LNWM Quarterly Commentary – Q1 2023

THE GREAT RESET AND ITS IMPLICATIONS

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> "Of all the hardships a person had to face, none was more punishing than the simple act of waiting."
>
> — Khaled Hosseini, *A Thousand Splendid Suns*

As eventful as 2022 was, you could call it a year of waiting. Investors eagerly awaited each month's inflation numbers, the Fed's next interest rate increase and comments to the press, as well as many other highly anticipated developments. But there was a much bigger waiting game going on. Simply put, many investors were – and still are – waiting for the economic and market environment to revert back to what many of us have experienced most of our adult lives (and for young people under 30, their entire lives): low inflation and low interest rates amid unconstrained and expanding globalization supported by easing fiscal and monetary policies.

The market results in 2022, however, speak to the sea change that has likely started to take place, potentially moving us into a new market regime. The long-term implications for investors are not yet clear, but the forces driving the change in macroeconomic variables seem to be long-term.

Covid-19 revealed fissures in "just-in-time" global supply chains; Russia's invasion of Ukraine has transformed these fissures into national security risks (not to mention the increasing risk of China taking action to absorb Taiwan). This has likely ushered in an era during which the political and economic connections between nations become more polarized as the "peace dividend" fades (see box top of next page).

IN BRIEF

Because of geopolitical, demographic, and economic trends, we appear to be transitioning to a new market regime defined by regionalization, higher inflation and higher interest rates vs. what we have been used to during the past decade (although not high by historical standards).

The implications for the markets are significant but not to be feared as much as the press would lead you to believe: Fixed income is regaining its role as a lower-risk income generator; Equities should continue to provide a hedge against inflation through growth in earnings and dividends. This environment is well-suited for long-term investors that do not need to sell into market weakness.

Because market regime change often takes years to manifest amid great uncertainty, we will be evolving our portfolios to enhance diversification and take advantage of opportunities as they arise.

How this era plays out remains to be seen. Increased geopolitical tension is likely to affect where and how goods are produced – domestically (onshoring), closer to final distribution (near-shoring) or in allied countries (friend-shoring). Resulting shifts in production may keep inflation higher than it has been in the past decades. Additionally, the ramp-up in defense spending, especially by Western economies, could lead to more government borrowing, keeping interest rates higher than what we have become used to in recent decades.

On top of geopolitically induced changes, there are underlying factors that could keep inflation and by extension interest rates higher for longer (although not necessarily above historical standards): an aging/retiring workforce in developed economies; slowing growth in China; higher energy and other input costs in Europe as they decouple from energy dependence on Russia; the global energy transition to cleaner energy; and much less support from US monetary and fiscal policy.

While all of this sounds ominous -- and to some extent the world has become a riskier place -- we posit that the previous market regime could have been the aberration and that we are returning to a more normal time less distorted by the artificial stimulants of fiscal and monetary policies and probably more favorable, as a result, to skilled investors.

What's more, new market regimes (despite the turmoil and the pessimistic headlines) tend to bring with them innovation, new positive trends, and opportunities. If you open the aperture of time, it would be difficult to argue that society is worse off today than it was 100 years ago -- with the exception being the state of natural resources and the planet. Transitions like these take time and the new risks and opportunities they create can take a while to become evident. We expect evolution (not revolution) in our portfolios as we diligently explore ways to benefit from the change ahead.

DWINDLING PEACE DIVIDEND

Starting in the early 1990s, lower military spending due to the end of the Cold War was termed "the peace dividend." And in fact, defense spending as a percentage of US GDP has been almost halved since 1989 to 3.5%, with Europe's allocation remaining much lower.

We would argue that the "peace dividend" defined a world without the ominous threat of world war, allowing for a dramatic expansion in free trade and the globalization of supply chains, integrating the world economy and helping to drive down inflation. These trends appear to be reversing course, as countries have become aware of the national security implications of global interdependencies.

WHAT IS NORMAL?

