Market Commentary

April 2022

Equity and Bond Market Update

(as of April 5, 2022)

Index	YTD	1-Year
Dow Jones Industrial Average TR	-4.2%	+6.5%
S&P 500 Total Return Index	-4.7%	+14.2%
Russell 2000 Total Return Index	-8.6%	-8.3%
MSCI EAFE Index (net)	-6.8%	-1.9%
MSCI Emerging Markets Index (net)	-6.1%	-13.4%
Barclays US Aggregate Bond TR	-7.0%	-5.5%

Recent Economic Indicators

	Statistic	Data as of
Unemployment Rate	3.6%	Mar 2022
Gross Domestic Product (GDP)	+6.9%	Q4 2021
Consumer Price Index (CPI)	+0.8%	Feb 2022
Consumer Confidence (1985=100)	107.2	Mar 2022
30-year fixed mortgage rate	4.89%	4/5/2022
Housing Starts (single family)	1,034,000	Feb 2022
10-Year Treasury Yield	2.42%	4/4/2022

Equity markets rallied during the second half of March, with all of the major equity indices, both foreign and domestic, gaining between 6% and 9% in the last two weeks of the month. As of today, all of these indices have retraced close to half of the pullback we experienced this year up to that point. Bonds, in aggregate, continue to see downward pressure as the Fed has begun, and signals the continuance of, raising short-term interest rates.

Even though we have seen a few down days to start out April, we have firmly set some strong S&P 500 Index support levels around 4,300 (we are currently trading around 4,465). We have discussed in past commentaries that corporate earnings are the main contributor to stock market performance, so where do we currently stand? Over the last few years, including pre-COVID, the S&P 500 Index was already trading at pretty lofty levels. The COVID-induced recession & recovery, paired with a quick and deep bear market and recovery was a good reset to bring market levels back to historical valuation averages. Currently, the S&P 500 Index is trading a bit overvalued based on 2021 earnings, but at fair value based on 2022 expected earnings and undervalued based on 2023 expected earnings. A Fed-created recession would negatively affect earnings into 2023, and that is a good reason why we are trading at a discount to that year's forecast.

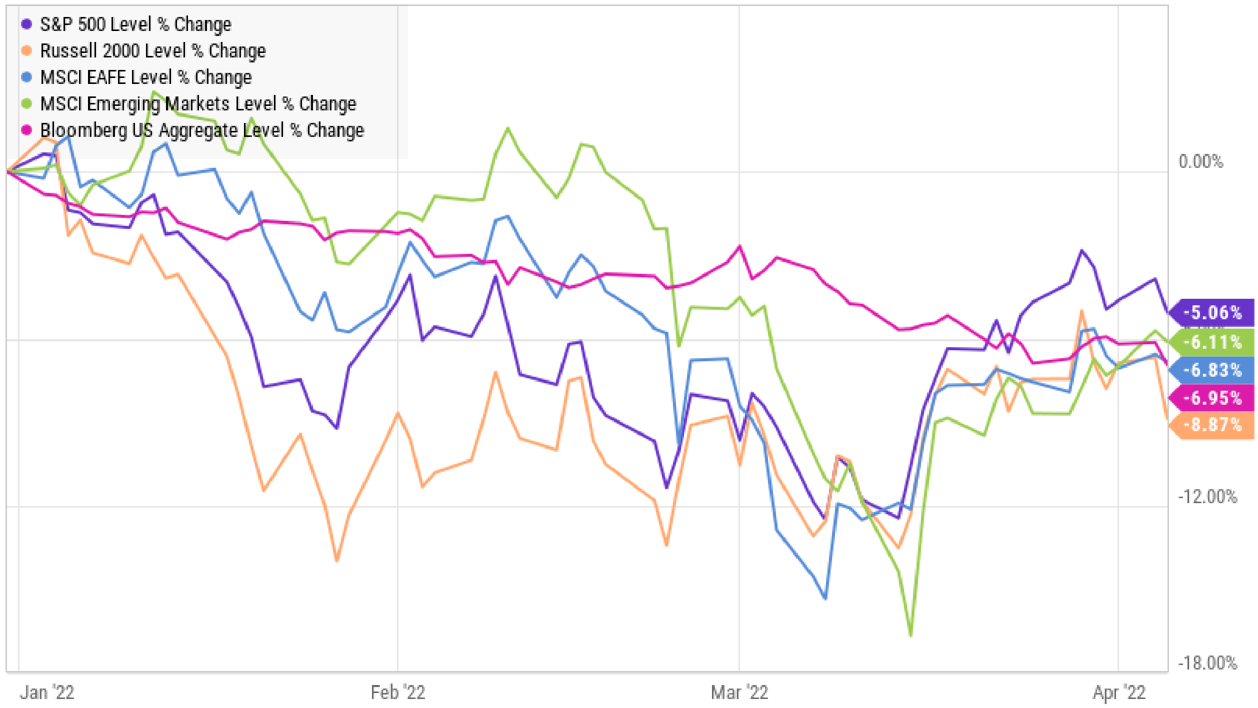
The sectors of the market that are performing better than the average this year include energy (+36%), utilities (+7%), and consumer staples (+1%). Sectors that are underperforming this year include consumer discretionary (-13%), communications services (-13%), and technology (-12%). The real estate sector also is outperforming the general stock market by about +1.5%. Value has outperformed growth in 2022 by about 10 percentage points. We expect this to continue into the coming months, but an underperforming growth market also signals great buying opportunities for longer-term investors.

