicating volatility at approximately 76% of the market index level during the past 12-months.[19] Over time, we seek to keep the strategy's beta close to 1.0 or below.

[19] Source: Bloomberg, using a mature representative account. The raw beta indicates that, over the year ending March 28, 2022, the strategy exhibited price fluctuations that were less than those (approximately 76%) of the S&P 500 Index. Beta is one key measure of volatility and risk. Over the three years ending 12-31-21, according to Morningstar, the representative account recorded a beta of 0.87 and a downside capture ratio of 76 (a measure of drawdown magnitude relative to the index with numbers below 100 indicating lower drawdowns).

Managed Equity Dividend

Our objective for this strategy continues to emphasize a cash dividend yield in the 3.5% to 4.5% range during the foreseeable financial market environment. As part of our risk management strategy, we deliberately balance leaders of mature industries (such as Energy and Pharmaceuticals) with leaders of longer-term, higher-growth economic trends (such as 5G wireless and Biotechnology innovation).

Although the strategy emphasizes a single factor for each holding – relatively high dividend yield – we carefully diversify across other factor types, such as capital structure, business model, cash flow sources and dividend yield. Well over half of the companies in the strategy maintain a dividend growth policy, which should help to steadily raise the portfolio's cash payout over time.

We focus on the portfolio yield, versus appropriate benchmarks, rather than that of any single holding. This approach is part of a risk management strategy as well as our total-return objective. At the time of this writing, the strategy's yield was approximately 3.9%. Due to the significant price appreciation of certain holdings, we continue to expect to "roll the yield" a bit higher by shifting capital from some of the lowest-yielding positions into higher-yielding options.

Given the high degree of economic, geopolitical and (tax and regulation) policy uncertainty, we continue to favor strong business models and balance sheets, with proven management teams, over higher dividend yields. The average Standard & Poor's credit rating of companies in the portfolio is approximately A-.[20]

Tactical Global Growth Strategy

There are currently two noteworthy "themes" expressed by the current asset allocation of the *Tactical Global Growth* strategy. First is a material underweighting of international markets versus domestic equities, with all three ETFs for international markets in an under-weight position. The second emphasis is on large-cap equities relative to small-cap and mid-cap stocks.

There will be four changes to the asset allocation for the upcoming quarterly holding period. The domestic small-cap sector was reduced from overweight to neutral, and the international small-cap sector dropped from neutral to under-weight. U.S. large-cap value will increase from neutral to overweight, while high-yield credit will increase to neutral from under-weight.

[20] Source: Bloomberg, Standard & Poor's

Tactical Global Growth Strategy
Asset Allocation for the Upcoming Quarter

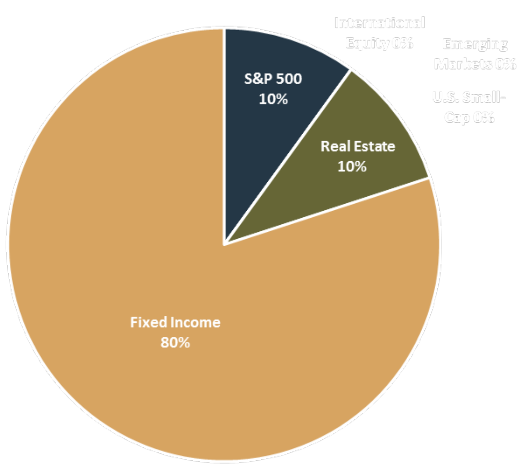
Asset Class	Current Weighting (4/1/2022)
U.S. Large-Cap Value	Overweight (17%)
U.S. Large-Cap Growth	Overweight (17%)
Real Estate	Overweight (17%)
U.S. Small-Cap	Neutral Weight (11%)
U.S. Mid-Cap	Neutral Weight (11%)
High-Yield Credit	Neutral Weight (11%)
International Small-Cap	Underweight (5%)
Emerging Markets	Underweight (5%)
International Developed Markets	Underweight (5%)

The *Tactical Global Growth* strategy provides a strategic allocation to nine major risk markets globally. Broad diversification across multiple geographies, factors, asset classes and market caps support the risk-adjusted return profile of the strategy. We strive to further enhance long-term returns by systematically adjusting the weightings among the nine sectors to overweight markets that demonstrate relative strength, while reducing the allocation to markets that exhibit relative weakness.

Dynamic Allocation Strategy

The strategy entered the new year in a relatively conservative position with 40% of its allocation in short-term Treasuries and cash reserves. It became more conservative at the end of January when the allocation to short-term reserves increased to 60%, and then shortly after the Russian invasion on March 7th, the portfolio reached its maximum defensive position with 90% of its assets set aside in short-term reserves.