By the end of 2020, $18.4 trillion in global government debt had negative rates: the lenders were paying the borrowers! Is this normal? As of Jan. 5, 2023, negative yielding debt was down to $0[1], which makes more sense. In equities, 5 big tech companies comprised 23% of the S&P 500's value on Dec. 2021, and US equities represented ~60% of world equity market capitalization -- likely not normal. From a geopolitical perspective, we could equally argue that the past 30 or so years were an anomaly. Prior to that, the 20th century was studded with regime-changing events: two world wars, the oil crisis in the early 1970s, and the dissolution of the Soviet Union in the late 80's/early 90's.

1. Source: "Last bonds with negative yields vanish in latest major market milestone," MarketWatch.com, January 5, 2023.

WHAT HAPPENED IN 2022

2022 was a year for the record books. All told, approximately $35 trillion of wealth was wiped out (at least on paper), with equities accounting for about $25 trillion and the global bond market nearly $10 trillion -- equivalent to about one-third of world GDP[2].

The Dow, filled with lower-valuation equities, was the "winner" dropping only 9%, while the tech heavy Nasdaq sank 33%.

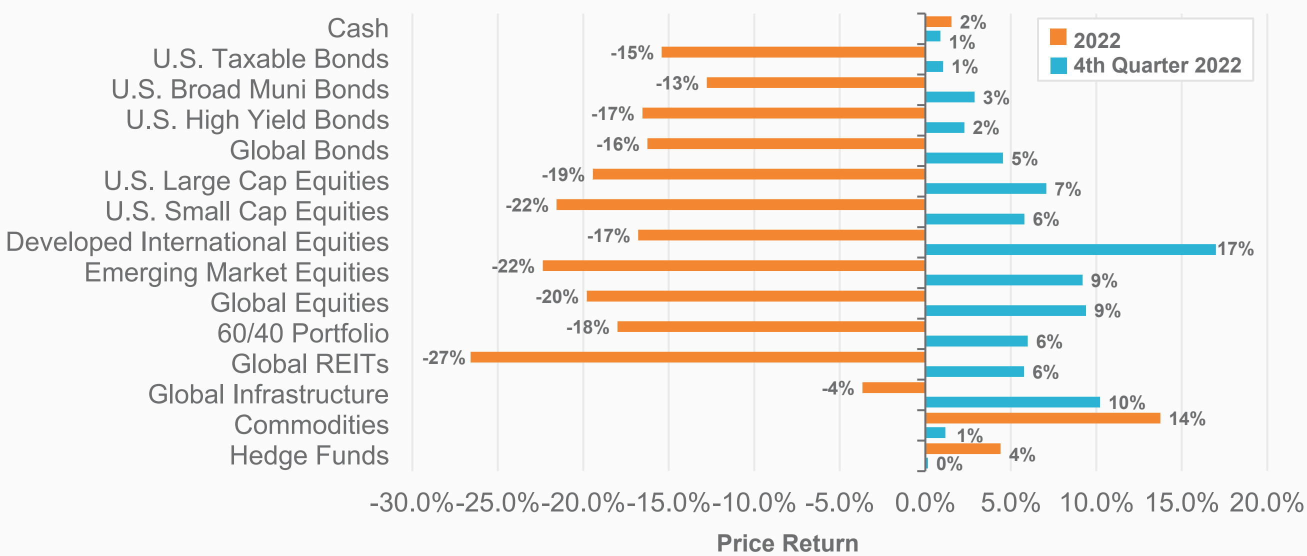
The S&P 500 lost over 19%, its worst year since 2008, with only one stock managing to end at a record high (Howmet Aerospace). Most of the damage (61%) was done by just 7 mega-tech stocks (Apple, Amazon, Microsoft, Tesla, Meta, Nvidia and Google), the same group that accounted for 45% of the S&P 500's returns from the beginning of 2020 to the end 2021. Foreign equity markets weren't much better as elevated inflation was a global phenomenon, the US dollar rallied strongly on swiftly rising US rates, and persistent Covid and the war in Eastern Europe weighed on markets.

