PDS Wealth Management

Quarterly Investment Report – Q3 2022

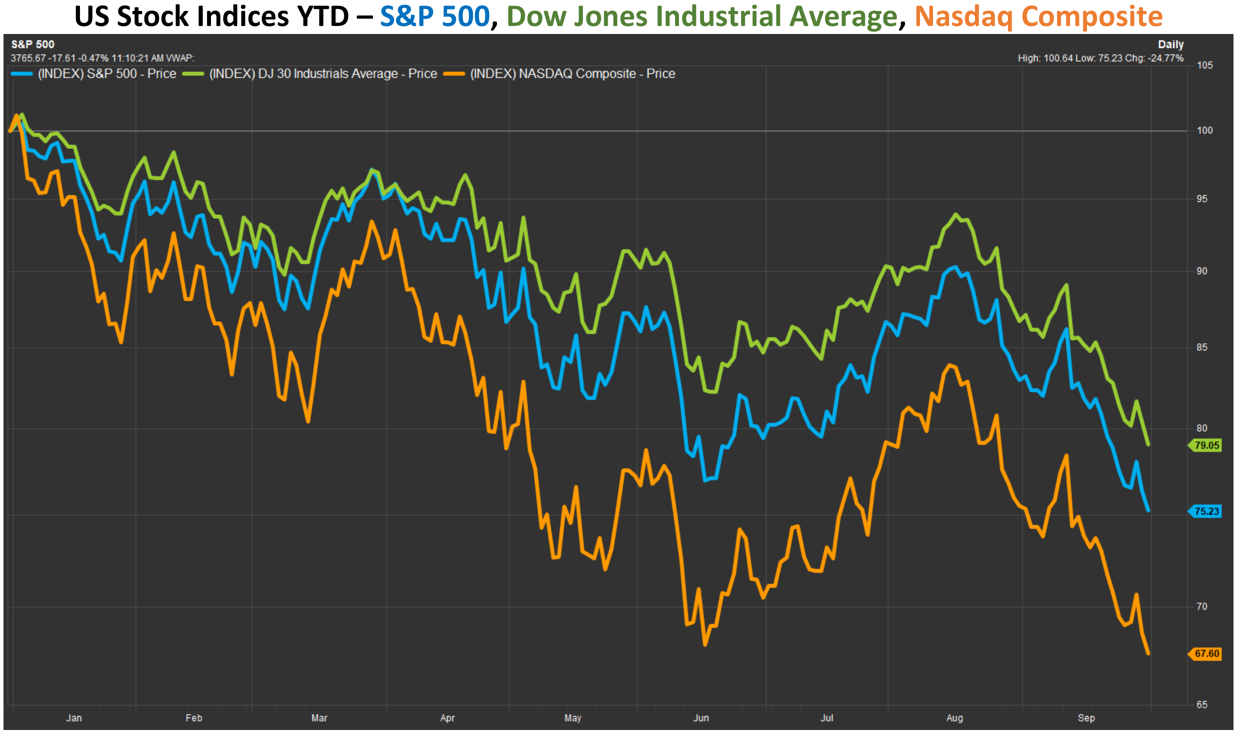
It was another rough quarter for investors. Stocks enjoyed a respectable rebound from mid-July through mid-August, but ended September near the lows of the year. Stock, bond, commodity, and currency markets are swinging wildly, buffeted by a constant stream of dour geopolitical and economic headlines. The list of worries is long, but well-telegraphed by now – war, China tensions, COVID, high inflation, rising interest rates, and recession risk, to name a few.

Is there anything that could go right? Rather than add to the cacophony of doom, we attempt to highlight some potential positives below.

Markets Review

Stocks

US Stock Indices YTD – S&P 500, Dow Jones Industrial Average, Nasdaq Composite



Source: FactSet

The 3rd quarter of 2022 was another tough one for stocks and bonds. Markets managed a 17% rally in the early half of the quarter, but stocks sold off hard in August. For the quarter, the S&P 500 dropped 4.9%, the Dow Jones Industrial Average fell 6.6%, and the Nasdaq lost 3.9%. The only sectors to post positive returns in Q3 were consumer discretionary and energy. Communication Services and Real Estate both fell more than 10%.

