CAMBRIDGE TRUST

PRIVATE BANKING WEALTH MANAGEMENT

Q1 Market Update
and Our Outlook for 2023

February 10, 2023

Moderator:

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Taking away the Punch Bowl:

The Economy, the Election and Equities

- In 1955, William McChesney Martin, who served as Chairman of the Federal Reserve from 1951-1970, made a speech where he defined the role of the fed as essentially:

  "The Federal Reserve …. is in the position of the chaperone who has ordered the punchbowl removed just when the party was warming up"

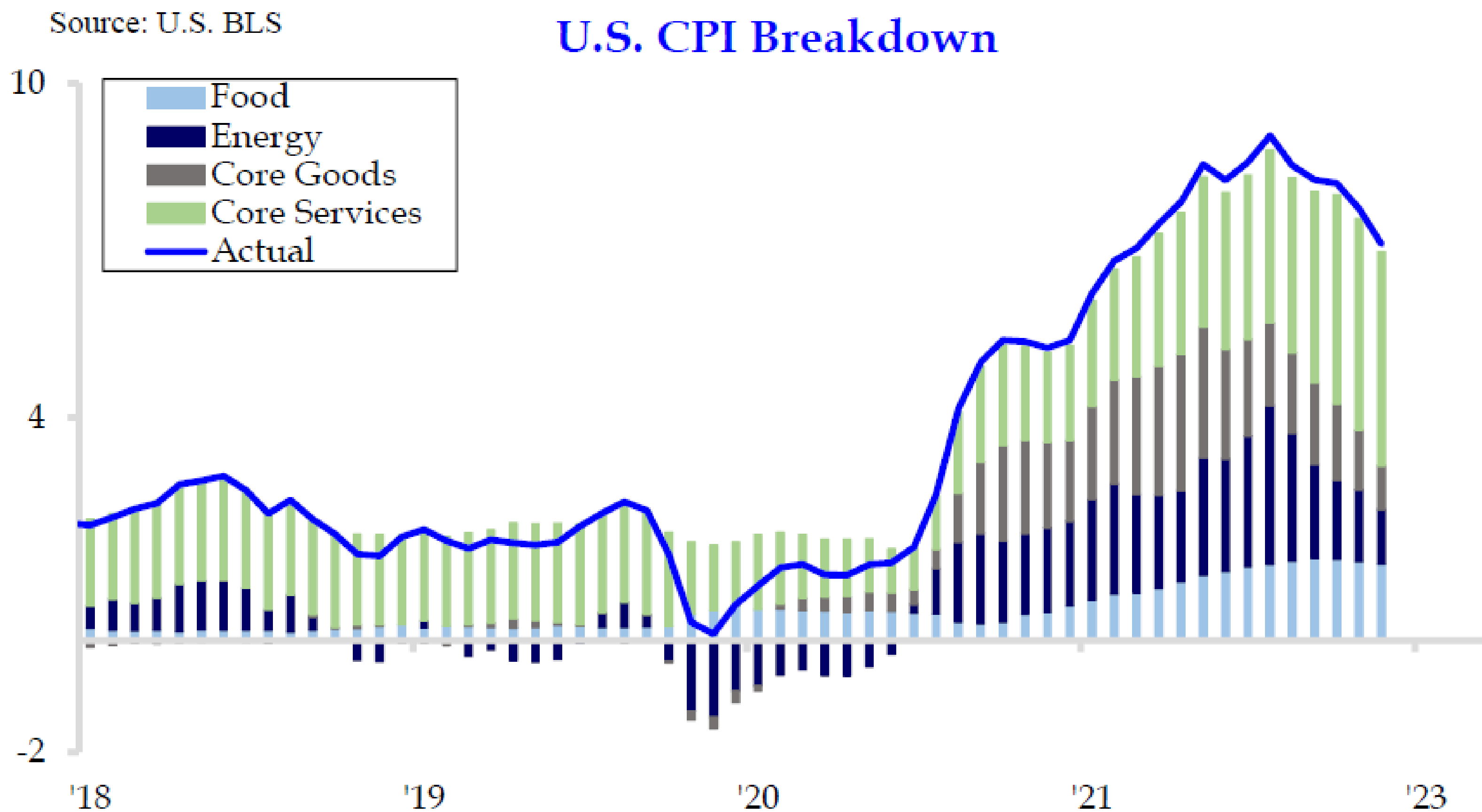
Themes for 2023

- **Inflation still too high**
  - It looks like we saw peak inflation in June 2022, when the CPI rose to 9.1%. In December, the CPI rose by 6.5%, the lowest annual rate in 2022.
  - The core PCE, the Fed's preferred inflation gauge, rose by 4.4% in December, driven primarily by declining goods prices.

- **Economy slowly cools**
  - GDP rose 2.9% in the fourth quarter. If inventories and trade are removed, the economy only grew at 0.2%, indicating a slowdown in growth.
  - The economy grew at 2.1% for the entire year of 2022. The Conference Board estimates US GDP will grow 0.2% in 2023.

- **Employment remains ebullient**
  - The January unemployment rate was 3.4%, a post-pandemic low.
  - Employers added 517,000 jobs in January, indicating a strong market as we enter 2023.
  - Wage growth was 4.4% year over year.
  - The participation rate sits at 62.4%, below the pre-pandemic peak of 63.4%. A strong job market is pulling people back into the labor market, but we still need more workers..

Inflation: Uncomfortably Hot



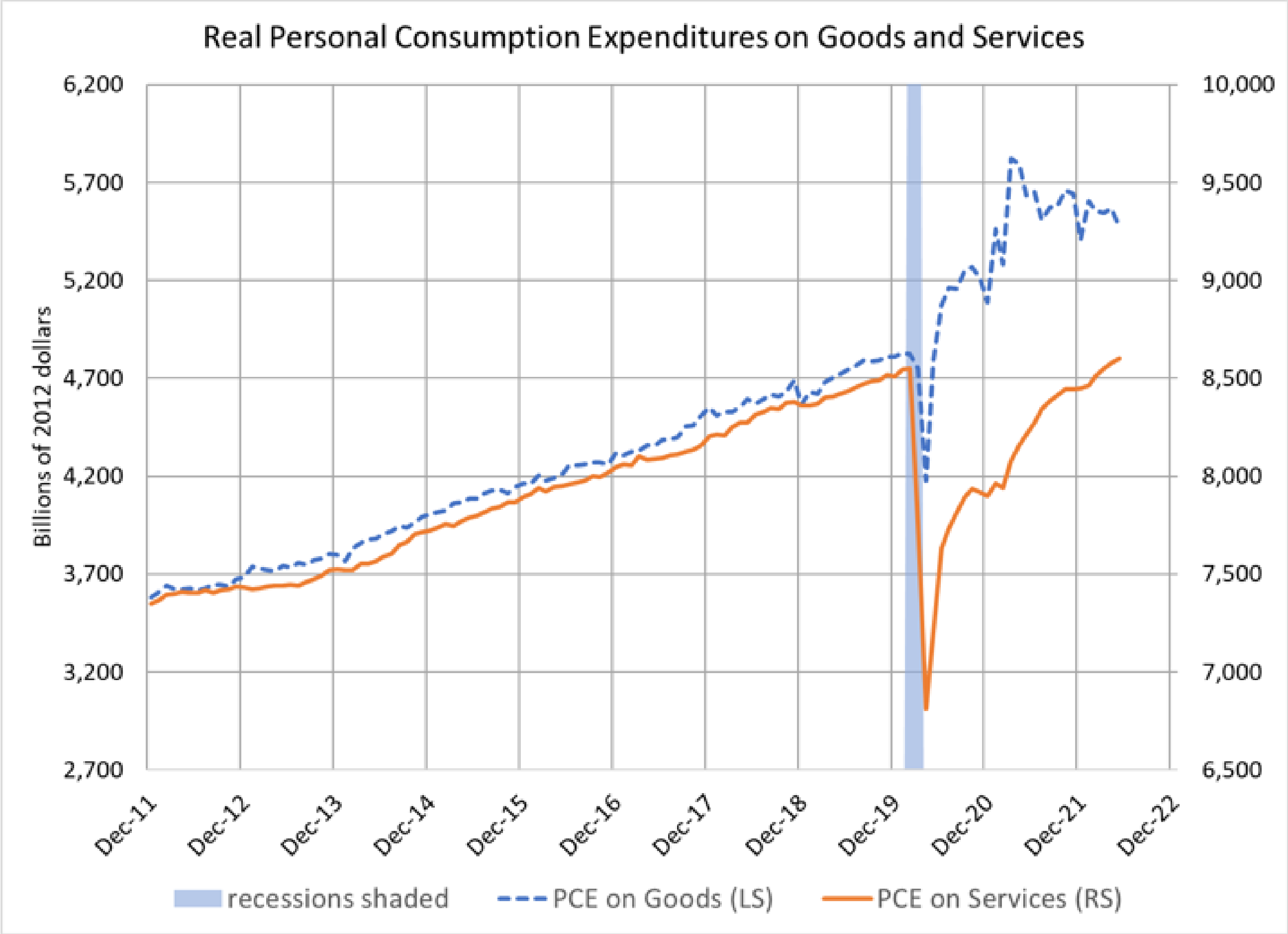
Source: Strategas, Qtrly review in charts 1/9/23

