The charts and themes from the past month that tell the current story in markets and investing.

**Bank Failures**

Silicon Valley Bank (SVB) was likely the fastest bank failure—from rumor to demise—in American history.

It’s not uncommon for banks to fail, as a few failures seem to happen every year. However, it is uncommon for banks of SVB’s size—$175 billion in deposits—which is what made this situation unique.

**Exhibit 1**

**FDIC Bank Failures**

Number of Bank Failures and Total Deposits of Failed Banks Since 2001

There were certainly aspects of SVB’s business, particularly concentration in technology industry bank clients, that made them vulnerable to a bank run.

On Bloomberg’s “Odd Lots” podcast, bank analyst Dan Davies made the interesting point:

“SVB’s risk department didn’t realize the extent to which their customers were not separate entities in terms of financial decision-making. The mistake was thinking that even within tech they were diversified. They thought they had thousands of customers with millions in deposits, but they actually had a few customers (mostly venture capitalists that ran in the same social circles) with billions who all coordinated leaving together, causing the run.”
The asset-liability mismatch in their bond portfolio and poor risk management were bad, but the false sense of diversification and herd nature of venture capital ultimately played a major role in their fate.

**Nothing Like 2008 ... at Least Not Yet**

A banking crisis immediately awakens memories of 2008 for many of us.

Jamie Dimon, CEO of J.P. Morgan, and a prominent figure during 2008, had this to say on SVB’s failure in his recent shareholder letter:

“Most of the risks were hiding in plain sight. This wasn’t the finest hour for many players.”

The “fear index,” or VIX, has mostly ignored this crisis, indicating this may be an issue specific to a few banks rather than the entire system. The VIX is currently hanging around its long-term average and well below recent peaks observed over the past year.

**Exhibit 2**

Stock Market Volatility
CBOE VIX Index

While financials are the worst-performing sector year-to-date, down 6%, it’s hardly the demise some might expect given the news cycle. Other sectors like technology, communications, and consumer discretionary have felt no impact—at least when it comes to share prices—and are all up more than double digits for the year.
The Last Hike?

The Fed hiked rates by another 25 basis points in March, the ninth-rate hike in the past 12 months. That brought the fed funds rate up to a new range of 4.75%-5.00%, a level we haven’t seen since September 2007.

However, among investors, more emphasis is placed on what the Fed says about the future than actions being taken in the present.

One big takeaway was the softer language the Fed used around future rate hikes. Via the Wall Street Journal’s Fed Statement Tracker, the Fed removed text signaling “ongoing increases” in the fed funds rate and replaced it with “some additional policy firming may be appropriate.”
Exhibit 5

Fed Statement Tracker
Feb 1, 2023 → Mar 22, 2023 hide changes

Recent indicators point to modest growth in spending and production. Job gains have been robust,picked up in recent months, and are running at a robust pace; the unemployment rate has remained low. Inflation has eased somewhat but remains elevated.

Russia’s war against Ukraine is costly. The U.S. banking system is sound and resilient. Recent developments are likely to result in tremendous human and economic hardship and is contributing to elevated global oil prices. Credit conditions for households and businesses and to weigh on economic activity, hiring, and inflation. The extent of these effects is uncertain. The Committee remains highly attentive to inflation risks.

The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. In support of these goals, the Committee decided to raise the target range for the federal funds rate to 4-1/23/4 to 4-3/4 percent. The Committee anticipates that ongoing increases in the target range will be closely monitored and assessed the implications for monetary policy. The Committee anticipates that additional policy firming may be appropriate in order to attain a stance of monetary policy that is sufficiently restrictive to return inflation to 2 percent over time. In determining the extent of

The market has taken this language as an indirect signal that March was perhaps the last Fed hike of this cycle. Fed funds futures are now expecting the Fed to pause rate hikes at the next FOMC meeting (May 3), followed by a rate-cutting cycle starting later this summer.

Exhibit 6

Federal Reserve Dot Plot
FOMC Participant Projections of the Federal Funds Rate

Whether or not this comes true will be dependent on several factors, including the path of inflation, follow-on effects from the banking crisis, and the general state of the economy.

Inflation Data Gives the Fed Ability to Pause
Recent inflation data helps the Fed’s case that there is an opportunity to slow down rate hikes. Looking across key categories of the inflation index, all of them are either below or well below their peak readings.
February’s 6.0% Consumer Price Index (CPI) reading was the eight-consecutive decline in the year-over-year rate of inflation and the lowest level since September 2021. There are increasing expectations that we will see another move lower when the March data is released.

And with the March rate hike, the fed funds rate (4.75% to 5%) is now above the Core Personal Consumption Expenditure (PCE) of 4.6% (which the Fed states as its preferred measure of inflation), potentially implying the Fed’s battle with inflation is nearing its final chapter.

**Diversification Keeps You in the Game**

With everything happening in the world, it’s easy to get lost in the minutiae. But from an investing standpoint, there’s an easy way to keep yourself in the game during periods of turbulence, which is being diversified.
To use a golf analogy, putting the ball in the fairway is likely the biggest predictor of success. In investing, diversification helps investors find the fairway.

Any single year of great investment performance is akin to birdieing a hole in golf; it's nice, but the 18-hole scorecard is what really matters. For many of us, birdies are hard to replicate. They only come around so often.

