NBW CAPITAL
LLC

INVESTMENT REVIEW & OUTLOOK
(March 31, 2022)

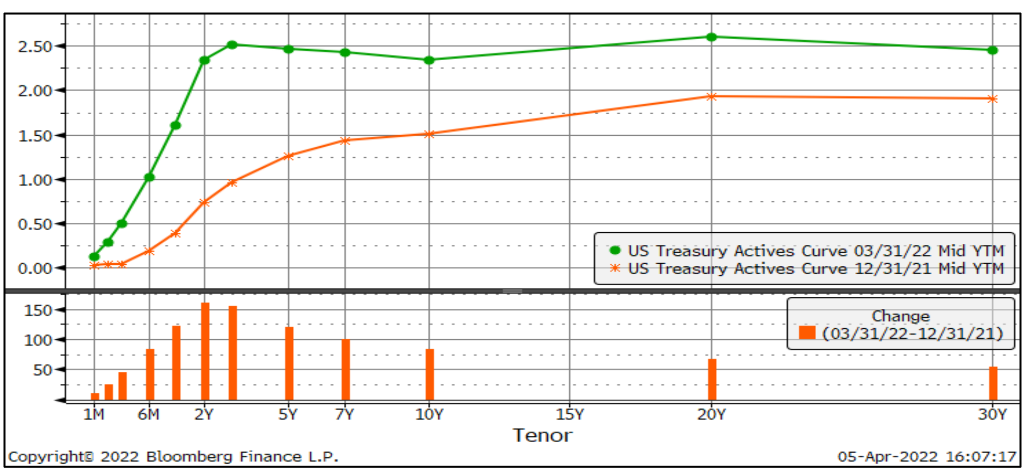
This edition of the INVESTMENT REVIEW & OUTLOOK includes a summary of returns for the financial markets for the first calendar quarter of 2022.

	Three Months Ended 3/31/2022 Total Returns	Twelve Months Ended 3/31/2022 Total Returns
S&P 500 (Equities)	-4.60%	15.65%
Bloomberg Barclays U.S. Aggregate Bond Index (Bonds)	-5.93%	-4.15%
Alerian Total Return Index (MLPs)	18.81%	36.56%
Russell 2000 (Small Cap Stocks)	-7.53%	-5.79%
MSCI EAFE (Foreign Stocks)	-5.79%	1.65%

*The above table is a performance cross section of market indices that best resemble strategies offered by NBW Capital. These are here to give you a better understanding of how these markets performed quarter-to-date and year-to-date. To locate your individual account performance, please reference the second page of your individual account statement(s).