- The Consumer Price Index (CPI) reached the highest levels since the 1980's driven by excess demand, fiscal stimulus, and supply chain issues. This poses a risk to both consumer wallets and corporate margins, though both have proven resilient so far. The Ukraine war has pushed commodity prices up further.

Consumer Spending: Goods vs Services

Consumer Consumption

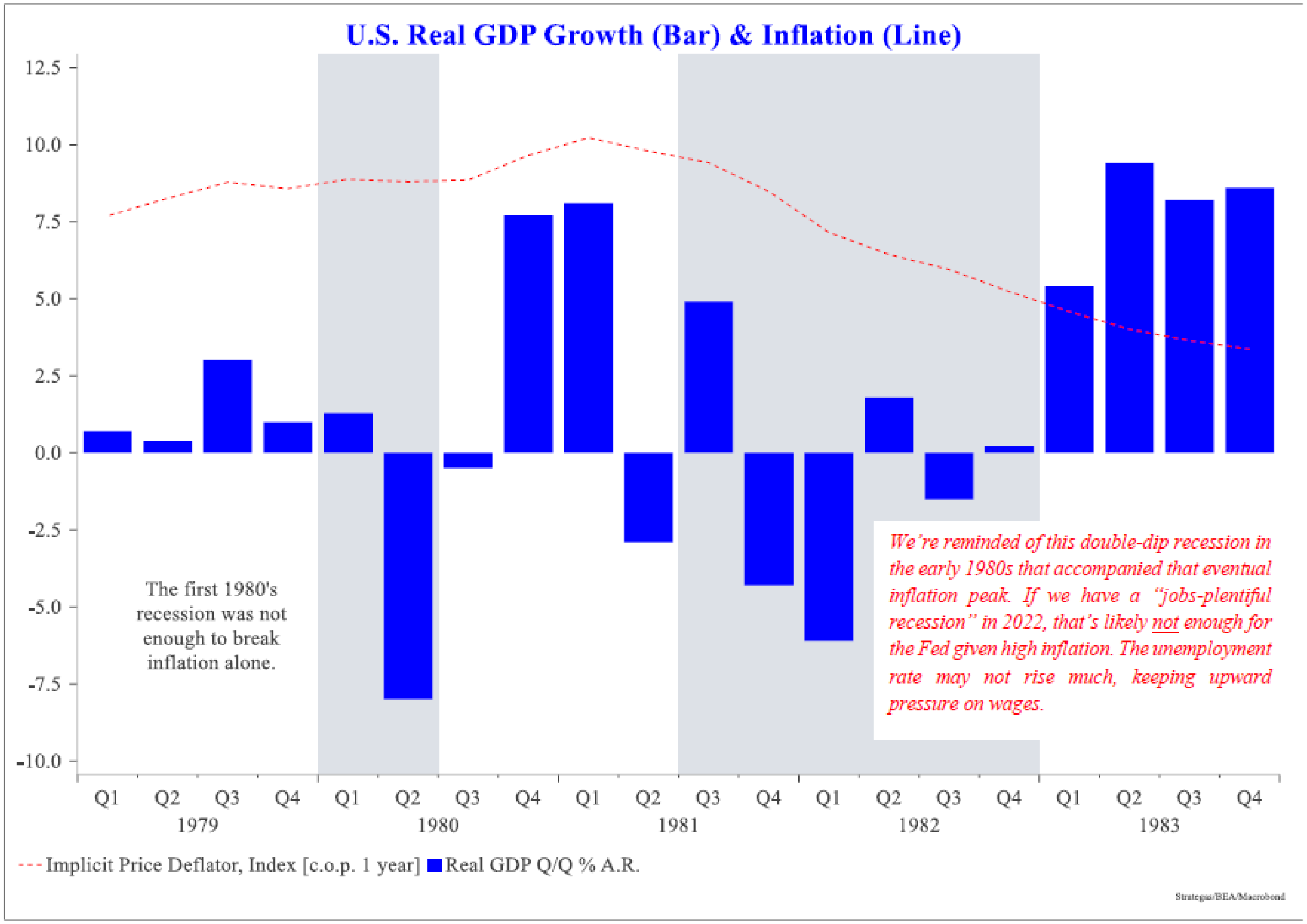
- The pandemic substantially altered the relative demand for goods and services.
- Real demand for goods relative to services has come down but still remains approx. $400 billion above the pre-pandemic trend.
- Real demand for services has increased but remains approx. $400 billion below the pre-pandemic trend.



