THE PRIVATE CLIENT GROUP

BALANCING LIFE & WEALTH

ECONOMIC & MARKET INSIGHTS

An Executive Summary for October 2022

After a difficult September, investors enjoyed a respite from the downturn in the capital markets. Global stocks surged on a wave of optimism as investors absorbed third quarter corporate earnings and hoped that the Federal Reserve and other central banks would slow the pace of monetary tightening. Fixed income again created headaches for investors as interest rates continued their upward trajectory. The yield curve remained inverted with short-term rates higher than long-term rates, a recessionary signal that has led to a rush of new money into cash and short-term fixed income.

Both the S&P 500 and developed market stocks advanced for the month. Emerging market stocks declined largely due to a drop in Chinese companies. The energy sector led the pack as company earnings far surpassed analyst expectations. Industrials and financials also outperformed. Lagging sectors included consumer discretionary and communication services. So far, third quarter earnings have been mixed, particularly in the technology sector. Overall profit margins have held up and earnings growth remains positive despite sharply rising costs. This modest good news was enough to drive the broad stock indexes higher. Stock market volatility was elevated with wide daily price swings, contributing to a VIX level above 30 for much of the month. Bond yields continued to push higher, resulting in negative returns across most bond markets. High yield, which often trades in line with equities, and inflation-sensitive TIPS were the only fixed income sectors to earn positive returns. U.S. Treasuries underperformed other government bonds as well as corporate and municipal bonds. Treasury prices have been volatile, affecting liquidity and pushing up financing rates for consumer credit. Default rates on corporate bonds have ticked up slightly but remain historically low. Most municipalities have healthy reserves and are well-positioned for an economic slowdown.

Politics were in the spotlight during October. The mid-term U.S. elections may result in a divided government that could put a damper on new legislation and create regulatory uncertainty. Chairman Xi consolidated power during the Chinese Communist Party Congress and seems poised to drive forward his political and ideological agenda even at the expense of economic growth. As China looks inwards and reshapes its economy, global supply chains and geopolitical relationships will be impacted. In the U.K., Rishi Sunak became the new Prime Minister and quickly began reversing the policies of his short-lived predecessor. The war in Ukraine grinds on while Russia has sowed instability by backing out of agreements to ease energy and grain shortages.

There was some good news for the Fed as it continues to fight inflationary pressures. Commodity prices have moderated, including energy prices which are a key inflation driver. The housing market appears to be slowing down with new construction and existing home sales weakening. Manufacturing and services business activity has declined. The labor market, while still stretched, shows signs of moderation, and wage growth is materially below inflation. As the next wave of the economic cycle commences, corporate layoffs will lead to downward pressure on wages. Pent up savings from the pandemic continues to support consumer spending but rising consumer credit levels suggest that this may be waning. The Fed has communicated mixed messages in recent weeks but appears determined to bring inflation closer to its 2% target. U.S. third quarter GDP growth at 2.6% was higher than expected and the latest Core PCE figure of 4.5%, along with solid employment and consumer data, suggest there is more work to be done to combat inflation.

Financial markets are being impacted by a shortage of capital triggered by the sharp rise in borrowing costs. M&A activity and the issuance of new securities have slowed to the lowest levels since the global financial crisis. This has raised concerns that some companies will struggle to cover rising interest costs. Liquidity has deteriorated in the U.S. Treasury market and the Fed is closely monitoring non-bank financial leverage for signs of distress. The recent turmoil in the U.K currency and government bond markets and a liquidity issue with Credit Suisse also raised alarms that a financial shock outside the U.S. could trigger a financial market crisis. Although corporate and consumer balance sheets are healthy, the Fed will have to consider these stresses as it contemplates future interest rate hikes. Portfolio diversification across and within asset classes while avoiding high volatility and leveraged investments has been essential to navigating the difficult economic and market environment.

