P3 Parks Capital

MARKET OUTLOOK Q2 2023
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Welcome to the Market Outlook for the second quarter of 2023. In our last outlook, we left you with a few key thoughts; let's recap them.

RECAP

1. We believed at the time that most of the inflation problem was priced into the financial markets, and we were then in the bottoming phase of this correction.
2. Inflationary pressures had also started to reduce, and we expected that trend to continue.
3. We also expected that the aggressive rate hike actions by the federal reserve should start to slow down and that the Fed is less likely to raise rates at the same pace in the future.
4. Lastly, because of those above points, we believed it was time to start deploying the cash reserve into areas of opportunity like the fixed-income market, the international markets, and many more.

Portfolio Overview

As we start the second quarter, I am happy to report that many of those critical points still hold true. Inflation in the United States is continuing to show signs of easing or at least is not growing at the same pace as last year; the Federal Reserve's rate hikes have also started to slow down, and the expectation of future rate hikes has significantly reduced. The economy is also showing signs of resilience, with unemployment levels still at near-all-time lows and consumer spending continuing at a healthy pace.

As per our last outlook, we have made significant changes to our portfolios in the previous quarter. We have deployed the cash we raised in January of 2022 in a new bond portfolio which comprises of short and intermediate-term bonds.

We have also made additions to our exposure in emerging and international markets, and allocated cash in areas of the markets that would benefit from a stable Federal Funds rate in the near term.

While all of the above changes to the portfolio align with what we discussed in our last outlook, we have also made additional changes to the portfolio that we still need to discuss.

Primarily, we have reduced our overall exposure to U.S. equities wherever possible, tax-wise, and wherever warranted. Today I want to discuss with you the reasons for this significant change.

Since we last talked, **two significant developments have given us cause for concern** in the near term for U.S. equities.

Concern # 1: Consecutive failure of two major banks

The first development is the consecutive failure of two major banks in March of this year: the Silicon Valley Bank and the Signature Bank. In March, I wrote in detail about our views of these bank failures; if you still need to read that article (*Silicon Valley Bank (SVB) – An unintended consequence of Government and Regulator Panic*), I encourage you to do so. This article is available on our website - ParksCapital.com). We are also happy to send you a printed copy of the article upon request.

What concerns us in the aftermath of these bank failures is not so much that many more banks would fail in the U.S.; although possible, it is less likely to happen. What concerns us is that due to these bank failures, regulators like the Federal Reserve, FDIC, and even Congress will impose stricter regulations on small and mid-size banks, leading to an overall reduction in lending to businesses and consumers.

In light of this developing situation, we have significantly reduced our exposure to small-cap stocks in the portfolio, as smaller companies are more likely to be affected by this change in lending conditions. For this reason, near-term caution is warranted.

This bank crisis also comes with a *silver lining for our portfolios*. The crisis significantly curtails the Federal Reserve's ability to increase interest rates in the near term. Why is that good?

s I had previously mentioned, we just installed a new bond portfolio this year; usually, a reduced expectation in future interest rate hikes by the Fed results in higher bond prices as investors are more comfortable holding bonds when they expect the rates to remain stable or reduce in the future.

So, there is something to celebrate in all this negativity around the bank crisis.

The last point I want to highlight about this crisis is that it also comes with a **valuable lesson for a long-term investor**. What we need to learn from the Silicon Valley bank failure is the value of liquidity. What is Liquidity? It is the ability to turn any investment into cash without any restrictions. In the case of the Silicon Valley Bank, its failure to prepare for a crisis like a bank run and its inability to liquidate its long-term bond portfolio quickly led to its ultimate demise. In the coming month, I will write a detailed article about the importance of liquidity and its role in our investment strategy while selecting investments for your portfolio.

Concern # 2: The looming Debt Limit Crisis

The second event that gives us cause for concern in the near term is the looming debt limit crisis in Washington. Unfortunately, it is not uncommon for the U.S. government to ask Congress to increase the debt limit to pay its bills. But this time around, the divisive political environment and the lack of progress in negotiating such a bill passing is a cause for serious concern.

I want to clarify what the true concern is here. It is not our concern that this issue will not be resolved in the long term and that the U.S. will default due to the inability to pay. The concern is that any delay in passing the debt limit that leads to a *delay in payments on the current debt* will create volatility and instability in the U.S. equity markets.

Gold has proven to be a haven in geopolitical panic and thus would serve as a hedge if this crisis were to come to fruition. In anticipation of this crisis, we have started a new gold position in our portfolios. We will continue to monitor the progress in Washington and manage our portfolio accordingly.

Despite the above mentioned concerns, many parts of the market still show vital signs of recovery. Bonds, technology stocks, and others have shown significant strength in this initial stage of recovery from the correction. We believe this trend to continue going into the second quarter. While volatility is still to be expected, we continue investing in these sectors for long-term growth.

Outlook

In summary, despite these near-term headwinds in the U.S. economy, our **long-term outlook for the equity and bond markets looks promising**. These headwinds are opportunities that, if appropriately managed, can provide an excellent catalyst for long-term gains.

Additionally, you know that charts primarily determine our outlook, and those charts continue to show underlying strength on a long-term basis. We are excited about the future and are confident that our investment strategy will continue to protect us in times of turmoil and generate positive returns in times of growth.

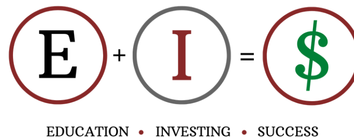
Remember, as long-term investors, we have the luxury of patience and the ability to parse out the noise.

Closing

I want to remind you again: the purpose of this update is not to predict the future. No one can do that. The purpose of this update is to inform you of what we are seeing and how we are preparing for it. Of course, if things were to change between now and the next update in three months, we would be reporting about those changes and how we adapted to them in the next update or during our next conversation.

We cannot close this piece without highlighting one obvious fact: the above view of the markets and the narration of the events is a general view. You know that every portfolio in Parks Capital is managed based on who you are; thus, they all look a bit different based on your risk tolerance and your individual goals. Please keep that in mind.

We are looking forward to talking with each of you in your quarterly meetings. Remember, education plus investing equals success!



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