Source: Bureau of Economic Analysis

Double Dip a Concern

IT TOOK A DOUBLE-DIP IN THE 1980s TO STOP RUNAWAY INFLATION



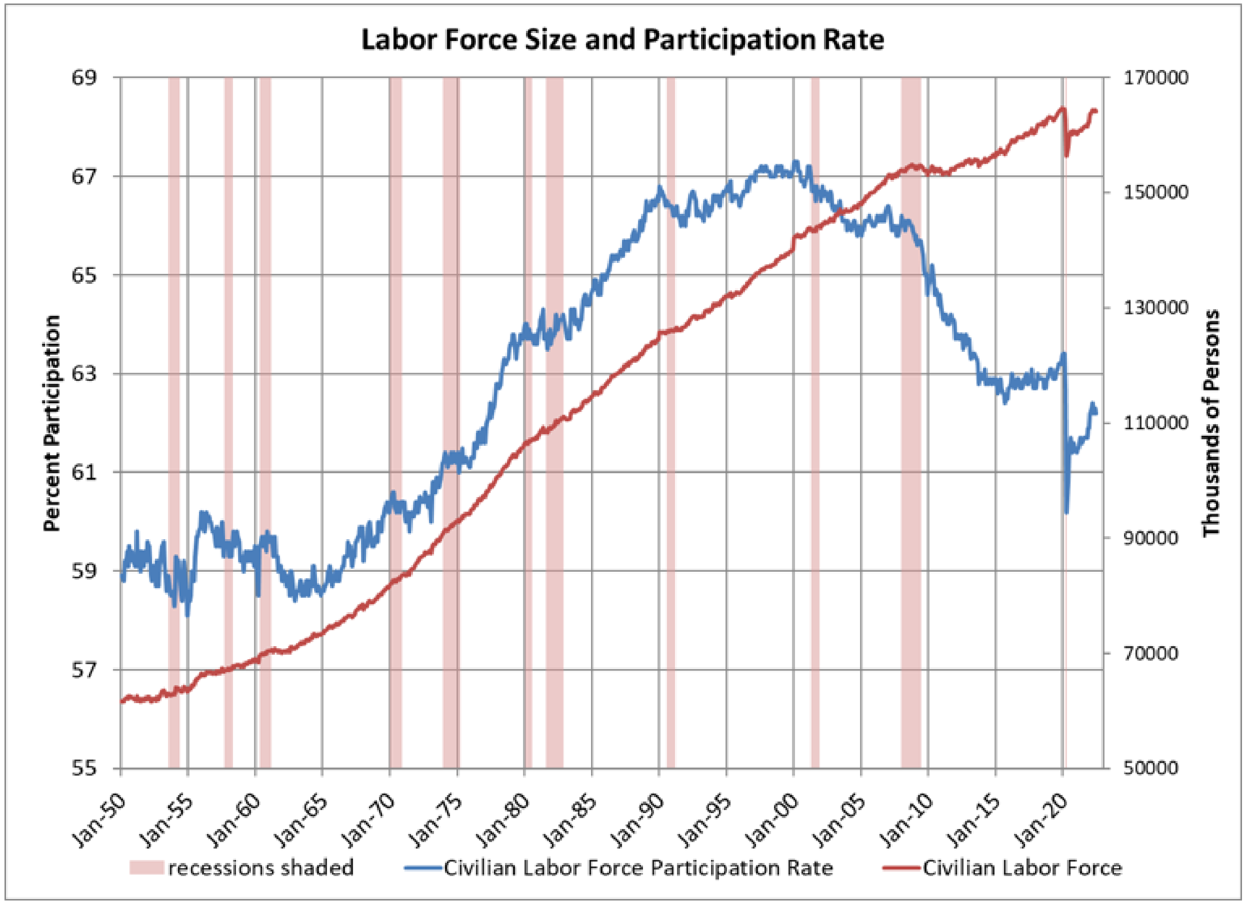
Source: Strategas

- The need for a double dip recession, as we had in the early 1980's, is the big fear of the fed and investors.

Employment: Continued Improvement

Labor Force Participation

- The U.S. labor force finally rose above the Dec 2019 peak by 262,000 in December 2022.
- Labor force participation has increased from its pandemic trough but remains at 62.3%, 1.1% below its January 2020 peak of 63.4%.
- Labor force growth faces a demographic headwind. The working age population increased only 1.4% from December 2019 to June 2022.
- If the current labor force achieved a 63.4% participation rate there would be 2.5 million more workers employed.



Source: Bureau of Labor Statistics

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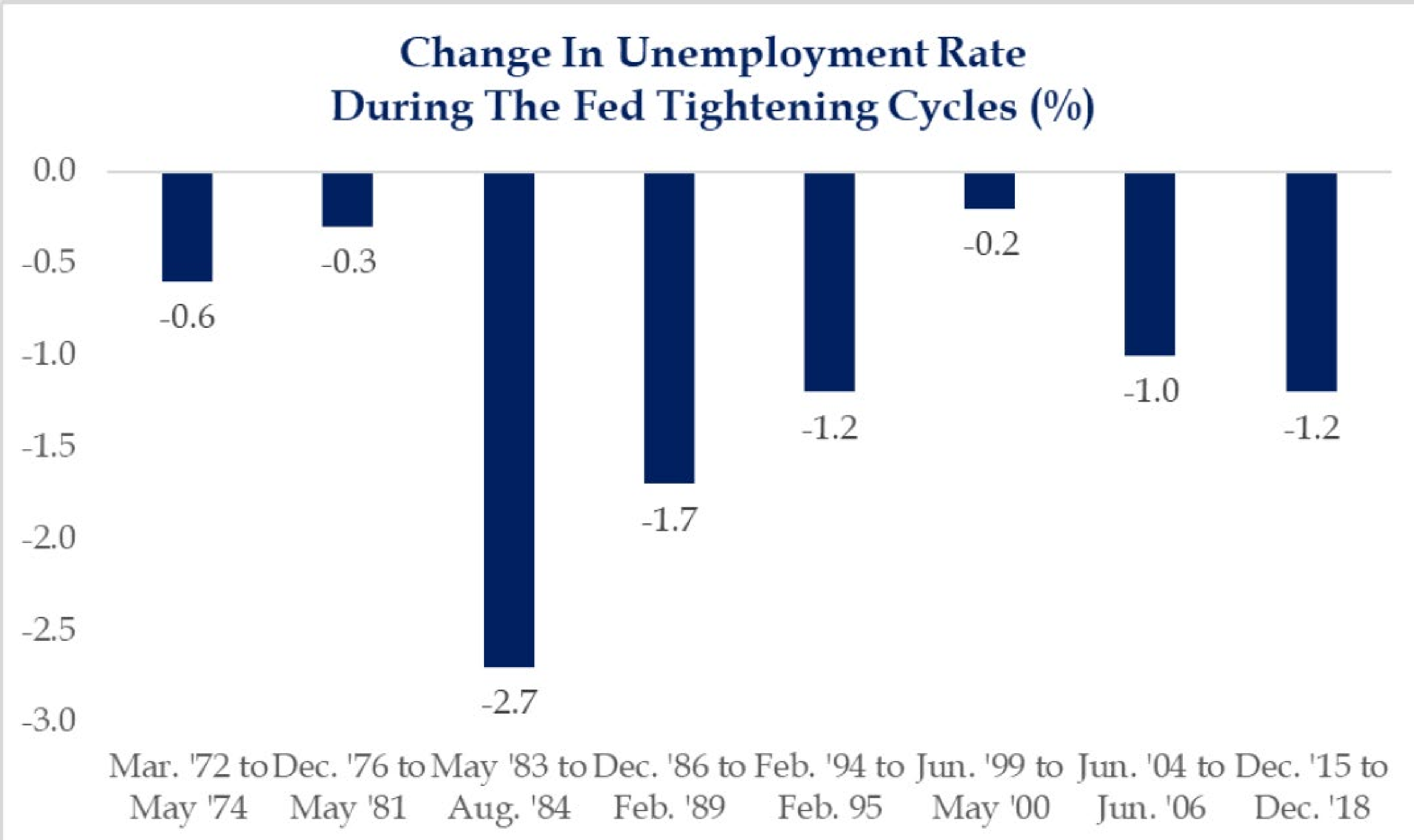
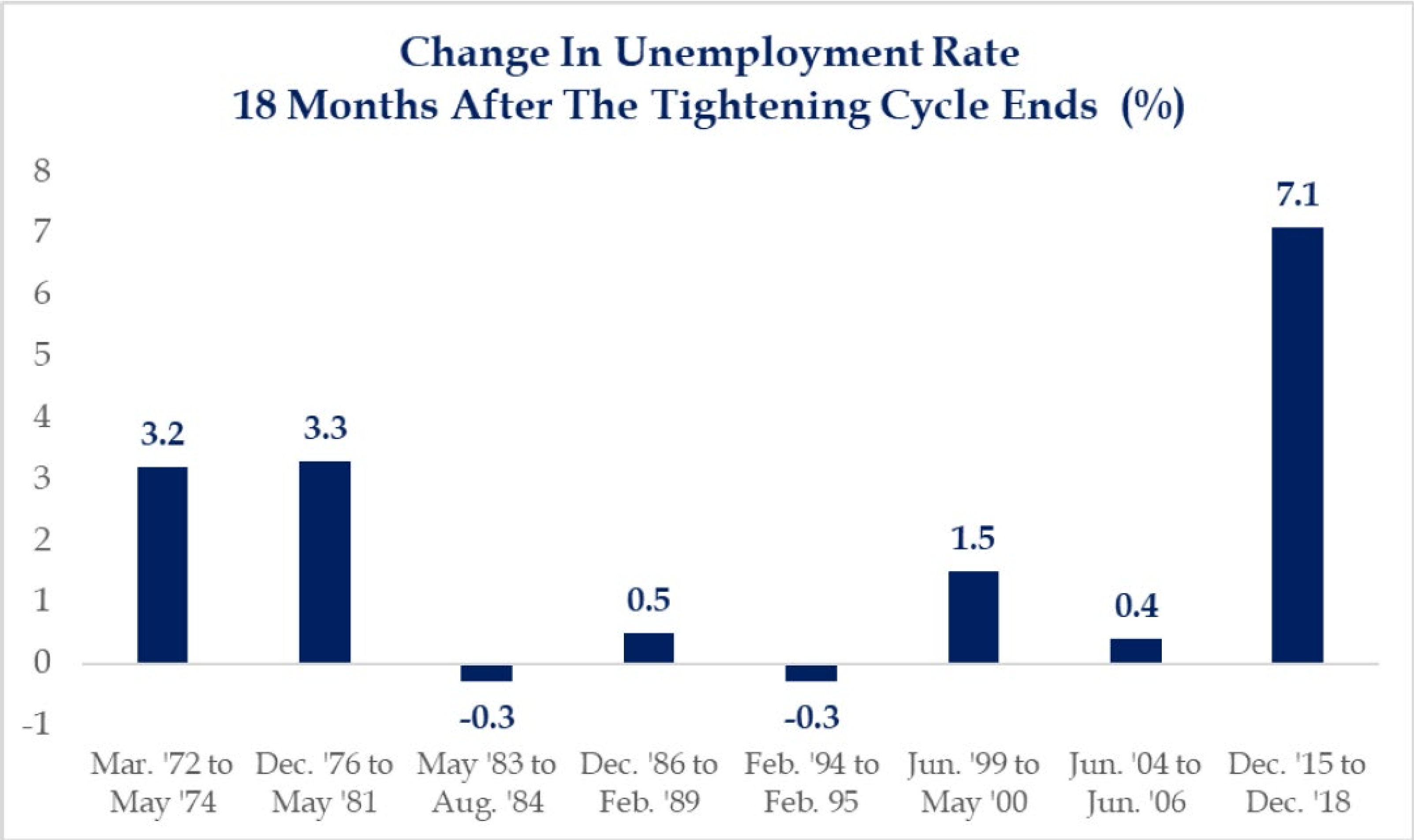
Employment challenging ahead