Current Allocation



Whenever a risk market sector is removed from the portfolio it remains on the sidelines until the ETF for that sector trades above its moving average trend line. This trading discipline seeks to respond to prevailing market conditions to participate in markets when they are healthy – as indicated by the relationship between the price of the market index relative to its moving average – while stepping aside when the trend turns downward. As of this writing the **Real Estate** sector has returned to the portfolio, bringing the allocation to risk markets back to a still very conservative posture of 20%.

Managed Credit Strategies

Within our *Managed Credit Strategies,* we have attempted to tilt the portfolios toward better credits, with roughly 70% of our clients' exposure to companies currently rated A- or better, on average.[21] We do believe our BBB exposure has better balance sheets than the broad market, but are willing and able to further reduce this exposure should we see specific situations worsen. We have also been modestly adding exposure to U.S. Treasuries as applicable to provide further credit diversification from a potential slowdown in the economy. Although investment grade corporate credit performed slightly worse than the broad bond market, our relatively defensive duration posturing provided some guardrails to an upward rise in rates.

Municipal Bonds

Following their stand-out performance in 2021 as the best performing investment grade bond asset class, municipal bonds reversed course and fell in value on a mark-to-market basis in line with their taxable counterparts.[22] Within our *Municipal Bond* portfolios, we continue to focus on "A" and above credits with strong debt coverage and liquidity profiles. We have also intentionally over-weighted essential service revenue bonds (water & sewer, utilities, etc.), and general obligation bonds with an average portfolio credit quality of "AA." Citing stretched valuations, portfolios have been generally positioned with less interest rate sensitively to rising rates relative to the benchmark.

ETF Bond Models

Within our *Aggregate Bond* (ETF) strategy we continue to emphasize "defined maturity," investment-grade corporate bond ETFs. Today, there is a relatively even laddered maturity structure of ETFs ranging between 2023-2027, thus remaining relatively conservative from an interest rate sensitivity perspective. Thankfully our overall defensive stance relative to the benchmark has provided some downside protection from rising rates in 2022. The same can be said for the upcoming discussion on the *Income Bond* (ETF) strategy.

[21] Source: Orion

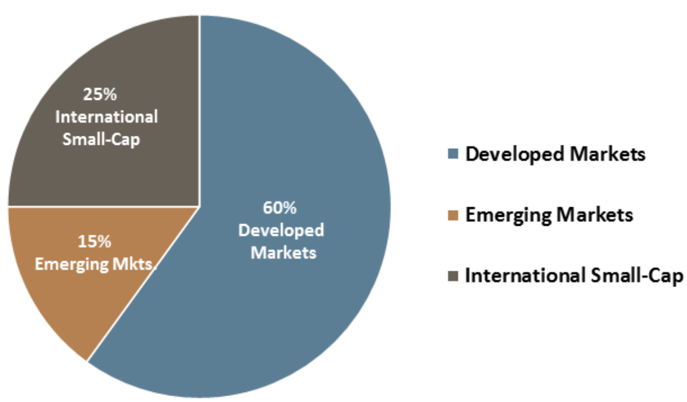
[22] Source: Bloomberg

Within our *Income Bond* (ETF) strategy we have focused on maximizing cash flows within the construct of balancing risks. In January we rotated out of a passively managed agency mortgage-backed securities fund into the **Janus Henderson Mortgage-Backed Securities ETF (JMBS ~ $50),** which is allowed to be both more opportunistic and defensive as needed versus a passive index approach. In March we became more cautious on lower quality corporate credit and sold our exposure to the **SPDR Blackstone/GSO Senior Loan ETF (SRLN: ~$45),** while increasing the allocation to investment grade credit through the **SPDR Intermediate Term Corporate Bond ETF (SPIB: ~$34)**.

International Focus Strategy

An extended period of under-performance for international equities relative to the U.S. has produced an unusually large valuation discount for these markets based upon common valuation metrics like price-to-earnings ratio, price-to-sales ratio, and dividend yield.[23] This valuation support may be at work in the recent market environment, where international equities have performed in line with domestic markets despite greater exposure to the negative effects of the war in Ukraine. The International Focus strategy has been further supported by its factor tilt toward value. The value sub-sector of the strategy includes numerous stocks in industries like natural resources, pharmaceuticals, and telecommunications, which have performed relatively well in 2022.[24]

Portfolio Allocation



The *International Focus* strategy provides a strategic commitment to international equities to expand the universe of companies for investment beyond the U.S. market. To enhance the potential diversification benefits of this expansion, the strategy seeks to capture a return premium relative to common international equity benchmarks through disciplined emphasis on three market factors that have demonstrated a long-term history of attractive risk-reward characteristics: Value, Momentum and Low Market Capitalization, or “small cap."