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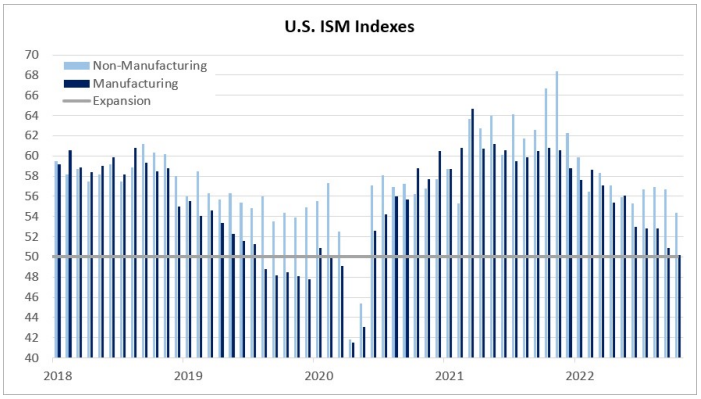

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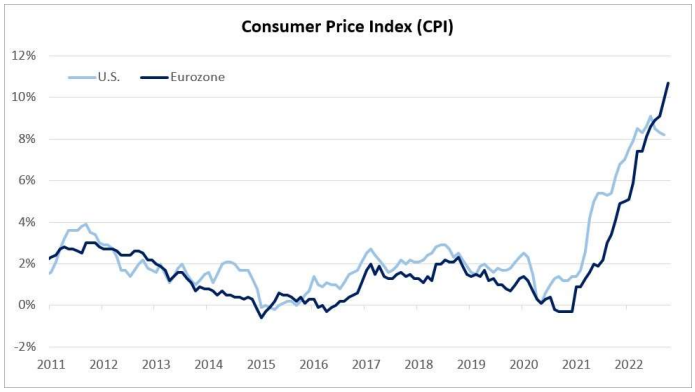
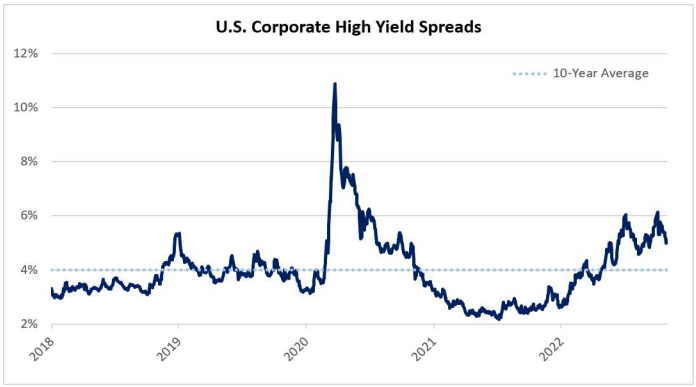


U.S. Bureau of Labor Statistics



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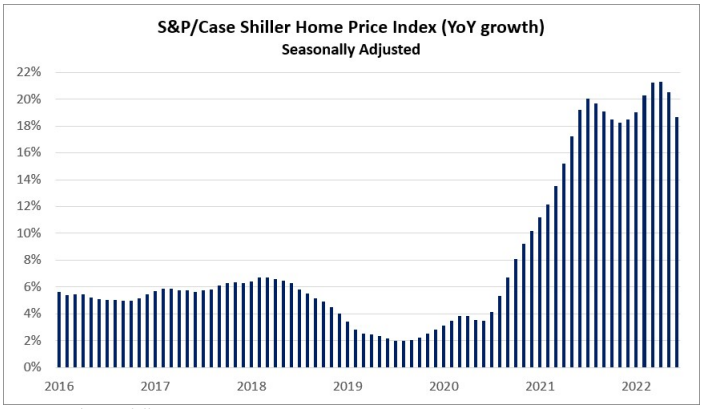
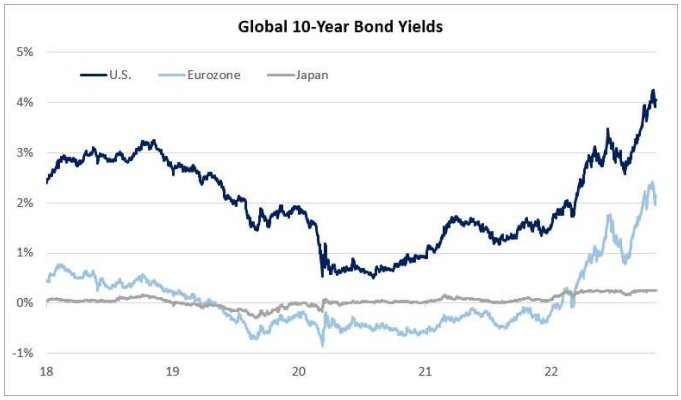


