Mainsail Quarterly Market Commentary

1ST QUARTER 2023

Return of the Jedi

While I'm sure Star Wars fans will have heard by now, in early April Lucasfilm announced plans for three more Star Wars films. While a huge fan of most of the films, I would have to say Return of the Jedi is definitely my favorite.

After a cruel and punishing year in 2022, Global Stocks rebounded in Q1, with beaten down Tech Stocks leading the way. Much like Luke in Return of the Jedi, when Luke returns to face and eventually defeats Vader against all odds, growth stocks staged an impressive rebound, despite severe macro headwinds. This rebound helped push equity markets higher with the S&P 500 adding 7.03%. Unlike last year, when most asset classes were in the red, Q1 saw Developed International Stocks, Emerging Market Stocks, Small Cap Stocks, and Investment Grade bonds all solidly in the green.

Maybe the most notable event of Q1 was the extreme volatility witnessed in the bond market. Over a period of 5 days surrounding the collapse of Silicon Valley Bank, the 2-Year Treasury yield fell an astonishing 100 basis points. To put this move in context, by some measures it was the largest 5 day move on record, surpassing the decline last seen right before the 1987 stock market crash. As investors quickly assessed how the troubles at Silicon Valley Bank (SVB) were likely to lead to a Fed pause in their rate hiking cycle, many were caught offside and the market expectations adjusted swiftly. Since then, many regional banks have succumbed to pressure but the 2-year yield has remained stable.

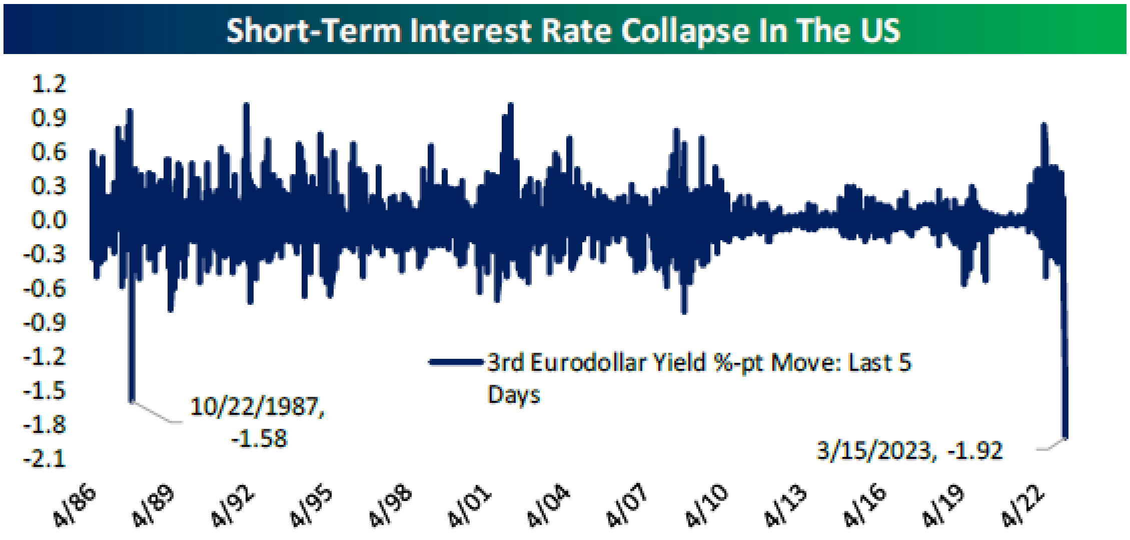


Table 1 - Source Bespoke Investment Group

As we have talked to clients over the last three months a few common questions/themes stick out. First, what is going on with the banks? Secondly, how will the debt ceiling negotiations affect my investments?

On the banking front, it is clear that a confluence of events has led to deep stresses in the regional and small banking sector. In our view, this was brought about by the following events: 1) banks brought in record deposits post COVID, 2) many banks took these deposits and bought Treasury bonds while yields were at historic lows, and as rates rose, these investments declined in value, 3) as Treasury yields rose, depositors also started withdrawing funds to buy high yielding Treasuries to maximize their return, leaving banks scrambling to keep deposits, 4) as contagion spread, many of the less diversified banks with higher percentages of uninsured deposits (SVB had over 89% of their deposits uninsured) were left vulnerable to would-be bank runs with no recourse. While we are in the camp that these bank failures are not likely to lead to systemic issues for the U.S. economy, we do think the result will be a challenging earnings environment for banks and a period of increased regulation to boot.

