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Perspective on First Quarter 2023 Economic & Market Events

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Despite ongoing recession concerns, markets were resilient in the first quarter of 2023, which was a welcome relief after a disappointing finish to 2022. The new year began on a fairly strong note, with interest rate expectations easing and both stock and bond prices increasing in response. The hope was that more moderate inflation reports in the prior few months would encourage minimal further rate hikes. However, stronger than expected economic data during the first quarter caused the Federal Reserve to indicate that the peak interest rate level may have to go higher than previously expected, meaning that rate increases may continue in the near-term depending on the data. The concern over the last year has been whether the Fed's interest rate actions will lead the U.S. economy into a recession. So far, the economic data remains stable. Unemployment levels are at near historic lows, wages are increasing, job openings are near record highs, and the layoffs seen in certain industries, such as technology, are currently contained and not impacting the broader workforce.

This year, inflation appears to be moderating despite continued high levels. The Fed continues to raise interest rates, but not as aggressively as in 2022. Investors are now hopeful that the Fed's interest rate increases combined with problems in the banking sector will not tip the economy into a severe recession. It is important to note that the three U.S. bank failures that have been in the headlines this year had unique business models, poor risk management and a limited amount of FDIC insured deposits. In its statement and at Powell's most recent news conference on May 2, the Fed made clear that it does not think its string of rate hikes have so far sufficiently cooled the economy, the job market and inflation. Inflation has dropped from a peak of 9.1% in June 2022 to 5% in March 2023 but remains well above the Fed's 2% target rate. [1]

Market indexes closed the first quarter positively, with the Dow Jones Industrial Average (DJIA) up 0.4%, after rising 302% in the last week of the quarter, its largest one-week gain since the week ending November 11, 2022. The S&P 500 gained 7.0% during the first quarter, which is its best three-month performance since the fourth quarter of 2021. The Bloomberg Barclays U.S. Intermediate Government/Credit Bond Index rose 2.33% during the first quarter. [2]

The Fed is attempting to engineer what is known as a "soft landing." This is where they raise interest rates just enough to reduce harmful inflation without creating a recession. Higher interest rates can create a recession because the cost of borrowing rises for both consumers and businesses.

Typically the stock market is forward-looking and a leading indicator of the economy. Therefore, even if the Fed interest rate hikes cause a recession, the stock market decline that occurred last year may have already priced in a worsening economy this year. Just as the stock market has declined in anticipation of a potential recession, it would not be surprising to see it begin to recover during an economic downturn as it anticipates an eventual recovery. This is precisely what happened during the 2020 recession caused by the pandemic. One positive aspect of the Fed raising interest rates is that yields on many newly-issued fixed-income securities have increased. This means investors can now earn a better interest rate on many bonds, CDs, and money

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market funds. Also, due to last year's stock market decline, stocks are more fairly valued than they have been in a long time.

The Fed is now grappling with a standoff around the nation's borrowing limit, which caps how much debt the government can issue. Treasury Secretary Janet Yellen warned that the nation could default on its debt as soon as June 1 unless Congress agreed to lift the federal borrowing limit. A first-ever default on the U.S. debt could potentially trigger an economic downturn so even though the first quarter ended in a positive position, the higher market volatility that we saw for the better part of 2022 has become a factor in 2023.

The large swings in market performance began back in early 2022 due to heightened concerns around the persistent higher inflation and the onset of the Russia-Ukraine war. While markets appeared to stabilize a bit in late 2022 and to start the new year, higher market volatility came back once again. One of the most unsettling aspects of large market fluctuations is the fact they are out of our control. However as we have all experienced, downturns do happen and equity markets do not go up in a straight line - they go up, they go down and then they go up again. Furthermore, significant market downturns are not rare events and in fact happen with some regularity. While past performance is no guarantee of future performance, history has shown that larger equity market selloffs typically have not lasted for extended periods. During times of heightened market volatility, we are committed to being available to discuss any questions or concerns that you may have.

In an effort to encourage a paperless environment, our custodian, Pershing, LLC, has made us aware of the following updates to their fees that are being implementing:

- Paper statements and confirmations will be $2.00 per month per account assessed quarterly effective August 31, 2023. This fee will increase to $3.00 in January 2024 and to $5.00 in June 2024.
- Paper tax documents fee will be $10.00 per year per account assessed in March 2024.
- Paper check fee will be $10.00 per check effective July 31, 2023. This fee does not apply to checks set up to be automatically sent on a periodic basis.

As technology has become more accessible to most folks, firms have been going in this direction for several years. Please consult with your Investment Advisor Representative if you have any questions about these fees or ways to help minimize the possible impact to your accounts. We appreciate the trust and confidence you place with our people and our organization.

1. https://www.forbes.com/advisor/investing/fomc-meeting-federal-reserve/
2. barrons.com, 3.31.2023

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