[23] Source: MSCI; Standard & Poor’s

[24] Source: Bloomberg

DISCLOSURES

This presentation is not an offer or a solicitation to buy or sell securities. The information contained in this presentation has been compiled from third party sources and is believed to be reliable; however, its accuracy is not guaranteed and should not be relied upon in any way, whatsoever. This presentation may not be construed as investment advice and does not give investment recommendations. Any opinion included in this report constitutes the judgment of Capital Advisors, Inc. as of the date of this report, and are subject to change without notice.

This commentary does not purport to be a statement of all material facts relating to the securities mentioned. The information contained herein, while not guaranteed as to accuracy or completeness, has been obtained from sources believed to be reliable. Opinions expressed herein are subject to change without notice.

The investment return and principal value of an investment will fluctuate so that an investor's portfolio may be worth more or less than its original cost at any given time. Due to differences in portfolio timing and position weightings, the returns for any individual portfolio managed by Capital Advisors may be lower or higher than any performance quoted.

The **S&P 500 Index** is a stock market index based on the market capitalizations of 500 leading companies publicly traded in the U.S. stock market, as determined by Standard & Poor's. The index is calculated on a total return basis with dividends reinvested and is not assessed a management fee.
The **Russell 1000 Growth Index** seeks to track the investment results of an index composed of large- and mid-capitalization U.S. equities that exhibit growth characteristics.
The **Russell 1000 Value Index** seeks to track the investment results of an index composed of large- and mid-capitalization U.S. equities that exhibit value characteristics.
MSCI EAFE Index is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the U.S.
MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets.
MSCI EAFE Small-Cap Index is a free float-adjusted market capitalization index that is designed to measure the equity market performance of small- and mid-cap stocks in the developed markets, excluding the U.S.

Estimated portfolio yield represents the 12-month run-rate of interest and/or dividend payments in a strategy divided by the market value of the securities and cash reserves invested in the strategy. Estimated interest/dividend payments and market values are calculated by a portfolio accounting system from *Orion* using a single client portfolio that Capital Advisors believes to be representative of clients' portfolios invested in the same strategy. The actual portfolio yield for any single client portfolio may be lower or higher than the yield quoted. The underlying holdings of any presented portfolio are not federally or FDIC-insured and are not deposits or obligations of, or guaranteed by, any financial institution.

Security Recommendations: The investments presented are examples of the securities held, bought and/or sold in the Capital Advisors strategies during the last 12 months. These investments may not be representative of the current or future investments of those strategies. You should not assume that investments in the securities identified in this presentation were or will be profitable. We will furnish, upon your request, a list of all securities purchased, sold, or held in the strategies during the 12 months preceding the date of this presentation. It should not be assumed that recommendations made in the future will be profitable or will equal the performance of securities identified in this presentation. Capital Advisors, Inc., or one or more of its officers or employees, may have a position in the securities presented, and may purchase or sell such securities from time to time.

Items of Note Regarding Exchange Traded Funds: An Exchange Traded Fund (ETF) is an investment company that typically has an investment objective of striving to achieve a similar return as a particular market index. The ETF will invest in either all, or a representative sample of the securities included in the index it is seeking to imitate. Like closed-end funds, ETFs can be traded on a secondary market and thus have a market price that may be higher or lower that its net asset value (NAV). If these shares trade at a price above their NAV they are said to be trading at a premium. Conversely, if they are trading at a price below their NAV, they are said to be trading at a discount.

The information provided is supplemental to a fully compliant presentation. A complete list of Capital Advisor's portfolio models and compliant presentations are available by contacting Capital Advisors at the number listed below. The actual return and value of an account fluctuate, and at any time the account may be worth more or less than the amount invested.

Additional information, including management fees and expenses, is provided on Capital Advisors' Form ADV Part 2, available upon request or at the SEC's Investment Adviser Public Disclosure site, https://adviserinfo.sec.gov/firm/summary/104643

As with any investment strategy, there is potential for profit as well as the possibility of loss. Capital does not guarantee any minimum level of investment performance or the success of any portfolio or investment strategy. All investments involve risk (the amount of which may vary significantly) and investment recommendations will not always be profitable. The investment return and principal value of an investment will fluctuate so that an investor's portfolio may be worth more or less than its original cost at any given time. ***Past performance is not a guarantee of future results.*** Capital Advisors, Inc. does not provide tax or legal advice and recommends you consult with your tax and/or legal adviser for such guidance. Presentation is prepared by: **Capital Advisors, Inc.** Contact Capital Advisors for a list and description of all firm composites and/or copy of our most recent Form ADV Part 2: 1-866-230-5879 **www.capitaladv.com**