HIGHLAND

Multi-Asset Solutions
Weekly Commentary
May 1, 2023

Highland Associates

Stocks: Back to The Top End OF The S&P 500's Trading Range; Small Caps Large Caps for 7th Straight Week.

Volatility returned as earnings season ramped up in a big way and a flurry of economic data releases provided both bulls and bears with reasons to press their position. The S&P 500 ended the week with a 0.8% gain, but sector leadership remained quite narrow with communication services and information technology again outperforming amid some high-profile earnings beats (MSFT, FB) during the week. The small-cap Russell 2000 fell 1.2% on the week and has now underperformed the S&P 500 for seven consecutive weeks dating back to early March, a trend indicative of persistent concerns surrounding credit availability, slowing U.S. economic growth, and lackluster investor risk appetite. For us to embrace the view that the year-to-date rebound in the S&P 500 is something more than just a move back to the high end of the index's 3,800 to 4,200 trading range, sector leadership needs to broaden-out and the relative performance of small caps needs to improve.

- The MSCI EAFE developed markets index fell 0.2% on the week and lagged the S&P 500 for a change as France, Italy, and Spain were notable underperformers, while Germany, Japan, and the U.K. turned out more modest losses. The MSCI Emerging Markets index also closed the week lower by 0.2% as India was a standout performer on the upside. While China rebounded and contributed to the MSCI EM's modest weekly gain, South Korea and Taiwan continued to lag.
- Microsoft and Meta Platforms (Facebook) came to the market's rescue last week, with each stock rising sharply on earnings beats, pulling the communication services and information technology sectors at-large along for the ride and stemming a tide of selling pressure mid-week. Interestingly, with 54% of the S&P 500 having posted quarterly results, just shy of 80% have topped the consensus earnings estimate, an encouraging figure in-line with what we've grown accustomed to in the post-COVID world. However, while 1Q23 results have so far proven better than feared, the consensus estimate for full-year 2023 S&P 500 earnings per share (EPS) ended April at $219.64, down just $0.02 during the month and valuing the S&P 500 at 19X expected full year results. For comparison, the consensus estimate for '23 EPS stood at $228.91 at the end of December. While last week was a big one for earnings, releases will continue at a fast and furious pace this week as over 20% of the S&P 500's market cap is set to report this week with consumer-oriented bellwethers Apple and Starbucks, along with notable reports from the health care, industrials, and information technology sectors, potentially poised to move markets.
- While the S&P 500 closed out April with a 1.6% gain, under the surface we continue to see reasons for caution. One such yellow flag is the relationship between consumer staples

This is more than business. This is moving the world forward.

and consumer discretionary which we monitor for what it may be telling us regarding the state of risk appetite and sentiment. While the S&P 500 consumer staples sector gained 3.6% in April, the consumer discretionary sector lost 1.1%, a notable about-face given staples meaningfully lagged discretionary in 1Q23. Staples resurgence during April could be a function of pricing power displayed by earnings releases from companies such as Procter & Gamble and Hershey, or it could be signaling that investors believe higher prices on staples will eat into disposable income typically spent on discretionary items. This relationship remains worth monitoring.

Bonds: Mixed Messages on The Economic Front Lead to A Volatile Week in The Rates Market; Stagflation Narrative Could Gain Traction Post-GDP, PCE.

Fixed income investors remain focused on the debate over raising the debt ceiling with concerns that it may be more than political posturing this time around. The U.S. Treasury took "extraordinary measures" back in February to buy Congress time to raise the debt ceiling, but we are fast approaching the "X-date" when Treasury's ability to fund government operations is expected to run out. Ever since Treasury stepped in back in February, the June through August timeframe has been highlighted as when the "X-date" would arrive, with the timing heavily dependent upon tax collections While we're just two weeks removed from the April 18 tax filing deadline, tax receipts, to this point, have surprised to the upside, and may provide Congress with some breathing room before "X-date" arrives. Nevertheless, evidenced by the 3-month T-bill yielding 5.10% versus the 1-month T-bill yield of 4.35%, investors remain fearful that Congress and the White House may not be able to come to terms on a debt ceiling deal before August. Congress will ultimately get its act together, but volatility in the rates market and dislocations on the short end of the Treasury curve are likely to remain in place for some time as both sides jockey for position/leverage in the debt ceiling debate.

- U.S. economic data released last week continued to paint a mixed picture versus a dire one. On the constructive side of the ledger, durable goods orders for March surprised to the upside (+3.2% month over month vs. +0.7% expected), while initial jobless claims for the week ended April 22 came in at 230k, shy of the 250k estimate, evidence of continued tightness in the labor market. On the more concerning end of the spectrum, a preliminary read on first quarter GDP fell well short of the consensus estimate, showing the U.S. economy grew just 1.1% during the quarter versus the 1.9% consensus estimate. The most troubling aspect of the hot start gave way to a muted February and read on 1Q23 GDP is how quickly economic activity appears to have slowed as January's a downright disappointing March as consumers appeared to scale back

spending during the month in a meaningful way.

