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THE TEMPO VANTAGE

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Let History Be Our Guide

The market is all about expectations and rarely moves due to things already on our near-term radar.

Exogenous events, or things we don't expect, are more often the culprit, especially for significant declines.

That was certainly the case when Russia invaded Ukraine in the first quarter of 2022.

Although there were some concerns about Russian troop build-up on the Ukraine border in December 2021, the market was not worried about this as we entered 2022. In fact, the market reached a near-term peak on January 3, 2022.

As the possibility of an attack became more real, the market reacted swiftly and negatively. The markets also did what they seem to do best – overreact.

By February 23, 2022, the day *before* the actual invasion, the market had already fallen by 11%. Over the first two weeks of the war, the market fell a bit more, making the peak to trough decline 13%.

While there many reasons to be upset about the war, from an investment perspective the biggest impact is the price of oil, which is about the only area where Russia affects the global economy.

The rise in the price of oil gave fuel (pun intended) to the existing fear that inflation is getting out of control, which is certainly bad for the markets.

Once cooler heads prevailed, the market realized that near-term inflation might be just that – near term. From February 23 to the end of the quarter the market gained 8.6%.

For the quarter, the S&P 500, which was the best performing sector, was down 4.6%. Small caps were down 5.6%, and international stocks were down 7%.

The sector leaders were energy (+33%), commodities (+24%), defense (+7%), utilities (+4%), and infrastructure (+1%). Healthcare (-9%) and technology (-13%) lagged.

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Over the quarter the yield on 10-year Treasurys rose from 1.8% to 2.3%. Higher interest rates mean lower bond prices, which translates to negative returns for bond holders. Bonds had as bad a quarter as stocks, or worse!

Across the board, bonds lost money in the first quarter: emerging market bonds (-8%), intermediate bonds (-6%), muni bonds (-6%), convertible bonds (-5%), global bonds (-5%), high-yield bonds (-4%), Short-term (-3%), inflation bonds (-2%), bank-loan bonds (-0.5%.)

As an investment advisor, vendors have been gently reminding me of two particular historical charts. One shows how the markets have historically reacted after the Fed starts raising interest rates (which they did). The other shows how the markets have historically reacted to major geopolitical events such as the war in Ukraine.

While the results over the short term (i.e. three months) can be dicey, both charts show that the prospect for a higher stock market six months and one year after these events is actually quite good.

This weekend I was reminded of one of Peter Lynch's (legendary stock fund manager from Fidelity, for those of you too young to remember) favorite methods for selecting stocks: Are stores busy?

On Saturday I went to the mall with my son (to buy pants, if you must know). I was shocked at how crowded it was. As crowded as I see at the December Holidays.

And, people were buying. There was a 15-minute line for us to check out with our purchases!

The pent-up demand I wrote about last July is alive and well!!!

Speaking of Peter Lynch, some of you may have seen an interview with Lynch from 1994 recently resurface. Essentially, he said he has no idea where stocks are going in the short run, but in the long run corporate profits rise about 8% a year and stocks will follow.

Sure enough, even while enduring some significant bear markets, stocks have risen between 8% and 9% per year over the past 28 years.

Putting it all together, I not only like the prospect for stocks better than bonds over the short to intermediate term, but I think that there is a good chance of an attractive return for stocks as we look out one year or more.

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Tempo Financial Advisors' 1st Quarter Investment Performance

Tempo's four investment strategies all had successful first quarters relative to benchmarks. One program was even able to generate a positive return in the face of negative returns for both stocks and bonds.

I'd normally consider the first quarter return of +1.4% for **Tempo Dynamic Growth** to be fair. But when you learn that the benchmark for Dynamic Growth returned -4.3%, and you realize that Tempo outperformed by nearly 6%, you appreciate that any positive return in this environment was spectacular.

How did Dynamic Growth do it? In a word: commodities.

While it certainly helped that we were at the lowest allowed allocation to equities (40%), commodities (18% of portfolios), which returned +24% in the quarter, did the heavy lifting. It also helped that our bond allocations (inflation bonds: -2%, bank loan bonds: -0.5%) performed significantly better than the BarCap Agg Bond Index (-5.9%).

Dynamic Growth portfolios have been adjusted for the second quarter. The biggest change is that commodities are gone in favor of small cap value. Although commodities performed extraordinarily well, our Dynamic models tend to shy away from the most volatile sectors, which commodities have been lately.

With most stock and bond categories down 5% or more in the first quarter, you might expect that the benchmarks for Tempo Lifestyle would be down in that range as well.

You'd be right.

The benchmarks for conservative to aggressive Lifestyle accounts ranged from -4.5% to -5.5% in the first quarter. I am quite happy that actual **Tempo Lifestyle** returns ranged from -2.5% for conservative accounts to -4.5% for aggressive accounts. That translates to outperformance between 1% and 2% for the quarter.

The source of our outperformance did not come from the equity side of the ledger, where tactical overweights (infrastructure, healthcare, technology) had mixed success. Rather, our strategic allocations to specific bond sectors (i.e. bank loan) and alternatives (i.e. managed futures, commodities) allowed the "lower risk" portion of portfolios to significantly outperform the BarCap Agg Bond Index.

That also explains why conservative accounts outperformed the benchmark by more than aggressive accounts (2% v. 1%), since conservative accounts have a higher allocation to bonds & alternatives.

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Tempo's two income strategies, Dynamic Income and Diversified Income, also did a nice job of avoiding the worst of the bond market in the first quarter.

Tempo Diversified Income had the better of it with a return of -1.4% in the first quarter, versus -2.9% for **Tempo Dynamic Income**. Both look great as compared to the BarCap Agg Bond Index (-5.9%)

Even more significant is that Diversified Income and Dynamic Income returned +3.4% and +2.8%, respectively, over the 12 months ending March 31, 2022. Over the same time period the BarCap Agg Bond Index returned -4.2% and short-term bonds returned -2.8%.

Company News

With a pandemic and a war in Ukraine, it seems frivolous to tout my winning the Five Star Wealth Manager award with my usual fanfare. This year marked my 11th win.

What is not frivolous is my gratitude to you, my fabulous clients. Thank you for your support and confidence. Your financial well-being is my focus every day.

Reminder

Please contact us if there has been a change in your financial circumstances that would warrant a fresh perspective on your portfolio.

Dan

Daniel J. Traub

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