Source: Strategas

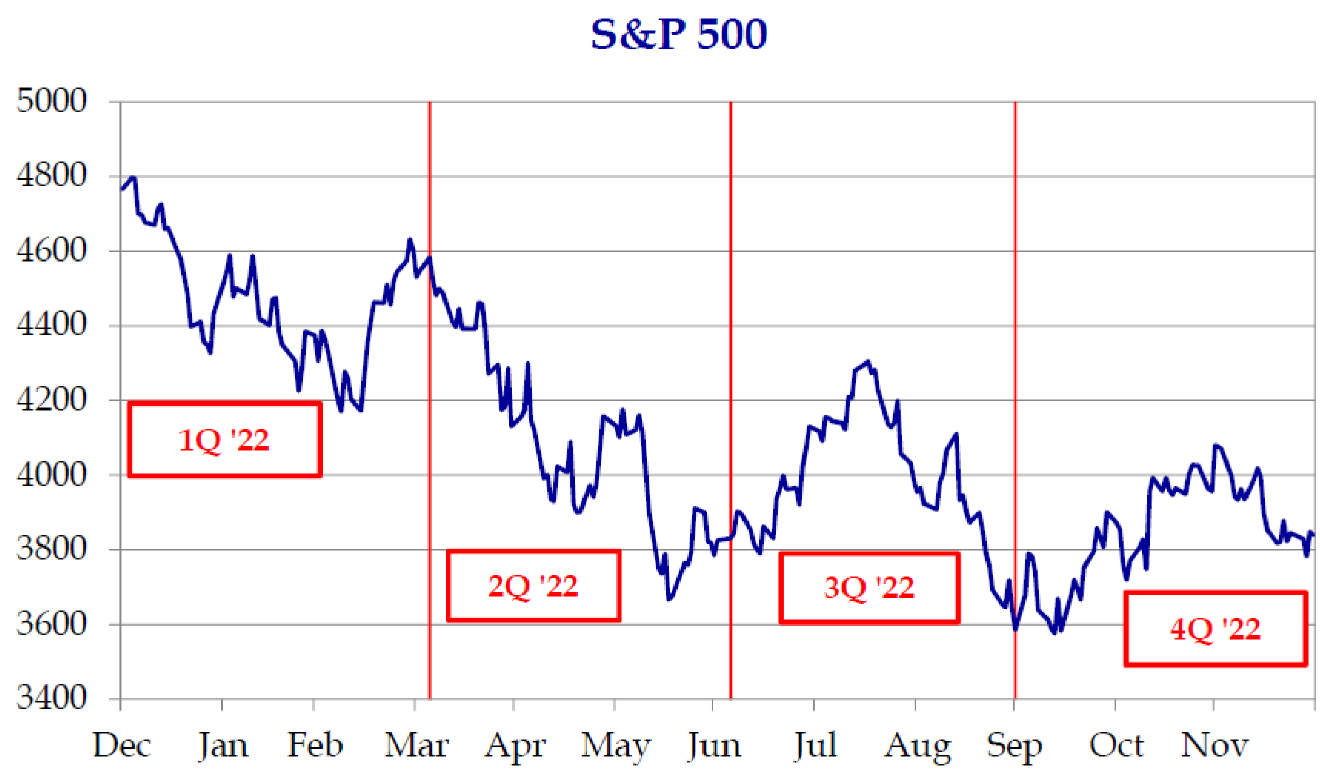
Employment challenging ahead



Source: Strategas

Equities

U.S. Equities: A Painful First Half of the Year



Source: Strategas, Qtrly review in charts 1/3/23

- Through June, domestic stocks posted their worst first-half in 50 years, driven primarily by persistent inflation, rising interest rates, and deteriorating economic conditions.
- The second half of the year was characterized by shifting views of Fed Policy.

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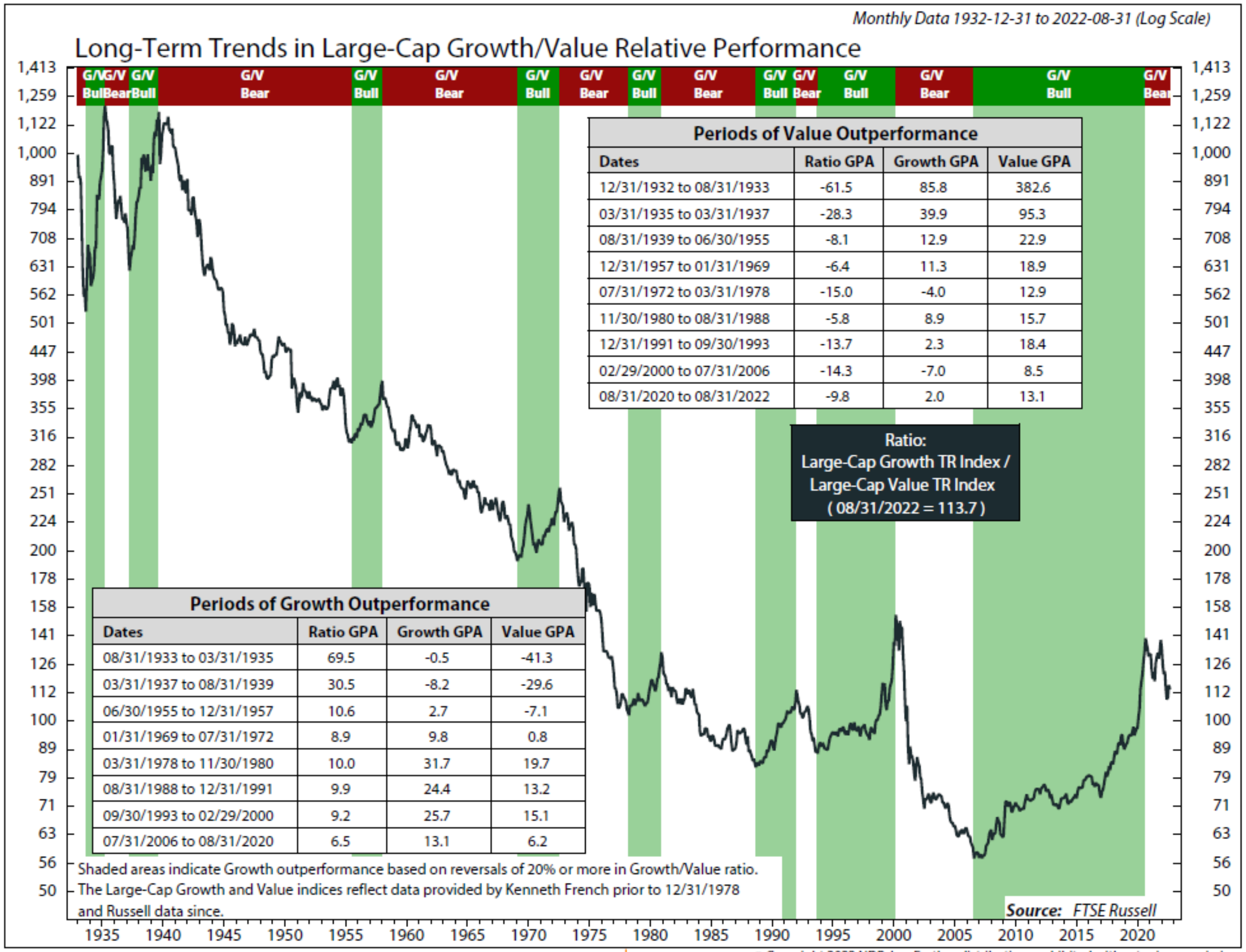
Growth vs Value: A Potential Change in Direction



