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Market Update: December 2022

Global stock markets declined by nearly 4% in December, closing out a down year on a down note. During the fourth quarter, stocks actually rallied, with U.S. and foreign equities advancing by 7% and 14%, respectively. When it was all said and done, however, equity investors had their worst year since the 2008 financial crisis … as their holdings lost about one-fifth of their value.

Bonds were relatively flat for the month, but like stocks, rallied during the fourth quarter. Still, for the year, investors registered double-digit losses in what is considered to be the worst year on record for fixed income markets. The yield on the 10-year U.S. Treasury note ended the year at 3.826% … well above the 1.496% yield at the end of 2021. *(Remember, bond prices fall as yields rise.)*

> **The story for the U.S. economy this year has largely been about battling record-high inflation, which has left both equity and fixed income markets bumpier than a ride on Santa's sleigh.**
>
> **J.P. Morgan Asset Management – Market Insights 12/26/22**

Higher interest rates hurt some of the most popular investment plays of the past few years, most notably technology shares. The technology heavy Nasdaq Composite Index lost one-third of its value in 2022. Cryptocurrencies and other speculative assets imploded, culminating in the recent collapse of the crypto exchange FTX. Has anyone talked about meme stocks, SPACs or NFTs lately?

> **How did things go so badly? In short, investors and policy makers were burned by bets that 2021's inflation surge would prove to be transitory.**
>
> **Akane Otani – WSJ 12/30/22**

The U.S. economy continues to downshift, as inflation eases and consumer spending softens. The personal-consumption expenditures price index (PCE deflator), the Federal Reserve's preferred measure of inflation, rose 5.5% in November from a year earlier, down from the 6.1% rise in October. On a month-to-month basis, the PCE deflator rose 0.1% in November, decidedly below October's 0.4% increase.

The Commerce Department also reported earnings for the average American rose 0.4% in November, well ahead of the rate of inflation. However, consumer spending increased only 0.1% during the month. Spending was basically flat for the month, when adjusted for inflation, and well below the 0.9% advance in October. Overall, households are currently spending less on goods but more on services.

> **It's the latest bit of conflicting data that has left investors with a muddled outlook going into 2023.**
>
> **Nicholas Jasinski – Barron's 12/23/22**

The Fed hiked the benchmark federal-funds rate by 50 basis points (0.5 percentage point) and signaled plans for more hikes going forward. The increase was less than the previous four consecutive 75 basis point hikes and raised the rate range to between 4.25% and 4.5% … a fifteen year high. Economic projections suggest the rate will peak at levels between 5% and 5.5% in 2023, and hold there until sometime in 2024.

> **Rate increases work with what economists call long and variable lags, which means the central bankers may not know for a year or more if they have tightened too much or not enough.**
>
> **Nick Timiraos – WSJ 12/14/22**

Economic data suggests that the economy is slowing down, and inflation data and labor markets are clearly cooling off. So, it's not surprising that investors seemed somewhat baffled by the Fed's hawkish messaging at its December meeting.

> **After raising interest rates by the expected half-percentage point on Wednesday (Dec 14), Fed Chairman Jerome Powell and his colleagues laid out an economic and interest-rate forecast premised on a painful, drawn-out battle with inflation completely at odds with the markets.**
>
> **Greg Ip – WSJ 12/15/22**

Central banks around the world are raising interest rates as they battle inflation. Just two years ago, the world-wide sum of negative-yielding debt was greater than $18 trillion. The total currently stands at just $271 billion, with most of the remaining debt being held by Japan.

> **Negative yields on government bonds look like they are about to ride off into the sunset.**
>
> **Matt Grossman – WSJ 12/28/22**

Japan's core inflation rate rose in November at the fastest pace in over 40 years. While the Bank of Japan still maintains a target interest rate in negative territory, it surprised markets by allowing the yield on the 10-year Japanese government bond to rise as high as 0.5%. Before the decision, 137 yen was needed to buy a dollar on foreign-exchange markets … at the beginning of this year, the dollar was trading at approximately 115 yen.

