Investment Review & Outlook
2022 First Quarter Market Report

There's no sugar-coating the news: the U.S. and global markets took a hit in the first three months of 2022, offering investors an experience that they haven't been accustomed to during the long bull market This is a bit of red ink on their performance statements. The only bright spot is commodities, but it's doubtful that anyone with recent experience at the pump is cheering the turmoil in global oil prices.

Just about every investment declined in value in the first quarter. Looking at large cap stocks, the widely-quoted S&P 500 Index of large company stocks is down 4.95% for the first quarter.

Small cap stocks were down as well with the Russell 2000 Small-Cap Index down 7.53% in the year's first three months. The technology-heavy Nasdaq Composite Index is down 9.10% for the year, as tech stocks are, for the first time in a while, underperforming the market as a whole.

International investors were full participants in the downturn. The broad-based EAFE Index of companies in developed foreign economies lost 6.61% in the first quarter. In aggregate, European stocks, whose companies are close to the action in Ukraine, are down 11.34% so far this year, while EAFE's Far East Index has lost 6.68%. Emerging market stocks of less-developed countries, as represented by the EAFE EM Index, also joined in the global decline, falling 7.32% in dollar terms in the first quarter.

The S&P GSCI Index, which measures commodities returns, shone brightly in gaining 29.05% in the first quarter, largely driven (as you might expect) by rising oil prices, and also a price rise due to a global wheat shortage.

These market declines are always a bit nerve-rattling, but from the start of the year to the end of the quarter, the picture becomes a bit more positive. The first two months of the year saw the S&P 500 Index of large companies drop from 4,770 down to 4,173, more than meeting the technical definition of a market correction. And then, in the second half of March, a lot of ground was made up to reach back up to the 4,630 level. Nobody, of course, knows what's going to happen next, but if you simply looked at the markets at the end of December and then checked back in on April 1, the one-quarter downturn would have looked like an insignificant blip in a generally positive 13-year upturn.

That said, there are enough clouds on the horizon to raise the possibility that we'll have to endure further declines before the markets again touch new highs. The most obvious one is the uncertainty that comes with a continuing, grinding war in Ukraine, and the sanctions and oil/grain supply disruptions associated with it.

Another is the possibility that the U.S. economy is approaching a recession. Saying the word 'recession' out loud today is a bit like shouting 'fire!' in a crowded theater; a recession is defined as six months of economic decline, and there is no evidence that we are experiencing that at this time. But some might find it worrisome that, in a recent survey of economists, most of them were backing off of the robust growth projections that they were making late last year. Their consensus now is that, when we finally measure the first quarter's GDP growth sometime next month, it will come in around 1.8%—far below the 3.9% prediction in the previous survey. The new forecast probably reflects the fact that there was 0% GDP growth in both December and January.

Meanwhile, there's another recession indicator that will probably get more press coverage than it deserves. The bond markets have recently shifted close to what is known in the trade as an inverted yield curve, which is a fancy way of saying that short-term bonds are offering higher rates than longer-term ones. The problem, of course, is that this 'signal' has not exactly been a perfect predictor of recessions in the past, and even when it has, the time frame could be one year or five. Moreover, it might be a stretch to call this a signal at all, since the yield spread between, say, one-year and 30-year Treasuries is still pretty robust. One might better describe the 2/10 year inversion as a small kink in the yield curve rather than an inversion.

More optimistically, it is not easy to ignore the fact that the U.S. economy added 431,000 new jobs in March, after a gain of 678,000 in February. U.S.-based corporations experienced their most profitable year since 1950 in calendar 2021. People who see the glass half-empty certainly have some data on their side, but so too do the optimists among us—and what's interesting is that this has always been true. In retrospect, we will see who was right, but in the moment, as we look at the future, there tends to be good, compelling clues that lead us to expect very different possible outlooks.

If the markets continue their choppy course, you will see a lot of pundits, soothsayers and (even less reliable) market economists telling us with confidence what's going to happen next. Some of them, by the law of averages, will be right, and will trade on that credibility through several false predictions to come. It's like the story of the huckster who would go to the racetrack and tell different people which horse was going to win the next race—and this clever person would give different people the names of different horses.

Inevitably, one of the horses would win, at which point the clever tout (avoiding the people to whom he gave incorrect predictions) would approach the happy winners and offer to sell his next surefire winning prediction. The only difference is that market economists are better at this game.

And so we wait, perhaps impatiently, for the next time the markets test new highs. Even if we don't know when that will happen, history offers encouraging evidence that it will, and all the anxiety and excitement that the markets produce in the meantime will have been, depending on your temperament, wasted energy or pure entertainment.

Please reach out with any questions you may have. If your circumstances have changed, please let us know so we can discuss any needed changes.

The FAM Team