S&P / Case Shiller



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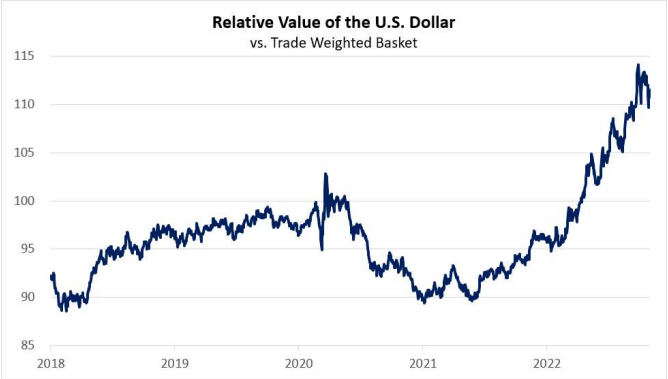

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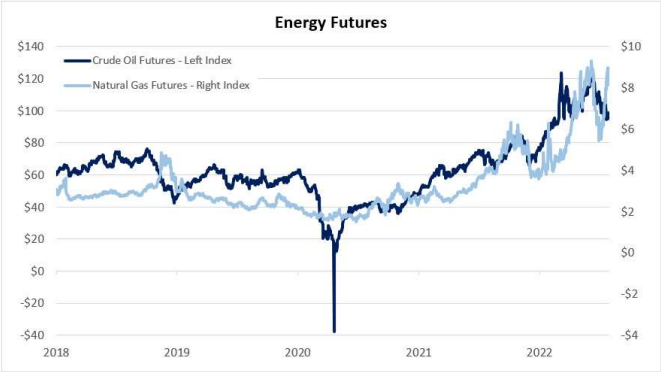

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The S&P Case-Shiller Home Price Index measures the value of single-family housing within the U.S. The index is a composite of single-family home price indices for the nine U.S. Census divisions. Leading economic indicators (LEI) are statistics that precede economic events. They predict the next phase of the business cycle. The OECD Composite leading indicators (CLIs), designed to anticipate turning points in economic activity relative to trend, continue to strengthen in most major economies. The Consumer Price Index (CPI) is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. The Consumer Confidence Index is a measure based on a survey administered by The Conference Board that reflects prevailing business conditions and likely developments for the months ahead. This monthly report details consumer attitude, buying intentions, vacation plans and consumer expectations for inflation, stock prices and interest rates. A Treasury Bill (T-Bill) is a short-term U.S. government debt obligation backed by the Treasury Department with a maturity of one year or less. The ISM manufacturing index, also known as the purchasing managers' index (PMI), is a monthly indicator of U.S. economic activity based on a survey of executives covering all North American Industry Classification System's businesses in the manufacturing sector. The ISM Non-Manufacturing Index is a monthly indicator of U.S. economic activity based on a survey of executives covering all North American Industry Classification System's businesses in the services (or non-manufacturing) sector. Data in this newsletter is obtained from sources which we, and our suppliers, believe to be reliable, but we do not warrant or guarantee the timeliness or accuracy of this information. Consult your financial professional before making any investment decision. Past performance is no guarantee of future results. Diversification/asset allocation does not ensure a profit or guarantee against a loss. Economic and market forecasts presented herein reflect our judgment as of the date of this presentation and are subject to change without notice. These forecasts are subject to high levels of uncertainty that may affect actual performance. Accordingly, these forecasts should be viewed as merely representative of a broad range of possible outcomes. These forecasts are estimated, based on assumptions, and are subject to significant revision and may change materially as economic and market conditions change. These forecasts do not take into account the specific investment objectives, restrictions, tax and financial situation or other needs of any specific client.

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