So, what may come next for stocks? The below chart may offer some perspective. It comes from Ryan Detrick, Chief Market Strategist at Carson Investment Research, and shows forward returns for the S&P 500 following the worst starts to a year. History doesn't always repeat, but it may not be the worst time to be an investor in stocks.

Wake Me When September Ends

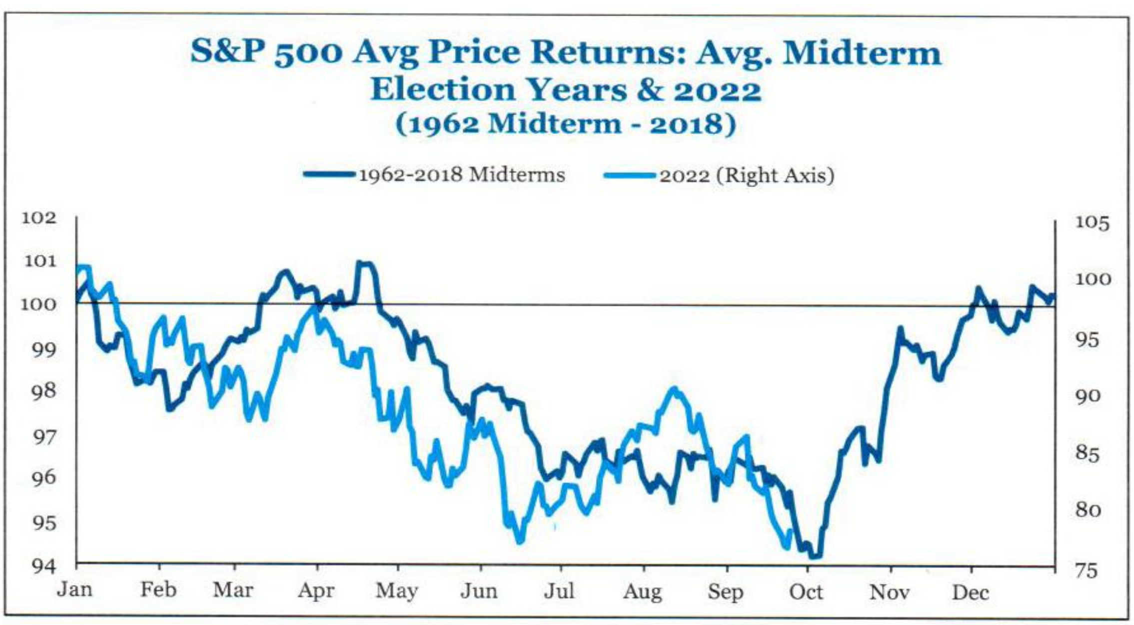
10 S&P 500 Worst Starts To A Year Ever (End September) And What Is Next

		S&P 500 Future Performance		
Year	YTD End Of September	Next Quarter	Next Two Quarters	Next Four Quarters
1974	(34.9%)	7.9%	31.2%	32.0%
2002	(29.0%)	7.9%	4.0%	22.2%
2022	(24.8%)	?	?	?
1962	(21.4%)	12.1%	18.3%	27.4%
2001	(21.2%)	10.3%	10.2%	(21.7%)
2008	(20.6%)	(22.6%)	(31.6%)	(9.4%)
1966	(17.2%)	4.9%	17.8%	26.3%
1981	(14.4%)	5.5%	(3.6%)	3.6%
1990	(13.4%)	7.9%	22.6%	26.7%
1953	(12.1%)	6.3%	15.4%	38.4%
1960	(10.6%)	8.6%	21.6%	24.7%
	Average Return	4.9%	10.6%	17.0%
	Median Return	7.9%	16.6%	25.5%
	% Positive	90.0%	80.0%	80.0%

Source: Carson Investment Research, FactSet 10/04/22 (1950 - Current)
@ryandetrick

Source: Twitter, Carson Investment Research

Another potential encouraging tailwind for stocks is seasonality. Stock markets have historically bottomed in October in mid-term election years, in which we currently find ourselves.



Source: Strategas Research Partners

Bonds

Bonds fell in tandem with stocks for the third quarter in a row - the first occurrence in history where both asset classes have fallen in tandem for three straight quarters. With falling bond prices comes more attractive yields, however. During the quarter, the yield offered by 2-year Treasury Notes improved 130 bps to 4.22% while the yield on the 10-year Note increased by 88bps to 3.86%.

