Market Perspectives
March 2023

KEY HIGHLIGHTS

- March marked the 1-year anniversary of the Fed's current tightening cycle.
- Fed hikes again in ongoing fight to tame persistent yet falling inflation.
- Banking crisis averted?
- The yield curve remains inverted.
- Despite ongoing volatility, markets posted strong returns for the month.

FIGHTING INFLATION

Just over one year ago, in March of 2022, the Federal Reserve began the fight against inflation and hiked the fed funds rate by 0.25% ushering in a new tightening cycle. Fast forward to March 22, 2023, and the Fed announced their ninth consecutive hike bringing the federal funds target rate to 4.75%-5.0%. The Fed's goal of taming persistent inflation resulted in a pace and magnitude of rate hikes over the past year that has not been witnessed in decades. This in turn led to dismal performance of both stocks and bonds in 2022. There has been deep debate on whether the Fed has done too much or not enough to squash stubborn inflation. Given that rate hikes typically take many months to be felt in the

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economy, we feel we are in the ninth inning of this tightening cycle as data show inflation is now firmly moving in the right direction. February CPI fell to 6% which is down substantially from the peak of 9.1% set in June of 2022. While the labor market remains strong, there are signs of softening in the data which lead to a higher probability of a Fed pause in the coming months.

BANKING CRISIS

Inflation concerns and the Fed's ongoing response to them were overshadowed by the unexpected banking crisis and accompanying liquidity scare that came to light on March 10th. Both Silicon Valley Bank (SVB) and Signature Bank (SBNY) failed in extraordinary fashion due to a combination of extensive duration risk in their respective bond portfolios and a run on the bank from depositors. The situation was circular in nature and as their stock prices fell, depositors pulled funds requiring the banks to sell securities at steep losses (due to rise in rates) to fund the withdrawals. This led to the run on the bank scenario, and fears of contagion worsened matters across the banking industry. To remain solvent, First Republic Bank (FRCB) received lifelines from larger banking

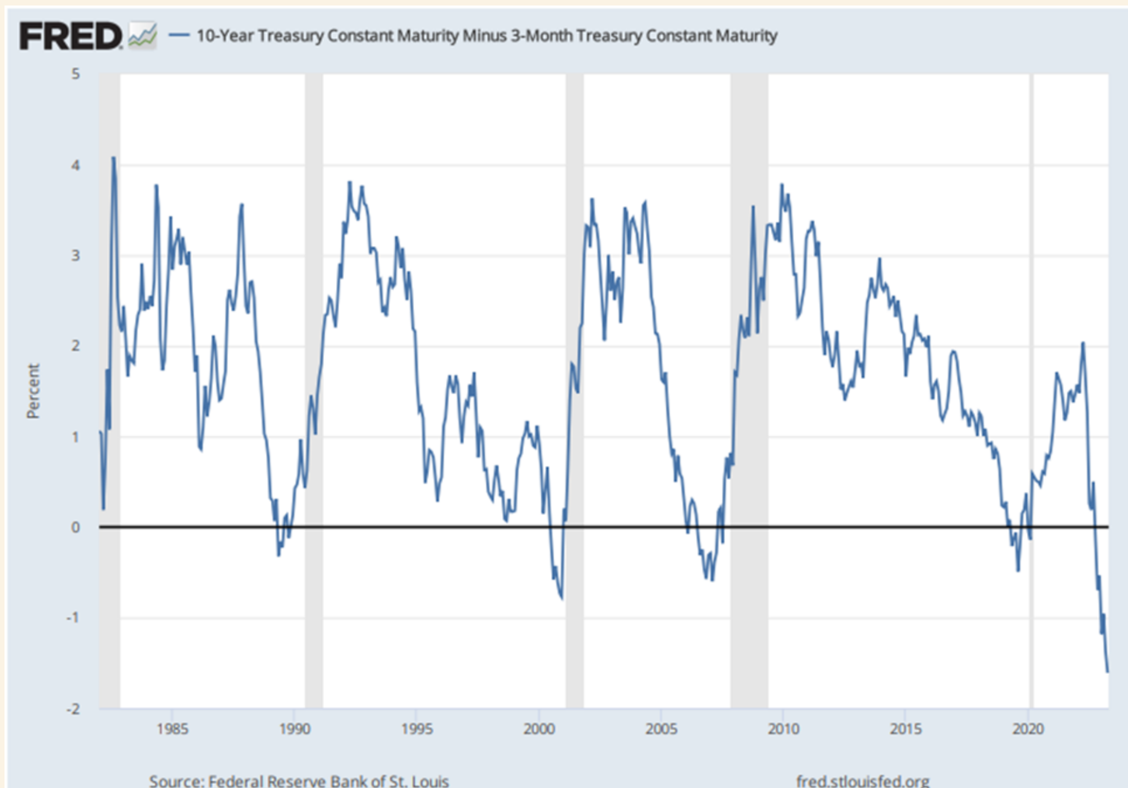
Index	MTD	QTD	YTD	1 Year	2022
S&P 500	3.67	7.50	7.50	-7.73	-18.11
Dow Jones Industrial Average	2.08	0.93	0.93	-1.98	-6.86
Russell 2000	-4.78	2.74	2.74	-11.61	-20.44
NASDAQ Composite	6.78	17.05	17.05	-13.28	-32.61
Europe, Australia, & Far East (EAFE)	2.61	8.62	8.62	-0.86	-14.05
MSCI Emerging Markets	3.07	4.02	4.02	-10.30	-19.78
Bloomberg Barclays U.S. Aggregate Bond	2.54	2.96	2.96	-4.78	-13.04

