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MARKET MINUTE

2022 VOLUME 1: DECEMBER REVIEW

This month's Market Minute reflects the views of Clearstead's Research Team and was composed by
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OVERVIEW

Much of what spooked the markets in November unwound in December. Fears that the quickly spreading Omicron COVID-19 variant would be more deadly and disruptive to the US economy faded as cases exploded, but hospitalizations and deaths decoupled and remained muted relative to the overall positive cases. As these fears abated, markets naturally returned to the prospect that strong employment and mounting inflationary pressures are likely to spur the Federal Reserve to speed up the tapering of its bond buying activities and raising rates sooner than was generally anticipated at the beginning of the quarter. As the year ended, the S&P 500 Index returned over 28%, while the end-of-pandemic-related monetary policy and the prospect of Fed tightening next weighed on bond returns and the Bloomberg US Bond Index finished the year -1.5%—one of only four negative years in the past 35 for US bonds.[1]

DOMESTIC EQUITY *As of December 31, 2021*

U.S. EQUITY MARKETS				
Index	1 Month	Quarter-To-Date	Year-To-Date	1 Year
DJIA	5.5%	7.9%	20.9%	20.9%
S&P 500	4.5%	11.0%	28.7%	28.7%
Russell 2000	2.2%	2.1%	14.8%	14.8%
Russell 1000 Growth	2.1%	11.6%	27.6%	27.6%
Russell 1000 Value	6.3%	7.8%	25.1%	25.1%

The S&P 500 quickly shook-off the end-of-November Omicron variant fears and climbed throughout the month before reaching a record high on December 29th at over 4793.06. In total, the S&P 500 recorded four separate record highs in December and ended the month just 56 basis points below the December 29th record high.[2] For the year, the S&P 500 Index returned 28.7%, leading most other major indices.

US Large and mid-cap value stocks led US equity returns in December with the Russell 1000 Value Index and Russell Mid Cap Value Index both gaining +6.3%. In contrast, US large cap stocks (Russell 1000 Growth Index) gained +2.1% in December and mid-cap growth stocks (Russell Mid Cap Growth Index) gained +0.4%. US small cap stocks (Russell 2000) lagged their large and mid-cap peers gaining only +2.2% during the month and, like the broader market, small cap value stocks (Russell 2000 Value +4.1%) outperformed small cap growth stocks (Russell 2000 Growth +0.4%).

INTERNATIONAL EQUITY *As of December 31, 2021*

INTERNATIONAL EQUITY MARKETS				
Index	1 Month	Quater-To-Date	Year-To-Date	1 Year
MSCI ACWI ex USA	4.1%	1.8%	7.8%	7.8%
MSCI EAFE	5.1%	2.7%	11.3%	11.3%
MSCI Emerging Markets	1.9%	-1.3%	-2.5%	-2.5%
MSCI EAFE Small Cap	4.4%	0.1%	10.1%	10.1%

Unlike last month, non-US equities outperformed US equities in December amid a more stable foreign currency environment—the US dollar largely traded sideways against most foreign currencies—and European markets performing particularly well (MSCI Europe Index +6.6%). Emerging markets continued to lag developed markets (MSCI EM Index +1.9%) for the month, while Chinese equities continued their slide (MSCI China Index -3.2%) during December as stringent COVID-19-linked lockdowns continued in parts of China.

Unlike in the US, small cap stocks (MSCI ACWI ex US Small Cap Index +4.2%) slightly outgained their large cap peers (MSCI ACWI ex US Index +4.1%), but like US markets, value stocks outperformed growth stocks on a relative basis for the month (MSCI ACWI ex US Value Index +5.2% vs. MSCI ACWI ex US Growth Index +3.0%).

FIXED INCOME *As of December 31, 2021*

FIXED INCOME MARKETS				
Index	1 Month	Quarter-To-Date	Year-To-Date	1 Year
BarCap US Aggregate	-0.3%	0.0%	-1.5%	-1.5%
BarCap Global Aggregate	-0.1%	-0.7%	-4.7%	-4.7%
BarCap US High Yield	1.9%	0.7%	5.3%	5.3%
JPM Emerging Market Bond	1.4%	0.0%	-1.5%	-1.5%
BarCap Muni	0.2%	0.7%	1.5%	1.5%

As market concerns over Omicron subsided, appreciation for the current US macro-environment exerted itself during the month and interest rates moved higher across all maturities from 1-year treasury bills to 30-year government bonds. In this risk-on environment of December, spreads contracted across the board (IG spreads -7 bps, HY spreads -70bps, and EM spreads -23bps).[3] The major driver of performance for the Bloomberg US Bond Aggregate Index -0.3% was the movement up in the yield curve and longer duration bonds underperforming. For example, the Bloomberg US Treasury Index was down -0.51% for the month, but the US Long Treasury Index was down ¬1.42%, while the Bloomberg Intermediate Treasury Index was down only -0.26%.

CLOSING

After a bout of Omicron-related volatility towards the end of November and early December, a consensus viewpoint came to emerge in the subsequent weeks that the Omicron variant—while very fast spreading—was unlikely to make people sicker than earlier COVID-19 variants and therefore unlikely to derail the US economic trajectory as we headed into 2022. Equally, markets largely brushed aside the notion that President Biden would be unable to pass any further spending plans and focused on the outlook for 2022. This outlook features expectations of +9.2% earnings growth and stable profit margins for the S&P 500 companies, gradually declining inflation rates, a generally tight labor market, less monetary stimulus, and further pressure on US interest rates to rise.[4] Against this backdrop, Clearstead believes that US equities are positioned to grind out further gains—but most likely in the single digits range rather than double-digit gains registered in each of the past two years—amid heightened volatility. Meanwhile US fixed income markets could conceivably be faced with the prospect of back-to-back annual declines—something that has not happened since the Bloomberg US Aggregate Bond Index was created in 1977.

SOURCES:

1-4: Bloomberg LP