Market Update for the Quarter Ending December 31, 2022

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December Sell-Off Caps Turbulent Year

Markets sold off in December, contributing to mixed results for the quarter and declines for 2022. The S&P 500 lost 5.76 percent during the month, gained 7.56 percent for the quarter, and lost 18.11 percent for the year. Dow Jones Industrial Average (DJIA) declined 4.09 percent in December, gained 16.01 percent for the quarter, and lost 6.86 percent for the year. The Nasdaq Composite lost 8.67 percent in December, declined 0.79 percent decline for the quarter, and lost 32.54 percent for the year.

Per Bloomberg Intelligence, as of December 30, 2022, with 99 percent of companies having reported actual earnings, the blended earnings growth rate for the S&P 500 in the third quarter was 4.6 percent, up from estimates for a 2.6 percent increase. Better-than-expected earnings growth in the first and second quarters of 2022 shows businesses continued to successfully operate despite economic headwinds.

The S&P 500 ended the year below its 200-day moving average, as the year-end sell-off brought the index below trend after a brief stint above trend at the end of November and start of December. The DJIA finished December above trend—marking three consecutive months with technical support for the index—but the Nasdaq Composite ended the month below trend. Mixed technical indicators at the end of 2022 indicate uncertainty for equity investors to start 2023.

International markets were mixed in December, but results were similar to the U.S. on a quarterly and annual basis. The MSCI EAFE Index gained 0.08 percent in December, capping off a 17.34 percent return for the quarter. Developed international equities ended the year down 14.45 percent. The MSCI Emerging Markets Index lost 1.35 percent during the month, gained 9.79 percent for the quarter, and dropped 19.74 percent for the year.

Technicals were mixed for international markets to end the year. The MSCI EAFE Index finished the month above its 200-day moving average, which marked two consecutive months finishing above trend. The MSCI Emerging Markets Index, on the other hand, ended December below trend, marking 18 consecutive months with the index finishing below its 200-day moving average.

Fixed income markets also experienced declines in December and for the year. The 10-year U.S. Treasury yield rose from 1.63 percent to 3.88 percent by year-end. The 1-year U.S. Treasury yield surged from 0.4 percent at the start of 2022 to 4.73 percent at year-end. The rise in yields was primarily due to higher rates from the Federal Reserve (Fed) as the central bank hiked the federal funds rate 4.25 percent in 2022 to combat inflation.

The Bloomberg U.S. Aggregate Bond Index dropped 0.45 percent during the month, notched a 1.87 percent gain for the quarter, and lost 13.01 percent in 2022. The Bloomberg U.S. Corporate High Yield Bond Index saw a 0.62 percent decline for the month, a 4.17 percent gain for the quarter, and an 11.19 percent decline for the year. High-yield credit spreads widened notably last year, increasing from 3.05 percent at the start of 2022 to 4.81 percent at year-end.

Economic Updates Remain Positive

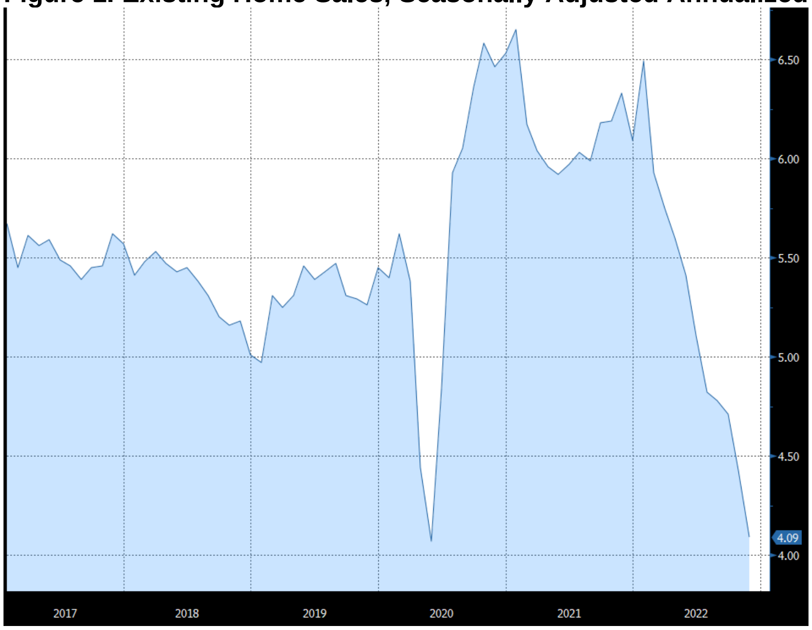
The labor market saw signs of surprising strength toward the end of the year, as the November employment report revealed 263,000 jobs added against calls for 200,000. The unemployment rate ended November at 3.7 percent, which was down from the start of the year.

