UPLAND
Capital Management LLC

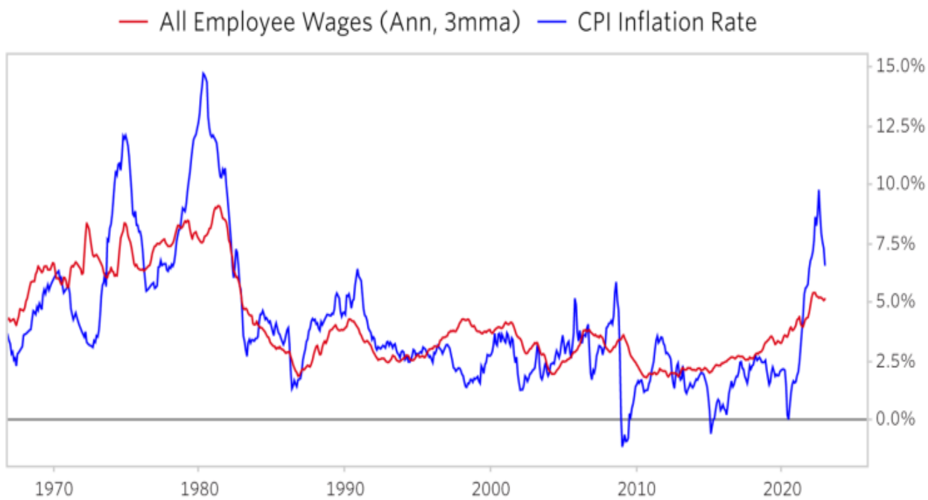
2022 YEAR-END REVIEW AND COMMENT

Asset prices staged a broad-based recovery in the year's final three months. U.S. equity and bond markets rebounded as inflation, while still high, decelerated for a fifth straight month and the Fed moderated it's December rate hike to 'only .25%'. Nearly all sectors in the MSCI All Country World Index moved higher. Treasury's bonds rallied; credit spreads tightened; most fixed income sectors finished the quarter with positive returns. The S&P 500 Index gained 7%. The energy, industrial and consumer staples sectors were the quarters strongest performers, while the consumer discretionary sector was a notable laggard, down 10%. Notably, the growth-heavy Nasdaq Composite continued to lag, declining for a fourth consecutive quarter. The U.S. dollar moved sharply lower. International developed and emerging markets also experienced exceptionally strong fourth quarter performances. European stocks, boosted by the euro's strong appreciation against the U.S. dollar, generated the largest gains among the world's developed economies, advancing 19%. The market's rally off the mid-October lows seems to have been premised on the expectation that central banks would pivot, cutting rates before their economies deteriorated much further. *Notwithstanding this broad fourth quarter strength, most asset categories finished the year with double digit percentage price declines.* The S&P 500 Index finished the year down 18%, *the Index's worst performance since 2008.* The U.S. dollar gained a further 9% against a basket of trading partner currencies. During the year, the *Federal Reserve raised interest rates seven times* including four 75bp increases, bringing the current Fed Funds rate to 4.25 - 4.50%. *U.S. Treasury bonds posted their worst annual loss in its history, down 12.5%.*

COMMENT:

HEAVY FOG

At the start of 2023, markets appear overly sanguine about the impact of tighter financial conditions and persistent inflation on corporate margins and consumer demand. *In our view, it seems more likely that markets will continue to face choppiness in 2023 with increasing headwinds from declining earnings, tightening financial conditions, and the rising risk of a recession in major economies.* Even if we dodge that outcome, the unfavorable growth-inflation mix is a threat to corporate margins and earnings potential as central banks reiterate ever more hawkish determination. Indeed, the speed and magnitude of monetary tightening in 2022 was among the most aggressive in history. *Yields in most major markets more than doubled.* Global manufacturing activity decelerated further in Q4, with new orders slumping and inventories rising. While the rate of inflation is expected to slow materially in coming months, persistent cost pressures may keep it elevated, keeping rates higher for longer. Categories where price increases tend to be more persistent, particularly service sectors wages, now account for the bulk of current inflation drivers. What this means is that even if goods inflation falls to 2% or below, if wage inflation remains near 5%, overall inflation will tend to revert toward 5%.



Source: 2023 Bridgewater Associates

Another leading recessionary benchmark is the recently inverted Treasury yield curve (higher short-term rates than longer-term rates). The Treasury yield curve hasn't been this inverted since the early 1980s. Historically, an inverted yield curve has been a reliable leading indicator of future economic weakness, though uncertain in scale and timing. Recessions are typically only identified in hindsight. However, the leading indicators for the world economy, produced by the Organization for Economic Cooperation and Development, can offer an important signal in benchmarking recessionary periods. In this index, a drop below 99 has tended to happen right around the start of a global recession. It's a repeating story, and it's now below 99 again, signaling another potential recessionary period.

OECD leading indicators point to a global recession

Source: Organization for Economic Cooperation and Development, Bloomberg data as of 12/2/2022

Even in calm years, markets still experience some ups and downs. While 2023 could be a sideways choppy market, we see the potential for significant volatility as earnings estimates are revised meaningfully lower. We continue to manage the portfolios with a defensive tilt, focusing our underweight equity position on value stocks and hedged equity investments. In this rising rate environment, our fixed income proxies remain heavily weighted toward higher quality, short duration bond investments and cash equivalents, recently yielding about four percent. It's worth noting that equity markets tend to bottom out months before earnings finally trough. *While we remain cautious of likely near-term market developments, there are lots of features in the financial landscape that could develop more positively and cause us to change our outlook.*