As of 3.31.23; Returns in percent

institutions, and Credit Suisse (CS) was bailed out by the Swiss government and ultimately UBS agreed to purchase CS for $3 billion, a fraction of its former valuation. Regulators acted swiftly to shore up the banking system and avoid/ minimize contagion risks by implementing the Bank Term Funding Program (BTFP) and other lines of additional forms of banking liquidity. Stability and confidence in our banking system are of paramount importance to the economy. We continue to closely monitor the evolving banking situation and the potential contagion in other areas such as commercial real estate.

THE TEN YEAR SPREAD

The 10-year Treasury bond finished the month yielding 3.47%, down from 3.92% at the end of February. As investors know, bond prices rise as yields fall and vice versus. Despite this recovery in bond prices, the yield curve remained inverted. An inverted yield curve has historically been a reliable indicator that a recession is likely to occur in the next 12 months. The often quoted 10-year and 2-year spread ended the month at -0.58% while the more accurate recession predictor, the 10-year and 3-month spread closed the month at -1.37%. This is the steepest inversion since 1980 for the latter.



Source: FRED as of 3.31.23

STAYING POSITIVE

Even with ample volatility, a ninth consecutive rate hike, hawkish Fed narrative, a banking crisis and an inverted yield curve, stocks and bonds climbed a wall of worry and rallied in March. The S&P 500 finished the month up 3.67% for the month and 7.48% for the quarter. Even beleaguered bonds were buoyed, and the U.S. Aggregate bond market posted a gain of 2.54% for the month, a welcomed reprieve from 2022. Of note is that most often gains yield more gains. Since World War II when the S&P 500 posted a gain in the first quarter, it has averaged a gain of 8.9% for the remainder of the year. Comparatively, when the index has been down in the first quarter, the average remainder of the year gain has equaled 2.6%. There have been ten years where first quarter gains followed down years and during those periods, the remainder year gains averaged 15.9% and all were positive.

A LOOK AHEAD

Looking ahead to April, all eyes will shift from the Fed (next FOMC rate decision on May 3rd) to earnings. 96% of S&P 500 constituents will report in April and the consensus is for earnings to decline by 6.6% on a year over year basis but to increase for the full calendar year by 1.5%.

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