CARMEL | CAPITAL PARTNERS

Quarterly Brief

Exclusive updates and insights for discerning investors.

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General Commentary

The financial markets' performance in the first half of 2023 proved why market timing is so hard and a foolish pursuit. At the end of 2022, with a backdrop of rapidly rising interest rates, one could have easily concluded that 2023 would be a challenging investment year. As Spring rolled around, those views looked valid as numerous bank failures occupied the daily headlines. However, as the year progressed, the Federal Reserve Bank continued to raise rates, putting further pressure on the economy. Again, one could have safely concluded that poor returns from the equity markets would be the most likely outcome. How wrong this view turned out to be.

Today, the bank failures and panic from the Spring are a distant memory as the government took the necessary steps to restore calm to the banking system. As a result, the equity markets are all positive for the year— not at all what one would have expected in this type of environment. Once again, this shows that short-term market forecasting and timing are hard, and the better path forward is to adopt a long-term investment mindset and ignore the short-term noise.

While we spend no time forecasting the economy or the stock market, we pay close attention to what's happening worldwide and include this view in our investment process.

The best way to describe our posture is that of a driver on the freeway who suddenly starts to see brake lights illuminate from all the cars ahead. In this position, one might conclude that everyone is slowing down to be cautious or that there is an accident ahead and traffic will soon stop. It's only once we get further down the freeway that the cause of the braking reveals itself. We believe that we are currently in a similar position in that economic brake lights are starting to illuminate; however, we are not sure that it's simply a slowing or crash. But make no mistake, we are seeing brake lights.

What's contributing to the slowing traffic?

- Student loan payments restarting ($1.6T total debt owed by 20MM people paying $200 - $400 per month)
- Consumer debt has risen to all-time highs, while interest costs on this debt increased sharply.
- A sizable amount of corporate debt needs to be refinanced in the next 12 – 18 months, all at higher interest rates.
- Commercial real estate mortgages need refinancing; these, too, will need to be at higher rates.
- COVID stimulus has been spent, and consumer savings is plunging.

The conclusion – it's a highly complex environment for investment decision-making. As if this was not troubling enough, there is a considerable divergence in the equity markets. Anything tech AI-related has experienced material appreciation; companies outside this group have struggled. Stated differently, those parts of the market that reflect the broader economy are struggling, while the technology landscape that reflects the A.I. hype is thriving.

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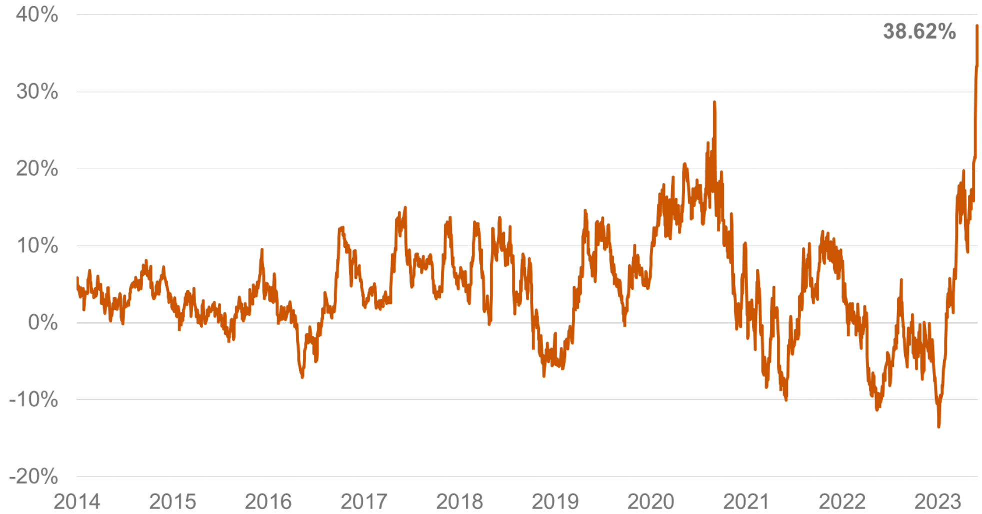
Just how extreme is this? The chart below shows the difference in return of Technology stocks in the SP-500 and non-Technology stocks in the index. At the end of July, the technology cohort outperformed the non-technology cohort by 38.62%. It's unlikely the hype will remain.

SPX InfoTech Minus Ex-InfoTech (5-Month Rolling Returns)



Source: S&P Dow Jones Indices

Thankfully, we are not trying to figure out the next two weeks or two months but rather invest with our long-term mandate to first preserve capital, and then grow capital. We believe there are still clouds over the horizon and continue to position portfolios to reflect this.

Equity Update

We continue to hold a portfolio of what we believe to be high-quality, well-run, durable, with market-leading companies. Irrespective of how the economy performs in the coming months or quarters, we expect the companies we hold to perform well over the long term.

Fixed Income Update

As interest rates have continued to rise, we have increased our allocation to fixed income where appropriate. We continue to see fixed income as an attractive investment destination. Even though rates are higher and returns more attractive, given the "brake lights down the freeway," we focus on credit quality and default risk to guard against permanent capital loss.

Real Estate Update

During Q2 2023, we completed one new investment, loaning capital at an attractive double-digit interest rate to an industrial storage terminal in Maryland. We are earning a solid yield with an equally

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strong loan-to-value. The opportunity for us to lend capital at such an attractive interest rate indicates a challenging lending environment where capital is scarce and those with cash can command high rates of return.

Private Equity Update

New opportunities are limited as the gap between buyers and sellers is still quite wide. Many sellers are still expecting valuations consistent with a lower interest rate environment.

Buyers are making offers to reflect materially higher borrowing costs. If interest rates remain elevated, we expect sellers to capitulate slowly over time, and a more fruitful investment opportunity set will develop.

Summary & Firm Updates

As Carmel Capital has grown, we remain committed to transparency, open communication, and access. A single mandate guides us – focus on what's best for the client and always serve the client's interests; with this in mind, we've recently welcomed to our team Stephanie Cunningham to serve the role of Client Services Manager. Stephanie brings a long-tenured and rich experience in the financial service industry.

At Carmel Capital Partners, we are grounded in the belief that financial markets function inefficiently from time to time, resulting in mispriced investment opportunities. We attempt to take advantage of these opportunities through discipline and patience, buying undervalued investments that we believe will offer superior returns and limited risk over the long term.

We hope you found this brief valuable, and we encourage you to share it with your fellow investors. For further discussion or personalized advisory, please reach out to info@carmelcap.com, 858-457-7544, or visit our Contact Page.

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About the Founder

Russell Silberstein

Prior to forming Carmel Capital Partners in 2002, Russell was a managing partner at Bedell Investment Counseling, LLC, a San Francisco Bay Area firm with $120 million in assets under management. He held the position of Director of Research & Portfolio Manager from 1996 to May 2001 at Bedell Investment Counseling, LLC. He was also the managing partner of the Harmony Fund, LP, a long/short investment fund. Russell graduated from San Diego State University.

About Carmel Capital Partners

Carmel Capital Partners was founded in 2002 by Russell Silberstein with the goal of delivering stable long-term returns to individuals, families, and entrepreneurs through opportunistic, value-oriented investments. The firm serves individuals, families, and entrepreneurs across California and manages approximately $400m in assets as of March 2023.

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