High-quality US bonds (as tracked by the Bloomberg Aggregate US Bond Index) were down nearly 15%, their worst year since the index was started 35 years ago. At its lowest, the 30-Year US Treasury bond was down 36%(!), on par with the Nasdaq. This led to traditionally stable balanced portfolios (60% stocks/40% bonds) experiencing one of their worst years in history.

Hedge fund strategies were one of the few bright spots, as they outperformed broadly, and in some cases, even contributed positive returns. Real assets also held up, with oil the greatest beneficiary of the tumult in Ukraine and poor weather (+9%) while REITs faced the dual headwinds of rising interest rates and a weaker economy.

We would be remiss if we also didn't point out the turmoil experienced by the cryptocurrency markets. Fortunately, we have not recommended direct exposures to specific cryptocurrencies while any indirect exposures through blockchain-focused strategies or venture funds were de minimis.

Asset Class Performance 2022 & 4th Quarter
(As of Dec. 31, 2022)



Source of Data: Morningstar, Bloomberg, Hedge Fund Research, ICE Data Services. Global Bonds return is calculated using total return.

[2] Source: "Breakfast with Dave," Rosenberg Research, January 3, 2023.

Where Are We Now

Inflation and the Fed's response remain the most important topic for investors. During 2022, the annualized rate of inflation as measured by the Consumer Price Index peaked at 9.1% in June, was down to 7.1% in November and at 6.5% in December. Inflation does not seem to be spiraling out of control and could surprise on the downside.

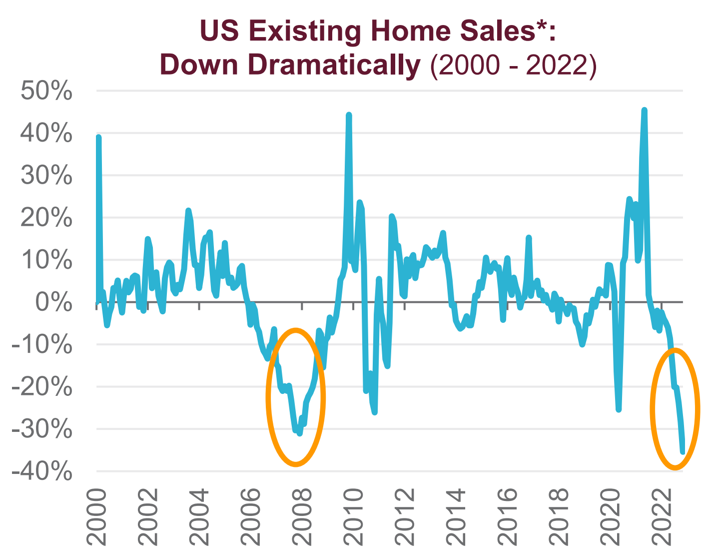
Source: Bloomberg.

In the near to intermediate term, the biggest risks are:

- Policy mistake by the Fed -- raising interest rates too far (triggering credit stress and/or liquidity issues here and abroad) or lowering them too quickly, re-igniting inflation
- US recession that is not mild
- Escalation of the Russian invasion of Ukraine
- A dysfunctional US Congress creating turmoil in the markets with showdowns regarding the debt ceiling and federal budget.

It appears evident that rising interest rates are cooling economic activity. Future-looking economic indicators continue to weaken, including various consumer and corporate confidence readings, plans for future hiring, and corporate pricing power and revenue projections. Residential real estate, a critical economic driver, saw existing home sales down nearly 40% in November (on an annualized basis), the worst decline since the 2008 financial crisis.

A dramatic decline in real estate-related activity can have significant negative impacts on the economy since it not only affects the housing sector, which accounts for about 2.4 million jobs. Other sectors dependent on the real estate market make up approximately 9x that amount in employment, or approximately 21.6 million jobs[1].



*Annualized. Source: Bloomberg.