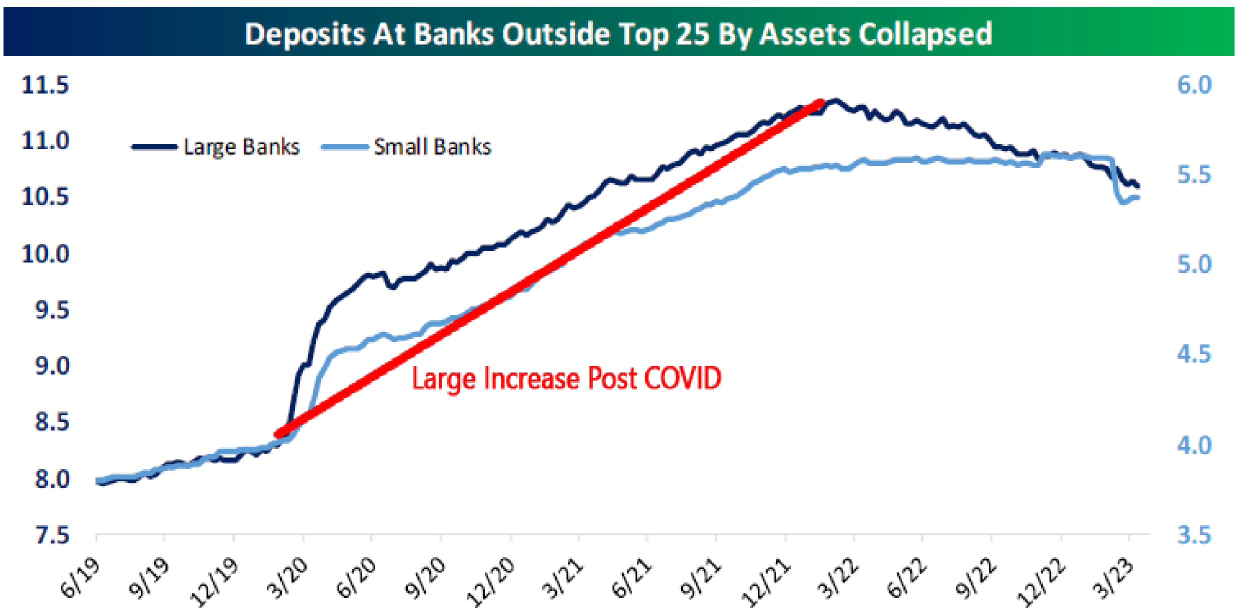


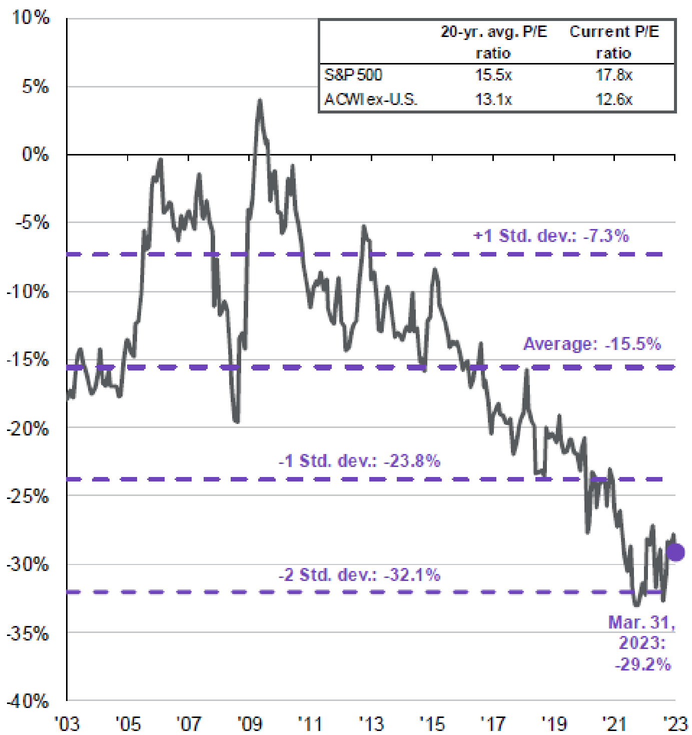
Table 2 - Source Bespoke Investment Group

As for the debt ceiling. While it is impossible to opine on what Congress is thinking and what legislators might do, history has shown that markets have tended to look past these sorts of events with an assumption that they eventually get solved. The last time we had a scare similar to what clients are worried about was 2011. At that time, S&P Global Ratings downgraded U.S. debt from AAA to AA+ with the rationale that Congress was too dysfunctional to keep the AAA rating. Pundits opined that a possible downgrade would lead to skyrocketing interest rates, a collapse in the dollar, and market turmoil. What instead followed was a sharp drop in rates, a run-up in the dollar and a market rally. While this would not have been the outcome the Mainsail Investment Committee would have envisioned, it was the result, nonetheless. The reason we share this story is to show that it is very hard to guess what Congress will do and even harder to predict the market response. As such, we don't believe such binary and temporary events are to be traded around or should cause investors to fundamentally change their long-term investment allocations.

