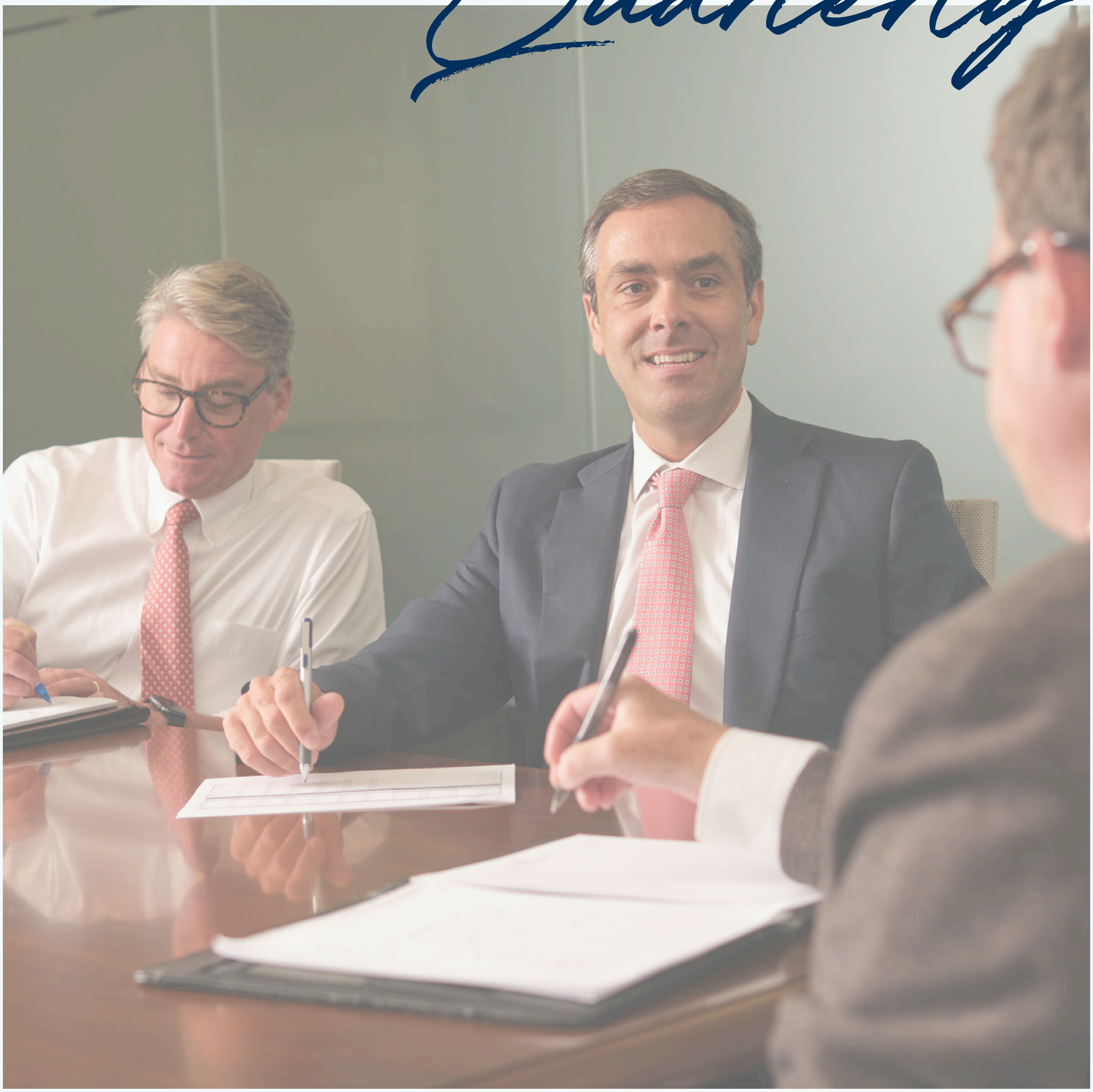
EST 1913
COLONIAL TRUST
COMPANY

1ST QUARTER
2023

COLONIAL TRUST *Quarterly*



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4TH QUARTER MARKET RETURNS

THE EQUITY MARKET HAD ITS BEST THREE MONTHS OF THE YEAR, BUT THE POSITIVE QUARTER RETURNS WERE OUTWEIGHED BY THE WORST YEAR FOR STOCKS SINCE 2008.