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- After a long period of growth style factor outperformance, the value style factor had two recent periods of meaningful outperformance. There might be more to go in this rotation after such a long period of growth outperformance, although timing can be very difficult and quality growth companies are still very solid long-term holdings, particularly if economic growth becomes scarce in the coming quarters.

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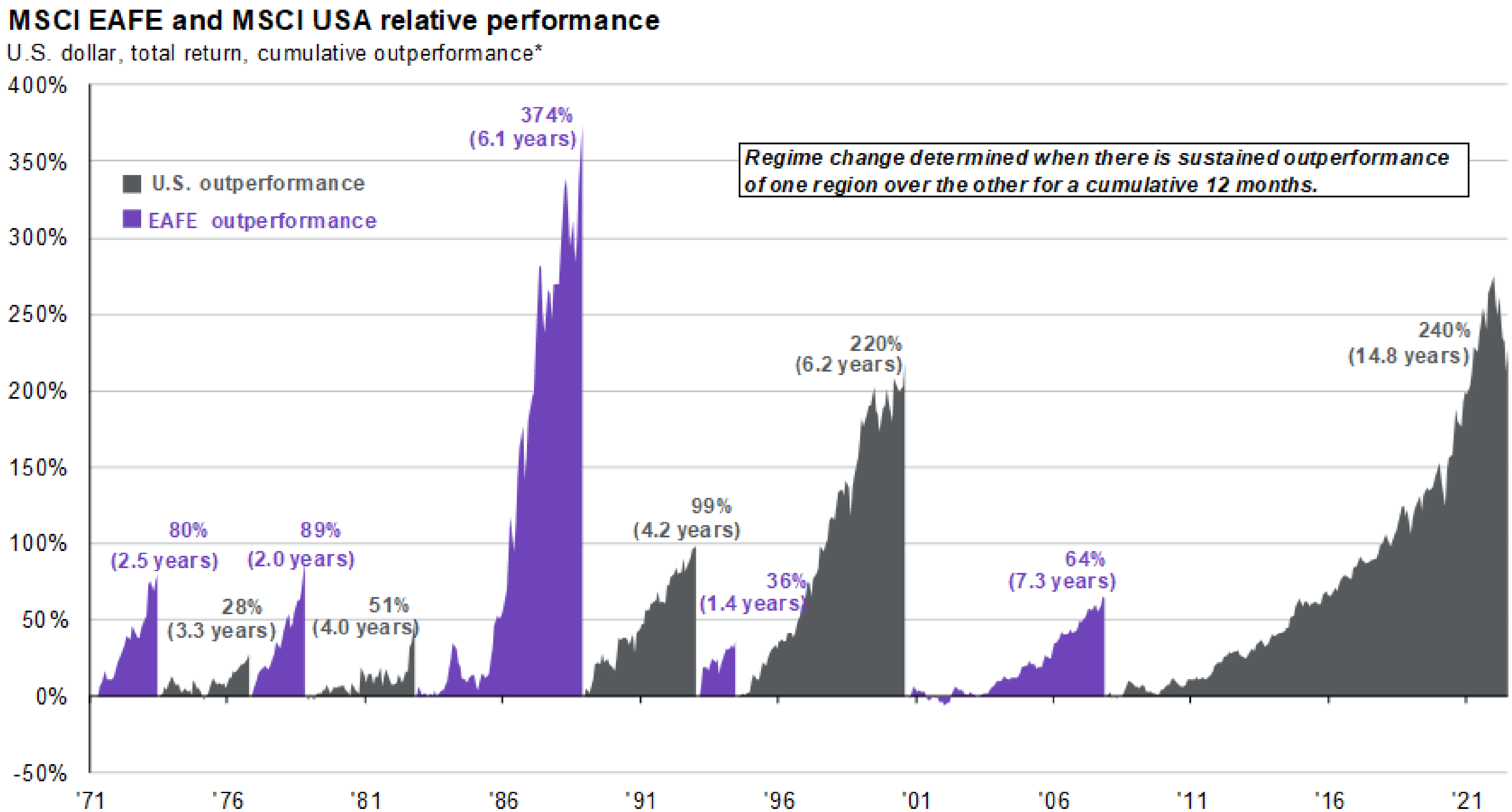
International Equities: New Risks Put Opportunity on Pause



Source: JP Morgan; Data as of 8/26/22

- U.S. equities have outperformed international equities for extended periods of time and continue to outperform this year. We remain underweight international equities. Valuations and economic prospects were looking better at the start of the year, but the war in Ukraine poses new geopolitical and recession risks, especially to European countries. We continue to monitor global events for attractive entry points.

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Deglobalization, Inflation & Markets

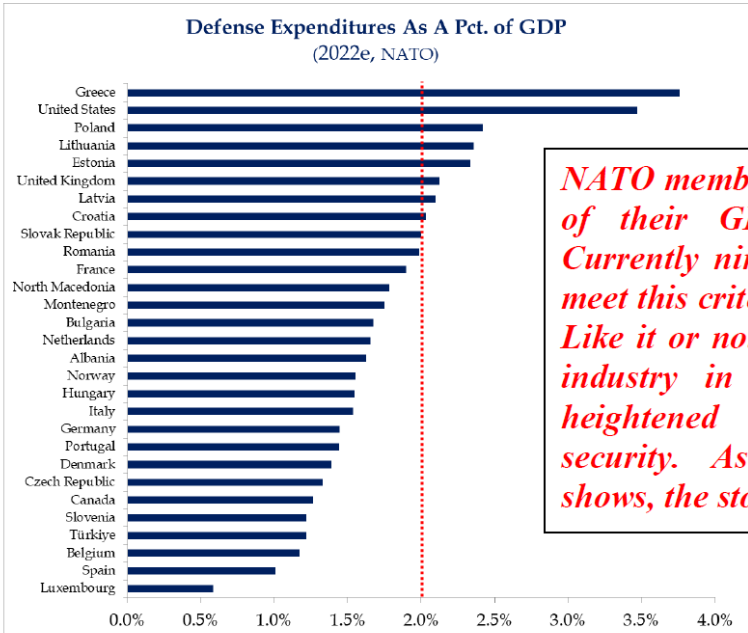
Globalization *"The World is Flat"*

- Berlin Wall falling in 1989 marked the beginning of a major globalization push.
- Significant decrease in global defense spending. U.S. only remaining superpower.
- Companies sought lowest cost of **Labor & Energy**. *(outsourcing – no borders)*
- Importation of **Deflation**. *(i.e., Wal-Mart)*
- 1994 – NAFTA established. *(free-trade zone)*
- 2001 - China joins World Trade Organization (WTO).
- 2013 – Last U.S. heavy armor unit leaves Europe.

