PARKSIDE INVESTMENTS

Market Commentary

May 4, 2022

Dear Clients/Friends:

The risks in the market (including higher interest rates, Ukraine war, supply chain issues, etc.) have not changed much since our quarterly letter to you last month – however market sentiment has become more cautious. The excesses from years of easy monetary and fiscal policy have unwound rapidly. While high quality companies avoided much pain during the first quarter, April was not nearly as kind.

Equity markets continued to slide in April, with the S&P 500 Index losing 8.7% during the month and 13% YTD. This was the worst January through April stretch for the benchmark dating back to 1939. Bonds have also suffered dramatically in 2022, with the Bloomberg Barclay's Intermediate Aggregate Index down 2.5% for April, bringing its year-to-date losses to 7%. The declines in both the stock and the bond markets are truly historic.

Speculative parts of the equity markets (typically newly public companies with limited or no earnings and questionable business models) are experiencing a significant downward reevaluation. Half of the Nasdaq's components are down 50% from their highs, while 22% are off by 75% and 5% have registered a 90% drawdown.

Despite the negative market tone, we note the following constructive elements:

- The financial system is stable, with banks well capitalized and no visible signs of broad stress in the credit markets;
- Valuations for highly profitable companies outside of the technology cohort are largely very reasonable and bordering on cheap;
- Corporations are in relatively strong financial condition - high debt service coverage ratios and limited near-term maturities.
- Inflationary pressures in the supply chain, the biggest near-term challenges facing corporations, are showing signs of stabilization and/or improvement.

Bond markets already reflect expectations for more than 200 basis points (2.00%) of additional Fed interest rate hikes over the remainder of the year, even after today's 0.50% Fed rate hike. Although it is difficult to predict a market bottom, we believe the bond market is at or near a point of stabilization. With the 10-year U.S. Treasury hovering around 3%, bonds now offer far better returns for the next 5-10 years, even after adjusting for some inflationary pressure. As such, we believe bonds with modest durations (3-7 years until maturity) are more compelling today than they have been in many years.

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Determining the timing for when equity volatility eases and stocks resume an upward track is more of a challenge. The price/earnings ratio on the S&P 500 has fallen from over 22x at the beginning of 2022 to less than 18x today. Though this appears to be a reasonable level given interest rates are likely to remain low by historical standards even after the Fed completes its hiking cycle, equity markets often overcorrect before returning to equilibrium levels.

Despite the current gloom in the market, we remain positive toward companies and industries with reasonable valuations, generating high levels of cash flow, and a proven commitment to share profits with shareholders through increasing dividends and/or share buybacks. We are adding to a few positions that have increased 2022 distributions at a far higher rate than at any point in the past decade. Additionally, we are using the current market weakness to selectively add to positions of profitable and growing companies that have been oversold while also proactively harvesting tax losses to offset gains taken earlier in the year when we increased cash positions.

Should you have any questions, feel free to give us or anyone on the Parkside Team a call.

Sincerely,

Alan Cole **Chris Engelman**

President Managing Director

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