That being said, for clients who have been leaning into equities in their allocations over the past 10+ years due to low interest rates, we have been advising a re-think and have been moving many down the risk spectrum towards a more balanced strategy. This is a reflection of our belief that bonds offer a compelling risk/reward for strategies in a way they haven't for some time. In addition, cash is now a reasonable alternative for those looking to lower risk and plan for cash flows in retirement. With Money Market yields north of 4.5%, you can finally get paid to be conservative. As long as your strategy is balanced and aligned with your needs for cash flow, there likely isn't a reason to make short term changes based upon current events.

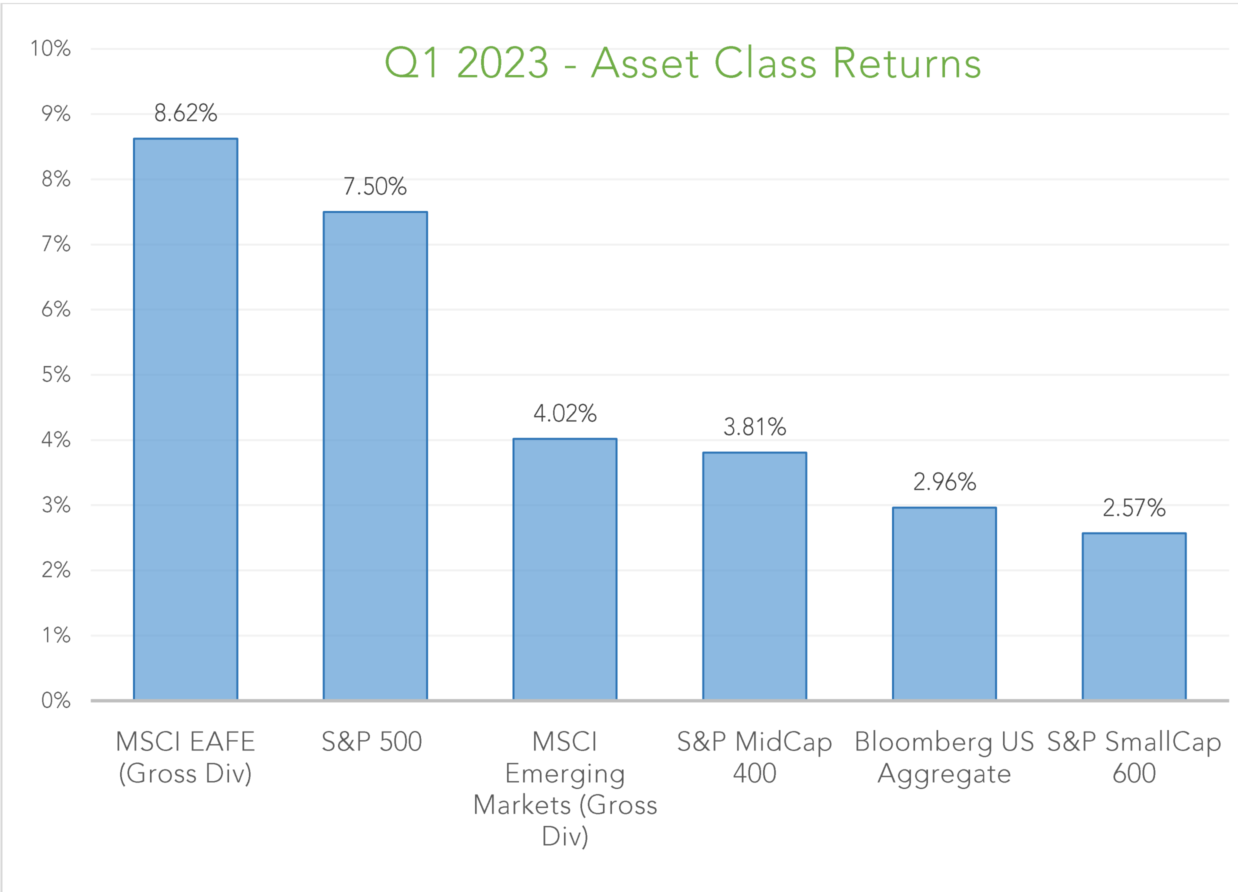
Finally, the MIC has turned much more favorable on Developed International stocks for the first time in over 5+ years. There are several tailwinds which we believe make this asset class attractive. For one, the US dollar, after a sharp run-up post COVID it seems to have peaked in 2022. If the dollar continues to decline relative to other currencies, this should help returns for international stocks. Secondly, we believe that valuations are finally compelling enough to warrant optimism. Much of the bad news from the war in Ukraine and preceding inflation spikes seem to be priced into equities as PE multiples contracted to a record spread as compared to US equities in 2022. Given the current low unemployment rates and the global slowdown in earnings growth rates, investors might discover favorable risk-adjusted returns by focusing on traditionally defensive companies within the investment universe of Developed International markets. Additionally, dividend yields for Developed International Stocks are significantly higher than their U.S. counterparts (see chart below). As such, for clients in our asset allocation strategies as well as our retirement income focused strategy, we have been adding to this asset class through the latter part of 2022 and into Q1 of 2023.