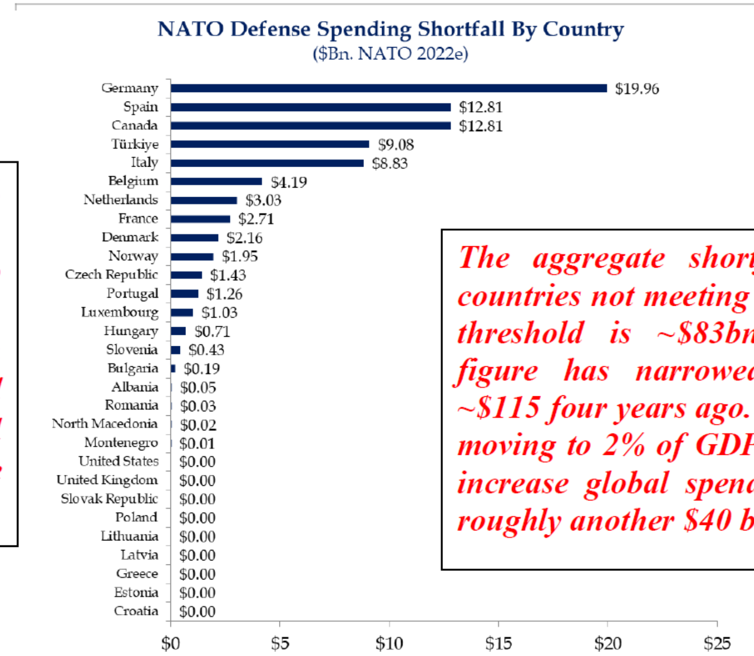
Deglobalization – A More Dangerous World

- Recent global events have led to a push towards deglobalization, which we believe will likely increase **inflation**.
- The **global pandemic** showed extreme vulnerabilities of global supply chains.
- A more assertive **China** is very worrisome to western governments. *(i.e., Taiwan)*
- The **Russia/Ukraine** war in Europe has created an energy supply crises.
- Defense spending seen growing for years to come.
- National security issues with Chinese manufacturing dominance.

Defense Spending Increasing



NATO members are expected to spend 2% of their GDP on defense spending. Currently nine countries are expected to meet this criteria based on 2022 estimates. Like it or not, defense could be a growth industry in an era of populism and heightened concerns about national security. As the table on the next page shows, the stocks are not, however, cheap.

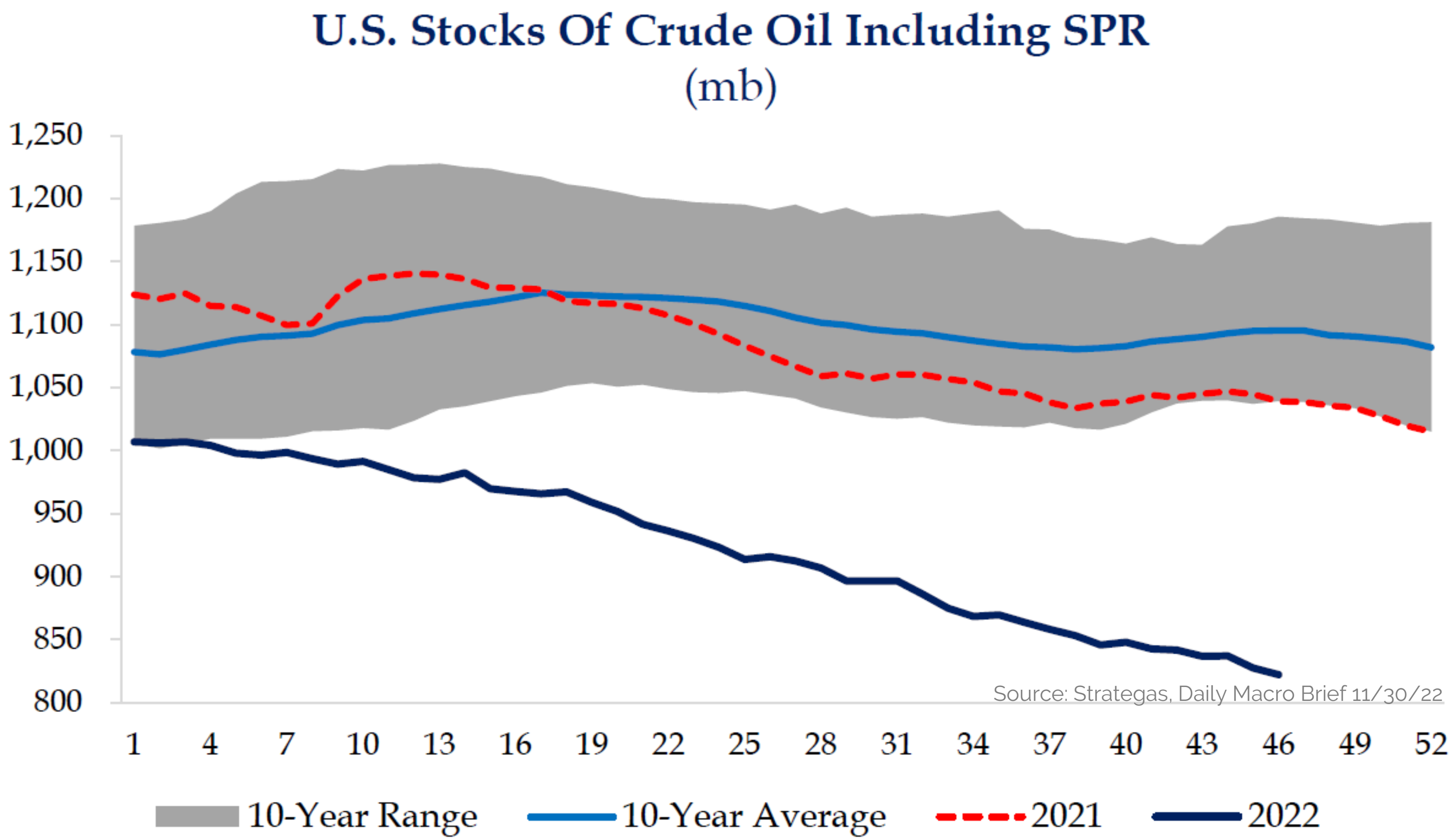


The aggregate shortfall of countries not meeting the 2% threshold is ~$83bn. This figure has narrowed from ~$115 four years ago. Japan moving to 2% of GDP would increase global spending by roughly another $40 billion.

Source: Strategas- Investment Strategy Report, 11/28/22

- Russia's war against Ukraine has dramatically increased fear and volatility after shattering decades of relative peace in Europe. Sweden & Finland have applied to join NATO.
- Defense spending is increasing globally, especially in the U.S. and Europe. There is a renewed emphasis on the 2% rule for NATO defense spending.
- Rising tensions in the Pacific have led to a major increase in Japanese military spending and produced a significant nuclear military agreement between the U.S. and Australia.

Significantly Lower SPR Inventories



- The **Strategic Petroleum Reserve** is at the lowest level since December 1983, at 371.5 million barrels as of January 2023.
- SPR inventory decreased over 37% or 221 million barrels in 2022. (Dec. 21'-Dec. 22')
- The SPR will be restocked at $70 per barrel per the Biden Administration.

Energy Transition Inflation

- Original sticker price for 2022 F-150 Lightning (fully electric vehicle) was $41,669 in early 2022.
- After three separate prices increases during the year, the price of the 2023 model now stands at $58,514.
- This represents a whopping 40% increase in less than a year!
- Ford has blamed the price increases primarily on increased raw material prices for *lithium, cobalt and nickel* which are all key components of the lithium-ion batteries powering the vehicle.

