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Market Review **DECEMBER 2022**

"Last year was definitely a year for the history books. But the Santa Claus rally delivered all its joyous cheer to the markets. History generally indicates that market returns tend to be attractive when Santa comes to town."

The Santa Claus rally is said to occur during December's last five trading days and the first two in January. These seven market days generally provide investors with positive returns, according to research that dates back to the 1950s. But, of course, there are always exceptions to the heuristic in non-ordinary times. For example, the Santa Claus rally lost big in 2000 as the dot-com bubble began to prick. Another poor outlying year occurred in 2008 during the severe economic recession. Nevertheless, this year's (2023) Santa Claus rally ended well with positive returns, consistent with history and potentially indicating a solid foundation for the remainder of the year.

Entering last year (2022) seemed like business as usual. However, inflation had already hit a 40-year high, and some signs of weakness were starting to pop up in specific regions and sectors of the equity markets. Still, and probably of significant importance, the Federal Reserve's forward guidance maintained that inflation was transitory that kept interest rates at bay. It wasn't until March that the Federal Reserve started to acknowledge the real danger of persistent inflation and began to move rates higher in response.

The rest of last year is probably best characterized as possessing consistent uncertainty and volatility as interest rates climbed to levels not seen in over a decade. As a result, asset prices built to live in a zero-percent interest rate world quickly re-rated to reflect the new reality. Investors stood by and watched as stock markets fell into a bear market, defined as prices that have declined over twenty percent from the prior high mark. Complicating matters further were the Russian invasion of Ukraine and Chinese policy towards zero-covid. Both impacted inflation in unique and particular ways, with the Ukraine crisis affecting energy prices and China hitting supply chains.

Another critical event touching people's lives in 2022 was the US mid-term election. The elections may not have ended as most experts might have predicted, but the historical pattern of stocks in a mid-term year seemed to meet the general expectations. Observing stock market behavior in mid-term years going back in time reveals that stocks tend to sell off ahead of mid-term elections. And, sure enough, last year was consistent with history as US large-cap stocks bottomed in October, right before November's election. Fortunately, history indicates that stock market years following a mid-term election tend to be good. In addition, the stock market has put up some of its best years historically when the White House has a Democrat and Republicans control the Congress. Of course, history doesn't always repeat itself.

What has challenged markets until now certainly did not simply disappear at the stroke of midnight on New Year's Eve. For instance, the Federal Reserve remains hawkish, meaning interest rates could get to five percent, and the Fed still plans to shrink its balance sheet. Additionally, inflation maintains above what the savings rate is on bonds. However, the future outlook is looking better as job demand and wages remain robust despite what the Fed has done to the credit markets. Also, now that mortgage rates have gotten to sub-seven percent, housing price increases in the inflation data are expected to slow. Softer housing gains could lead to more modest inflation prints in the future. Some experts even believe that if analysts strip energy, food, and housing from the inflation reports, the economy could potentially be looking at deflation. Those sorts of findings might lead the Fed to pause or reverse course on some of its latest policy changes. In any event, today's market prices likely reflect some possibility of a policy pivot.

Last year was definitely a year for the history books. But the Santa Claus rally delivered all its joyous cheer to the markets. History generally indicates that market returns tend to be attractive when Santa comes to town. Maybe it's excessive optimism, or just plain luck. But everyone can probably agree that 2023 has the potential to deliver better investing outcomes relative to 2022, especially if progress can be made with the economy, inflation, and interest rate policy.

Asset Categories	US STOCKS	FOREIGN STOCKS	US BONDS	FOREIGN BONDS	HARD ASSETS	HYBRIDS
Monthly	-5.31%	-1.68%	-0.49%	0.81%	-3.36%	-2.17%
Year to Date	-15.74%	-19.03%	-9.60%	-14.17%	-10.79%	-16.16%

*DATA USED IS SOURCED FROM MORNINGSTAR®, DATE ENDING DECEMBER 31, 2022.

US STOCKS

US Stocks lost more ground in December, despite the Santa Claus rally of the last few days in the month. Large-, mid-, and small-cap losses were similar and generated a -5.31% average loss in December. Year-to-date losses among the group were closely aligned, too. However, mid-caps outperformed in 2022 with losses of -14.01%, but better than the average annual loss of -15.74% from all three category averages combined.

FOREIGN STOCKS

Foreign Stocks rolled returns back in December similar to the domestic markets. However, the monthly loss wasn't as sharp relative to US stocks. In December, the average loss in the foreign categories was only -1.68%. That brought the year-to-date average back down to finish 2022 with a -19.03% loss. Year-to-date losses from developed market stocks mirrored US stock losses; it was the emerging markets and small caps that lost most value for the year.

US BONDS

US Bonds experienced only modest losses in December. This category average finished last month with an average loss of -0.49%. However, bank loans provided investors with a slight gain in December. Overall, virtually all bond categories declined in 2022. Bonds suffered from inflation and the sudden rise in interest rates, and those bonds with the longest maturities were generally hurt the most.

FOREIGN BONDS

Foreign Bonds generated some modest gains in December. Overall, the category's average monthly return was 0.81%. Emerging market bonds have started to see some life again as they've experienced gains in two consecutive months. Yet, emerging market bonds lost -14.50% in 2022, while the global bond category average declined -13.84% over the same time period.

HARD ASSETS

Hard Assets performed poorly in December, resulting in an average monthly loss of -3.36% for the category. Energy and real estate were among the hardest hit areas—both experienced losses exceeding -5% for the month. Hard assets provided some diversification with a -10.79% year-to-date loss. Energy was essentially the only hard asset sector that generated a gain in 2022, while the other hard asset categories suffered losses that were in the double digits.

HYBRIDS

Hybrid Assets fell another -2.17%, on average, in December. The category was weighed down by more underperformance from convertible debt. Convertible bonds generated -17.50% in investor losses in 2022. Year-to-date performance in preferred stocks succumbed to a -14.82% loss. Overall, the category's performance fell by -16.16% as the average year-to-date return.

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