JANUARY 2023 MARKET RECAP

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The equity market sprinted out of the gate as the S&P 500 was up by +6.3% in January, the best start to a calendar year since 2019. Overall, the market has been on a solid run over the past several weeks. Since reaching a closing low for the year of 3,577 on October 12, 2022, the S&P is up by +14.5% since. Despite the strong period, the S&P 500 is still in bear market territory (a decline of -20% on a closing basis without a subsequent +20% increase) and now sits about -13.5% below the all-time high.

- **Market Cap**: Small (+9.8%) outperformed Mid (+9.2%) and Large (+6.3%) Caps.
- **Style**: Growth (Russell 1000 Growth: +8.3%) exceeded Value (Russell 1000 Value: +5.2%).
- **Sector**: Eight of eleven sectors were positive in the month with Consumer Discretionary (+15.0%) and Communication Services (+14.5%) as the top performers and Health Care (-1.9%) and Utilities (-2.0%) as the laggards.

January was a reversal of what took place in 2022, with last year's laggards producing the strongest returns and vice versa. Speculative parts of the market performed best with the Nasdaq (+10.7%), Small Caps (+9.8%), and Emerging Markets (+7.9%) leading the way. Meanwhile, defensive sectors in the United States, including Consumer Staples (-0.9%), Health Care (-1.9%), and Utilities (-2.0%) were all negative after delivering strong relative performance last year. The worst twenty performers in the S&P 500 last year increased by an average of +21% in January. The market often undergoes these violent rotations that could make an under-diversified investor feel like a genius one day and a fool the next. Rather than making risky concentrated bets, we prefer to construct diversified portfolios across regions, countries, market caps, factors, styles, sectors, and industries and tilt toward the areas we feel provide the most potential benefit.

While we are pleased with the market rebound to start the year and since mid-October, we are turning more cautious in the near-term. Most investors would have gladly accepted +6% returns from equities and +3% from fixed income for all of 2023. We just received those returns in a month. Investing is rarely this easy (see most of 2022 as the latest example of a more difficult market). Furthermore, the market still faces significant risks, including inflation, monetary policy, a potential recession, cuts to corporate earnings estimates, and the Russia/Ukrainian war. In our opinion, the fundamentals of the stock market do not support a rapid recovery back to all-time highs. Valuations are close to 10-year historical averages but probably do not have much room for upside given the level of interest rates (Please see our **Client Question on Why Interest Rates Impact Stock Prices**). While earnings estimates are being revised downward for 2023 and may still decline further. Putting it all together, we expect that volatility will continue over the next several months.

Over the long-term, we remain optimistic as we suspect this difficult economic and market environment over the past year has created a strong opportunity for investors willing to live with some short-term discomfort. The attached chart, **Investing After Market** Declines, utilizes S&P 500 month-end data from 1940 – 2021 and shows that investing when the index is down more than -10% from the all-time high has produced both strong average annualized returns and a high percentage of positive outcomes. We believe those who were able to either stay invested, rebalance, or add to their existing holdings will eventually be rewarded. Historically, equity markets have recovered from recessions and downturns; however, past performance is no guarantee of future returns. It is important to consider your own risk tolerance, financial circumstances, and time horizon.

The markets have several major events over the next month, including, the conclusion of Q4 Earnings Season, FOMC Meeting (2/1), JOLTS Job Openings Report (2/1), OPEC+ Meeting (2/1), January Employment Report (2/3), President Biden's State of the Union Address (2/7), CPI Inflation (2/14), and PCE Inflation (2/24).