The S&P 500 posted a total return of 7.6% for the quarter, with October and November particularly strong. The markets continue to view strong economic data as market negative as it increases the pressure on the Federal Reserve to increase interest rates.

We saw this inverse relationship between economic data and market returns throughout the quarter. We began the quarter with falling job openings and weak manufacturing data and the S&P 500 rallying 5.7% in two days. These gains were reversed when we learned 263,000 jobs were created in September and the S&P made new lows on October 12th. This market action captures the current market sentiment. The S&P 500 reached the high for the quarter on November 30th, up 13.8% in two months. December was a down month, with the index falling 5.9%, as the awaited Santa Claus rally did not materialize.

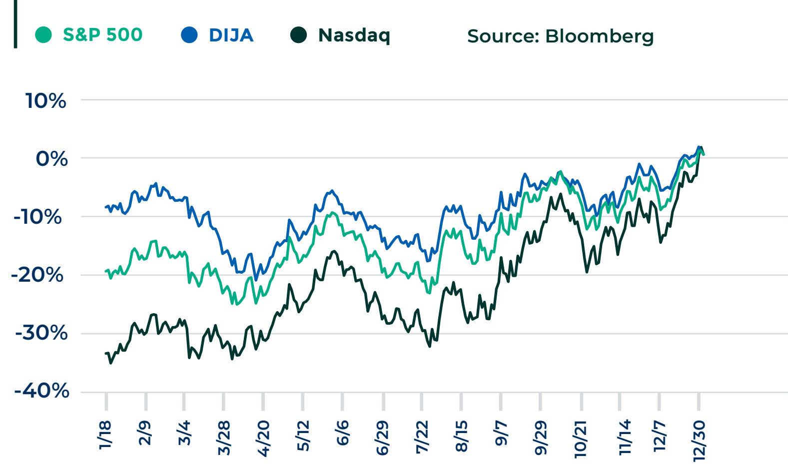
Total Return	4Q	2022
S&P 500	7.55%	-18.13%
DJIA	16.01%	-6.86%
Nasdaq Composite	-0.78%	-32.51%
Russell 2000	6.62%	
MSCI EAFE	17.4%	-13.92%
MSCI Emerging Markets	9.62%	-19.94%
US Agg Bond Index	1.87%	-13.01%

Source: Bloomberg, LP

The S&P 500 underperformed the Dow for the quarter by a large margin. International indices also outpaced the S&P 500, with the MSCI Developed Market index returning 17.4% and the Emerging Market index up 9.6%. Bonds posted a positive quarter as 10yr treasury yields ended the year at 3.875%, compared to 3.829% to start the quarter.

The divergence between the Dow and the Nasdaq is noteworthy. The Dow outperformed the Nasdaq in every quarter of 2022, but the divergence grew significantly during the last quarter. The top holdings of the tech-heavy Nasdaq are Microsoft, Apple, Amazon, Google, and Nvidia. The top holdings of the Dow are United Health, Goldman Sachs, Home Depot, McDonald's, and Amgen. The Dow's superior performance points to a change in leadership in the equity market. Mega-cap tech stocks led the market from the pandemic lows through 2021 as interest rates were low and liquidity high. As this environment reversed in 2022, "old economy" stocks with lower valuations have outpaced higher valued tech stocks. The S&P 500 constituents are more diversified across eleven sectors and its performance falls between the Dow and Nasdaq Composite.

