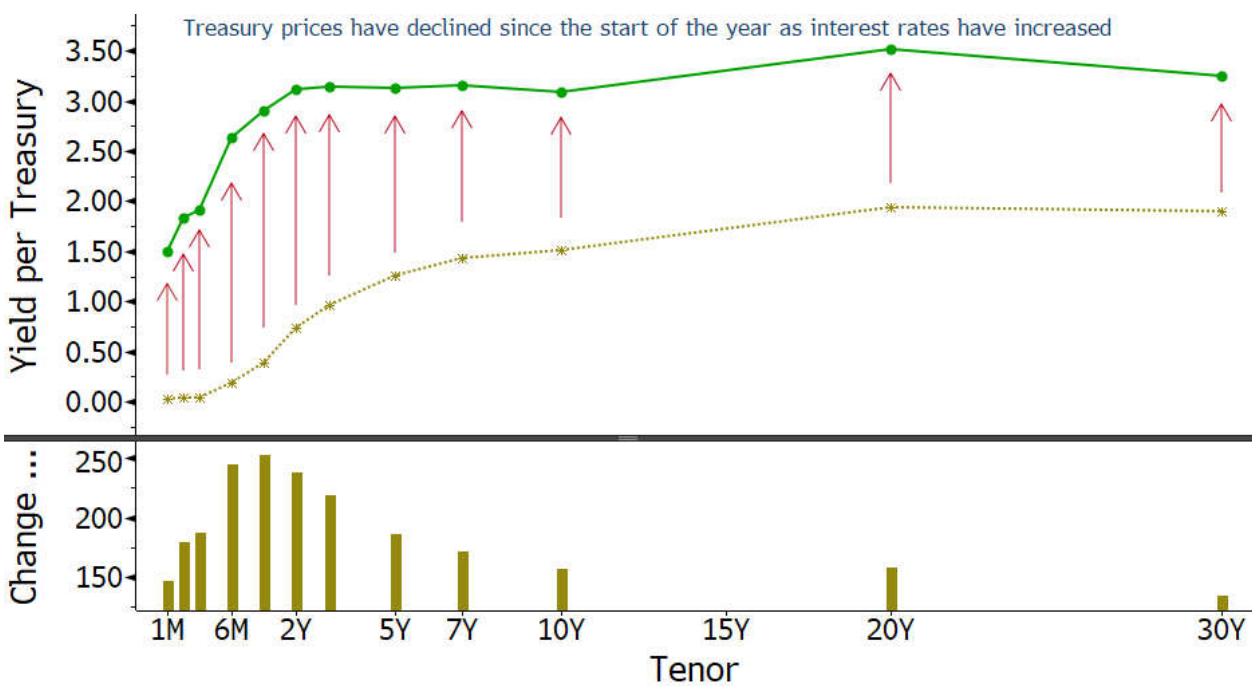
June 30, 2022

Market Commentary - 2022 Q2

What a rough first half of 2022. Since the start of the year the S&P 500 has declined -20.7%.

Normally, when equities decline, investors run to treasuries for safety but this year treasuries have also declined as interest rates have increased between 95bps to 240bps across the yield curve. With the S&P 500 declining and bond prices falling there was really nowhere to hide in the market.



Fortunately, there is not much more bad news that can hit the market that we are aware of at the moment. The market has been struggling to price in a worst case scenario as it pertains to both inflation and the potential actions available to the Fed to adjust short term rates and the money supply. Since World War II the stock market has increased over 20% in a calendar year twenty different times. The average decline after an increase of more than 20% in the following year has averaged around -11%, usually starting in the first quarter. The good news is that when the decline happens in the first half of the year the market gets back to breakeven by the end of the year every time. Summer is typically marginal for stocks so we do not expect any real improvement until the 4th quarter.

Based on the available information today the market has done a pretty good job of pricing in worst case scenarios. There are three possible ways we could see the market move higher;

- An end to the Ukraine – Russian conflict (low probability)
- A reopening of China in earnest. Portions of China has been totally locked down are opening up
- Inflation burning itself out

Even if we can pull out historical positive patterns, the FOMC could still throw the economy into a recession as it raises short term rates somewhat aggressively. Some of our clients may recall the 1970's when Federal Reserve Chairman Paul Volcker unleashed significant interest rate hikes to quell runaway inflation. We have seen significant inflation lately relative to recent history but nothing like the double digit numbers that were crashing the economy. Volcker then increased the fed funds rate to 20% at a time when inflation was 14%. Investors are trying to gauge and determine the impact of inflation that we last saw 50 years ago.

Market returns in a midterm election year are typically down. As we discussed before, when the market is up over 20%, the following year the market declines initially. In addition, since World War II, the second year of a presidency saw below average stock market returns of around 5% compared with an average gain of 9.2% in all years since.

In addition to the above information, consumer confidence is conveying the consumer is concerned in a similar manner to the 2008-2009 economy. Overall, the question of growth revolves around the consumer backing away from spending.

It goes without saying that this has been a tough year as a portfolio manager. Nonetheless, our objective stays the same. We continue to look for opportunities to buy fixed income securities at higher values and add to equities at attractive valuations. With this plan, we hope to counter the inflation and volatility in the market to provide the security that we strive to provide for with you at American National Bank & Trust.