

## Market Commentary—Third Quarter of 2022

The major equity market indices ended the third quarter on the lows for the year. These major indices have all fallen at least twenty percent from their highs, which is technically called a bear market. Currently, less than 10% of stocks are trading above their 50-day moving average. That is down from over 90% from a month earlier. Stock market volatility is extremely high due to recession worries. Third quarter earnings season is beginning, and earnings are estimated to grow by 5%. However, the trend for estimates have fallen by over 10% since the June peak reflecting expected future earnings weakness. Recent weakness clearly reflects still-hot inflation and a "don't fight the Fed" mentality.

The table below provides year to date and third quarter returns as of 9/30/2022 (percentages are for total returns):

Time Period	Dow Jones Industrial Average	S&P 500 Index	Nasdaq Composite	Barclays U.S. Aggregate Bond
Year To Date	-19.7%	-23.9%	-32.0%	-14.6%
Third Quarter	-6.2%	-4.9%	-3.9%	-4.8%

### Recession Versus Soft Landing

Historically, the Federal Reserve has raised interest rates 13 times to bring down inflation. In those 13 times, there have been 10 recessions and 3 soft landings. A soft landing is the better outcome, meaning that a recession was avoided, however, most signs are pointing towards a recession by the end of 2023. What can you expect during a recession, first and foremost a slowdown in economic growth, and weakening employment. The most recent employment reports illustrated that job openings have decreased; layoff announcements are up. There is also a lower demand for discretionary goods and services. Home sales are down because of higher interest rates, as mortgage rates have more than doubled since the beginning of the year.

Rising inflation and interest rates do not bode well for the stock market. By raising interest rates, the Federal Reserve will eventually curb inflation. However, this leads to pressure on businesses. Businesses that have a large amount of debt will find it difficult to meet interest payments. Rising inflation leads to increased costs with payroll and purchased goods for production. Corporate earnings will be challenged, and earnings outlooks reduced. The financial markets are taking this into account, which has led to market declines this year and may lead to continued lower stock market performance until the Fed's tightening cycle ends.

### Appropriate Actions to Take

We have taken a more value-oriented approach given this market environment and will continue to do so until inflation subsides, and interest rates normalize. Over the last quarter and into the final quarter of the year, we are trimming weightings in high tech growth companies, and reinvesting the proceeds by adding to the healthcare, defense, and consumer staples sectors. Our focus for equity allocation is on quality; companies with strong balance sheets, low debt, immediate cash flows and companies who pay dividends.

Volatility in the markets create opportunities for those with a longer time horizon. U.S. Treasuries are yielding over a 4% rate for multiple time horizons. This is a much better alternative than having funds sit in a savings account at your local bank. Such attractive yields have not been seen in years and we are taking advantage of this opportunity by buying highly rated individual corporate, municipal and treasury bonds with 4 - 5% yields to maturity.

Please review this report and contact us if you wish to schedule a time to discuss your investment portfolio, the current markets and economy or any other related financial matter in person or over a video/phone call.