U.S. INDICES

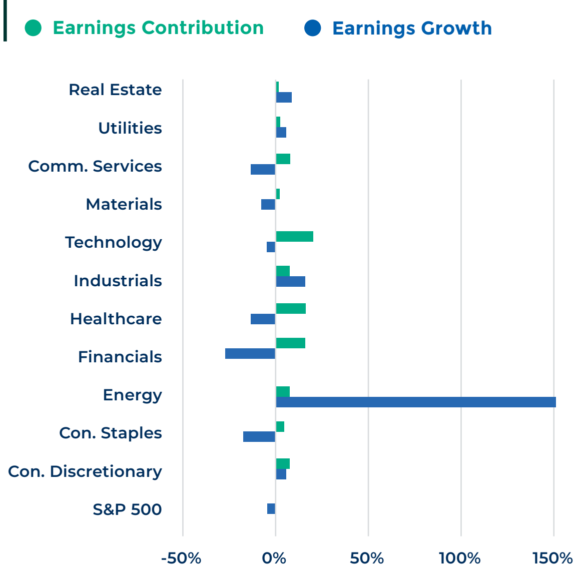


ECONOMIC CLIMATE

THE THIRD QUARTER EARNINGS SEASON WAS DISAPPOINTING, WITH ONLY 68.4% OF COMPANIES BEATING WALL STREET'S EARNINGS ESTIMATES.

This is the lowest number since the first quarter of 2020, during the Covid lockdowns. S&P 500 operating earnings as compiled by Standard & Poor's fell 3.2% for the quarter. The underlying performance was worse than it appears. Energy stocks reported 155% earnings growth and S&P 500 operating earnings growth ex-energy was -10.4%. Earnings for the tech sector were down 8.2%, while communication services were down 19.9%. This earnings weakness is due to falling profit margins in the face of higher inflation. The S&P 500 operating margin for the third quarter was 11.3%, down from 13.2% during the same quarter of 2021. Sales growth outpaced inflation for the quarter, with revenues 13.0% higher year-on-year. However, falling profitability has caused earnings to decline.

3RD QUARTER EARNINGS

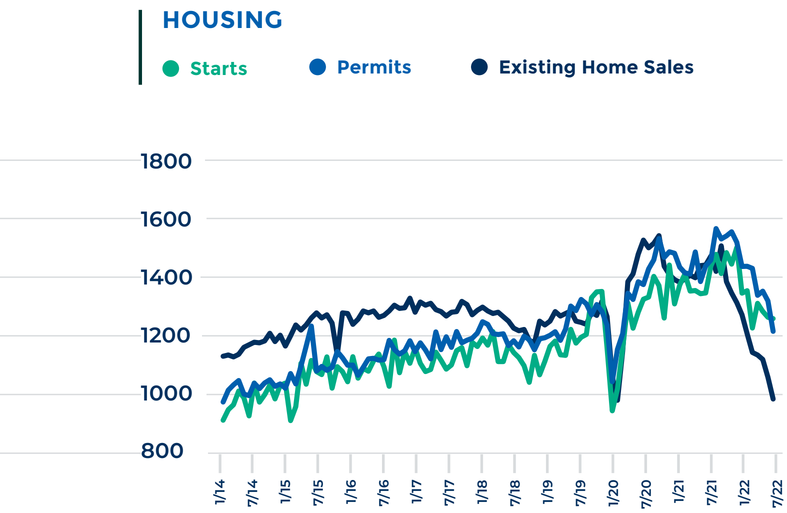


The economic data for the fourth quarter was mixed. Backward looking data, particularly third quarter GDP growth was strong. After two negative quarters in the first half of 2022, GDP for the third quarter increased 3.2%, with strength in consumer spending on services. Consumer spending was strong for October and November, up over 7.6% and 7.9% respectively. The consumer is employed and is seeing wage gains. For the first two months of the quarter, job growth averaged 274,000 and December is expected to show 200,000 new jobs. Average hourly earnings increased at a 5.0% average rate for the quarter. Job growth and wage gains are not sufficient to keep pace with 7.1% CPI inflation. This strong spending has been financed with lower savings and higher revolving credit. The savings rate has declined to 2.4% of income, down from 7.5% to begin the year, and is at its lowest level since 2005. Revolving credit has increased by $129.5 billion this year as consumers rely on credit cards to maintain spending.