At Winthrop Wealth, we follow a Total Net Worth Approach and we believe the right mindset paired with a comprehensive financial plan and a thorough investment process can provide confidence in pursuing your long-term financial goals, especially during times of heightened market volatility. We help our clients navigate challenging markets by seeking to ensure their short-term cash flow needs are met while managing the rest of their investments in a globally diversified portfolio. By having two to three years of scheduled cash flows invested in ultra-short fixed income instruments, we seek to decrease the likelihood that we will need to sell out of risk assets after a market decline to fund distributions. Please remember that no strategy assures success or protects against loss. Please see our recent Client Questions that can help put things into context:

- **Framework for Navigating Current Conditions**
- **Our Favorite Charts of 2022**
- **Market Timing Does Not Work**
- **Bond Primer**

Fixed Income Market

The bond market also started the year with a bang. The Bloomberg Barclays US Aggregate Bond index (Agg), which acts as a proxy for the investment-grade bond market, increased by +3.1% in January. While 2022 was the worst calendar year performance for the Agg (-13.0%) since inception of the index in 1976, the bond market just had its best January since 1988. A decrease in interest rates helped fuel the rally as the 10-Year Treasury yield decreased by -37 basis points to 3.51% in January (bond prices move inversely to interest rates and credit spreads).

Our objective with fixed income is to provide ballast, stability, and income to portfolios. Ballast means that, ideally, the fixed income holdings are increasing when equity markets are declining. Bonds did not provide ballast for most of 2022 as interest rates rapidly increased during the first half of the year. We continuously stated that we expect the negative correlation between stocks and bonds to return in the future once yields level out and that all else equal the fixed income markets need yields to stabilize rather than decrease to achieve positive returns. We will point out that from June 14, 2022 through the end of January 2023, the 10-Year Treasury yield was relatively flat with an increase of only 4 basis points and over the same period the Aggregate Bond index increased by +2.7%. Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and bonds are subject to availability and change in price.

The Treasury yield curve is still inverted with both the 3-Month (4.64%) and 2-Year (4.20%) higher than the 10-Year (3.51%) yield. In general, the Fed controls shorter term Treasury yields by setting the target federal funds rate while the market controls long term rates as investor demand will vary based on future expectations of inflation and economic growth. An inverted yield curve is a sign of a pessimistic economic outlook and typically signals that investors expect the Fed to cut rates soon. If the Fed does cut rates as investors expect, the 3-Month and 2-Year yields will fall below the 10-Year and the yield curve will be upward sloping again. Please see our **2019 Client Question of the Month** where we provide details on a **Yield Curve Inversion**.

The yield to maturity of various bond indices remain at their highest levels in years. Yield to maturity is defined as the estimated annualized rate of return an investor can expect on a bond if purchased today and held to maturity, assuming the issuer makes all their interest and principal payments (i.e., no defaults). The yield to maturity on the US Aggregate Bond index increased to 4.6% at the end of the month, which is the highest level since 2009. In other words, future returns from the Agg bond index have not been this attractive in 14 years.

Monetary Policy

The latest FOMC meeting took place from January 31st to February 1st where the Fed raised the federal funds rate by 25 basis points (bps) to 4.50% to 4.75%. The 25bp hike was a downshift from 50bps in December and four consecutive 75bp rate increases from June through November last year. Over the past eleven months, the Fed has increased interest rates from near zero to their present level for one of the quickest tightening cycles in history.

The markets breathed a sigh of relief this year as signs point to the Fed being one or two 25bp rate hikes away from completing their tightening cycle. The FOMC's most recent Summary of Economic Projections (SEP), released in December of 2022, showed that the median participant expected the federal funds rate to peak at 5.1% this year. The market expects the Fed will a peak rate slightly lower at 4.9% in May.

At his latest press conference, Fed Chair Powell acknowledged that the "disinflationary process" is underway. Powell also passed on the opportunity to scold financial markets for increasing over the past several weeks. Easing financial conditions (high stock prices and lower bond yields) make the Fed's job of fighting inflation more difficult. Investors interpreted Chair Powell's complacency as a green light for the market rally to continue.

Going forward, we expect the Fed to become more data dependent and that upcoming inflation readings will determine how much further the FOMC will increase interest rates. Inflation still remains the key to the markets in the near term.

Inflation

The increase in inflation since early-2021 was driven by supply chain bottlenecks, surging energy prices, strong consumer demand caused by a solid labor market, and massive amounts of stimulus. Although most readings have decelerated from peak levels over the past few months, inflation is still too high. The Fed has divided inflation into three buckets: goods (decelerating as supply chains normalize), housing (decelerating under rising mortgage rates but not showing up in inflation data until mid-2023), and non-housing related core services (still elevated due to the strong labor market and robust average hourly earnings).