Since we're highlighting potential positive indicators, the yield available from high yield bonds compared with treasury bonds, the "spread," has not spiked as it has in previous economic downturns, perhaps a sign that corporate fundamentals remain healthy.

High Yield Spreads

Source: St. Louis Fed

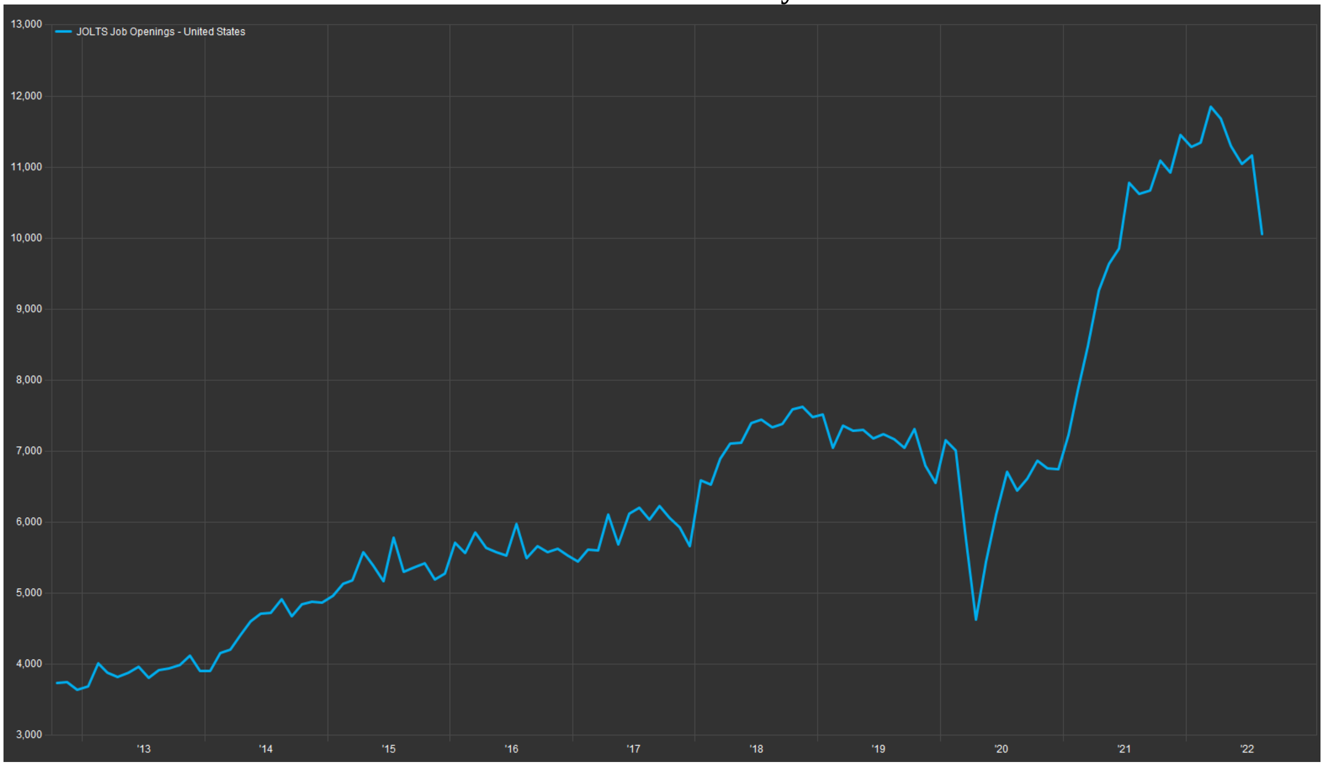
Economic Review

As expected, the Federal Reserve raised rates by 0.75% at both its July and September meetings, leaving the Fed Funds target range at 3.0% - 3.25%. We are now in a perverse environment where good economic news is viewed negatively by the markets as it gives the Fed more cover to continue their aggressive rates hike path. Investors are cheering for poor economic data in the hopes it will lead the Fed to ease up on its hiking cycle.

