Looking Back at Fourth Quarter, 2022 and Ahead to 2023

We continued to experience volatility in the markets during the fourth quarter of 2022. December saw a sell-off, reversing some of the bounce from October and November and leaving markets up for the quarter. Unfortunately, that only reversed a small part of the damage done earlier in the year. 2022 closed as one of the worst years in recent memory for financial markets. According to Argus research, in the 40-plus years since Ronald Reagan became president, stocks have turned in a positive performance almost 80% of the time. The average annual gain has been 13%. But 2022 was a clunker, as the S&P 500 entered a bear market and fell nearly 20% for the year. Even fixed income was down for both the month of December and the year.

The reason for the universal declines was the significant rise in interest rates during the year. With inflation running at a 40-year high, the Federal Reserve increased the federal funds rate from 0.08 percent at the start of the year to over 4 percent at year-end. Higher interest rates typically mean lower stock and bond values, which is just what we saw. Looking back, there was no place to hide last year.

While financial markets performed poorly, the economy actually did well in 2022. The fundamentals remained solid during the year, with job growth running much stronger than expected and consumer spending continuing to increase. Business sentiment and investment also improved. It was almost as if the economy and the markets were disconnected.

Looking ahead to 2023

The markets are more likely to generate normal returns than in the past three or four years, even if volatility remains high. The start of the year may be difficult, as the Fed continues to raise rates, the economy flirts with recession, and the Russian invasion of Ukraine continues. The Fed should gradually move to the sidelines and interest rates at the long and short end of the curve are likely to climb slower than in 2022.

Stabilizing interest rates will help equity valuations, which already have come down from elevated levels. Keep in mind that stocks historically have led the economy out of recessions, typically bottoming during the middle of the pullback. The S&P 500 has posted 13 down years out of the past 60. The years following the down years are up 77% of the time, and the average increase is 13%. Given low unemployment, we don't think an economic slowdown in 2023 will be particularly long or deep, allowing for an earnings recovery in the year’s second half. In addition, the third year of the presidential cycle is historically strong, as the party in power increases spending to help generate electoral momentum.

Big picture, 2022 was a terrible year. 2023 has its own challenges, but at this point, they look better than what we saw in 2022. And that is a good way to start the year.

Happy 2023!

Sincerely,

Mike

Nick

Michael R. Ovshak, CFP®
President, Owner

Nick Ovshak
Financial Advisor / Team Lead

This letter is a general communication being provided for informational purposes only. It is educational in nature and not designed to be a recommendation for any specific investment product, strategy, plan feature or other purpose. Any examples used are generic, hypothetical and for illustration purposes only. Prior to making any investment or financial decisions, an investor should seek individualized advice from a personal financial, legal, tax and other professional advisors that take into account all of the particular facts and circumstances of an investor's own situation.

The S&P 500 Index is a broad-based measurement of changes in stock market conditions based on the average performance of 500 widely held common stocks. The Nasdaq Composite Index measures the performance of all issues listed in the Nasdaq Stock Market, except for rights, warrants, units, and convertible debentures. All indices are unmanaged and investors cannot invest directly into an index.

Certain sections of this commentary contain forward-looking statements based on our reasonable expectations, estimates, projections, and assumptions. Forward-looking statements are not guarantees of future performance and involve certain risks and uncertainties, which are difficult to predict. Past performance is not indicative of future results. Diversification does not assure a profit or protect against loss in declining markets.

Parts of this commentary are authored by Mike Ovshak, President and Owner at FPS Financial, Inc.; by Nick Ovshak, Wealth Advisor; and by Brad McMillan, CFA®, CAIA, MAI, managing principal, chief investment officer, at Commonwealth Financial Network®