BULLS&BEARS

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Rocky Start

Increased uncertainty and volatility appear to be the themes for the first half of 2022. The war on Ukraine has only added to this and brought more market risks along with it. Heightened tensions with Russia could result in an energy shortage and weakened consumer confidence; despite this and omicron, elevated inflation, and supply chain shortages, we do anticipate economic growth and the surge in energy prices to provide support for company earnings.

The U.S. bond market just exited its worst quarter in years, with Treasuries down 5.6%, corporate bonds down 7.4% and a broad municipal bond index down 6.2%. After shaking off the rise of inflation in 2021, a swing in the Federal Reserve policy outlook led to a jump in interest rates this year with the 10-year Treasury yield increasing from 1.51% to 2.71% currently.

U.S. stock prices experienced a correction, but they bounced back to post less severe losses and modestly outperformed non-U.S. equities.

As asset markets recalibrate to the evolving economic environment, we expect continued volatility and have reduced risk levels accordingly in portfolios. Later in 2022 we see support for earnings and potential for better returns as uncertainty clears.

Russia-Ukraine

Heightened geopolitical risks are casting a cloud over markets and economy. The war in Ukraine is far from over. Peace talks have been floated but few believe they will amount to anything –especially after the devastating footage coming out of the Kyiv suburbs. The resulting increase in Russian sanctions from the western world further pushes this conflict past the point of no return.

Any expectations (or hopes) that inflation was still transitory took a big hit with Russia's invasion of Ukraine. Beyond the notable – and now at risk – amount of oil and natural gas coming from Russia, the prospect of reduced global crop production this growing season is a real risk. Russia/Ukraine planting of wheat (29% of global harvest) may be disrupted, and farmers are dealing with shortages in global fertilizer supply (of which Russia produces ~8%). Ukraine and Russia are also major producers of several industrial metals.

This war is unlikely to be the last – and its impact will echo for years. Uncertainty often causes fixation on the negative, but opportunities also arise. Considerable investment may be needed in coming years (supply chain reorientation as one example). As we wait, a well-diversified portfolio can protect against incoming fire.

Break the Back

According to the March "dot plot" released by the Federal Open Market Committee, members anticipate the terminal rate to be 2.8% — which it expects to reach in 2023. However, many are starting to question whether the terminal rate could be so low given such high inflation. There is a school of thought that interest rates must exceed the inflation rate in order to "break the back" of inflation. We do not believe that's the case; however, that doesn't mean the Fed won't be on an aggressive track in the shorter term.

Fed Governor Lael Brainard recently proclaimed that moving inflation back to the Fed's 2% target is the central bank's "most important task." This was the latest in a series of comments that indicate the FOMC is focused on aggressively fighting inflation. As a Fed official historically perceived to be "dovish," Brainard's comments have reinforced market views that the Fed has made a very hawkish pivot and will likely be aggressive in tightening monetary policy in the coming months.

Please contact us at 1-855-829-7192 if we may be of assistance.

Market Indicators

3/31/22 Year-to-Date Change	
S&P 500	-4.60%
NASDAQ	-8.95%
Russell 2000	-7.53%

Interest Rates	3/31/22	9/30/21
10-Year Treasury Note	2.35%	1.49%
3-Month Treasury Bill	0.52%	0.04%

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