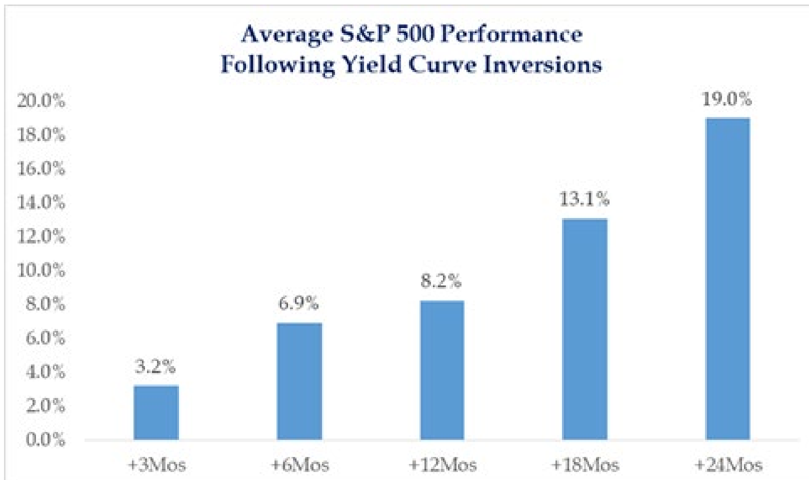
INFLATION CONCERNS WEIGH ON MARKETS

Equity markets have struggled year to date, with the S&P 500 down 4.60%, as inflation concerns have moved front and center on investor's minds. We have mentioned in our past several quarterly letters that inflation trends did not appear transitory and the Federal Reserve (Fed) may be falling behind the curve. Since the beginning of 2022, that sentiment has become market consensus and the Fed now seems intent on reigning in inflation. While it is not our base case scenario, it is not out of the realm of possibilities that the central bank's response could induce a mild recession. With the debate now shifted to whether the rate hikes will be 25 or 50 basis points, the bond market has begun pricing in the expected actions. Over the first quarter, both the short end and long end of the yield curve shifted upward.



As the preceding chart indicates, two-year yields showed the greatest increase in rates in the first quarter. Portions of the yield curve briefly becoming inverted with one of the traditional measures (two-year yields > ten-year yields) is generating a lot of attention, as a potential indicator of a pending recession. It is our opinion that the two-ten year inversion is an important warning of a potential policy mistake by the Fed; however, the most reliable indicator of recessions is an inversion of the three-month vs. ten-year portion of the yield curve. This portion of the curve remains very steep and is not yet signaling potential problems ahead.

While we would agree the rate hiking cycle brings increased risks to the financial markets, more important to us is what this inversion means for future equity returns. Here, the message is more mixed over the past six episodes (dating back to the 1970s), where the subsequent returns after two-year vs. ten-year yield curve inversion were on par with (or even better than) long-term averages.



Source: Strategas

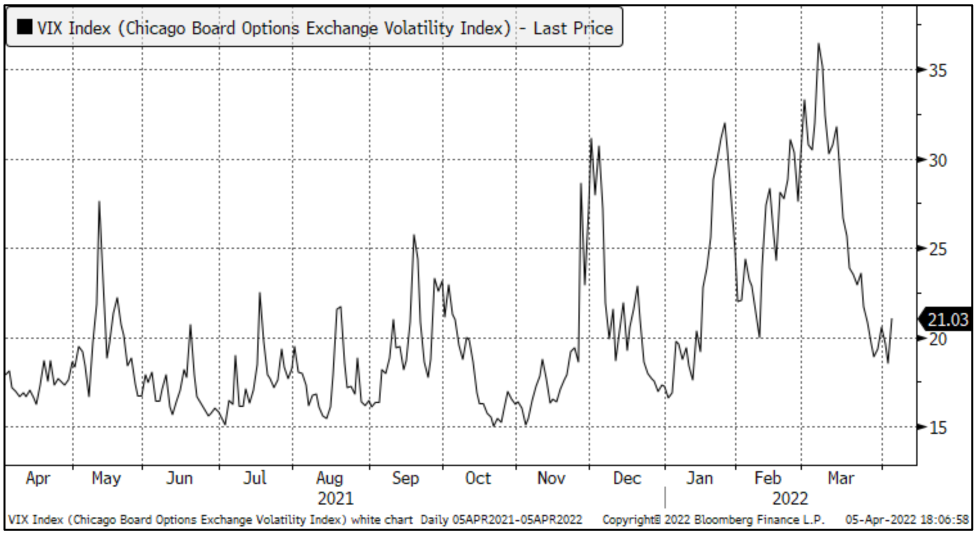
GEOPOLITICS JOIN THE LIST OF CONCERNS

In addition to concerns about inflation and rising interest rates, geopolitical concerns weighed on equity markets as many were surprised by the magnitude of Russia's invasion of Ukraine. The buildup of forces at the border certainly offered warning signals, yet the atrocities witnessed bring the reality home to roost. The U.S., our NATO allies and most countries around the world have responded appropriately with what will prove to be very punishing economic sanctions against Russia. While we can all speculate if more could be done, or the situation handled better, I think most agree avoiding a nuclear confrontation is in everyone's best interest. NBW Capital will be monitoring the impact that sanctions have on the global economy. At this time, it appears that the economies of the European Union will be hurt the most by costs associated with imposing sanctions.