The Fed's latest Summary of Economic Projections show the median participant expects Core PCE Inflation to fall to 3.5% in 2023, 2.5% in 2024, and 2.1% in 2025.

- **Consumer Price Index (CPI)**: tracks the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. The index does include food and energy prices.
  - Latest Reading (December): 6.5%.
  - Prior Reading (September): 8.2%.
  - Peak (June): 9.1%.
  - Source: Bureau of Labor Statistics.

- **Core Personal Consumption Expenditure (PCE) Index**: measures the prices paid by consumers for goods and services based on surveys of what businesses are selling. Core means that the index excludes food and energy prices. This is the Fed's preferred inflation measure, which they target at an average of 2%.
  - Latest Reading (December): 4.4%.
  - Prior Reading (November): 4.7%.
  - Peak (February): 5.4%.
  - Source: Bureau of Economic Analysis.

- **Average Hourly Earnings**: tracks total hourly renumeration (in cash or in kind) paid to employees in return for work done (or paid leave). Data is from the Current Employment Statistics (CES) survey.
  - Latest Reading (December): 4.6%.
  - Prior Reading (November): 4.8%.
  - Peak (April 2020): 8.0%.
  - Source: Bureau of Labor Statistics.

Economic Data

The economy continues to slow from the post-pandemic boom due to fading stimulus, rising inflation, and Fed tightening. The current period is best characterized by a lot of uncertainty and recessionary fears. After increasing by +5.9% in 2021, Real GDP Growth is estimated at +2.1% in 2022 and +0.5% in 2023. Economic growth estimates have been decreasing over the past several weeks as economic indicators, manufacturing, consumer spending, and the housing market have all weakened while inflation has decelerated but remains above the Fed's 2% target.

The strength of the economy currently lies with the labor market as the unemployment rate remains at a 50-year low of 3.5% and according to the BLS Job Openings report there are still over 10 million vacancies. However, we do expect the unemployment rate to tick up over the next few months as several major firms have begun to announce hiring freezes or layoffs. According to a recent PWC survey of over 700 executives, 50% of firms anticipate a reduction in headcount over the next 6 to 12 months.

While consumer spending is still in decent shape, the pace is slowing as individuals continue to spend down their excess savings accrued during the pandemic. We are also monitoring a clear increase in consumer credit balances and household debt payments to disposable income. All signs point to a consumer that is stretched after dealing with high inflation levels for the past two years.

The open debate on whether the economy has already fallen into a recession will continue for a while longer. The agency charged with maintaining official records of expansions and recessions, the National Bureau of Economic Research (NBER) Business Cycle Dating Committee, has stated the current period does not meet their definition of a recession as a significant decline in economic activity. According to the Federal Reserve, the probability that a recession will start within the next 12-months is about 50/50.

The economy can potentially avoid an official recession if inflation continues to quickly moderate over the next few months. This would take pressure off the Fed from continuing to aggressively tighten monetary policy. In our opinion, a mild recession is likely inevitable, and it does not really matter when the official start date is. Our view is still that the potential recession would be far less severe than previous economic declines like the Global Financial Crisis of 2007 – 2009.