Could the markets drop significantly from here? Absolutely. If the most-anticipated recession in recent history is upon us, or imminent, and it becomes protracted and/or deep, a combination of earnings' declines, corporate margin pressure and compression in valuations could drive markets down, by some estimates another 15-25% from current levels based on historical precedent.

[1] Source: "Updated Employment Multipliers for the US Economy," Economic Policy Institute (epi.org), Jan. 23, 2019.

Unfortunately, attempting to step aside due to the risk is highly unlikely to pay off, especially for investors with a long-term perspective. Consider that since Laird Norton Wealth Management opened its doors in 1967 through 2022, there have been 8 bull markets and 8 bear markets – a nice symmetry. However, that's where the symmetry ends. The average cumulative gain on the S&P 500 during those 8 bear markets was 270% (or about 3.7x your money) while the average decline was 36%. Additionally, the average bull market lasted 4.5x longer.[3]

S&P 500 Performance 1967 - 2022

	Cumulative Return		Avg. Duration (Days)		Bull-to-Bear Ratio (Duration)
	Bull Market*	Bear Market*	Bull*	Bear*	
Average	270%	-36%	2,090	465	4.5x

*Bear market: S&P 500 loses 20% or more in calendar year; Bull market: S&P 500 gains 20% or more in calendar year.
Source: Yardeni Research.

What This Means for Portfolios

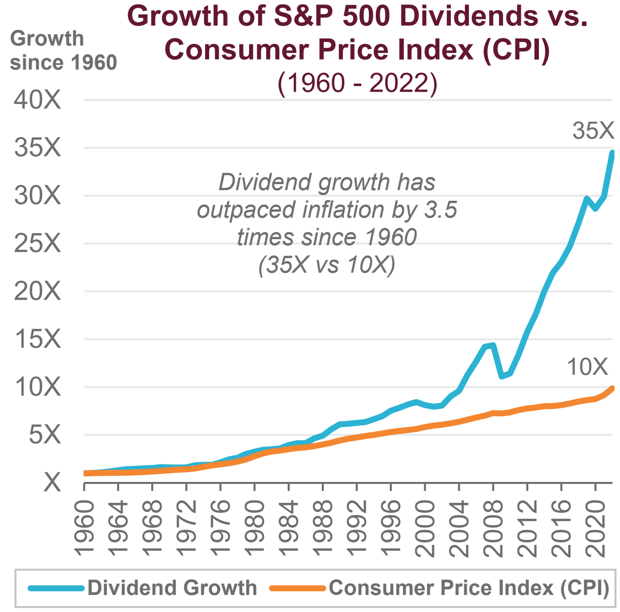
We have updated our view of risks and opportunities (see table on page 7), adding more opportunities than when we rolled this out in 2022. After an era when seemingly anyone could put money in virtually any index and see it gain in value, skill (while always important) should become even more so for both corporate executives and asset managers. Our focus will continue to be on sharpening OUR skills to build portfolios that have a blend of indexed exposures to minimize decision risk while owning active strategies in areas we believe are best-suited to navigate a different and more challenging economic and market environment.

A notable seismic shift in the opportunity set is the role cash and bonds can now play in portfolios. Bonds are once again playing their traditional role as income generators after years of almost exclusively playing a stabilizing role in portfolios (with the exception of 2022). In the reset toward normalcy, cash in savings and/or money market accounts has once again become attractive. The lure is obvious: low risk, low volatility, and moderate return (although less than inflation for the time being).

Taking a step further, both investment-grade and lower-quality credit appear reasonably attractive versus recent history. Since 2017, except for the height of Covid-19 uncertainty, the additional compensation investors received for taking corporate credit risk was well below long-term historical averages.

Today, with "spreads" over Treasuries of 1.3% for investment grade and 4.8% for high-yield credit, these bonds now yield roughly 5.4% and 9.0%, respectively, highlighting how the income has returned to the asset class. Additionally, private credit is looking more attractive. Experienced managers in this asset class are well-positioned to define attractive terms with businesses that have strong operating models and in many cases are in defensive sectors.