International: Price-to-earnings discount vs. U.S.
MSCI All Country World ex-U.S. vs. S&P 500, next 12 months



International: Difference in dividend yields vs. U.S.
MSCI All Country World ex-U.S. minus S&P 500, next 12 months

Source: FactSet, MSCI, Standard & Poor's, J.P. Morgan Asset Management.
Guide to the Markets – U.S. Data are as of March 31, 2023.



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The companies engaged in business related to a specific sector are subject to fierce competition and their products and services may be subject to rapid obsolescence. Sector investments are companies engaged in business related to a specific sector. They are subject to fierce competition and their products and services may be subject to rapid obsolescence. There are additional risks associated with investing in an individual sector, including limited diversification.

INDEX DEFINITIONS

Inclusion of these indexes is for illustrative purposes only. Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance. Individual investor's results will vary. Past performance does not guarantee future results.

The S&P 500 is an unmanaged index of 500 widely held stocks that is generally considered representative of the U.S. stock market.

The Barclays Capital US Aggregate Index is an unmanaged market value weighted performance benchmark for investment grade fixed rate debt issues, including government, corporate, asset backed, mortgage backed securities with a maturity of at least 1 year.

The S&P SmallCap 600® measures the small-cap segment of the U.S. equity market. The index is designed to track companies that meet specific inclusion criteria to ensure that they are liquid and financially viable.

The S&P MidCap 400® Index provides investors with a benchmark for mid-sized U.S. companies. The index, which is distinct from the large-cap S&P 500®, measures the performance of mid-sized companies, reflecting the distinctive risk and return characteristics of this market segment.

Dow Jones U.S. Select Dividend Index represents the country's leading stocks by dividend yield and is made up of one hundred stocks which are selected to the index by dividend yield, subject to screens for dividend-per-share growth rate, dividend payout ratio and average daily dollar trading volume.

The Dow Jones U.S. Select REIT Index intends to measure the performance of publicly traded REITs and REIT-like securities. The index is a subset of the Dow Jones U.S. Select Real Estate Securities Index (RESI}, which represents equity real estate investment trusts (REITs} and real estate operating companies (REOCs} traded in the U.S. The indices are designed to serve as proxies for direct real estate investment, in part by excluding companies whose performance may be driven by factors other than the value of real estate.

MSCI Emerging Markets is designed to measure equity market performance in 25 emerging market indexes. The index's three largest industries are materials, energy, and banks.

NASDAQ Composite Index is an unmanaged index of securities traded on the NASDAQ system.

The Barclays US Corporate High Yield 2% Issuer Capped Bond Index is an issuer constrained version of the flagship US Corporate High Yield Index, which measures the USD-denominated, high yield, fixed-rate corporate bond market. The index follows the same rules as the uncapped version but limits the exposure of each issuer to 2% of the total market value and redistributes any excess market value index wide on a pro rata basis.

MSCI World Ex-U.S. (Net Div) Index captures large and mid-cap representation across 22 of 23 Developed Markets (DM} countries*-

-excluding the United States. With 1,023 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.

ASSET CLASS DEFINITIONS

U.S. Large Cap Equity

Russell 1000 Index: Based on a combination of their market cap and current index membership, this index consists of approximately 1,000 of the largest securities from the Russell 3000. Representing approximately 92% of the Russell 3000, the index is created to provide a full and unbiased indicator of the large cap segment.

U.S. Mid Cap Equity

Russell Midcap Index: A subset of the Russell 1000 index, the Russell Midcap index measures the performance of the mid-cap segment of the U.S. equity universe. Based on a combination of their market cap and current index membership, includes approximately 800 of the smallest securities which represents approximately 27% of the total market capitalization of the Russell 1000 companies. The index is created to provide a full and unbiased indicator of the mid-cap segment.

U.S. Small Cap Equity

Russell 2000 Index: The Russell 2000 Index measures the performance of the small-cap segment of the U.S. equity universe. The Russell 2000 is a subset of the Russell 3000 Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership. The Russell 2000 Index is constructed to provide a comprehensive and unbiased small-cap barometer and is completely reconstituted annually to ensure larger stocks do not distort the performance and characteristics of the true small-cap opportunity set.