Source: Car and Driver

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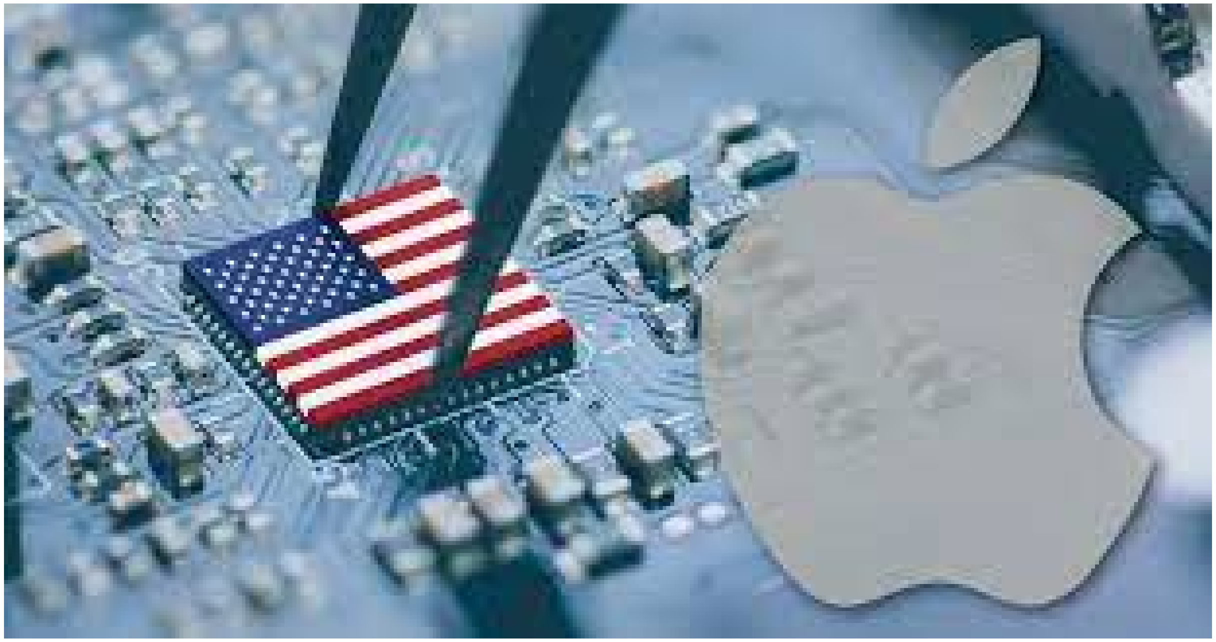
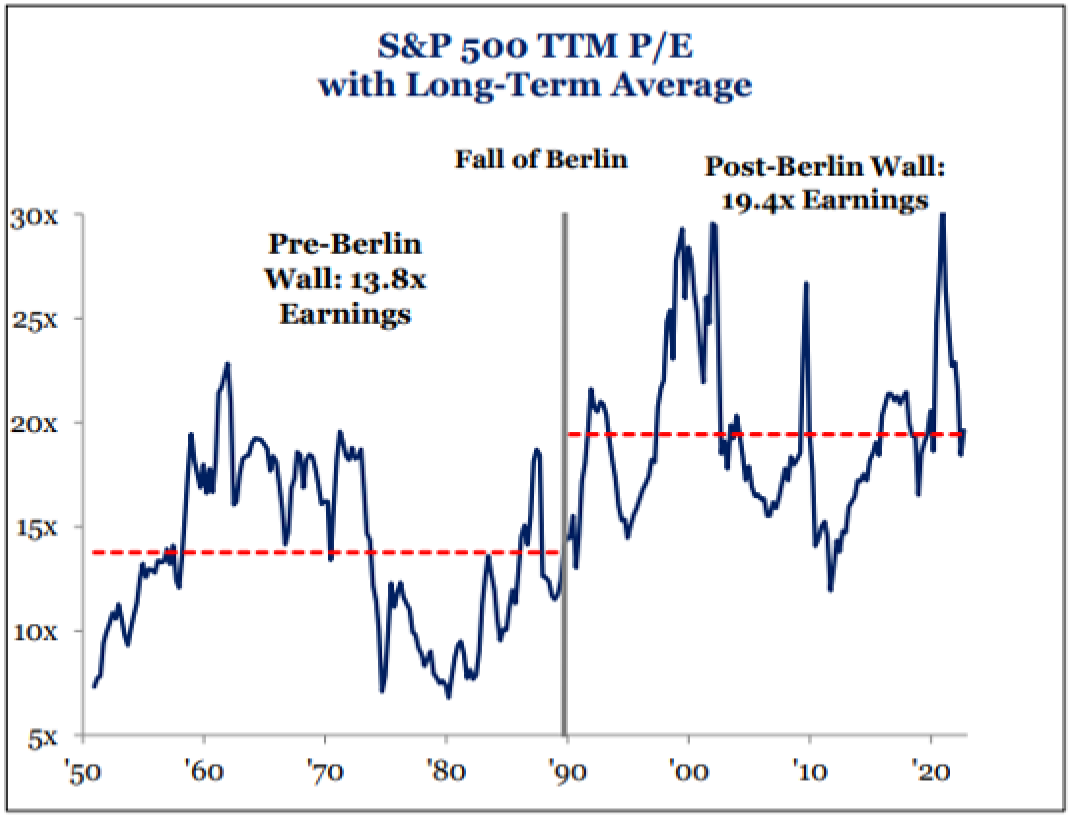


Source: Nikkei Asia

Semiconductor "Reshoring" Inflation

- Apple will become one of the first customers for Taiwan Semiconductor Manufacturing Co.'s new $12 billion plant in Arizona by early 2024.
- The TSMC facility will initially produce 4 and 5 nanometer chips, which are currently used in the iPhone 14 and iPhone 14 Pro.
- While this is welcomed news from a national security and investment standpoint, these U.S. manufactured chips are forecasted to be approximately ***50% more expensive than the same chips produced in Taiwan.***

New Period of Deglobalization



Source: Strategas

The World is Entering A Period of Deglobalization

✓ Multipolar World (U.S. vs. China)

✓ More Domestic Production & "Friend Shoring"

✓ Higher Inflation Likely

✓ Higher Long-Term Interest Rate Potential

✓ Lower P/Es for Stocks a Possibility

✓ Growth Over Value In Question

- Deglobalization will result in structural changes to the world economy for years to come.
- Potential for higher inflation that could pressure price to earnings (P/E) multiples and lead to a higher sustained interest rate environment.
- The significant outperformance by growth stocks over value stocks seen in the past decade is most likely over.

Market Outlook

Cambridge Trust Market Outlook – February 2023

Economy & Markets

- For the fourth quarter, GDP rose 2.9%. If inventory growth and trade are removed, the economy only grew at 0.2%, indicating an underlying slowdown in growth.
- For the full year, the economy grew at 2.1%. Most recent estimates of U.S. GDP growth are at 0.5% for 2023.
- Inflation is slowly ebbing from peak levels seen in mid-2022. In December, the CPI rose by 6.5%, the lowest annual rate in 2022.

Equities

- Despite a healthy rally in stocks for January, our positioning remains defensive with a focus on high-quality, short-duration, strong cash flow companies trading at reasonable valuations.
- 2023 earnings estimates remain vulnerable to further negative revisions. We expect layoffs to worsen throughout the 1st half of 2023, leading to reduced growth and consumer demand.

Fixed Income

- Fixed income started the year with positive returns as interest rates and credit spreads declined. High quality continues to be more attractive in the face of uncertain economic conditions.
- We are neutral in our fixed income allocation to offset further equity volatility while still taking advantage of more attractive rates.