Growth of S&P 500 Dividends vs. Consumer Price Index (CPI)
(1960 - 2022)



Source of Data: NYU Stern, FRED.

[3] Source: Laird Norton Wealth Management, Bloomberg.

We have also highlighted public global equities as an exposure that mitigates risk if inflation settles in at a level higher than the 2% Fed target (but not high by historical standards). There are two reasons for this: (1) Owning dividend-paying equities via the broad indices can mitigate the impact of inflation since dividend growth has historically outpaced inflation by a sizable multiple; (2) An environment with higher inflation means nominal GDP can stay elevated, thereby providing a tailwind for nominal corporate earnings and asset valuations.

LONG-TERM GROWTH OPPORTUNITIES

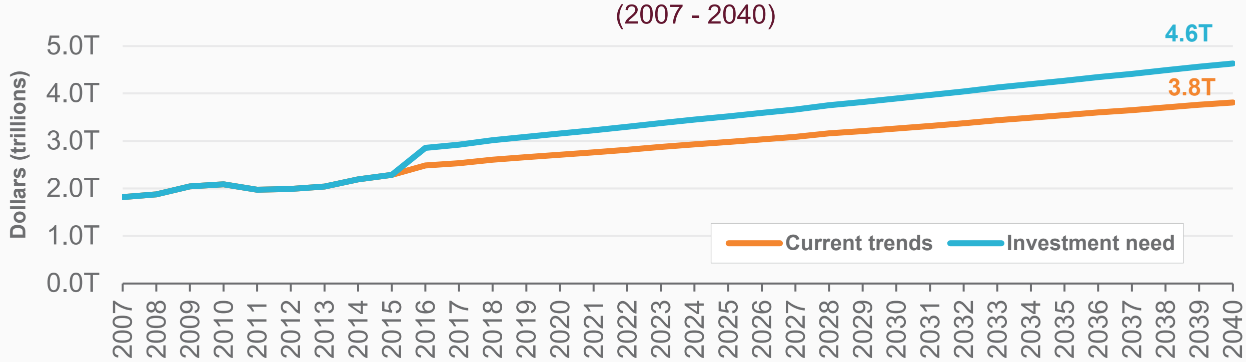
- **Supply Chain Restructuring.** Given the disruption of the past few years, corporate executives have been compelled to understand their supply chain at a granular level – not just locations and sourcing, but also energy use and how to attract and retain workers. We think this is big positive. In fact, despite all the headlines bashing ESG and impact investing, we think well-managed companies will out of necessity become more resilient, more able to identify and manage their risks, and more efficient at utilizing resources. All of this should be accretive to shareholder value.

- **New Technologies.** Billions in new investment is going into up-and-coming technologies, including clean energy generation and storage, quantum computing, robotics, artificial intelligence (AI) and bioengineering. Related to this, the semiconductor industry is one poised for strong growth over the next decade due to its importance across a broad range of industries as well as the need to ensure supply is protected as part of national security, evidenced by recent passage of the CHIPS Act to encourage US production.

- **Sustainability.** Whether or not you are a proponent of ESG investing, the investment opportunity set related to the net-zero carbon transition across sectors (such as industrials, building construction/renovation, transportation, waste and agriculture) has considerable appeal. According to McKinsey, the size of the addressable market related to this transition is estimated to generate revenue of more than $12 trillion per year by 2030[4].

- Infrastructure. Investing in infrastructure looks to be yet another area of opportunity as countries tackle issues associated with restructuring the global supply chain, reducing dependence on fossil fuels, and transitioning to sustainable agriculture. The current rate of investment is expected to continue increasing sizably into the next decade, and yet there is a rising gap between the projected investment and the need for investment as illustrated by a joint study between Blackrock and the World Bank. Infrastructure also brings diversifying elements to portfolios by being somewhat inoculated from the economic cycle, an inflationary hedging component, and oftentimes an income producer.