Personal income and spending rose in November for the fourth consecutive month. Consumer spending growth was relatively consistent last year, supported by Covid-19 pandemic-era savings and a strong labor market. Core durable goods orders rose in November following a solid jump in October, indicating that businesses continued to spend and invest to meet high levels of demand toward year-end. Consumer and service sector confidence also showed improvements toward the end of the year.

Housing Continues to Slow

Not all economic news for 2022 was positive as the housing sector showed signs of continued slowdown at year-end. After serving as a bright spot in 2020 and 2021, the housing sector slowed in 2022 due to low supply of homes for sale, high prices, and rising mortgage rates. As shown in Figure 1, the pace of existing home sales fell in November to its lowest level since the lockdown-induced nadir in May 2020.

Figure 1. Existing Home Sales, Seasonally Adjusted Annualized Rate, 2017–Present



Source: National Association of Realtors/Bloomberg

The average 30-year mortgage started 2022 at 3.3 percent and hit a high of 7.35 percent in November before ending the year at 6.66 percent. While there were signs at year-end that housing price growth has started to fall—and in some cases even turn over—the housing sector is expected to experience ongoing, short-term slowing growth as high rates and prices serve as a headwind for prospective home buyers.

Inflation Slowing but Risks Remain

A major market and economic risk last year was high inflation. The Fed responded by hiking rates and tightening monetary policy throughout 2022, which caused sell-offs across equity and fixed income markets. The worst might be behind us, but inflation stayed high on a year-over-year basis.

While markets continue to price in slighter higher short-term yields in the first half of this year, expectations call for looser policy toward year-end. This could lead to additional market volatility if these expectations aren't met, so the Fed and inflation bear monitoring in 2023. Political risks are set to take center stage as last year's midterm elections led to a split federal government. It's likely we'll be reading about debt ceiling debates and a potential government shutdown at some point this year.

Abroad, the main risks to start the new year are the ongoing Russia-Ukraine war and the slow reopening of China as the country eases Covid-19 restrictions. The Ukraine war's impact on markets declined toward the end of 2022, but continued conflict could lead to further uncertainty. China's reopening efforts are widely viewed as a positive development for the global economy following months of lockdowns. The country could be a source of additional uncertainty if medical risks rise.

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We enter 2023 with a relatively positive backdrop. While risks remain, economic fundamentals are solid, and market valuations are more attractive now than they were at the start of 2022. Given the potential for further short-term uncertainty, a well-diversified portfolio that matches investor goals with timelines is the best path forward for most. If you have questions or concerns, you should reach out to your financial advisor to discuss your financial plans.

All information according to Bloomberg, unless stated otherwise.

Disclosure: *Certain sections of this commentary contain forward-looking statements based on our reasonable expectations, estimates, projections, and assumptions. Forward-looking statements are not guarantees of future performance and involve certain risks and uncertainties, which are difficult to predict. Past performance is not indicative of future results. Diversification does not assure a profit or protect against loss in declining markets. All indices are unmanaged and investors cannot invest directly into an index. The Dow Jones Industrial Average is a price-weighted average of 30 actively traded blue-chip stocks. The S&P 500 Index is a broad-based measurement of changes in stock market conditions based on the average performance of 500 widely held common stocks. The Nasdaq Composite Index measures the performance of all issues listed in the Nasdaq Stock Market, except for rights, warrants, units, and convertible debentures. The MSCI EAFE Index is a float-adjusted market capitalization index designed to measure developed market equity performance, excluding the U.S. and Canada. The MSCI Emerging Markets Index is a market capitalization-weighted index composed of companies representative of the market structure of 26 emerging market countries in Europe, Latin America, and the Pacific Basin. It excludes closed markets and those shares in otherwise free markets that are not purchasable by foreigners. The Bloomberg Aggregate Bond Index is an unmanaged market value-weighted index representing securities that are SEC-registered, taxable, and dollar-denominated. It covers the U.S. investment-grade fixed-rate bond market, with index components for a combination of the Bloomberg government and corporate securities, mortgage-backed pass-through securities, and asset-backed securities. The Bloomberg U.S. Corporate High Yield Index covers the USD-denominated, non-investment-grade, fixed-rate, taxable corporate bond market. Securities are classified as high-yield if the middle rating of Moody's, Fitch, and S&P is Ba1/BB+/BB+ or below.*

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