The manufacturing economy weakened during the quarter. ISM Purchasing Managers Index (PMI) for manufacturing activity fell to 49 in November. A read below 50 signifies contraction and this reading began the quarter at 50.9 and the year at 58.8. ISM's Services PMI remains strong at 56.5, essentially flat for the quarter and down from 62.3 at the beginning of the year. The year-on-year growth in Industrial Production and Durable Goods Orders decelerated during the quarter, with industrial production up 2.5% and durable goods orders ex-aircraft up 3.4%. These readings began the year at 3.7% and 10.1%, respectively.

THE WEAKEST ECONOMIC SECTOR DURING 4Q WAS HOUSING AS HIGHER MORTGAGE RATES CURTAILED ACTIVITY.

Existing home sales fell 13.2% for the quarter and 32.8% from December 2021. Fed rate hikes and quantitative tightening caused mortgage rates to double in 2022, reducing affordability. This has lessened activity for existing home sales and new construction. This is impacting home prices, with the Case-Shiller Home Price Index falling for four consecutive months from July through



October. The index is down 2.4% from all-time highs in June.

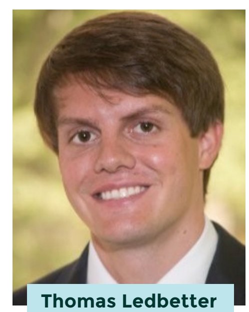
There is weakness in the manufacturing economy and housing. The consumer continues to spend, largely on travel and services, but this spending is being financed with credit and a reduction in savings. This economic slowdown is being orchestrated by the Federal Reserve to reduce demand and bring inflation back towards its 2.0% target. During the quarter, the Fed raised the Fed Funds Rate (FFR) by 0.75% on November 2nd and by 0.5% on December 14th. This brought the upper bound of the FFR to 4.5%, up from 0.25% in March. The Fed has continued to reduce the size of its balance sheet through quantitative tightening. For the quarter, the Fed's balance sheet contracted by $245bn and by $414bn since quantitative tightening began in April.

It does appear this policy is having its desired effect. Core CPI, which excludes volatile food and energy prices, reached a 40 year high of 6.6% in September. This reading was 6.0% in November. Other inflation readings tell a similar story, with the Producer Price Index and Consumer Expenditure Core Price Index all falling in the last several months. It does appear inflation peaked in the beginning of the fourth quarter, but it remains

2022 FORECAST SCORECARD

One year ago, we expected economic activity to moderate, and equity returns to be more muted. We thought supply chain issues would improve and inflation would be elevated but would moderate during the year. Our expectation on monetary policy was for the Fed to become hawkish and begin to raise interest rates and reduce the size of its balance sheet. Directionally, we were in the neighborhood, but we did not expect a war in Ukraine nor CPI to rise to 9.1%. The persistence of inflation was the wildcard in 2022 and the Fed was forced to raise rates much higher than we expected a year ago. The Fed's policy derailed our expectations for earnings growth and modest equity returns. Additionally, Fed policy caused the worst one-year performance for the Bloomberg Agg Bond index since its inception in 1976, by a

IN THE SPOTLIGHT


Thomas Ledbetter

THOMAS LEDBETTER, Investment Analyst and Associate Portfolio Manager joined the Colonial Trust Greenville office in November 2022. He served as an Investment Analyst in Wells Fargo's Private Bank for five years in Charlotte, NC, and Greenville after moving in April 2022. Thomas will contribute to the firm's investment strategy and manage clients' portfolios with diligence and care. Thomas is pursuing the Certified Financial Analyst (CFA) Designation and recently passed the CFA Level II exam. He is a graduate of Clemson University with a Bachelor's in Economics. Thomas met his wife Ellison in Charlotte, who returned with him to his hometown of Greenville, where he attended Christ Church Episcopal School. His interests include running with his German Shorthaired Pointer, reading,

