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INVESTMENT MANAGERS

ECONOMIC UPDATE NOVEMBER 2022

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Stocks finally found their footing in October, turning in the best monthly performance since the 1970's after very poor year-to-date performance. Large cap stocks in the S&P 500 index gained 8.1% for the month bringing their year-to-date loss to -17.7%. Small cap stocks in the Russell 2000 were up 11.0%% leaving them with a year-to-date loss of -16.9%. International stocks in the MSCI EAFE index were up 5.4% and emerging market stocks bucked the trend and were down -3.1%. Their year-to-date returns are -23.2% and -29.4% respectively. Yields rose in October, resulting in a -1.3% monthly loss and -15.7% year-to-date loss for the Barclays US Aggregate Bond Index.

After two quarters of negative economic growth, GDP rose in the third quarter by 2.6%. While it was nice to see a positive number this quarter, we don't expect growth to trend higher over the next several quarters. Many leading economic indicators point to slow or negative growth at least through the first half of next year with a recession likely. The major factor supporting the economy right now is very low unemployment. That is expected to remain low throughout the economic slowdown because of demographic trends. Hopefully that will be enough to prevent a deep recession.

Inflation continues to be the major factor affecting returns. There are signs that inflation is beginning to come down from 40-year highs, but it will take time to see significant improvement. Inflation is a comparison of current prices versus a year ago which means prices can stay at their current high levels even if the inflation rate declines. Since wages are rising at a slower rate than price levels, purchasing power has been impaired for a large portion of the population. In addition, recent legislation and executive orders appear to have exacerbated the problem causing the Fed to pursue more aggressive rate hikes.

The Fed's primary tool for combatting inflation is raising interest rates. Higher interest rates slow the economy which is adding to recession concerns. The Fed has acted very aggressively this year, hoping to get inflation under control. The year began with the Fed Funds rate at 0%-0.25%. Many Fed watchers complained that holding rates so low would contribute to high inflation. Beginning in March the Fed hiked rates by 0.25% and since then we have seen rates hiked aggressively 5 more times including today and we currently have a Fed Funds rate of 3.75% to 4.0%. Recent comments by Fed Chairman Jerome Powel left markets with the expectation that further rate increases should be expected. First Trust economist Brian Wesbury believes the significant growth in money supply from the pandemic stimulus is adding to the problem and it will take time to work off the excess supply of dollars before rate hikes are effective at lowering inflation.

The market appears to agree with Brian Wesbury as yields on Bonds resumed an upward course, appearing to price in the expectation that inflation will be more persistent than previously expected. We are beginning to see yields on longer term bonds rise to levels we haven't seen in several years making them more attractive as a secure income source.

The October rally was very encouraging, but we still see several months of sub-par growth at best. We continue to encourage investors not to try and time the market by trading in and out. Instead, we advocate for investing according to risk tolerance.