Zevin Asset Management

Q1 2023

MARKET OUTLOOK

You are probably aware of the phrase "you break it, you buy it." Alter the phrase slightly to "you break it, you own it," and you're left with an apt description of the turmoil currently facing U.S. financial regulators. Let's unpack this. The Fed spiked interest rates higher by 4.75% in the past year, cognizant that such a shock to financial markets could " break" something. They were more fearful of looming inflation at the time and therefore willingly took that risk. Now the risk has come to roost – the tipping point being two significant bank failures which were victims of mismanagement combined with bond portfolio losses due to the surge in interest rates. The reverberations are far from over.

As these things tend to go, one error often has a rippling effect. Now, we're facing fresh challenges: the scare of the first bank run in years, uninsured bank deposits nationwide being closely evaluated, rising costs associated with the shoring up of a few banks, and borne by the many, in the form of higher Federal Deposit Insurance Corporation (FDIC) insurance and heightened regulation, and tighter lending conditions that will limit future economic growth. The chance of a recession in 2023 has increased, and the magnitude of the slowdown is now likely greater. The Fed owns this. Interest rate policy mistakes have repercussions. Bank overseers own this. Measures to test the health of banks that are not thoughtfully constructed and fail to incorporate the consequences of current and conveyed interest rate hikes are halfwitted.

The ultimate resolution of this global financial market dilemma may not appear all that rosy, but maybe it's better than it seems. So why is a looming recession in the aftermath of the pandemic's financial bubble not frightfully ominous? The answer to this could be a rolling recession, which we may be experiencing right now. Rolling recessions are often muted downturns, because different parts of the economy endure their periods of suffering at different times. If you think about it, we've already endured a massive pullback in global growth stocks as well as employment in the technology and other high growth sectors. We've already seen a slowdown in the real estate sector, as sharply higher rates crowded out affordability and project financing. Lastly, we are at, or very close to, a cyclical peak in interest rates in the U.S. These devel-opments have collectively de-risked some of the market sur-prise and downside that one expects from a recession.

Inevitably, there will be more pain to come in this economic cycle due to weaker profits, job losses, and stock declines, but maybe we're well along in this process already. Only time will tell, but in the meantime our investment team is keenly focused on identifying investments that both amply reflect the gloom and can materially appreciate on signs of its end. We continue to believe that a global portfolio that is constructed with these risks in mind can weather whatever lies ahead, as has been proven in past economic slowdowns.

IMPACT UPDATE

This quarter, we led two initiatives to advance equity and authenticity: an investor comment letter in support of the Federal Trade Commission's proposed ban on noncompete clauses, and a letter voicing our disappointment and concern to Vanguard over the company's backpedaling on its proxy voting behavior related to climate change. We also partnered with Climate Finance Action to equip pension fund trustees with the right questions to address climate risk in asset ownership. Lastly, we vehemently opposed the building of an Atlanta police training facility-dubbed "Cop City" – and sent letters to companies implicated in this project which perpetuates mass incarceration. You can learn about these initiatives and more in our **Q1 Impact Update**.

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