Employment

Job growth remains strong and the unemployment rate hovers near historic lows at 3.5%. There are too many job openings when compared with the number of people looking for them, which is keeping upward pressure on wages, and thus, inflation. However, the "slack" is improving as evidenced by the modest decline in job openings reflected in the below JOLTs survey data.

JOLTS Survey

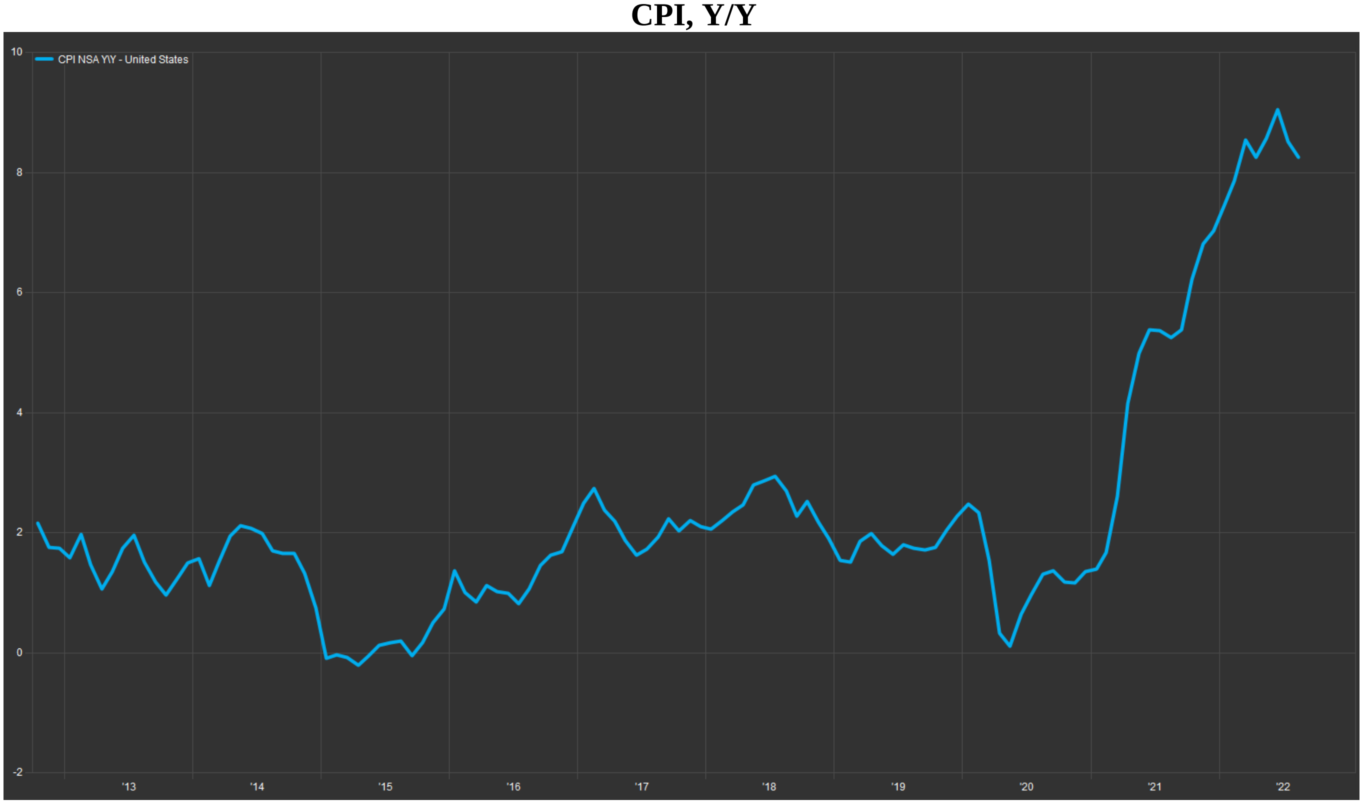


Source: FactSet

Inflation

While the pace of year-over-year price increases has moderated, inflation continued to come in above expectations in Q3, as seen in the chart of CPI below. This needs to come down before the Fed can take a pause.

CPI, Y/Y



Source: FactSet

We hope you're able to find a few nuggets of positivity in this report.

Best of luck as we close out '22!

Paul Spencer, CFA®

Director

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