THE YEAR AHEAD

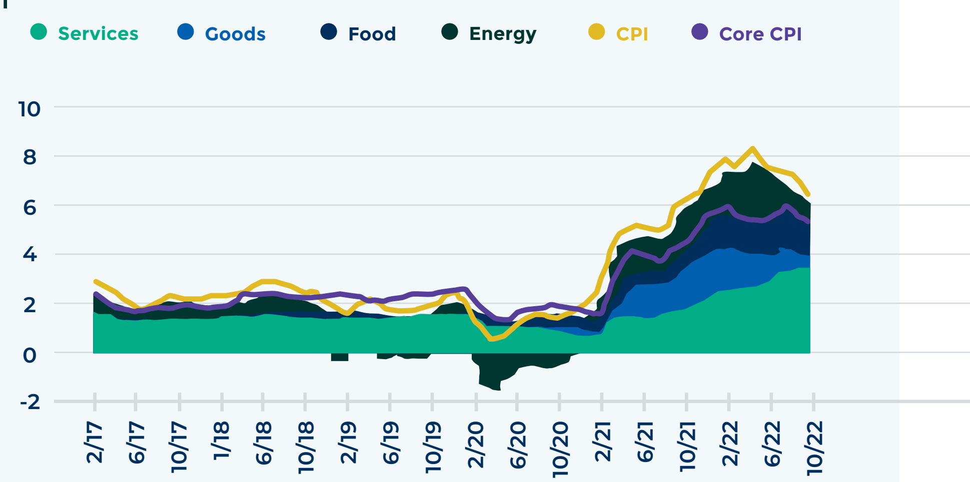
The consensus view among economists and market prognosticators is for a significant slowdown in 2023 and possibly a recession. The path of the economy, earnings, and asset prices will be determined by monetary policy and its effects on the economy. A Bloomberg, LP monthly survey of economists forecasts 2023 GDP growth of 0.3%, and this estimate has fallen for ten consecutive months, from 2.3% to the current 0.3%. This survey asks economists for their estimate of the probability of recession in the next twelve months and this measure has increased from 15% in March to 65% today.

Consumer spending represents 68% of US economic activity and it is expected to slow from 2.3% growth in 2022 to 0.9% in 2023. Private investment is projected to fall 2.5%, largely due to continued weakness in the housing market. Economists expect unemployment to rise to 4.8% in 2023, up from 3.7% today, and for wage pressures to moderate. The silver lining to this forecast is that there are fewer imbalances in the financial system that could cause a recession to morph into a financial crisis, as banks are much healthier than they were going into 2008.

The interplay between a slowdown or recession and Fed policy will likely determine the depth and length of any recession. As the economy slows, inflation pressures taper and Fed policy should become less restrictive. The Fed is forecasting a FFR of 5.1% in 2023, up from 4.33% today. The markets are projecting a high-water mark of 4.96%, with rate cuts of 0.5% coming the back half of 2023. If inflation moderates in 2023, the Fed will likely pivot, and the slowdown or recession could be shallow and short-lived. Persistent inflation will lead the Fed to tightening above what is currently expected, creating additional economic and market pain in 2023. For that reason, the path of inflation is perhaps the most important variable driving economic and market performance in 2023.

Headline CPI reached 9.1% in June and has fallen to 7.1% for November. Many of the factors driving inflation higher in the summer have improved. Most notably, oil prices have fallen from $123.7/bl to $80.57/bl at year-end. Inflation in consumer goods retreated during the second half of 2022. Improving supply chains and shifting consumer spending to services left many retailers and manufacturers with excess inventory that was marked down in the Christmas season. Inflation for services has not peaked and is driven by housing/rental costs and wages. CPI captures changes in rental rates with a lag and monthly data from Zillow shows month-over-month declines in rental rates in October and November.