As can be observed below, investing follows a similar track. 2022’s "birdie" was commodities, up 16% for the year. But look at how commodities performed in years prior. Among major asset classes, commodities were the worst performer in seven of the 10 years prior to 2022.

Exhibit 9

Asset Class Performance
Total Returns

If you only play for birdies, you’re bound to end up with bogeys or worse on many other holes. Meanwhile, a diversified approach (measured by the balanced portfolio) provides a more consistent outcome, helping you find the proverbial fairway.

Disclosures

Opinions expressed are as of the current date, such opinions are subject to change without notice. Morningstar Investment Management shall not be responsible for any trading decisions, damages, or other losses resulting from, or related to, the information, data, analyses, or opinions or their use. This commentary is for informational purposes only. The information, data, analyses, and opinions presented herein do not constitute investment advice, are provided solely for informational purposes and therefore are not an offer to buy or sell a security. Please note that references to specific securities or other investment options within this piece should not be considered an offer (as defined by the U.S. Securities and Exchange Act of 1934) to purchase or sell that specific investment. Performance data shown represents past performance. Past performance does not guarantee future results.

All investments involve risk, including the loss of principal. There can be no assurance that any financial strategy will be successful. Morningstar Investment Management does not guarantee that the results of their advice, recommendations, or objectives of a strategy will be achieved. Diversification is an investment method used to help manage risk, it does not ensure a profit or protect against a loss.
This commentary contains certain forward-looking statements. We use words such as “expects,” “anticipates,” “believes,” “estimates,” “forecasts,” and similar expressions to identify forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties, and other factors that may cause the actual results to differ materially and/or substantially from any future results, performance, or achievements expressed or implied by those projected in the forward-looking statements for any reason. Past performance does not guarantee future results.

Morningstar® Managed Portfolios® are offered by the entities within Morningstar’s Investment Management group, which includes subsidiaries of Morningstar, Inc. that are authorized in the appropriate jurisdiction to provide consulting or advisory services in North America, Europe, Asia, Australia, and Africa. In the United States, Morningstar Managed Portfolios are offered by Morningstar Investment Services LLC or Morningstar Investment Management LLC, both registered investment advisers, as part of various advisory services offered on a discretionary or non-discretionary basis. Portfolio construction and ongoing monitoring and maintenance of the portfolios within the program are provided on Morningstar Investment Services behalf by Morningstar Investment Management LLC. Morningstar Managed Portfolios offered by Morningstar Investment Services LLC or Morningstar Investment Management LLC are intended for citizens or legal residents of the United States or its territories and can only be offered by a registered investment adviser or investment adviser representative.

Fixed-income securities are influenced by interest-rate sensitivity and credit risk. They have varying levels of sensitivity to changes in interest rates, but in general, the price of a fixed-income security tends to fall when interest rates rise and vice versa. The value of a fixed-income security with a longer duration or maturity is typically impacted more by a change in interest rates than one with a shorter duration or maturity.

U.S. Government securities are issued by the United States Treasury and backed by the full faith and credit of the U.S. Government. U.S. government agency securities are an indirect obligation of the U.S. government and are issued by federal agencies and government sponsored entities. They have different levels of credit support and therefore different degrees of credit risk.

Portfolios that invest in lower-rated debt securities, commonly referred to as “junk bonds,” involve additional risks because of the lower credit quality of the securities in the portfolio. The investor should be aware of the possible higher level of volatility and increased risk of default.

A debt security refers to money borrowed that must be repaid that has a fixed amount, a maturity date(s), and usually a specific rate of interest. Some debt securities are discounted in the original purchase price. Examples of debt securities are Treasury bills, bonds, and commercial paper. The borrower pays interest for the use of the money and pays the principal amount on a specified date.

The indexes noted are unmanaged and cannot be directly invested in. Individual index performance is provided as a reference only. Since indexes and/or composition levels may change over time, actual return and risk characteristics may be higher or lower than those presented. Although index performance data is gathered from reliable sources, Morningstar Investment Management cannot guarantee its accuracy, completeness, or reliability.

About Morningstar’s Investment Management Group

Your investment goals matter to us. Our mission is to empower investor success by building investment portfolios selected by your financial advisor. Our world-class investment strategies draw on our core capabilities in research, asset allocation, investment selection and portfolio construction. Our investment professionals are located around the world, which provides both a global point of view and local market expertise.

Based on a proprietary valuation-driven asset-allocation process, our strategies offer investors a range of multi-asset, risk- and outcome-based strategies designed to help meet a variety of goals. Also, our separately managed accounts offer concentrated portfolios of our portfolio managers’ best ideas. We
put more than 35 years of investment experience to work in every portfolio we manage to offer you a better investing experience, because your journey matters.

For More Information
Phone: + 1-877-626-3227
Email: ManagedPortfolios.US@morningstar.com
Online: www.mp.morningstar.com

MORNINGSTAR

22 West Washington Street
Chicago, IL 60602 USA

© 2023 Morningstar Investment Management LLC. All rights reserved. The Morningstar name and logo are registered marks of Morningstar, Inc. Morningstar Investment Services LLC is a registered investment adviser and subsidiary of Morningstar Investment Management LLC. Portfolio construction and ongoing monitoring and maintenance of the model portfolios discussed herein are provided on Morningstar Investment Services’ behalf by Morningstar Investment Management LLC.