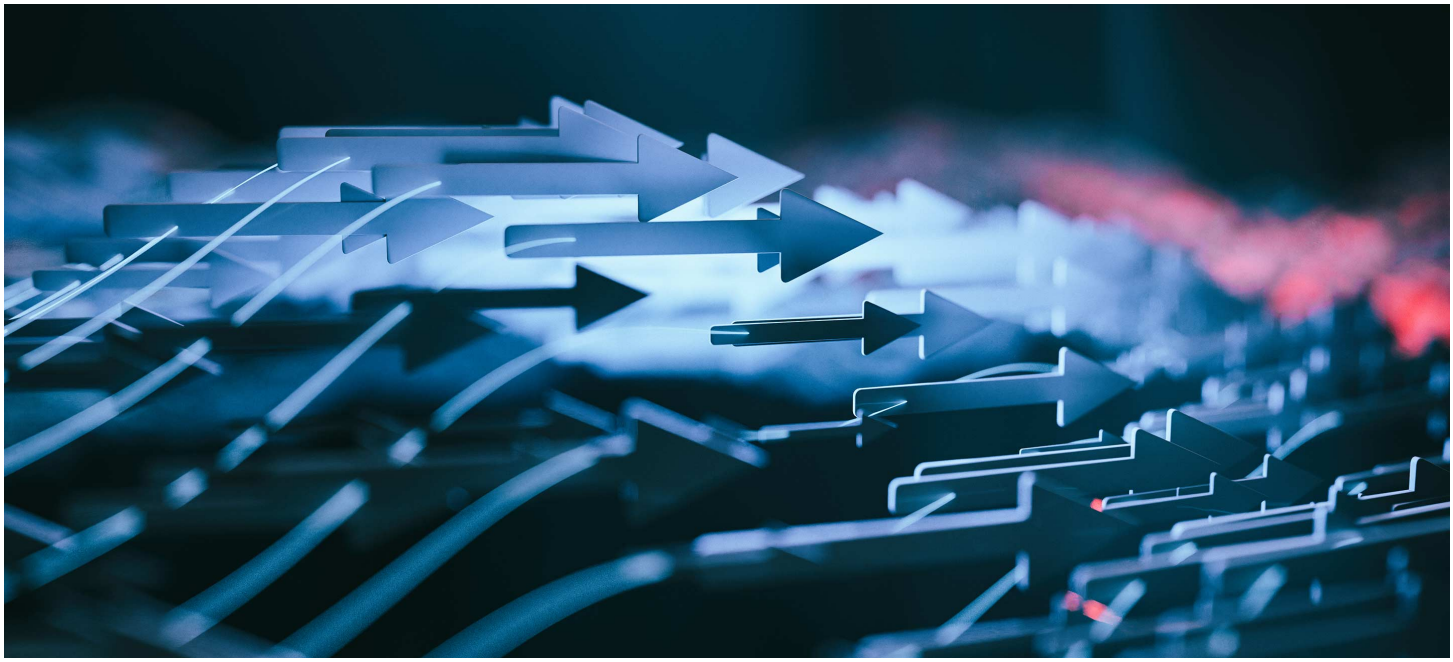
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# Market Thoughts 5.6.2022

U.S. stocks sold off sharply yesterday in one of the worst trading days of 2022. The S&P 500 Index of large-cap U.S. stocks fell more than 3.5 percent and the technology-oriented NASDAQ Index fell almost 5 percent. These moves erased the indexesâ?? big gains from Wednesday as markets rallied after Federal Reserve Chairman Jerome Powell ruled out larger interest rate hikes. This weekâ??s major market moves highlight an already-challenging year for stock investors. The bond market is experiencing a similarly challenging time.

Coming into 2022, U.S. large-cap stocks, as measured by the S&P 500, had doubled over the prior three years. This remarkable run included two years where investors captured returns greater than 25 percent and experienced little anxiety, with only a few short-lived periods of market volatility.

Itâ??s important to remember that periods like 2019 through 2021 are anomalies and that pullbacks of 5 to 10 percent typically happen about every year. Pullbacks of 10 percent or more have happened every three to five years. In other words, periods of volatility like the one we are currently experiencing are more the rule than the exception.

Investors are grappling with several macroeconomic concerns, including inflation at levels not seen in decades, the uncertain impact of the war in Ukraine, and the risk of a Fed policy mistake that over- or under-shoots the hoped-for soft economic landing without sending the economy into recession. No doubt, the Fed faces a very difficult task, and it is too early to know if it will be able to orchestrate the desired outcome.

These macroeconomic forcesâ??and their resulting headlinesâ??are the current drivers of recent stock market moves, pushing more than half of the companies in the S&P 500 into bear-market territoryâ??down more than 20 percent from their highs. Interestingly, industry analysts remain optimistic, forecasting continued growth in corporate revenues and earnings for 2022 and 2023. Clearly, this message has been obscured by recent news.

While stock markets have been grabbing the headlines, bond markets have also been hit. After 40 years of smooth sailing, investors were reminded in early 2022 that bonds are not risk free. They have provided little or no diversification benefit during this period of stock market volatility. However, there are two significant differences between stock market volatility and bond market volatility.

First, absent a default, a bondâ??s expected return is always known, captured by its yield to maturity. While bonds can generate price losses, assuming no credit impairment, the bondholder will eventually receive the interest payments and principal, earning the yield to maturity stated at the time the bond was purchased.

As importantly, short-term pain can often lead to longer-term gains in bond markets. History tells us that bond market pain generally translates to a more favorable future. For example, an investor who bought a 2-year Treasury on January 1 could expect an annual return of 0.78 percent over the life of the bond. Today, an investor purchasing that same security can expect a 2.71 percent annual return.

As always, a well-diversified portfolio tailored to your appetite for risk and unique financial goals and objectives is the best long-term strategy and can help provide the peace of mind necessary to stay the course through volatile markets. You should expect continued market volatility as investors weigh new data and adjust their expectations. This recalibration can take time as trends and a better understanding of the risks and impacts emerge.

Periods like the one we are experiencing are causes of concern, but they also create opportunity for long-term investors. Market pullbacks provide investors with catalysts to consider their asset allocations and ensure that they are taking an appropriate level of risk. They also provide opportunities to rebalanceâ??by buying the weaker asset class with proceeds harvested from the strongerâ??to keep portfolio risk levels in check.

We will be following developments closely and will keep you up to date. If you have questions or concerns, please do not hesitate to bring them to our attention.

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