FINANCIAL MARKETS HIGHLIGHTS

First Quarter 2022

Financial markets struggled to find normalcy for much of the first quarter. What began as a quarter plagued by a steep rise and fall in COVID cases, ended overshadowed by the tragic events occurring in Ukraine. Supply chain issues that were beginning to ease as COVID infection rates declined, have been tangled due to war.

The S&P 500 Index of large and mega-capitalization US stocks declined -4.6%, its first negative quarter since Q1 2020, as some of its largest constituents such as Apple, Amazon, Alphabet, NVidia, Meta and Tesla were down. Other segments of the stock market generally fared worse. The Russell 2000 Index of small-cap US stocks declined -7.5%, the MSCI EAFE Index of international, developed market stocks -5.9%, and the MSCI Emerging Market Index -7.0%.

The devil remains in the details, though, and if one squints closely, they will observe some interesting price action. Notably, the recent outperformance of value stocks over growth stocks is meaningful by historical standards. The broad Russell 3000 Value Index declined only -0.9% during the quarter, while its counterpart the Russell 3000 Growth Index returned -9.3%. Over the past 20 years, in only two other calendar quarters did value stocks generate such relative outperformance.

Over time, value stocks and growth stocks exhibit cyclical relative returns. Growth may outperform value for an extended period, as had been the case for quite some time, but inevitably this is followed by a reversal. Timing these shifts is a fool's errand, and thus we advise maintaining a diversified portfolio with exposure across multiple asset classes and security types.

The investment-grade bond market, as represented by the Bloomberg US Aggregate Bond Index, returned -5.9% during Q1. This was the third worst quarter for the Bloomberg US Aggregate Index *ever*; only two quarters in 1980 were worse. Meanwhile the Bloomberg High Yield Index, comprised of bonds rated below investment-grade, declined -4.8%.

Both the stock and bond markets are under significant pressure as US monetary policy makers at the Federal Reserve Board (the "Fed") have begun, in earnest, an interest rate hiking cycle to mitigate inflation levels (*i.e.,* rising consumer prices) not observed since the early 1980's. The Fed raised its short-term Federal Funds rate by 0.25% on March 17, to a range of 0.25% - 0.50%, and signaled its intent to aggressively continue that course over the remainder of 2022 and 2023, data dependent. The current median projection by the Fed's Open Market Committee participants is for a Fed Funds rate of 1.75% - 2.0% by the end of 2022 and ~ 2.75% by the end of 2023, suggesting roughly seven more rate hikes in 2022 and an additional four in 2023.

The effects of sharply higher interest rates include inhibiting finance-enabled spending, inducing savings, and decelerating the velocity of money in the economic system, all with the intent of easing price pressures. The risk is that these actions cause a recession, and the market is beginning to price in that distinct possibility.

Selected Index Returns (%) as of March 31, 2022 (Source: Morningstar Direct). 3, 5, 10 year returns are annualized.

	Jan.	Feb.	Mar.	QTR	YTD	1 Year	3 Year	5 Year	10 Year
S&P 500	-5.17	-2.99	3.71	-4.60	-4.60	15.65	18.92	15.99	14.64
S&P 400	-7.21	1.11	1.38	-4.88	-4.88	4.59	14.14	11.10	12.20
Russell 2000	-9.63	1.07	1.24	-7.53	-7.53	-5.79	11.74	9.75	11.04
Wilshire U.S. REIT Index	-6.93	-3.34	6.85	-3.87	-3.87	29.14	11.94	10.04	9.90
MSCI EAFE	-4.83	-1.77	0.64	-5.91	-5.91	1.16	7.78	6.72	6.27
MSCI Emerging Markets	-1.89	-2.99	-2.26	-6.97	-6.97	-11.37	4.94	5.98	3.36
Bloomberg Aggregate Bond	-2.15	-1.12	-2.78	-5.93	-5.93	-4.15	1.69	2.14	2.24
Bloomberg High Yield	-2.73	-1.03	-1.15	-4.84	-4.84	-0.66	4.58	4.69	5.75

FINANCIAL MARKETS HIGHLIGHTS

First Quarter 2022

Surging energy prices have been a significant contributor to inflationary pressures. The Bureau of Labor Statistics February 2022 Consumer Price Inflation data revealed a +6.4% year-over-year increase in consumer prices, ex food & energy. Inclusive of those items, the increase was +7.9%, driven by a +25.6% increase in energy costs. West Texas Intermediate crude oil surged +33% during the quarter, Henry Hub Natural Gas +51%, and the average cost of a gallon of regular gas is up almost a full dollar from the start of the year.

Energy demand has been outpacing supply for some time now, due to robust economic activity, regulatory discouragement of increased fossil fuel extraction, and a greater focus among corporate oil “majors” on fiscal prudence as opposed to expensive exploration and development. Exacerbating this price pressure is Russia’s invasion of Ukraine and the resultant sanctions levied against Russia, one of the world’s largest energy producers. Where possible, Russian supply is being removed from the marketplace, and that is a substantial supply not quickly replaced.

Oil producing countries such as the US and OPEC+ have sought to moderate price pressures by increasing production, where possible, or releasing strategic reserves. The latter is a temporary patch, and the former takes many months to *begin* to take effect.

The market’s favorite inflation hedge, gold, rallied +6.5% during the quarter. Bitcoin, sometimes referred to as digital gold and considered (*by some*) an inflation hedge because of its fixed supply, declined -4.1%. On the labor front, unemployment levels are at 3.6% as of April 1, near pre-pandemic levels and historically strong.

We are compelled to state the obvious; that the Russian aggression in Ukraine is tragic. Over time, however, the stock market delivers what seems a cold and bloodless verdict. It sides with capitalism, and its success rides on the broad shoulders of American businesses. Tragedies come and go, disasters of unimaginable proportions occur, disproportionately so, but the best American businesses continue to innovate and grow their earnings, assets and dividends … and stock markets climb a perpetual wall of worry.

As always, we wish you the best. If you have any questions or comments, please call us at 617-531-3100.

Selected Index Returns (%) as of March 31, 2022 (Source: Morningstar Direct). 3, 5, 10 year returns are annualized.

	Jan.	Feb.	Mar.	QTR	YTD	1 Year	3 Year	5 Year	10 Year
S&P 500	-5.17	-2.99	3.71	-4.60	-4.60	15.65	18.92	15.99	14.64
S&P 400	-7.21	1.11	1.38	-4.88	-4.88	4.59	14.14	11.10	12.20
Russell 2000	-9.63	1.07	1.24	-7.53	-7.53	-5.79	11.74	9.75	11.04
Wilshire U.S. REIT Index	-6.93	-3.34	6.85	-3.87	-3.87	29.14	11.94	10.04	9.90
MSCI EAFE	-4.83	-1.77	0.64	-5.91	-5.91	1.16	7.78	6.72	6.27
MSCI Emerging Markets	-1.89	-2.99	-2.26	-6.97	-6.97	-11.37	4.94	5.98	3.36
Bloomberg Aggregate Bond	-2.15	-1.12	-2.78	-5.93	-5.93	-4.15	1.69	2.14	2.24
Bloomberg High Yield	-2.73	-1.03	-1.15	-4.84	-4.84	-0.66	4.58	4.69	5.75