> **The inflationary forces that pushed the U.S. into rapid clampdown mode proved so powerful that even Japan's central bank, which long stuck to near-zero rates, felt it had to budge – in part to protect the value of the yen, analysts said.**
>
> **Megumi Fujikawa – WSJ 12/20/22**

Existing home sales in the U.S. declined in November for the 10th straight month, as rising mortgage rates and high prices have driven many buyers out of the market. According to the National Association of Realtors

(NAR), November sales were down 7.7% from the previous month and 35.4% from a year earlier.

According to the Mortgage Bankers Association, the monthly mortgage payment for the median U.S. priced home was up 43% in November from the beginning of the year.

Mortgage rates, which were around 3% to start the year, have more than doubled this year … the largest increase in any calendar year.

At 3%, a borrower purchasing a home for $500,000 with a 20% down payment would pay $207,000 in interest over the life of a 30-year mortgage. At current mortgage rates, total interest payments would be around $500,000 over that same period.

> **That has paralyzed people. If you say yes to a higher mortgage rate, you say no to savings, to travel and to just living comfortably within a budget.**
>
> **Justin Lopatin, Guaranteed Rate – WSJ 12/29/22**

While prices have dropped recently, they are still higher year-to-date as the supply of homes for sale remains at low levels. The median existing-home price in November was $370,700 according to the NAR … up 3.5% from a year earlier, but down from the $413,800 record high reached in June.

> **As the Federal Reserve continues to move interest rates higher, mortgage financing continues to be a headwind for home prices. Given the continuing prospects for a challenging macroeconomic environment, prices may well continue to weaken.**
>
> **Craig Lazzara, S&P Dow Jones Indices – WSJ 12/27/22**

China's economy continued to struggle in November, as Covid-19 restrictions shackled retail sales, and industrial production was restrained by declining overseas demand. Looking ahead, an economic turnaround is expected as Covid controls are loosened and China reopens its economy.

While reopening the economy presents an immediate threat to the overall health of China's population, faster growth in China for 2023 should help to lessen the global economic strain from the recessions that are anticipated for the U.S. and Europe.

> **The downbeat data illustrates the growing pressure that faced China's leaders as they made the decision to quickly dismantle a draconian approach to suppressing the coronavirus, which was in place for almost three years … a policy reversal that caught both Chinese citizens and overseas investors off guard with its speed and breadth.**
>
> **Douglas/Hua – WSJ 12/15/22**

The dollar, as measured by the Wall Street Journal Dollar Index, has risen in value by nearly 9% against 16 other currencies. Rising U.S. interest rates have attracted investors to the dollar. Since the dollar is the primary currency for trade and finance, its pricing has worldwide implications.

> **While the major emerging markets didn't experience anything near a crisis, there is a quieter crisis that has hit many parts of the world, especially a lot of low-income economies that don't tend to get a lot of attention. For many of them the surge in food and commodity prices, both of which tend to be significantly denominated in U.S. dollars, was an enormous hit.**
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> **Eswar Prasad, Cornell University – WSJ 12/29/22**

This is the time of year when everyone gives their predictions for the coming year. Apparently, the consensus expects a recession in Europe and the U.K. Most anticipate one in the U.S. as well … although some believe it could be "mild" at worst. A survey of economists and investors by the Federal Reserve Bank of Philadelphia suggests that GDP will fall in three or four quarters.

> **Just because economists are convinced of their predictions doesn't mean they are right, of course. Since the Philly Fed survey started, not a single recession was spotted a year in advance. Economists missed the 1990, 2001, and 2008 recessions completely.**
>
> **James Mackintosh – WSJ 12/4/22**

Almost everyone got their predictions for 2022 wrong. Wall Street pundits anticipated a year of modest positive returns, instead U.S. equities lost $12 trillion in market value. Five technology stocks alone accounted for about a quarter of the declines.

> **A number of investors were trying to justify nosebleed valuation levels. Now, leadership going forward is going to be more diverse.**
>
> **John Linehan, T. Rowe Price – WSJ 1/2/23**

Remember, diversification and discipline are the best ways to deal with market uncertainty. We should anticipate ongoing market turbulence as inflation diminishes and the economy begins to stabilize.

I hope you all had a happy and healthy holiday season.

Daniel G. Corrigan, CPA/PFS, CFP®