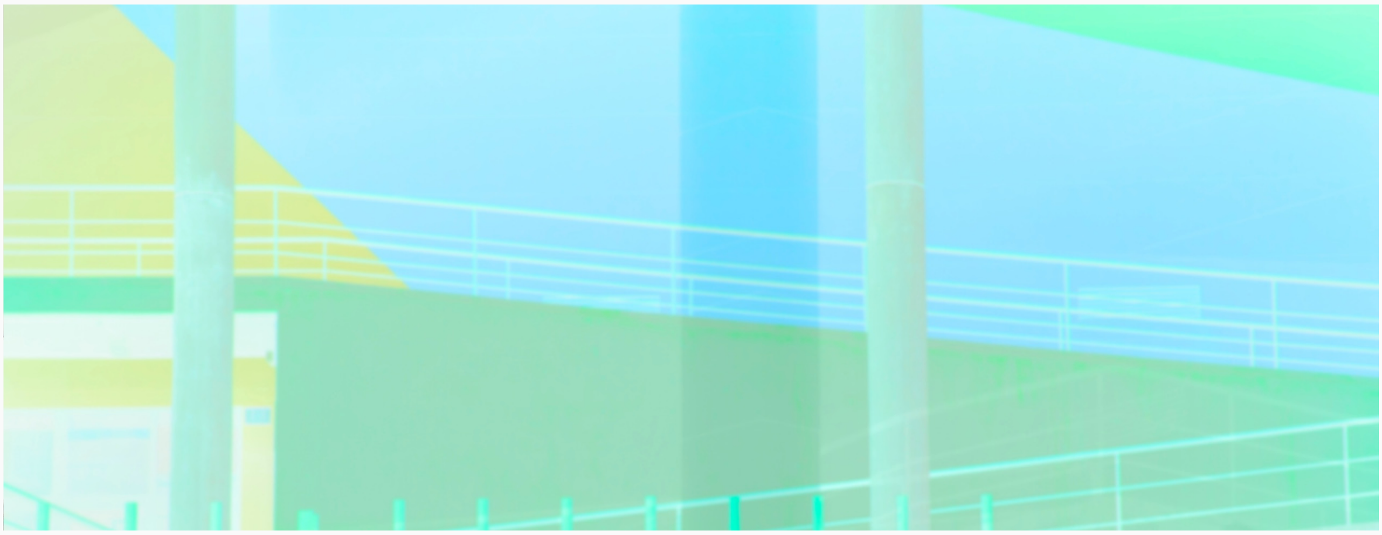
JANUARY 2023/Q4 NEWSLETTER

MOSAIC FI MARKET INSIGHTS

-Planning and Investing for Life



Q4 2022

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"Promote effectively the goals of maximum employment, stable prices and moderate long term interest rates'" has been the Congressionally imposed 'dual mandate' of the Federal Reserve since the 1970s. Notice in that statement nowhere does it indicate that the Federal Reserve should focus on or be responsible for economic growth.

Up until the second half of 2021 the stable prices (aka inflation) mandate has been a non-issue for the past few decades. However, by keeping interest rates at or near zero, the Fed took it upon itself to focus on optimal economic growth balanced with maximum employment.

The inflation of 2022 reminded the Fed to stick to their knitting. Chairman of the Federal Reserve, Jerome Powell, has made it clear through his messaging that his focus is now on inflation and employment; economic growth is not his priority.

Q4 2022:

"Promote effectively the goals of maximum employment, stable prices and moderate long term interest rates"

The employment situation remains strong. While we have been hearing about many layoffs in the technology and financial services sectors, beyond that, jobs are still plentiful. The unemployment rate ended the year at a historically low level of 3.5%

The Fed continued its march to higher interest rates in the 4th quarter. They raised rates 75 basis points in November and then another 50 basis points in December. The markets have viewed all of this in a positive light. Why?

The Fed is sending a clear message that they are determined to bring inflation back down to their target of 2%. This is instilling confidence in investors that the high inflation we have been experiencing will come to an end soon. If they can accomplish this in the first half of 2023 and the employment situation remain strong, we may avoid a recession.

While inflation and Fed action has been front and center for most of 2022, we had mid-term elections in the 4th quarter that gave Republicans control of the House and allowed Democrats to maintain control of the Senate. Not a great recipe for much progress to be made over the next two years…

The Equity Markets

Global equity markets, as measured by the MSCI All Country World Index, were up 8.1% in the 4th quarter and down -18.4% for the year. In Q4 and for all of 2022 international developed equity markets outperformed US equity markets.

Developed international was up 16.18% for the quarter and down -14.29% for the year. The US market, overall, was up 7.18% for the quarter and finished the year down -19.21%.

Emerging markets had strong performance in the 4th quarter, up 9.7% but ended the year down -20.09%. US REITs again underperformed the rest of the market, up 4.76% for the quarter and were down -25.96% for all of 2022.

Large cap stocks outperformed small cap stocks in the US but across the board value stocks outperformed growth stocks both in the 4th quarter as well as for the year overall. For the quarter, large cap value stocks were up 12.42% while large cap growth stocks were up 2.2%. For all of 2022, large cap value stocks were down -7.54% vs. large cap growth stocks which were down -29.14%.

The Fixed Income Markets

As we began to see glimmers of hope that the Fed's fight to tame inflation was working, we finally got a reprieve in the 4th quarter from the bond market selloff. For the first time in 2022, in the 4th quarter, the Bloomberg Barclays US Aggregate Bond index was up 1.87% and ended the year down -13.01%. The municipal bond market again outperformed the taxable market, up 4.10% for the quarter and ended the year down -8.53%.

The high-yield market once again had strong performance up 4.17% for Q4 but was down -11.19% for all of 2022. US TIPS (inflation protected securities) also had a good quarter. Overall, they were up 2.04% for the quarter but ended the year down -11.85%.

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So, what did all this mean for investors? It was refreshing to finally have a quarter of mostly positive returns. Depending on the asset allocation, a diversified portfolio returned between 5 and 9% for the 4th quarter. For all of 2022 returns ranged between -12% and -16%.

As investors, we all know that there is an element of risk when investing in the markets. In the years where we experience negative returns it is easy to get discouraged and question our long-term strategy. As you can see from the chart below, sticking with the plan that you agreed to during calmer waters will likely pay off.

Looking Ahead

As we look ahead, the focus for investors in the coming quarters will remain on inflation and whether the economy will avoid a recession in response to the interest rate hikes by the Federal Reserve.

Another looming concern to pay attention to is the brewing battle in Washington over raising the debt ceiling. Treasury Secretary, Janet Yellen, has already begun 'maneuvers' of essentially moving money around in order to continue funding the government. There will come a point when she will no longer be able to do this; currently that is estimated to be at some point this summer.

What happens if the US government were to default on its debt? It won't be pretty.

In the end the US will pay its debt. However, given that US treasuries are considered the 'risk-free' asset to the world, if a technical default occurred, and there was a period of time (even just a day or two) that US debt was in default, it could throw global debt and equity markets into a tailspin. It would likely be short lived with a quick recovery but there could be unintended consequences to this kind of disruption.

Recently we witnessed our representatives in Washington DC, playing a game of chicken with their political stances. We hope that they will appreciate the potential implications of this negotiation and come to an agreement well in advance.

As always, we would love to hear from you. Feel free to contact us at any time.