- Personal Consumption Expenditure (PCE) Deflator, the FOMC's preferred inflation gauge, was released Friday. March headline PCE rose 0.08% month over month, in-line with the 0.1% estimate, and core PCE rose 0.28% month over month, again, roughly in-line with the 0.3% estimate. Year over year, both the headline and core readings modestly exceeded the consensus estimate. Another 25-basis point hike to the Fed funds rate remains the most likely outcome when the Committee meets this week as the PCE release provides the Fed with the necessary cover to tighten policy further, and the likelihood of a quarter-point June rate hike have also increased. The combination of lackluster 1Q GDP, an elevated core PCE reading for March, and the ongoing debt ceiling debate may embolden those championing the stagflation narrative over coming weeks, preventing bond bulls forecasting a recession and lower yields from getting too aggressive, and likely supporting Treasury yields over the near-term.

What We're Watching:

- The Eurozone Consumer Price Index (CPI) for April is released Tuesday with a headline figure of 6.9%, in-line with the March reading, expected. Year over year Core CPI is expected to also remain static month over month at 5.7%.
- The Job Openings and Labor Turnover Survey (JOLTS) for March is released Tuesday and is expected to show 9.628 million jobs open during the month, down from 9.931 million in February.
- The Federal Open Market Committee (FOMC) concludes its two-day meeting on Wednesday and is expected to hike the Fed funds rate by 25-basis points, taking the upper bound of the central bank's target range to 5.25%.
- The April Nonfarm Payrolls report is released Friday and is expected to show 185k jobs were created during the month, down from 236k in March, with the unemployment rate ticking higher month over month to 3.6% from 3.5% in March. Average hourly earnings are expected to rise 0.3% month over month and 4.2% year over year in April, which would fall in-line with metrics from March.

Important Notes & Disclosures for Institutional Investors and/or their Representatives:

The content and any portion of this newsletter is for personal use only and may not be reprinted, sold, or redistributed without the written consent of Regions Bank. Regions, the Regions logo, and other Regions marks are trademarks of Regions Bank. The names and marks of other companies or their services or products may be the trademarks of their owners and are used only to identify such companies or their services or products and not to indicate endorsement or sponsorship of Regions or its services or products. The information and material contained herein is provided solely for general information purposes.

Regions does not make any warranty or representation relating to the accuracy, completeness or timeliness of any information contained in the newsletter and shall not be liable for any damages of any kind relating to such information nor as to the legal, regulatory, financial or tax implications of the matters referred herein. This material is not intended to be investment advice nor is this information intended as an offer or solicitation for the purchase or sale of any security or other financial instrument. Any opinions expressed herein are given in good faith, are subject to change without notice, and are only current as of the stated date of their issue. Regions Asset Management is a business group within Regions Bank that provides investment management services to customers of Regions Bank. Employees of Regions Asset Management may have positions in securities or their derivatives that may be mentioned in this report or in their personal accounts. Additionally, affiliated companies may hold positions in the mentioned companies in their portfolios or strategies. The companies mentioned specifically are sample companies, noted for illustrative purposes only.

The mention of the companies should not be construed as a recommendation to buy, hold, or sell positions in your investment portfolio. Neither Regions Bank nor Regions Asset Management (collectively, "Regions") are registered municipal advisors nor provide advice to municipal entities or obligated persons with respect to municipal financial products or the issuance of municipal securities (including regarding the structure, timing, terms and similar matters concerning municipal financial products or municipal securities issuances) or engage in the solicitation of municipal entities or obligated persons for such services.

With respect to this presentation and any other information, materials or communications provided by Regions, (a) Regions is not recommending an action to any municipal entity or obligated person, (b) Regions is not acting as an advisor to any municipal entity or obligated person and does not owe a fiduciary duty pursuant to Section 15 B of the Securities Exchange Act of 1934 to any municipal entity or obligated person with respect to such presentation, information, materials or communications, (c) Regions is acting for its own interests, and (d) you should discuss this presentation

HIGHLAND

and any such other information, materials, or communications with any and all internal and external advisors and experts that you deem appropriate before acting on this presentation or any such other information, materials, or communications. Source: Bloomberg Index Services Limited. BLOOMBERG® is a trademark and service mark of Bloomberg Finance L.P. and its affiliates (collectively "Bloomberg"). BARCLAYS® is a trademark and service mark of Barclays Bank Plc (collectively with its affiliates, "Barclays"), used under license. Bloomberg or Bloomberg's licensors, including Barclays, own all proprietary rights in the Bloomberg Barclays Indices. Neither Bloomberg nor Barclays approves or endorses this material or guarantees the accuracy or completeness of any information herein, or makes any warranty, express or implied, as to the results to be obtained therefrom and, to the maximum extent allowed by law, neither shall have any liability or responsibility for injury or damages arising in connection therewith.

Source: Bloomberg Index Services Limited. BLOOMBERG® is a trademark and service mark of Bloomberg Finance L.P. and its affiliates (collectively "Bloomberg"). BARCLAYS® is a trademark and service mark of Barclays Bank Plc (collectively with its affiliates, "Barclays"), used under license. Bloomberg or Bloomberg's licensors, including Barclays, own all proprietary rights in the Bloomberg Barclays Indices. Neither Bloomberg nor Barclays approves or endorses this material or guarantees the accuracy or completeness of any information herein, or makes any warranty, express or implied, as to the results to be obtained therefrom and, to the maximum extent allowed by law, neither shall have any liability or responsibility for injury or damages arising in connection therewith.

Investment, Insurance and Annuity Products:
Are Not FDIC Insured | Are Not a Deposit | May Go Down in Value | Are Not Bank Guaranteed
Are Not Insured by Any Federal Government Agency | Are Not a Condition of Any Banking Activity