

## **Fourth Quarter 2022 Commentary**

The past year was a harsh one for most American investors, as there was practically no safe haven in which to hide out from the economic storms. The S&P 500 index was down 18%, the Nasdaq fell 33%, and even the stalwart Dow Jones Industrial Average was down 7%. Stocks and bonds typically tend to move in opposite directions, but in 2022 even the aggregate U.S. bond index was down 13%.

The culprit behind all of these declines was the rise in interest rates which, in turn, was a response to high inflation. Interest rates act like financial gravity: the higher they go, the more they pull down on asset prices. The second half of 2022 saw the fastest-ever increase in rates imposed by the world's central bankers. The yield on the U.S. 10-year Treasury note, now above 4%, is the highest it has been in the last 15 years. However, that yield is also *lower* than it was at any time from 1965 through 2007. So while rates are indeed higher than they have been in recent memory, they are still relatively low in a historical sense. In any case, it seems that the days of easy money that borrowers have enjoyed in the years since the Global Financial Crisis are now finally coming to a close.

Let's look a little more closely at the bad numbers for 2022, and then turn our attention to what might transpire in 2023 and beyond.

### **Stocks Did Bad**

Stocks, in general, had their worst performance since 2008. The only sector that produced any meaningful gains last year was oil and gas. Big Tech was a big loser in 2022, with Apple and Amazon each losing more than \$800 billion in market value during the year. Between those two barbells, the carnage wasn't too terrible for most other sectors. Financial stocks overall were down a little more than 10%, and industrial and staples companies were down around 5%. Your largest holding, Berkshire Hathaway, was actually up about 3% during 2022, which is a pretty fantastic performance relative to the alternatives.

### **Bonds Did Bad**

As central banks around the globe raced to raise their interest rates in order to tame the rampant inflation arising from Covid-related stimulus, bond prices did what they naturally do in such cases: they fell. And they fell hard. It was the worst year for U.S. Treasuries in at least 100 years, and for investment-grade corporate bonds in more than 90 years.

### **Crypto Did Bad**

Though the FTX fraud last fall was just a fraction the size of the infamous Ponzi scheme run by Bernie Madoff, it was the first large-scale investor rip-off we've seen since then. This rippled throughout the crypto universe, dragging down the prices of most digital currencies. Bitcoin, still the flagship, tumbled in price by 64% in 2022. As of this writing, Bitcoin has underperformed all of the major U.S. stock indexes over the prior five-year period.



## What Will 2023 Bring?

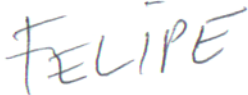
Famed investor Howard Marks notes that, in this new interest rate environment, “Investors can now potentially get solid returns from credit instruments, meaning they no longer have to rely as heavily on riskier investments to achieve their overall return targets. Lenders and bargain hunters face much better prospects in this changed environment than they did in 2009-21.”

As you may have noticed, we recently began buying short-term U.S. Treasuries for the first time in our existence. For those of you who own individual bonds, you perhaps have seen that we have been more active in purchasing new issues than we ever have. And, to Mr. Marks’ final point, we do hope that this year will be a better one for equity “bargain hunters” such as us.

However, we note that at the beginning of last year, no foreign affairs expert foresaw the troubles soon to unfold in Ukraine. No central bank manager in Europe thought that they’d been raising rates as often as they did, or as much as they did, in 2022. And certainly no one thought that the world’s richest man would voluntarily incinerate much of his fortune, while wasting much of his time, on a pet project unrelated to the two large companies of which he is CEO.

Therefore, we do not pretend to have any idea what the big stories of this year will be. We remain focused on individual securities, and trying to utilize them in a sensible way to protect and grow your hard-earned money. We appreciate that you have trusted us for this difficult task, and we look forward to reporting our progress on it in another three months.

Sincerely,



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