In the early days of the conflict, many questioned what the signal would be to China about their stalemate with Taiwan. We believe the magnitude of economic sanctions and the impact it will have on the Russian economy, as well as the near universal condemnation of the invasion, sent a clear signal about the use of military force. So, while Xi Jinping may have a clear desire to reunify Taiwan, it is safe to say he is a much more rational actor and moral person than Vladimir Putin (pretty low bar) so that concern should continue to subside.

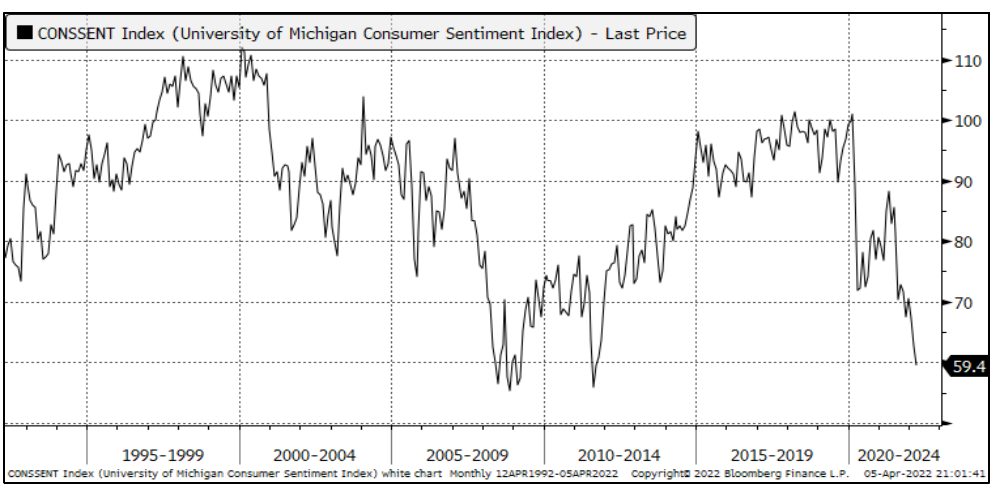
EXPECT HIGHER VOLATILITY THAN LAST YEAR

Overall, the impact of higher rates and geopolitics helped drive the Volatility Index to a one year high of over 35%. Roughly coinciding with that high mark was a 13% pullback in the S&P 500 index, putting the market in correction territory. As we highlighted last quarter, the year 2021 was a year of exceptionally low volatility, with a maximum drawdown of only 5.2% in the S&P 500 index. In many ways, the first quarter of 2022 just reintroduced us to a more normal market environment. While share price volatility is not pleasant, a strong rebound in March helped most equity indices finish the quarter down mid-single digits. Although we would like to say the worst is over, we should also caution that seasonality (summer months tend to be weak) and a mid-term election year may result in a very broad trading range over the near term.



U.S. ECONOMIC GROWTH REMAINS STRONG

The U.S. economy on the other hand continues to move in the right direction, with GDP coming in at 6.9% growth for the fourth quarter of 2021. Labor markets remain strong, with big gains in non-farm payrolls, low unemployment and jobless claims and even an uptick in labor force participation rates. Leading indicators, such as Purchasing Managers Index, are off their highs, but also remain well north of 50, suggesting further expansion of the economy. One surprisingly weak indicator though was the University of Michigan Consumer Sentiment coming in at 59.4, a level not seen since the financial crisis. Weighing on this indicator would be concerns about inflation (ex. higher food and gas prices).