Annual Global Infrastructure Funding: Needs vs. Current Trend
(2007 - 2040)



Source: Global Infrastructure Hub; A G20 Initative.

[4] Source: McKinsey Global Institute, December 2022.

In Closing

We leave prognostications regarding recession and the duration of the current bear market to the talking heads in the financial media. Instead, we will continue to focus on the ramifications created by the pandemic and increased geopolitical tensions and conflict. While the pervasive narrative now is predominantly negative, history tells a more optimistic story of society successfully innovating, adapting, and ultimately overcoming obstacles in the face of adversity. While everyone is focused on the risks, that's when we need to be leaning into the opportunities (see table below).

Risks and Opportunities by Asset Class

Risks	Fixed Income / Cash	Conservative Growth - Diversifiers	Global Equities - Public	Global Equities - Private	Real Assets - Public	Real Assets - Private
Downside Volatility	X	X				
Fed Goes Too Far	X	X				
A Step-Up in Steady-State Inflation			X		X	X
Recession	X	X				
Extended Conflict / Cold War II	X	X				

Opportunities	Fixed Income / Cash	Conservative Growth - Diversifiers	Global Equities - Public	Global Equities - Private	Real Assets - Public	Real Assets - Private
Volatility / Dislocation		X	X	X	X	X
Fed Goes Too Far	X	X		X		
Energy Transition			X	X	X	X
Innovation			X	X		
Regionalization			X	X	X	X
Sustainability			X	X	X	X
Tax Management			X			

I will end with this: Imagine we could jump into a DeLorean today with Doc Brown of "Back to the Future" and crash land into January 2033. Don't you think it more likely than not that we would be looking back at the preceding 10 years feeling rewarded for having continued to put capital to work during this period of turbulence and uncertainty?

ABOUT THE AUTHOR

Ronald G. Albahary, CFA® is Chief Investment Officer at Laird Norton Wealth Management. As the head of LNWM's investment team (see below), Ron determines the firm's investment strategy, directs the investment selection process, and works in tandem with LNWM's client services teams to deliver investment solutions structured to attain each client's unique goals. Prior to joining LNWM, Ron served as CIO or CEO at regional investment firms focused on ultra-high-net-worth families and foundations. Earlier in his career, he held leadership positions in the private client business of major global financial institutions, including Merrill Lynch and Northern Trust Private Bank. Ron has a degree in economics from the Wharton School at the University of Pennsylvania and currently serves as advisor to the Center for High Impact Philanthropy at the University of Pennsylvania.

The investment team resulting from the combination of Laird Norton Wealth Management and Wetherby Asset Management is comprised of 12 analysts and strategists working together to design and implement investment solutions for client portfolios. Six analysts at the firm hold the Chartered Financial Analyst® designation, with expertise spanning macroeconomics, public and private asset classes across the global capital markets, and impact investing. Collaborating with each other and with client advisors, the investment team's overarching goal is to help clients and their families preserve and grow their wealth over many generations.

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Laird Norton Wealth Management ("LNWM") has long partnered with its clients to help them achieve their greatest impact through their investments, legacy planning and philanthropy. Founded in 1967, LNWM is both an RIA (registered investment advisor) and trust company, providing comprehensive and integrated wealth planning to individuals, families, business leaders, private foundations and nonprofit organizations nationwide.

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INDEX DEFINITIONS

CASH: Morningstar US 1-3M T-Bill - The index measures the performance of fixed-rate, investment-grade US Treasury Bills with 1-3 months remaining until maturity. It is market-capitalization weighted.

U.S. TAXABLE BONDS: Bloomberg US Aggregate Bond Index – Covers the US Dollar-denominated, investment-grade, fixed-rate, taxable bond market of SEC-registered securities. The index includes bonds from the Treasury, Government-Related, Corporate, MBS, ABS, and CMBS sectors.

U.S. BROAD MUNI BONDS: ICE BofA US Municipal Securities Index - Tracks the performance of US dollar denominated investment grade tax-exempt debt publicly issued by US states and territories, and their political subdivisions, in the US domestic market.

