ALBION FINANCIAL GROUP

Guiding Clients
To A Lifetime of
Good Decisions

APRIL 2022

IN THIS ISSUE

The snow has mostly melted, the flowers are in full bloom, and tax season is behind us at last. As time propels us forward the Albion team is keeping stride to serve your needs along the way.

Ahead, our CEO and Co-Founder John Bird puts the Russian invasion of Ukraine into wider global context and then shines a light onto our related domestic concerns, with an eye for the silver lining. Our CIO Jason Ware takes stock of the economic challenges we have confronted so far this year and maps out what he expects for the near future. From the Planner's Corner, Patrick Lundergan describes how the cash in your bank account is being impacted by rising interest rates.

Read through to the community segment for team and event updates.

Your fiduciary servants,

- The Albion Team

FROM JOHN BIRD'S DESK

It's a bit redundant to suggest that year-to-date 2022 has been an interesting one for investors and citizens alike; what year hasn't? While only three months in we've seen declines in our financial markets with most domestic indices down from high single digit percentages to well into double digit losses. There's no shortage of factors driving investors away ranging from continued supply chain induced shortages and tight labor markets, a distressing war taking place in Ukraine which has a side effect of driving

oil prices higher, and all of the above contributing to inflation. However there are also powerful drivers keeping investors in the market, including record low unemployment and its positive impact on consumer spending, recognition that covid-induced supply chain issues which helped drive inflation higher are resolving, constant innovation across all sectors, and the reality that Russia’s economy is quite small relative to other developed countries.

It helps to put our economic concerns in perspective, particularly around Russia’s hostile actions toward its neighbor. Russia wants to be recognized as a significant global power. Yet in economic terms it is way down the list with a $1.67 trillion economy that ranks it below South Korea, Italy, Brazil, and Canada among many others. Based on 2019 IMF data the Russian economy is 7.5% the size of ours. Further, 60% of Russia’s GDP is based on natural resource extraction. While this gives them leverage, particularly in the energy markets and specifically over Western Europe, it does not give them the depth and breadth of creative innovation we are seeing across most western nations. Energy aside, Russia’s presence in international markets could shrink dramatically yet cause barely a ripple in the global economic system. Russia is clearly inflicting tremendous damage and pain on Ukraine which the world must stand up to and condemn. However, from an economic perspective Russia is not a significant player.

The Russian invasion highlights the deep challenge of increasing illiberalism around the world as countries once hailed as functioning democracies push toward autocracy. Unfortunately the very word – liberalism – has become a lightning rod. Yet the actual definition is a political and social philosophy that promotes individual rights, civil liberties, democracy, and free enterprise. Illiberalism is the erosion and undermining of these values.

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Our country has some basic principles upon which all else rests including the rule of law, individual liberties, freedom of speech and religion, and the concept of equal opportunity. Our guarantee of free speech affords us the luxury of disparaging our principle based system and the exceptional value free-enterprise has created.

It is troubling how many disparage our country for its shortcomings without acknowledging the far more extreme challenges created by alternative political and economic systems. Yes our core principles allow us to be critical which is right and appropriate. But we also have a duty to acknowledge what we have done right and continue to improve upon what we are not doing well. The goal is to strive for a more perfect union. While such a union must be our core and enduring objective there is nothing anywhere that says it will ever be achieved. We must always learn and improve. In our personal relationships, in our businesses, and in our nation.

Free enterprise in action is astounding. Millions of individual decision makers allocate capital to creative projects they favor; workers migrate to better jobs; companies find the best locations for their plant, warehouse, or office. It is these millions of small decisions that lead to the best overall choice of direction.

Right now our politics - that which gives us the ability to make our union more perfect - is polarized to the point of absurdity. The problems do not belong to one party or the other, nor do the solutions. Yet partisanship has made collaboration nearly impossible, especially at the federal level. Ideology is crushing possibility. Compromise and openness to change are core principles of democracy yet the present moment finds compromise to be impossible. We can and must acknowledge both our exceptional history and flaws in the same breath. To continue our exceptional history we must never lose sight that a more perfect union is a goal for which we strive, not a destination already reached.

We are fortunate to have a broad, deep and diverse economy populated by millions working to make their product or service better, faster or cheaper each day. Citizens for the most part follow the rule of law rather than arbitrary dictates which provides predictability for each of us as we make decisions and work to improve. And we can, and will, continue to make our experiment more perfect. But only if we ditch the vilification, listen to one another, and work together to make it happen. I am optimistic that our country and the countries around the globe committed to democratic principles will continue to thrive and lead the way for the rest. It is that optimism that keeps me excited not only about the opportunities I see as an investor but also about working with the thoughtful group of professionals at Albion on your behalf.

