2Q22 Market Commentary

Bad news bears

After a tumultuous start to 2022, the second quarter's economic news seemed to get worse by the day—high inflation remained high, consumer confidence continued to decline, job openings shrank. And, after what was already a bad first quarter in both the stock and bond markets, losses only deepened. The S&P 500 Index reached bear territory (down 20% from a high) in June and the Bloomberg Aggregate Bond Index continued its brutal decline, closing the quarter down another 5%—the worst start to any calendar year in history. While it's often hard to pinpoint why the stock market moves up or down on a given day, this time the reason is crystal clear: inflation.

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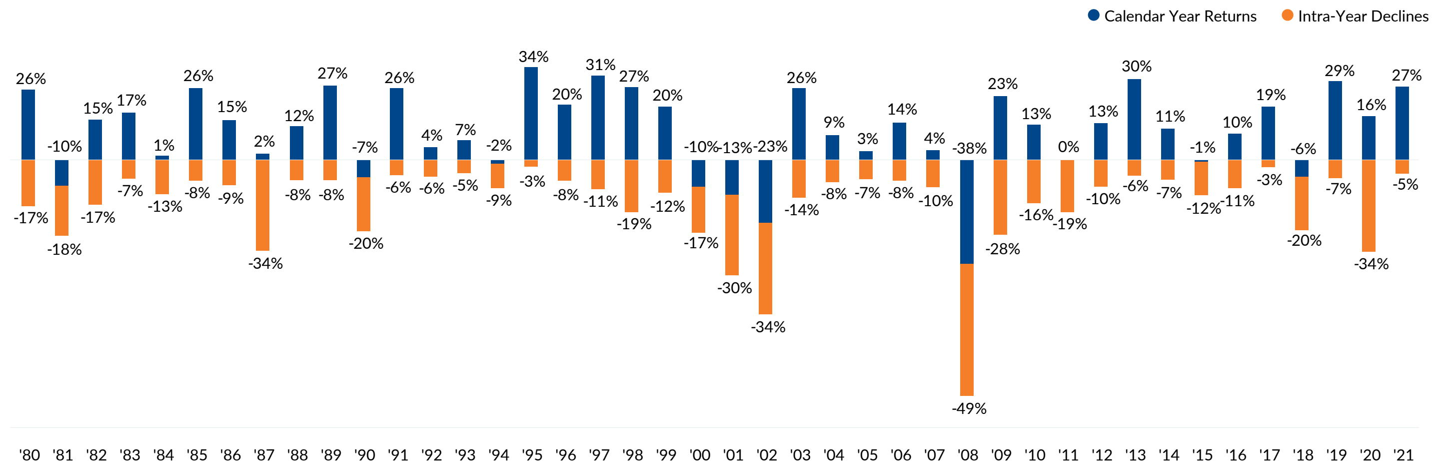
Whip inflation now

Inflation numbers remained elevated during the quarter, hitting yet another multi-decade high. The higher-than-expected reading for May's year-over-year rate of inflation (8.6%) caused the Federal Reserve to swiftly raise interest rates by .75%. At its previous meeting, the Fed raised rates by .50%, which, at the time, was the largest increase since the 1990s. The Fed has maintained an aggressive stance, stating it will do whatever it takes to tamp down inflation, essentially throwing its "soft landing" scenario out the window. While the Fed still maintains it can achieve this goldilocks scenario of bringing down inflation without causing a recession, the market is finding it increasingly unlikely.

Fears of a recession are deepening and certain data points do look ominous. Consumer spending accounts for 70% of US GDP, which means a slowdown in spending can wreak havoc on growth. Consumer spending has started to show signs of weakness with certain sectors seeing declines in recent weeks. Consumers are also shifting from discretionary items to staples as necessities such as food and gas become more expensive. This will almost certainly slow GDP growth for the rest of this year. Whether growth turns negative, is anyone's guess because consumers are still in a relatively healthy place. Most Americans have more savings than they had a decade ago and many people have received big raises over the last few years. Higher interest rates mean investors can earn a more substantial return on their cash savings for the first time since the global financial crisis in 2008. This will allow US consumers to absorb higher prices, at least for a short time. If the Fed can tame inflation in relatively short order, the soft landing is a still possibility, as is a relatively mild recession.

INTRA-YEAR DECLINES VS. CALENDAR YEAR RETURNS



Source: First Trust. Past performance is not indicative of future results.

Market metrics

Right now, there are mixed opinions on whether the market has sold off enough, too much, or not enough. While no one can know for certain, the only certainty investors can rely on in times like these is that markets go up and down all the time. In fact, markets often sell off quite a bit during any given calendar year, only to regain footing and end the year in the black. Going back to 1980 (in the chart above), the S&P 500 Index has closed only nine calendar years with a negative return. Of course, there were multi-calendar year stretches with negative returns (2000–2022) and some pretty big losses at times (38% during 2008). But every single calendar year saw negative stretches in returns, with the majority of them ending the year in positive territory.

This is not to say the market has hit a bottom or that investors should expect a rebound in the near future that erases the losses for the year. It's possible the S&P 500 Index finishes the year lower than it is now, but over the long-term the index has averaged gains of more than 10% per year. Patience wins in times like these. In fact, studies show that investors who hold positions longer (years versus months, for example), face a lower probability of loss.

So, what should investors do in a time like this? In this case, ignorance can be bliss. According to several behavioral economists, investors who checked their portfolio balances infrequently had significantly higher profits over time than those who checked balances more often. This is tied to the pain of losing, which tends to be more powerful than the pleasure of gaining. Investors who checked balances frequently tended to hold lower allocations to stocks (because stocks are more volatile than bonds or cash), lowering return potential over time.

Experts recommend three tips during market stress:

1. Have a set time (perhaps annually) to check investment balances to ensure you are on track to meet your retirement goals. Resist the temptation to check more frequently, whether the market is going up or down.
2. Take a hands off approach—invest in a target date fund or set up regular rebalancing (quarterly or annually is typically recommended) to eliminate the need to check your investments.
3. Slow down your decision making. A long-term financial plan should only change when your personal situation has changed, not because the stock market is going down. If you feel the need to make a change, take time to think about it before reacting.

The below table shows returns for major indexes through June 30.

	Total Return (%)					
Name	2Q2022	YTD	1 Yr	3 Yr	5 Yr	10 Yr
S&P 500	(16.10)	(19.96)	(10.62)	10.60	11.31	12.96
MSCI EAFE	(14.51)	(19.57)	(17.77)	1.07	2.20	5.40
MSCI Emerging Markets	(11.45)	(17.63)	(25.28)	0.57	2.18	3.06
BBg Agg Bond	(4.69)	(10.35)	(10.29)	(0.93)	0.88	1.54

Source: Morningstar as of 6.30.22. Past performance is not indicative of future results.

About Mesirow

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Sources: US Trust, Morningstar

The Bloomberg Aggregate Bond Index is a broad-based, market capitalization-weighted bond market index representing intermediate-term investment grade bonds traded in the United States.

The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets.

The MSCI EAFE Index is designed to represent the performance of large and mid-cap securities across 21 developed markets, including countries in Europe, Australasia and the Far East, excluding the U.S. and Canada.

The S&P 500 Index is a market-capitalization-weighted index of the 500 largest U.S. publicly traded companies.

The indices are unmanaged and does not incur management fees, transaction costs or other expense-associated with investable products. It is not possible to directly invest in an index.

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