The strength of the economy is a double-edged sword for the equity markets, as strong current revenue and earnings growth prospects are offset by the uncertainty about future rate hikes. As we head into the first quarter's earnings season, we would note that there were very few negative preannouncements prior to quarter end. This dynamic bodes well for full year consensus earnings estimates for the S&P 500, which have actually increased from $220 at the beginning of the year to $226 at the end of the quarter. While we are cautious on companies with foreign exposure or those less able to pass on raw material price increases, we expect the overall earnings season to be positive.

TINA STILL APPLIES, AS BOTH BONDS AND EQUITIES UNDERPERFORM

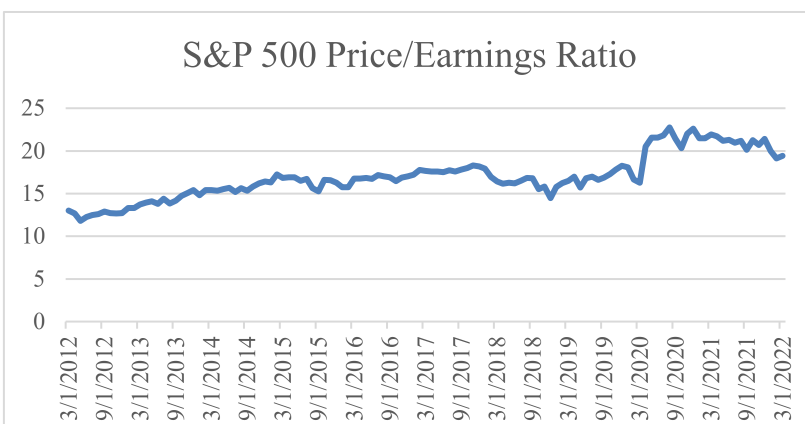
As it relates to owning equities, we commented about TINA (There Is No Alternative) last quarter. Given the pullback in the equity market, we feel it is important to revisit the topic. To the extent that higher than expected inflation is weighing on the equity market, long duration bonds (maturities more than a couple years) did not provide much safety or diversification, as the Bloomberg Barclays U.S. Aggregate Bond Index was also down 5.93%. While one quarter does not make a trend, investors should be concerned that the negative correlation between bond and equity prices that have been in place for the last 20 years may be coming to an end.

Indeed, the previous 100+ years generally saw positive correlations between bond and equity prices, as higher discount rates applied to a company's future cash flow typically resulted in lower equity prices. As we enter a period of inflation, and potentially higher interest rates, which the U.S. has not seen in over 30 years, it's possible this principle of investing could return. This situation would be particularly challenging for strategies with names such as Risk Parity, Low Volatility or Dynamic Asset Allocation. All of these have benefitted from low or negative correlations across asset classes. Our preference in this environment is to stay in short duration fixed income assets for those clients seeking lower volatility.

OUTLOOK

While 2022 has brought challenges on the inflation and geopolitical front, the overall economy remains in good shape. We believe record high household net worth and strong employment trends will help sustain strong consumer demand even in the face of higher interest rates. Raw material costs are showing signs of peaking, and most companies have been able to pass through costs and maintain margins. As is most often the case, earnings growth drives stock prices, and with over 10% growth in the consensus S&P 500 forecast (with an upward bias), we see a favorable backdrop on business fundamentals.

Furthermore, valuation has become more attractive. The combination of strong earnings growth, continued upward revisions to earnings estimates and a pullback in the market have brought the price/earnings multiple down to 19.5x earnings. While this valuation level is more attractive than the 22x multiple from a year ago, most would not call the market cheap (unless interest rates stay low). With the market digesting the negative headlines from the first quarter, we see the market range bound within the past year's levels over the near term.



Source: Bloomberg

We stand by our comment from last quarter that, longer term, we see equities as one of the best ways to protect your wealth against inflation. The noise of market sentiment can be distracting during periods like the one we are in. To the extent we may modestly raise and lower cash, it is done through a disciplined process of mostly trimming winners and adding on pullbacks when our technical model gives us confirmation. A lesson learned over many years, the key to investing in more volatile times is to stick to a disciplined process.