Q4 2022

Commentary

2022 was a difficult, turbulent, and disappointing year. Global supply chain issues, and high energy, food, and housing costs fueled the fire, prompting the Fed to tighten monetary policy a total of 7 times throughout the year. This tightening was as we expected; however, it was anticipated to be more gradual given the telegraphed communication from the Fed around its 'transitory' nature. As we mentioned at the end of the 3rd quarter, the Fed playing catchup with a heavy-handed monetary policy perpetuated the frustrating investment environment and emphasize the continued regime of heightened market and economic volatility, which would carry forward, through the end of the year. The result was a year rife with volatility, uncertainty, and negative returns across both equity and fixed income asset classes, culminating in the most prolonged bear market since the Global Financial Crisis and the worst year for equities since 2008. Perennial optimists, we did observe silver linings in the dark clouds of 2022; peak inflation, labor market resilience, strong corporate balance sheets and some slight positive momentum for equities in the fourth quarter.

Portfolio Review

While the 4th quarter of 2022 rebounded and started off with a roar, ultimately, the equity market ended the year on a whimper as the markets again retreated in December. During the quarter, the Sapphire Star Mid Cap Strategy performed well producing significant returns for our investors by gaining 10.28% net versus a gain of 6.90% for the Russell Mid Cap Growth Index and a gain of 9.18% for the Russell Mid Cap Index. For the 2022 calendar year the strategy performed relatively well losing (18.29%) Net versus a loss of (26.72%) for the Russell Mid Cap Growth Index and a loss of (17.32%) for the Russell Mid Cap Index. The three sectors that led positive relative performance included technology services, non-energy minerals and process industries while health technology, finance, and transportation comprised the three sectors that hindered relative performance the most during the quarter. From a holding's perspective, Steel Dynamics +38.18%, KLA Corp +25.01% and Bunge Limited +21.59% contributed the most to positive absolute performance. Repligen Corp. (9.51%), TriNet Group (11.81%) and Tenet Healthcare Corp. (15.43%) hindered absolute portfolio performance the most during the quarter. From an attribution perspective, the Sapphire Star Mid Cap strategy outperformance is attributable to both stock selection and sector allocation during the quarter with most of the outperformance attributable to stock selection. During the quarter, the strategy experienced minimal turnover achieving 34.41% turnover for the year. The strategy ended the quarter and year with electronic technology, finance, and producer services as the three highest weighted sectors and consumer non-durables, utilities and health services, were the three sectors with the smallest representation in the strategy.

7826 Leary Way NE
Suite 201
Redmond, WA 98052
Phone: 425.576.4083

Looking Forward

As we look forward to 2023, we see a much more dynamic equity market environment, with large performance dispersions between market capitalization, growth versus value styles and economic sectors. We see the current "un-official recession" bottoming in the quarters ahead and are optimistic that the market will begin to "climb a wall of worry" in advance of the economy bottoming as it has historically. We believe that we are currently working our way out of a two-year rolling cyclical "bear" market that will slowly gain positive momentum in fits & starts as equity valuations become richer due to earnings decelerating and bottoming. Previous Inflation peaks have coincided with market bottoms, and we believe that inflation has peaked. While our preference would be for the Fed to pause immediately, our wish is that the deteriorating economic data catches up and the Fed doesn't go too far down the path with further rate hikes in 2023. At current levels, the markets are pricing in a final rate hike in March during this cycle. The actions of the Fed have large and lasting effects on the economy, which are historically lagged, and we believe these effects have not yet been fully felt. We feel that whether or not the bottom is in, the current environment provides a historically great entry point for long-term investors invested in the "sweet-spot" of the equity market space, the mid cap space. We see opportunity in mid cap stocks as the market begins to rebound, while small cap stocks have historically led markets into and out of cyclical bear markets, mid cap stocks have historically placed second in both boom and bust cycles which is why mid cap stocks are considered the "sweet spot," perennially coming in second results in placing first in the long term. We strongly believe that active management will prevail as it solely has the ability to identify the strongest, most fundamentally superior companies which will be key during the uneven equity market recovery as interest rates are rising.

As always, we welcome any questions or concerns that you have and thank you for confidence in the Sapphire Star Mid Cap Strategy.

Regards,

Michael J. Borgen
Founder & CIO
Sapphire Star Capital LLC

Meghan N. Chicoine
COO & CCO
Sapphire Star Capital LLC

Important Disclosures:

7826 Leary Way NE
Suite 201
Redmond, WA 98052
Phone: 425.576.4083

Sapphire Star Capital LLC is a registered investment adviser and the information contained herein has been prepared by Sapphire Star Capital LLC. Such information is obtained from and based upon sources believed to be reliable, but accuracy cannot be guaranteed. Sapphire Star Capital LLC and its affiliates and representatives disclaim all liability for any inaccuracies and omissions contained in these materials. All opinions and estimates constitute Sapphire Star's judgement as of the date of the creation of these materials and are subject to change without notice. Information presented is not intended to be an offer of solicitation for the sale or purchase of any securities, investments involve risk and are not guaranteed. Any decision to purchase securities mentioned herein must consider existing public information on such security. Projections contained herein are based on a variety of estimates and assumptions and there can be no assurance that the assumptions made in connection with the projections will prove accurate, and actual results may differ materially. Past performance is not indicative of future results.

7826 Leary Way NE
Suite 201
Redmond, WA 98052
Phone: 425.576.4083