CONSUMER PRICE INDEX



This leaves wage growth as a key inflation driver in 2023. Demand for labor remains robust as evidenced by the US economy having 1.7 job openings for every unemployed person. Layoff announcements increased in 2022, particularly in technology, but there has not been a discernible increase in unemployment claims. This indicates those laid off from Amazon, Meta, Cisco, Goldman, and many others have quickly been able to find new employment. The Fed would like to slow the economy to reduce job openings and therefore reduce wage pressures. It appears the job market is weakening, but with 10.3 million job openings, its pace is not sufficient to reduce inflation. Monetary policy is a blunt tool to address structural mismatches between the supply and demand for labor, but it is the only tool they possess.

We estimate economic growth will slow in 2023 and likely enter recession in the middle of the year. Unemployment will likely increase marginally, and consumer spending should be flat versus 2022. Private investment will probably be hampered by a weak housing market; however, spending in infrastructure and onshoring will keep business investment elevated. Government spending will remain high, as the President just signed a $1.7bn budget bill that was 4,100 pages long and read by no one. We believe inflation will moderate in 2023, moving down to 3.5%-5.0% range by year-end. This slowdown or recession should be short lived as the structural imbalances in the labor market should prevent the unemployment rate from rising too high. Additionally, businesses and the financial system are healthy, which should prevent a recession from becoming a credit event. The biggest risk to the upside or downside for our expectations is if inflation falls significantly faster or slower than expected – which in turn will change how the Fed reacts.

The fortunes of capital markets will also depend on the path of Fed policy in 2023. We enter the year with more attractive valuations than when we finished 2021. The forward P/E of the S&P 500 is 17.0x, down from 21.2x at this point last year. Operating earnings for 2022 are projected to come in at $200.19 per share for the S&P 500. This compares to $208.21 for 2021 and is a 3.9% decline in earnings for 2022. Expectations for S&P 500 earnings growth in 2023 call for 13.1% growth, putting estimates for 2023 at $226.51/share. Analyst estimates for 2023 have fallen 9.0% since June 2022. We expect estimates to fall further as the economy slows and margin pressures remain.

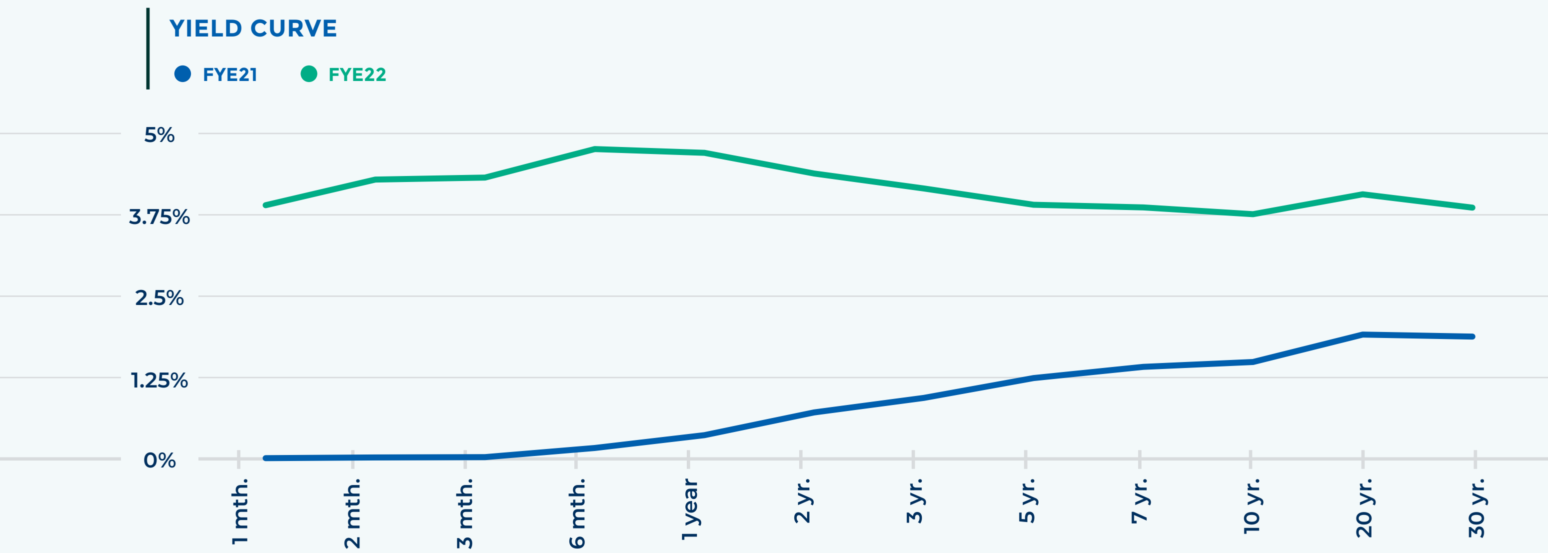
Characteristics	3/24/2000	10/9/2007	2/19/2020	12/31/2021	12/31/2022
Index Level	1,527	1,565	3,386	4,766	3,840
P/E Ration (Fwd.)	25.2x	15.1x	19.2x	21.2x	17.0x
Div. Yield	1.4%	1.9%	1.9%	1.4%	1.8%
10yr Treasury	6.2%	4.7%	1.6%	1.5%	3.9%

