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Markets

Last week, the Dow gained 3.2%, the S&P 500 rose 3.5%, and the Nasdaq advanced 3.4%, while the Stoxx Europe 600 rose 5.1%. The U.S. 10-year Treasury yield increased 10bps to 3.48%. In March, the S&P 500 rose 3.7% on multiple expansion and a modest increase in EPS. Growth styled equities increased +6.8%, which outperformed Value -0.5%, while Small Caps declined -4.8% and underperformed Large Cap +3.7%. From an industry sector perspective, 7 of 11 sectors within the S&P 500 delivered positive returns, with Technology and Communications gaining more than 10%, and Financials declining -9.6%.

For the quarter, the technology-heavy Nasdaq Composite increased more than 17.1% for the quarter, while the S&P 500 Index rose approximately 7.5%, MSCI Emerging Markets Index rose nearly 3.5%, while the Non U.S. developed index measured by MSCI EAFE returned +8.0%. In the U.S., growth stocks dominated value stocks for the quarter, with the Russell 1000 Growth Index returning 14.4%, in sharp contrast with the 1.0% return for the Russell 1000 Value Index.

Bond markets also provided positive returns across the board for the quarter, from Treasury indices through investment grade — both taxable and tax-exempt. Last week, the difference between two- and 10-year Treasury yields became more negative (a signal of a pending recession)—with short-term rates increasing more than longer-maturity yields—but the yield curve remained less inverted than in early March. There continues to be weakness in bonds issued by some real estate investment trusts (REITs) as commercial real estate concerns continue to emerge. For example, bonds issued by riskier office REITs remained under significant pressure and underperformed the broader market.

Rising oil prices helped energy stocks, which make up a significant part of value indexes. U.S. benchmark West Texas Intermediate crude oil rose more than 9% last week plus approximately 6% to above $81 as of 4/4/23. This is a meaningful move on the back end of the stress in the financial sector that had dragged oil prices as low as $67 in March. Elevated oil prices weaken the downward inflation and interest rate narrative investors have crafted for the Federal Reserve. Data released last week showed that the core personal consumption expenditures index — the Fed's preferred measure of inflation — softened in February. Investors are pricing in a better than even chance of a 25bps rise at the central bank's next meeting in May. The core PCE is the Federal Reserve's preferred measure of inflation. While the recent February 2023 reading of 4.6% was below the recent high of 5.4% reached in February 2022, it is still well more than the Fed's 2% long-term inflation target.

Risk and Opportunity

The relationships between actual events and future outcomes are imprecise and inconsistent for the results to be predictable. For example, three U.S. banks recently failed, requiring material government intervention in the face of sticky inflation, margin pressures, above long-term average P/E multiples and the S&P500 and tech heavy Nasdaq are up 7% and 17%, respectively during Q1 2023.

The uncertainty of the future is what creates risk. The catalyst event will meet, exceed, or disappoint market expectations. London Business School professor Elroy Dimson has said, "Risk means more things can happen than will happen."

Higher interest rates, economic uncertainty, fundamental weakness, bank sector volatility and geopolitical dynamics have many investors confused. We believe high quality fixed income and dividend focused equity strategies will help provide portfolio balance as the markets try to price the uncertainty of these various events.

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Disclosures

Investment Commentary Sources: Bloomberg and https://www.federalreserve.gov/newsevents/pressreleases/monetary20230312b.htm

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