JANUARY 2023 MARKET RETURNS

US Equity											
Index	**2023**	**2022**	**2021**	**2020**	**2019**	**2018**	**1-Year**	**3-Year**	**5-Year**	**10-Year**	**20-Year**
S&P 500	6.28%	-18.13%	28.68%	18.39%	31.47%	-4.39%	-14.83%	7.88%	8.34%	12.05%	9.97%
Russell 3000	6.89%	-19.22%	25.64%	20.88%	31.01%	-5.25%	-15.38%	7.30%	7.80%	11.61%	10.05%
Dow Jones Industrial Average	2.93%	-6.86%	20.95%	9.72%	25.34%	-3.48%	-4.08%	7.86%	7.27%	11.71%	10.00%
Nasdaq	10.73%	-32.51%	22.21%	45.05%	36.73%	-2.82%	-27.90%	5.61%	8.30%	14.16%	12.15%
S&P 400	9.22%	-13.10%	24.73%	13.65%	26.17%	-11.10%	-6.91%	8.39%	6.18%	10.11%	10.84%
Russell 2000	9.75%	-20.46%	14.78%	19.93%	25.49%	-11.03%	-13.02%	4.32%	3.63%	8.46%	9.53%
Russell 1000 Growth	8.33%	-29.14%	27.59%	38.49%	36.39%	-1.51%	-24.30%	7.19%	9.62%	13.71%	10.94%
Russell 1000 Value	5.18%	-7.56%	25.12%	2.78%	26.52%	-8.28%	-5.84%	6.90%	5.94%	9.64%	8.97%
International Equity											
MSCI Index	**2023**	**2022**	**2021**	**2020**	**2019**	**2018**	**1-Year**	**3-Year**	**5-Year**	**10-Year**	**20-Year**
EAFE	8.10%	-14.45%	11.26%	7.82%	22.01%	-13.79%	-10.99%	1.62%	0.56%	4.14%	6.68%
Europe	11.55%	-17.86%	13.54%	7.89%	23.20%	-16.90%	-14.83%	1.26%	-0.77%	3.85%	6.12%
Japan	6.21%	-16.65%	1.71%	14.48%	19.61%	-12.88%	-13.24%	-0.55%	-0.68%	5.25%	5.48%
China	11.78%	-21.93%	-21.72%	29.49%	23.46%	-18.88%	-21.17%	-6.14%	-6.87%	1.97%	10.30%
Emerging Markets	7.90%	-20.09%	-2.54%	18.31%	18.42%	-14.57%	-20.09%	-1.16%	-3.01%	1.32%	8.77%
ACWI ex US	8.11%	-16.00%	7.82%	10.65%	21.51%	-14.20%	-13.89%	1.01%	-0.21%	3.39%	6.95%
US Fixed Income											
Bloomberg Barclays Index	**2023**	**2022**	**2021**	**2020**	**2019**	**2018**	**1-Year**	**3-Year**	**5-Year**	**10-Year**	**20-Year**
Aggregate	3.08%	-13.01%	-1.54%	7.51%	8.72%	0.01%	-12.06%	-3.42%	0.26%	1.14%	3.11%
Treasury Bills	0.34%	1.52%	0.04%	0.54%	2.21%	1.83%	1.66%	0.68%	1.22%	0.73%	1.21%
Corporates	4.01%	-15.76%	-1.04%	9.89%	14.54%	-2.51%	-13.93%	-3.73%	0.66%	2.07%	4.11%
Securitized MBS/ABS/CMBS	3.23%	-11.67%	-1.04%	4.18%	6.44%	0.99%	-11.25%	-3.43%	-0.20%	0.86%	
High Yield	3.81%	-11.19%	5.28%	7.11%	14.32%	-2.08%	-9.46%	0.04%	2.23%	3.89%	7.12%
Munis	2.87%	-8.53%	1.52%	5.21%	7.54%	1.28%	-6.49%	-1.40%	1.52%	2.11%	3.63%
US Equity Sectors											
Index	**2023**	**2022**	**2021**	**2020**	**2019**	**2018**	**1-Year**	**3-Year**	**5-Year**	**10-Year**	**20-Year**
Technology	9.32%	-28.19%	34.52%	43.88%	50.27%	-0.30%	-24.72%	10.46%	14.36%	18.31%	13.52%
Real Estate	9.90%	-26.21%	46.14%	-2.17%	29.00%	-2.23%	-20.95%	1.36%	6.39%	6.16%	
Industrials	3.72%	-5.51%	21.10%	11.05%	29.32%	-13.32%	-0.90%	8.72%	6.33%	11.35%	10.19%
Energy	2.81%	65.43%	54.39%	-33.68%	11.81%	-18.10%	43.20%	24.71%	8.51%	5.14%	9.86%
Consumer Discretionary	15.02%	-37.03%	24.43%	33.30%	27.94%	0.82%	-32.58%	1.28%	4.34%	11.16%	10.59%
Communication Services	14.50%	-39.89%	21.57%	23.61%	32.69%	-12.53%	-38.50%	-3.72%	0.86%	4.01%	6.33%
Consumer Staples	-0.89%	-0.62%	18.63%	10.75%	27.61%	-8.39%	0.84%	9.44%	8.63%	10.47%	10.05%
Utilities	-2.00%	1.56%	17.67%	0.52%	26.35%	4.11%	5.48%	4.16%	10.45%	10.69%	10.97%
Materials	8.98%	-12.28%	27.28%	20.73%	24.58%	-14.70%	-6.35%	13.22%	6.70%	9.36%	9.83%
Financials	6.86%	-10.57%	34.87%	-1.76%	32.09%	-13.04%	-11.55%	6.96%	5.12%	11.54%	5.67%
Health Care	-1.87%	-1.95%	26.13%	13.45%	20.82%	6.47%	5.64%	13.37%	11.29%	14.30%	10.56%
	Calendar Year Returns						**Annualized Returns**				