The bond market, as previously mentioned, has been struggling since around September of last year. We started seeing increased inflation numbers around the first quarter of 2021, and if we recall were described as "transitory", and to a certain extent they were. However, once these inflationary pressures persisted, and then heated up even further around September of last year, the bond market reacted with higher yields coming into play (as a result of expected Fed movement discussed in the next paragraph), and hence downward pressure on bond prices. We currently feel this struggling bond market has reached its peak downward pressure due to expectations and going forward losses have been baked in.

Currently, it is expected that the Federal Reserve will hike interest rates at each of their remaining 2022 meetings, of which there are six remaining. If there are 0.25% hikes at each remaining meeting, we would be sitting at 1.75%-2.00% by the end of this year. However, with current levels of inflation hitting multi-decade highs over the last few months, we may see some of these meeting decisions go to 0.50% hikes instead of 0.25%. The expected policy would be to get rates as quickly as possible to the current estimated terminal rate of between 2.50% and 2.75% by the end of next year.

There is much discussion about the current state of the yield curve, and its potential signaling of a coming recession. Many are already saying that we are seeing an inversion of the yield curve since there has been a negative spread between the 2-year Treasury yield and the 10-year Treasury yield. We did see a very brief negative spread at the beginning of April, but that has since gone positive (albeit still very

Major Market Indices Price Return (YTD through April 5, 2022)



small at +11bps spread). We like to alternatively watch the spread between the **3-month** Treasury yield and the 10-year Treasury yield, which currently sits at +194bps. The reason we have such a relatively large spread between the 3-month and 10-year Treasury yield is because we are still in an accommodative environment with very-short term yields still close to zero, coupled with a 10-year rate of 2.65% that is closer to the aforementioned Fed terminal rate of 2.75%. Through the next couple of years, as the Fed increases short-term rates, this spread will tighten, and potentially go negative. As a precursor to any of our last six recessions going back to the 1970s, we have never seen a recession take place while this 3-month to 10-year spread remained positive. Given this, we do not anticipate any recession taking place until at least the latter part of 2023.

Lastly, some thoughts about the Russia-Ukraine conflict. We have recently seen some very horrific images and video coming out of certain regions in Ukraine. The main issue this conflict has on our markets really has to do with how long this will last, and that is most certainly something nobody has an answer to at this time. Currently, aggregate foreign and emerging markets, as well as small-cap U.S. stocks are the only markets that have retreated since the invasion started in late February, but only by a slim -1% - 2% margin. Large-cap U.S. stocks, on the other hand, are up about +3% during the same time period. We remain underweight in emerging markets due simply to the risks involved with carrying Russian and Chinese equities. Exposure to developed countries remains at an equal weight.

Always keep in mind that fear, panic, and optimism are not investment strategies, but rather emotions that drive short-term markets.

Please contact Lifestyle Asset Management, Inc. at (281) 612-2035 or by email at **pjackson@lsaminc.com** should you have any questions or comments.

Sources:

S&P Dow Jones Indices website (us.spindices.com)
MSCI Barra website (http://www.mscibarra.com)
The Conference Board (www.conference-board.org)
Bureau of Economic Analysis (www.bea.gov)
JP Morgan Guide to the Markets
FTSE Russell (www.ftserussell.com)
Bankrate.com (www.bankrate.com)
Bureau of Labor Statistics (www.bls.gov)
United States Census Bureau website (www.census.gov)