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MARKET MINUTE

AUGUST REVIEW 2022

This month's Market Minute reflects the views of our Investment Office and was composed by
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OVERVIEW

The Federal Reserve Bank of Kansas City's Economic Policy Symposium began in 1978 and was moved to Jackson Hole, Wyoming in 1982. As the story goes, the Kansas City Fed thought the move to Jackson Hole would ensure that then Federal Reserve Chair Volcker would attend — Volcker was an avid fly fisherman and who could turn down the opportunity for some of the best fly fishing around. The rest, as they say, is history. Jackson Hole was the name of the game in August, which could otherwise be characterized as having mixed economic news as the backdrop to a rising interest rate environment. For a month otherwise typified by the proverbial summer doldrums, markets awoke following the August 26th speech from current Federal Reserve Chair Powell.

Powell's hawkish message happen to be coincident with a S&P 500 that was struggling to break above key technical levels and had recovered half of the losses witnessed in the first half of the year.[1] In recent years Jackson Hole speeches had rarely elicited any noteworthy response from markets. In fact, since 2012 in the five days following the speech the S&P 500 produced average gains of +0.5%[2] and then equities have experienced a subsequent average gain of +4.5%[2] through year end. Inflation (or price stability) was hardly a concern in those years as growth was the more pertinent concern, and so these observations would not matter this time around as markets heeded Powell's hawkish message around the Fed's commitment to fighting inflation.

DOMESTIC EQUITY *As of August 31, 2022*

U.S. EQUITY MARKETS				
Index	1 Month	Quarter-To-Date	Year-To-Date	1 Year
DJIA	-3.7%	2.8%	-12.0%	-9.1%
S&P 500	-4.1%	4.8%	-16.2%	-11.2%
Russell 2000	-2.0%	8.2%	-17.2%	-17.9%
Russell 1000 Growth	-4.7%	6.8%	-23.2%	-19.1%
Russell 1000 Value	-3.0%	3.5%	-9.9%	-6.3%

All about the macro, with Q2 earnings season out of the way, attention shifted to the Federal Reserve in August. The month was trending favorably for equity markets as the S&P 500 was up +1.8%[1] in the month through August 25th. Following Powell's speech, the S&P 500 would lose -5.8%[1] through month end, the worst 5-day stretch following the Jackson Hole Speeches since 2012.2 By month's end the S&P 500 would be down -4.1%[1] for August weighed down by technology stocks, a reversal from July's significant strength. Within large cap domestic markets, value-oriented indices outperformed their growth counterparts with the Russell 1000 Value index declining -3.0%[1] as compared to the Russell 1000 Growth index which lost -4.7%[1]. Small cap stocks beat large cap stocks in the month, while the growth-value performance differences were the reverse of large cap as small cap growth (Russell 2000 Growth) declined only -0.9%[1] while small cap value (Russell 2000 Value) dropped -3.2%[1].

INTERNATIONAL EQUITY *As of August 31, 2022*

INTERNATIONAL EQUITY MARKETS				
Index	1 Month	Quater-To-Date	Year-To-Date	1 Year
MSCI ACWI ex USA	-3.2%	0.1%	-18.3%	-19.5%
MSCI EAFE	-4.7%	0.0%	-19.6%	-19.8%
MSCI Emerging Markets	0.4%	0.2%	-17.5%	-21.8%
MSCI EAFE Small Cap	-4.4%	1.9%	-23.3%	-26.0%

Led by India, the MSCI India Index gained 4.4%[1], while the MSCI Emerging Markets index rose 0.4%[1] and was the star of the month, beating U.S. and developed market indices. Developed international markets modestly underperformed U.S. markets in the month as U.S. dollar strength continued, reaching the highest level versus its trade-weighted peers in over twenty years. The MSCI EAFE index lost -4.8%[1] in August, though those losses were paired back to -2.3%[1] when removing the impact of the stronger dollar. Like the U.S., small cap developed market stocks beat their larger peers as the MSCI EAFE small cap index lost -4.4%[1] in the month.

FIXED INCOME *As of August 31, 2022*

FIXED INCOME MARKETS				
Index	1 Month	Quarter-To-Date	Year-To-Date	1 Year
BarCap US Aggregate	-2.8%	-0.5%	-10.8%	-11.5%
BarCap Global Aggregate	-3.9%	-1.9%	-15.6%	-17.6%
BarCap US High Yield	-2.3%	3.5%	-11.2%	-10.6%
JPM Emerging Market Bond	-1.2%	2.0%	-17.2%	-18.8%
BarCap Muni	-2.2%	0.4%	-8.6%	-8.6%

With Fed Chair Powell throwing cold water on any notion of a pivot from current policy, interest rates continued to drift higher post Jackson Hole. Over the course of the month interest rates (10-Yr U.S. Treasury yield) rose by 55bps[1] to 3.20%[1], the highest level since mid-June. Meanwhile, the 2-Yr U.S. Treasury yield — a reasonable barometer for where markets expect the Fed's main policy interest rate to be six to nine months from now — rose by 60bps[1] to a fifteen year high of 3.5%[1]. Credit spreads were mixed as emerging market and investment grade debt spreads tightened, while high yield spreads widened modestly. So once again, the drivers in bond markets were rising interest rates, particularly on the short end, which left most bond markets with negative returns during the month. Against that backdrop, the Bloomberg Aggregate bond index declined -2.8%[1] in August, while the shorter duration profile of high yield bonds (Bloomberg High Yield Index) left the index with losses of -2.3%[1]. Meanwhile, like in equities, emerging market bonds outperformed with the J.P. Morgan Emerging Markets Bond index retreating only -1.2%[1] for the month. Fund flows in the municipal bond markets remain weak and Muni markets generally tracked the taxable bond markets in August as the Bloomberg Municipal Bond index returned -2.2%[1] for the month.

CLOSING

Markets enter September now with more information than less thanks to Jackson Hole. That said, macro uncertainty remains as investors seem to be awakening to the idea that the Fed is more prone to overshoot than to ratchet back, lessening the idea that the Fed can orchestrate a soft landing. For our part, we continue to believe that the combination of decades' low unemployment and corporate balance sheet strength are mitigants to the severity of any eventual recession. On the earnings front, visibility is similarly faced with increased uncertainty as expectations for 2023 continue to come down, but the earnings growth for the S&P 500 is still expected to grow by a healthy +8.2%[3], and that figure stood at +9.4%[3] as of June 30. Lastly, in the spirit of good news is bad news, core inflation (excluding food and energy) is trending down as higher interest rates gradually slow demand which will most likely have a negative impact on corporate profits. For investors the sum of these dynamics is likely to result in continued volatility in coming weeks — this is the "new normal" that investors need to anchor expectations on.

SOURCES

1 Bloomberg 8/31/2022
2 https://www.bloomberg.com/opinion/articles/2022-08-25/jackson-hole-federal-reserve-symposium-is-rarely-an-economic-waterloo
3 Factset Earnings Insight, August 5, 2022