Employment

- In January, the unemployment rate declined to 3.4%, a new low for the post pandemic era. Job gains were 517,000 versus an estimate of 188,000.
- Job openings rose to 11 million in the latest report. This means there are now 1.9 job openings for each unemployed worker.

Federal Reserve

- The Fed Funds rate was increased by 0.25% and future increases are still expected.
- Powell noted slowing in economic activity but also cited the strong labor market as reason for continued vigilance against inflation.

Issues to Watch

- Geopolitical tensions remain, including Russia, Ukraine, and China. U.S. debt ceiling negotiatic will also see tense political brinkmanship.
- China's return to full activity after relaxing its COVID restrictions could boost global trade.

Economic Metric	2023[1] *as of 1/31/23*	2023 *Year-end Projections*	
GDP (y-o-y) [2]	2.0%	0.5%	▲ [6]
Global GDP (y-o-y) [3]	3.1%	2.1%	
Inflation (CPI)	6.5%	3.75% [4]	▼
Fed Funds	4.50 – 4.75%	4.65% [5]	▼
10yr Treasury	3.51%	3.39% [4]	▼
Unemployment	3.4%	4.2% [4]	▼
Crude Oil (WTI)	$78.87	$75-110	

[1] *Data provided by Bloomberg. Metrics are as of month-end or most recent publication.*
[2] *Provided by U.S. Real GDP Economic Forecast Survey Median.*
[3] *Provided by World Real GDP Economic Forecast Survey Median.*
[4] *Provided by Bloomberg Intelligence Forecast.*
[5] *Provided by World Probability Forecast.*
[6] *Arrows represent a month-over-month change.*

Index Returns *as of 1/31/23*	1-Month	2022
S&P 500 *(Large-cap stocks)*	6.28%	-18.11%
Russell 1000 Growth *(Growth Stocks)*	8.33%	-29.14%
Russell 1000 Value *(Value Stocks)*	5.18%	-7.54%
MSCI ACWI Ex-U.S. *(Int'l. stocks)*	8.11%	-16.00%
MSCI EAFE *(Developed Market. Int'l stocks)*	8.10%	-14.45%
MSCI EM *(Emerging Market stocks)*	7.90%	-20.09%
Inter. Govt. / Credit Bond Index	1.87%	-8.23%
ICE BofA 1-10Y U.S. Muni Index	1.91%	-4.63%
Commodities *(Bloomberg Diversified Index)*	-0.49%	16.09%

Asset Allocation/ Tactical Positioning – February 2023

Asset Class	Over-Weight	Neutral	Under-Weight	Recent Change, if any[5]	Opportunity	Challenge
Equities[1]			✓		**Inflation Peak, Max Pessimism**	**Slowing Growth/Recession**
U.S. Equities		✓		▼	Long-Term Outperformance	Slowing Earnings/Valuations
International Developed Markets		✓		▲	Attractive Valuations	Inflation/Currency/Energy
Emerging Markets		✓		▲	Attractive Valuations	Dollar Strength/Global Growth
Fixed Income[2]		✓			**Attractive Yields**	**Inflation/Hawkish Fed**
U.S. Government			✓		Safe Haven Asset	Duration
Investment Grade Corporate	✓				Attractive Yields	Recession
Below Investment Grade[3]	✓				Lower Vol Equity Alternative	Recession
Alternative[4]	✓				**Diversification**	**Recession**
Income Fund	✓				Income Buffer	Market Disruptions
Cash	✓				**Risk Reduction**	**Inflation**

[1] *Equity tactical weights are relative to the Cambridge Trust Core Equity allocation and is comprised of 80% S&P 500 and 20% MSCI AC World ex-U.S. Index.*
[2] *Fixed Income tactical weights are relative to the Cambridge Trust Core Taxable allocation and is comprised of 100% Barclays Intermediate Gov/Credit Index.*
[3] *Below investment grade holdings include high yield, bank loans and emerging market debt mutual funds. Represents an out-of-benchmark allocation that will be reflected as an overweight position relative to the Barclays Intermediate Gov/Credit Index if any allocation is held.*
[4] *Alternative tactical weights represent an out-of-benchmark allocation that will be reflected as an overweight position when utilized.*
[5] *Direction arrow highlights any recent changes of the overall allocation after a recent tactical asset allocation or strategy change.*

Financial Planning

Financial Planning

Charting a course to build, protect, and transfer your wealth

Whether you're building your wealth, sustaining your lifestyle, or passing it on to the next generation, our Financial Planning Group takes a coordinated approach, working with both your internal team and external professionals to help you achieve your short- and long-term goals.

From saving for education and planning for retirement to managing taxes and reviewing your estate plan, we'll create a comprehensive financial plan that will achieve what matters most to you, providing you with confidence today and clarity for a financially secure tomorrow.

Financial Planning

Professional planning team

Our team of highly experienced financial professionals hold advanced degrees and designations including CFP®, CFA, CPA and JD and collaborate with your other advisors both internal and external to help you navigate the complexities of your financial life.

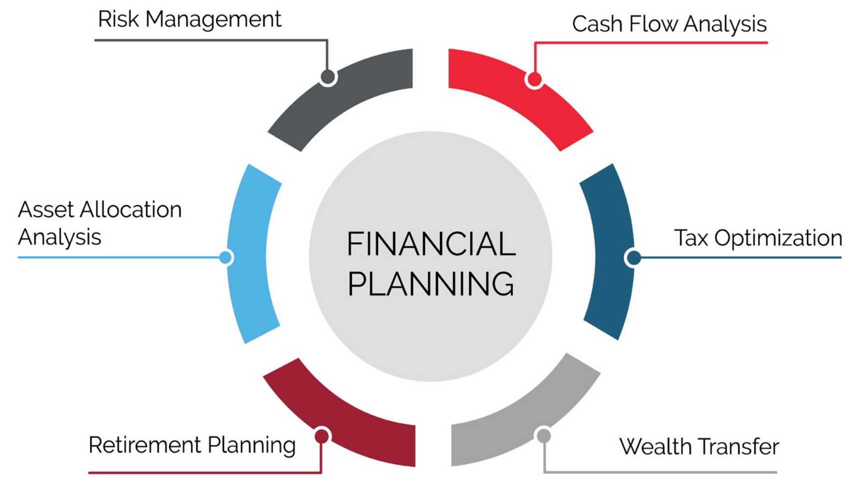
It all begins with a conversation

We'll work with you to gain a deep understanding of your goals, values, and concerns so that together, we can create and implement a comprehensive financial plan to help you achieve your current and future goals.

Financial review and analysis

Using state-of-the- art technology, coupled with our professional expertise, we'll analyze your assets, liabilities, taxes, and philanthropic goals along with your unique preferences to create a financial plan tailored to your desired outcomes.

Important financial considerations we'll address together



Cash Flow Analysis

Based on your cash flow analysis, we can deliver actionable insights that help you make informed decisions at key turning points in your financial life.

Tax Optimization

Planning for and mitigating the impact of taxes is a central focus. Being strategic about the taxes you pay can have a significant positive impact towards achieving your goals.

Wealth Transfer

We can analyze multi-generational wealth transfer and philanthropic giving strategies. We focus on your values and priorities to have a deeper understanding of what you want to leave for the next generation and/or charitable organizations.

Retirement Planning

We will help provide a roadmap and address critical issues such as maximum lifestyle affordability and tax efficient withdrawal strategies The considerations can be vast and complicated especially when combined with risk factors such as longevity, inflation, and market volatility.

Asset Allocation Analysis

By analyzing the structure and risk characteristics of your overall portfolio, we will guide you towards an appropriate mix of growth and income producing assets across all of your accounts.

Risk Management

Risk extends beyond market volatility. We provide valuable insight into the importance of protecting against various types of financial, health and legal risks.

Planning for your financial life

Our financial planning professionals will help you navigate the complexities of financial management and organization to help build, protect and transfer your wealth.

For more information on how we can help you create your personalized financial plan, contact your Cambridge Trust team or visit www.CambridgeTrust.com.

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