Source: Standard & Poor's

In a typical recession, earnings fall between 15% and 20%. Trailing twelve-month operating earnings for the S&P 500 reached a peak of $210.16/share in March 2022 and are forecast to contract by 4.7% through December 2022. We imagine analysts will reduce their estimates for earnings for the first two quarters of 2023 after fourth quarter earnings are released. Full year 2023 earnings are likely to be about equal to 2022 earnings of $200/share or slightly lower. This could result in choppy markets in the first half of 2023.

Markets are forward-looking and typically price in a return to growth before there is evidence the worst is behind us. We expect this to begin in the second half of 2023 as the economic slowdown lessens inflationary pressures and the Fed moves to a neutral stance. We don't expect a banner year for equity markets in 2023 but expect the back half to be better than the first half.

We also believe there are select areas of the market offering attractive opportunities. We expect quality companies in less cyclical parts of the market to perform better than the market in 2023. There are certain sectors, like REITs, that have historically offered an inflation hedge that have underperformed the market in 2022, offering discount valuation and attractive dividends. We expect capital spending to begin a multi-year increase in 2023, encouraged by the Chips Act, the Infrastructure Plan, and certain aspects of the Inflation Reduction Act. This will benefit companies leveraged to large capital projects. Lastly, there are many great companies who have seen the valuation reset to a degree that may be unwarranted. Great companies, with great business models, strong balance sheet, and great management have seen 40% reductions in their share prices. This too makes for attractive opportunities.



The bond market should offer attractive return opportunities for investors, for the first time in many years. The yield curve is inverted, with short-term rates higher than long-term rates. The most attractive part of the yield curve is 1yr to 3yr bonds. Treasury yields north of 4% are available for investors with low duration risk. Investment grade corporate and municipal bonds offer higher returns, about 5%-6% on a tax-equivalent basis. We expect short-to-intermediate term bonds to provide returns consistent with their coupons, as we don't expect significant change in 1yr-3yr interest rates. Longer term rates have drifted lower indicating the market believes either the Fed will tame inflation with its monetary policy, or a recession will tame inflation. Both outcomes relieve inflation and would send long-term yields lower. We expect the Fed to raise the FFR to 5.0%-5.5% in 2023 and keep rates elevated until inflation as receded. As evidence of this becomes apparent, intermediate, and longer-term bonds will offer additional value.

As we enter a new year, we expect it will be a bumpy one for the economy and the markets, especially in the first half. We have dusted off our Whip Inflation Now buttons and are hopeful the Fed's policy actions begin to bear fruit. We recognize this is a challenging time for investors, but we know that out of chaos comes opportunity. And we are looking for those opportunities in the wreckage of 2022. We believe 2023 will be a better year for markets than 2022, but we know we must get to the other side of these inflationary pressures. We pray that 2023 is a good year for our clients and friends – that it brings health, friendships, and appreciation of our own blessings and attention to the needs of others. We thank you for your trust in our firm and look forward to better times ahead.

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