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Content in this material is for general information only and not intended to provide specific advice or recommendations for any individual.

The economic forecasts set forth in this material may not develop as predicted and there can be no guarantee that strategies promoted will be successful.

All indexes mentioned are unmanaged indexes which cannot be invested into directly. Unmanaged index returns do not reflect fees, expenses, or sales charges. Index performance is not indicative of the performance of any investment. Past performance is no guarantee of future results.

The Standard & Poor's 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The S&P Midcap 400 Stock Index is an unmanaged index generally representative of the market for the stocks of mid-sized US companies.

The Russell 2000 Index is an unmanaged index generally representative of the 2,000 smallest companies in the Russell 3000 index, which represents approxi¬mately 10% of the total market capitalization of the Russell 3000 Index.

The prices of small cap stocks and mid cap stocks are generally more volatile than large cap stocks.

The MSCI EAFE Index is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US & Canada. The MSCI EAFE Index consists of the following developed country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland and the UK.

The MSCI EM (Emerging Markets) Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the emerging market countries of the Americas, Europe, the Middle East, Africa and Asia. The MSCI EM Index consists of the following emerging market country indices: Brazil, Chile, Colombia, Mexico, Peru, Czech Republic, Egypt, Greece, Hungary, Poland, Qatar, Russia, South Africa. Turkey, United Arab Emirates, China, India, Indonesia, Korea, Malaysia, Philippines, Taiwan, and Thailand.

International investing involves special risks such as currency fluctuation and political instability and may not be suitable for all investors. These risks are often heightened for investments in emerging markets.

The Barclays Capital US Corporate High Yield Bond index is an index representative of the universe of fixed-rate, non-investment grade debt.

The Bloomberg Barclays U.S. Aggregate Bond Index is an index of the U.S. investment-grade fixed-rate bond market, including both government and corporate bonds.

The Bloomberg Barclays US Treasury Bills 1-3 Month Index is designed to measure the performance of public obligations of the U.S. Treasury that have a remaining maturity of greater than or equal to 1 month and less than 3 months. The Index includes all publicly issued zero coupon U.S. Treasury Bills that have a remaining maturity of less than 3 months and at least 1 month, are rated investment grade, and have $300 million or more of outstanding face value.

Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and bonds are subject to availability and change in price.

The Bloomberg Commodity Total Return index is composed of futures contracts and reflects the returns on a fully collateralized investment in the BCOM. This combines the returns of the BCOM with the returns on cash collateral invested in 13 week (3 Month) U.S. Treasury Bills.

Government bonds and Treasury bills are guaranteed by the US government as to the timely payment of principal and interest and, if held to maturity, offer a fixed rate of return and fixed principal value.

Financial planning is a tool intended to review your current financial situation, investment objectives and goals, and suggest potential planning ideas and concepts that may be of benefit. There is no guarantee that financial planning will help you reach your goals.

Rebalancing a portfolio may cause you to incur tax liabilities and/or transaction costs and does not assure a profit or protect against a loss.

Asset allocation does not ensure a profit or protect against loss. There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio.

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