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Market Commentary

February 2023

- In February, equities declined following hotter than expected inflation and jobs data.
- Investors are now pricing in a higher federal funds rate for 2023.
- Technology stocks, as well as small cap stocks, performed modestly during the month, while emerging market equities fell notably.

MARKET RETURNS AS OF FEBRUARY 28, 2023[1]

	Feb %	QTD %	YTD %	1 Year %	3 Year %	5 Year %	10 Year %
S&P 500 TR	-2.44	3.69	3.69	-7.69	12.16	9.82	12.25
DJ Industrial Average TR	-3.94	-1.13	-1.13	-1.59	10.97	7.77	11.34
NASDAQ Composite TR	-1.01	9.61	9.61	-15.96	11.05	10.51	14.94
Russell 2000 TR	-1.69	7.89	7.89	-6.02	10.09	6.01	9.06
MSCI EM GR	-6.48	0.92	0.92	-14.91	1.34	-1.50	1.89
MSCI EAFE GR	-2.08	5.87	5.87	-2.64	7.35	3.14	5.32
Bloomberg US Agg Bond TR	-2.59	0.41	0.41	-9.72	-3.77	0.53	1.12

MARKETS

Equities retreated in the month of February, as hotter than expected inflation and jobs data led to a shifting of expectations for the Fed and rates in 2023.

- In terms of inflation, the consumer price index (CPI) rose 0.5% in January, after increasing 0.1% in December. Over the last 12 months, the all-items index increased 6.4% before seasonal adjustment.
- Furthermore, a very strong jobs reports from January showed that nonfarm payrolls increased by 517,000, far higher than the 187,000 market estimate. Despite all the headlines around layoffs, the demand for labor broadly remains high while supply is still constrained.

After a volatile start to 2023, the Nasdaq and S&P 500 are still positive for the year, while the Dow is now in negative territory.

THE FED AND RATES

Prior to the February inflation reports, the market was pricing in a ceiling on the federal funds rate of 4.80-4.90%. Expectations for the end of the year were that the federal funds rate would finish at 4.5%. These assumptions suggested that the Fed would cut rates in the second half of the 2023. Now, not only has the market priced in a higher ceiling on the federal funds rate of 5.25-5.50% by June, but the market is also no longer expecting that the Fed will cut rates in 2023. To achieve this new level, the Fed would need to hike interest rates by 25 basis points at each of the subsequent meetings between now and then, in March, May and June.

Fed officials have been quoted defending the central bank's historical 2% inflation target, despite prices remaining far higher and stickier than the goal. In order to achieve that target, inflation will still have to come down meaningfully and thus, further rate hikes appear to be necessary.

Despite inflation remaining elevated, there are parts of the market, such as housing, where the impact of rates has begun to appear. Sales of previously owned US homes declined for a 12th-straight month in January, extending a record decline and highlighting the impact of higher rates on home sales.

WHAT'S NEXT?

The month of January was a reversal of December trends, while February proved to be a reversal of January trends. All this whipsaw performance may have some clients running for the exit door. Some concepts to remember when you are talking to clients:

- **Stick to the plan.** Short term volatility is unlikely to derail a long-term allocation. Help your clients remember their plan during volatile periods instead of reacting emotionally.
- **Diversification matters.** We were all reminded of this in 2022. There are many ways to diversify a portfolio, whether it means dipping a toe into international equity markets, investing across the fixed income landscape, or exploring alternative investments.
- **Do not try to time the markets.** When investors feel worried about the outlook, their natural tendency is to sell and come back when there is more certainty. However, history suggests that trying to time markets in this way is a mistake. Focus on the horizon, not the waves.

As a reminder, most asset allocation models are built for the long term, with diversification inside. Please reach out if you want to learn more.

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FOOTNOTES:

Past performance is no guarantee of future returns.

The graphs and charts in this commentary are for illustrative purposes only and not indicative of any actual investment. Index returns do not reflect any fees, expenses, or sales charges. Stocks are not guaranteed and have been more volatile than other asset classes. Historical returns were the result of certain market factors and events which may not be repeated in the future. Financial professionals are responsible for evaluating investment risks independently and for exercising independent judgement in determining whether investments are appropriate for clients.

The information here is not intended to constitute an investment recommendation or advice.

Sources:

1. Data from Morningstar. Returns over one year are annualized.

Returns are based on the S&P 500 Total Return Index, an unmanaged, capitalization-weighted index that measures the performance of 500 large capitalization domestic stocks representing all major industries. Indices do not include fees or operating expenses and are not available for actual investment. The hypothetical performance calculations are shown for illustrative purposes only and are not meant to be representative of actual results while investing over the time periods shown. The hypothetical performance calculations for the respective strategies are shown gross of fees. If fees were included returns would be lower. Hypothetical performance returns reflect the reinvestment of all dividends. The hypothetical performance results have certain inherent limitations. Unlike an actual performance record, they do not reflect actual trading, liquidity constraints, fees and other costs. Also, since the trades have not actually been executed, the results may have under- or overcompensated for the impact of certain market factors such as lack of liquidity. Simulated trading programs in general are also subject to the fact that they are designed with the benefit of hindsight. Returns will fluctuate and an investment upon redemption may be worth more or less than its original value. Past performance is not indicative of future returns. An individual cannot invest directly in an index.

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