U.S. HIGH YIELD BONDS: ICE BofA US High Yield Index - Tracks the performance of US dollar denominated below investment grade corporate debt publicly issued in the US domestic market.

GLOBAL BONDS: Bloomberg Global Agg Index - A measure of global investment grade debt from a multitude local currency markets. This multi-currency benchmark includes treasury, government-related, corporate and securitized fixed-rate bonds from both developed and emerging markets issuers.

10-YEAR US TREASURY BONDS: BofAML US Treasury Current 10 Year Index – The market value weighted index of public obligations of the US Treasury with maturities of 10 years.

U.S. LARGE CAP EQUITIES: S&P 500 - The index includes 500 leading US companies and captures approximately 80% coverage of available market capitalization.

U.S. SMALL CAP EQUITIES: Russell 2000 Index - Measures the performance of the 2,000 smallest companies in the Russell 3000 Index, representative of the US small-capitalization securities market.

INT'L DEVELOPED EQUITIES: MSCI EAFE Index - A free float-adjusted market-capitalization index that is designed to measure developed market equity performance, excluding the US and Canada. Consists of the following 21 developed market country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Greece, Hong Kong, Ireland, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland and the United Kingdom.

EMERGING MARKETS EQUITIES: MSCI Emerging Markets Index - A free float-adjusted market-capitalization index that is designed to measure equity market performance in the global emerging markets. Consists of the following 25 emerging market country indices: Argentina, Brazil, Chile, China, Colombia, Czech Republic, Egypt, Hungary, India, Indonesia, Israel, Jordan, Korea, Malaysia, Mexico, Morocco, Pakistan, Peru, Philippines, Poland, Russia, South Africa, Taiwan, Thailand, and Turkey.

GLOBAL EQUITIES: MSCI ACWI Index - A free-float weighted equity index. It was developed with a base value of 100 as of December 31, 1987. MXWD includes both emerging and developed world markets.

GLOBAL REITs: FTSE EPRA/NAREIT Global REITs Index - A measure that tracks the performance of listed real estate companies and REITs worldwide.

GLOBAL INFRASTRUCTURE: S&P Global Infrastructure Index - Provides liquid and tradable exposure to 75 companies from around the world that represent the listed infrastructure universe. To create diversified exposure across the global listed infrastructure market, the index has balanced weights a cross three distinct infrastructure clusters: Utilities, Transportation, and Energy.

COMMODITIES: Bloomberg Commodity Index - A broadly diversified index of futures contracts intended to be representative of the commodities market. It currently includes 19 commodity futures in seven sectors.

LIQUID HEDGE FUNDS: HFRX Global Hedge Fund Index – A daily-valued index designed to be representative of the overall liquid hedge fund universe. It is comprised of all eligible hedge fund strategies; including but not limited to convertible arbitrage, distressed securities, equity hedge, equity market neutral, event driven, macro, merger arbitrage, and relative value arbitrage. The strategies are asset weighted based on the distribution of assets in the hedge fund industry.

ILLIQUID HEDGE FUNDS: HFRI Fund Weighted Composite Index – A global, monthly-valued, equal-weighted index of over 2,000 single-manager funds that is designed to be representative of the overall composition of the hedge fund universe. It is comprised of all eligible hedge fund strategies. Constituent funds report monthly net of all fees performance in US dollar and have a minimum of $50 Million under management or a twelve (12) month track record of active performance. The HFRI Fund Weighted Composite Index does not include Funds of Hedge Funds.

DIVERSIFIED PORTFOLIO: 10% US Municipal Bonds; 10% US Core Bonds; 25% US Large Cap Equities; 5% US Small-Cap Equities; 22% Int'l Developed Equities; 9% Emerging Markets Equities;4% Global Infrastructure; 13% Illiquid Hedge Funds; 2% Commodities.

60/40 PORTFOLIO: 60% Global Equities, 40% U.S. Taxable Bonds

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