May 4, 2022

Graves Light Lenhart April '22 Market Commentary

A Cruel Month All Around

Market Overview:

Markets continually weakened in April as shifting consumer habits and the prospect of sharp US interest rate rises forced investors out of one of the most lucrative trades observed in recent years. What helped buoy the economy in the depths of the pandemic was a concerted boost from both fiscal and monetary policy decision makers. Now, the reverse appears to be taking effect as fiscal stimulus is lacking and monetary policy is tightening vis-à-vis higher interest rates and balance sheet runoff. The resultant effects on markets were manifold as "higher for longer" inflation expectations continued to permeate through the global financial system.

Poor investor sentiment was compounded by disruptions related to the war in Ukraine and strict COVID lockdowns in China, coupled with increasingly aggressive rhetoric about interest rates and inflation from the Federal Reserve. Indeed, markets are now prepared for the Fed to raise its key benchmark rate by half a percentage point at multiple successive FOMC meetings with further rate hikes to come. Expectations have rapidly adjusted to start the year, with the market now pricing in the Fed's short-term federal funds rates to reach 3% in early 2023, compared to the current 0.25%-0.5% range. Unsurprisingly, most market assets have not enjoyed the capricious nature of the Fed's approach as illustrated by the sell-off in stocks as well as interest-rate sensitive fixed income securities. Importantly, domestic employment statistics continues to reveal that the number of job openings has exceeded the number of job seekers for eleven straight months, contributing to faster compensation growth. As this dynamic could potentially feed into a wage-price spiral, it endorses expectations for a fast Fed tightening cycle in 2022.

Asset Performance:

US stocks posted a disappointing performance for the month of April, after a series of earnings misses and pervasive concerns about the direction of interest rates and economic growth dragged all major indices lower. The S&P 500 was down nearly 9% in April, it's worst month since March 2020, when the pandemic wreaked havoc upon stocks. The Nasdaq's drubbing was even worse, declining more than 13%, which was the worst monthly performance since October 2008 during the Global Financial Crisis. Amongst the worst performing components in the equity markets were high-growth technology stocks that previously sparkled in a "stay-at-home" friendly environment created by the coronavirus crisis. The

MSCI World Growth Index – which tracks stocks with high earnings and sales growth and includes Tesla, Amazon and Nvidia – through month-end had declined 22% below its peak in November. That decline left it in a technical bear market, defined as a 20% or more fall from a recent high. Excluding the March 2020 drawdown, this marks the biggest peak-to-trough fall since the Financial Crisis. While underlying weakness has been evident in many stocks for quite some time, it's only recently in which these few largest-capitalization names have been at the forefront of market turmoil.

Returns for fixed income securities were broadly negative, particularly for long-dated high quality "haven" assets. The Bloomberg US Aggregate Index, which represents a large consortium of bonds from government to corporate securities, declined 3.8% for the month of April. This marks the 3rd worst monthly performance since the index's inception in 1976 (out of 556 observed periods). We emphasize the high duration profile (interest-rate sensitivity) of this index, which has underscored our recommended portfolio positioning to maintain a short duration bias for fixed income securities. Notably, for the first time since March 2020, the yield on 10-year Treasury Inflation-Protected securities, or TIPS, flashed in positive territory. In this context, a combination of both higher interest rates as well as wider spreads – which represents compensation for default risk in corporate and municipal bonds – is increasing our interest in certain segments of the fixed income market, including high yield bonds.

Key US Index Returns	YTD '22	April '22
S&P 500	-12.9%	-8.7%
Nasdaq	-21.0%	-13.2%
Dow Jones Industrial Average	-8.7%	-4.8%

Relevant Fixed Income Yields	YE 2021	April '22
US 10-Year Treasury Note	1.51%	2.89%
Investment Grade Corp. (C0A0)	2.4%	4.3%
High Yield Corp. (H0A0)	4.3%	7.0%

Source: Factset as of 05/02/22

Closing Thoughts:

In economic terms, the market appears to accept that the pandemic is over. The corollary is that what previously benefitted from overwhelming stimulus and quantitative easing is no longer receiving these attendant tailwinds. While the impact has been most discernable on securities which previously benefitted from artificially low interest rates (or poor pandemic sentiment), the recent and pronounced adjustment is undoubtedly causing short-term collateral damage along the way. While the ongoing market volatility is unsettling, we remind our clients that historically this is not unusual. At its core, this is why we strive to stress-test our clients' goals against unfavorable market environments which inevitably occur. Lastly, we reiterate our recommended positioning for long-term portfolio construction from our recent quarterly update (GLLW 2Q22 Market Commetary).

Warm regards,

Ash Heatwole, CFA
Portfolio Manager, Associate Director of Wealth Management

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