ECONOMY & MARKETS by Jason Ware

The first quarter of 2022, which included the rather quick rise and fall of Omicron; the horrors of war in Ukraine; soaring inflation; and a major rise in interest rates, has been tumultuous as evidenced by the drop and chop in equity and bond prices. Nevertheless – as we do every day on your behalf – taking stock of the underlying fundamentals is vital in both judging present conditions and shaping our outlook.

First, the exogenous factors.

The pandemic has seen daily US cases drop from over 1M in January to under 20K by mid-March having stalled out as the even more contagious Omicron ‘BA.2’ variant now accounts for ~75% of infections. Likewise, hospitalizations and deaths have fallen as the risk of mortality is low for most fully vaccinated (or naturally inoculated) persons. As a result, Covid impacts on the economy are fading fast. Save for a novel variant of concern that can evade immunity and is highly virulent, it seems this pandemic has finally entered an endemic phase. Over in Ukraine, amidst unspeakable human suffering brought on by an outrageous and criminal war, after weeks of fighting Russian forces have failed to seize Kyiv potentially setting the stage for a conflict that’s come off the boil and shifted to a protracted strategic simmer in eastern Ukraine. Disorder to Russian and Ukrainian supplies of food, energy, and other commodities has made worse the current inflation problem. Yet despite outrage over Putin’s barbaric hostility, Europe has not stopped using Russian oil and gas and the inclination of countries like China and India to continue working with Moscow on the economic front may limit some of the medium-term influences of the war on global commodity prices. More on inflation in a moment.

Switching gears to our core economic assessment.

The American economy boomed in 2021 (+5.7%). As we've said previously, we expect growth to moderate this year and next – by at least half. Nevertheless, pang about inflation amid a tight labor market renders it unlikely that D.C. will pass significant fiscal stimulus anytime soon. Meanwhile, all clues, including a study of history, suggest that the President's party will lose control of one or perhaps both Houses of Congress in November, reducing further the outlook for pro-growth fiscal spending through the 2024 election. I mentioned the labor market, which is quite strong. Above-trend wage gains ought to bring some workers off the bench helping fill a portion of the ~5M gap between open jobs and available workers. Even still, the jobs market is somewhat overheated and bears watching as it pertains to the importance of a well-balanced economy.

"This may all sound a bit dicey for now, but let us not forget that we are long-term investors. Ignoring the clatter is not easy."

Other fundamental elements, from retail sales to household balance sheets, all imply a solid first quarter for consumer spending. That said, as we've past opined, reduced inventory restocking and normalizing goods demand could cut first-quarter real GDP growth to scant levels. We do anticipate some rebound in the second quarter, however. Subsequently, fading fiscal stimulus, higher interest rates, slowing employment growth, and truncation of "reopening effects" likely produce that overall deceleration in calendar year 2022 that we've expected for some time.

Corporate profits are not immune to this path of diminution. After a superbly strong 2021, further earnings gains will be much more modest reflecting tough year-over-year comparisons, higher labor and interest costs, and slower nominal growth. Overall, we envisage S&P 500 operating earnings to expand by maybe +10% this year following a +50% gain last year.

Outside of the war in Ukraine, arguably the two most pressing matters for markets are inflation and the Federal Reserve (i.e., monetary policy). As to the former, although billowing commodity prices due to the war in Ukraine have thrown a crumple into headline inflation data we could get some calming here, while broader core pressures may finally hit their peak this spring. But

as we know, it's not all a matter of demand. Snarled supply has played an equal role in price burdens. Notwithstanding China's relentless "Covid zero" policy posing rolling threats to global production and logistics, supply chains are likely to recover in the year ahead. This, along with lower real growth in consumer incomes, should quell inflation in the goods sector. The sub-category to watch now is services given renewed gains in wages, rents, and even short-run inflation expectations helping keep prices stubbornly elevated for a while yet. Our core view though remains that high inflation will ultimately give way to disinflation in the back half of 2022 and into 2023.

How will this impact monetary policy? For the first time since 2018, in March the Fed (FOMC) raised its main policy rate by +0.25% officially getting us off "the zero bound." But they're not done. Fresh FOMC projections combined with speeches from key Fed officials – not to mention futures market pricing – all suggest a further +2% rise in the federal funds rate by the end of 2022. Else, it seems the balance sheet is now in play as the central bank plans a $95B monthly reduction in its asset holdings, probably commencing in May or June. Bottom line: a new Fed policy regime is upon us and with it more corrections and volatility in financial markets.

All told, by year's end inflation should be lower even if running above Fed target, with unemployment at generational lows and an economy (plus profits) still expanding. Provided that inflation does ease, Jerome Powell & Co. may decide to raise rates at a gentler stride in the back half of 2022 and into 2023 as it seeks to avoid tipping us into recession (i.e., dodging the dreaded "Fed policy mistake"). But for now, expect a sharp pitch up in Fed rate hikes in the coming months. It's possible we'll even get a +0.50% move or two as their work remains laser-focused on slaying the inflation dragon. Nonetheless, we don't see an imminent recession on the horizon.

This may all sound a bit dicey for now, but let us not forget that we are long-term investors. Ignoring the clatter is not easy. However the reality is that much of the abovementioned challenges are just that – noise. The signal remains prudent asset allocation, owning a collection of great companies / investments well-diversified, and controlling for behavior. This process remains our true north star. And despite the volatility (never fun), we have high confidence in these quality securities and our continued work with you. Many thanks for your trust in us.

PLANNERS CORNER by Patrick Lundgren

You may have heard about rising interest rates yet the interest you are earning on your checking and savings account has remained the same. Why is that? Banks make most of their money on the difference between what they pay customers to hold their deposits and what they can charge borrowers when lending that money. Rising interest rate environments can mean larger spreads between these two rates and more profit for banks. Usually, banks can't sit back and collect on this increasing spread for long - they need to raise interest rates paid to depositors to compete for new business. Not surprisingly, this leaves many people wondering why their bank still isn't paying them for their valuable deposits.

By the end of March, Fed Funds Futures markets were pricing in eight additional 0.25% rate hikes in 2022 and a year-end target rate floor of 2.25%. It would seem the perfect situation for banks to compete for new business by raising rates on deposits. A move like this would force other banks to follow suit until they reach equilibrium. But the banks don't need additional deposits. They are more concerned with how to lend the massive amount of consumer cash they already have.

In the year before COVID-19, total deposits increased by

4.7% at all U.S. banks. In 2020, they increased by more than 20%. Banks are flush with cash and not looking for more - not yet. Banks have been pinching pennies in a low-interest-rate environment for many years, relying on fee revenue and originating and selling loans. Fewer IPOs and new regulations on SPACs (Special Acquisition Companies) are also reducing fees for the country's largest banks. Unless lending drastically increases or pressure from competition drives rates higher, we should expect deposit rates to remain low for the foreseeable future. Low rates won't last forever but understanding why banks don't need to pay more for deposits right now might help ease some of the sting when stashing cash in the bank and earning next to nothing. Fortunately, there are other options for those strictly looking for more yield on their cash in the bank.

There is no shortage of high yield online savings accounts that will yield more than your traditional savings account. Without the overhead of traditional banks, they can generally offer higher rates on cash deposits. Whether these options are better will depend on what you want as a consumer. Below is a list of some advantages and disadvantages of online-only savings accounts.

Advantages:

1. Higher interest rates.
2. Tech-focused, faster to adopt new features.
3. Some claim customer service is better because company resources usually allocated to brick and mortar locations can now go to training and assisting with complex customer services issues.
4. The ability to easily link and transfer cash to other accounts online.

Disadvantages:

1. No face-to-face customer service at a physical location.
2. Might not offer other services such as mortgage loans.
3. They might not have their own ATMs.
4. Harder to deposit and withdraw cash unless you use ATMs affiliated with the online bank.
5. Can't access money when the online portal goes down.
6. May lose the personal relationship you get with a traditional bank.

It is okay if you aren't earning much on your cash. As we often remind clients, it is important to have at least 3 to 6 months of living expenses in cash as an emergency fund. And although the return we earn on cash is dismal, the point of the emergency fund is to be there when you need it rather than to provide a return on your investment. We generally don't know ahead of time when we are going to need to tap our emergency fund, and there is great peace of mind from knowing you have access to cash in a pinch. Low-interest rates aren't forever, but while we wait for banks to feel the pressure to raise deposit rates, it is nice to know there are options for your cash, such as online savings accounts.

ALBION COMMUNITY UPDATES

We are delighted to announce that Walter Joseph has joined the firm as the newest member of our Investment Team. A Denver native, Walter is the third University of Utah alumnus on Albion's team. He will be working closely with Michael Kessler and Jason Ware to perform security analysis, portfolio management, and trade execution.

Finally, the Women of Albion are hosting the seventh annual "Women, Wine, and Wildflowers" event on July 21st at the Alta Lodge up Little Cottonwood Canyon. Past attendees have ranked this activity among their favorite of the year. So get out your calendar now and save the date!