Accredited Wealth Management

"Live the Life You've Imagined"

Investment Commentary

December 2022

Investors anticipated a slowdown in the pace of central bank tightening which contributed to a second consecutive monthly gain for global stocks. Bonds also bounced back as Treasury yields declined and inflation slowed.

Return (%)	1 MO	3 MO	YTD	1 YR
S&P 500	5.59	3.63	-13.10	-9.21
Russell 2000	2.34	2.71	-14.91	-13.01
MSCI EAFE	11.28	6.36	-14.11	-9.70
MSCI Emerging Markets	14.85	-1.70	-18.64	-17.07
Bloomberg U.S. Aggregate Bond	3.68	-2.09	-12.62	-12.84

Data as of 11/30/2022, Performance in USD. Source. Morningstar.

- As expected, the Fed hiked interest rates another 75 bps in early November. The following week, data showed inflation moderated in October. This news, combined with mounting recession risks, led to growing expectations that the Fed and other central banks might slow their rate-hike campaigns.
- In this environment, the S&P 500 index rallied nearly 6% in November, even as year-over-year corporate and earnings outlooks generally weakened. Foreign developed markets rose even higher, delivering double-digit monthly gains.
- Emerging markets outperformed largely due to large gains in China and easing global commodity prices. A declining US dollar gave a boost to foreign assets in November.
- US inflation eased in October to 7.7% (there's a lag on the inflation data), and core inflation dipped to 6.3%. Against this backdrop, US Treasury yields declined in November, and bond returns rallied.
- In early December, the premise that central bank tightening will slow down is being challenged. Employment data has come in stronger than expected and China is beginning to loosen its Covid restrictions. The markets are likely to be data-dependent and may require further evidence of a slowdown in inflation and rate tightening for the rally in financial assets to continue.

This month we focus on some of the investment themes we expect in 2023 and beyond.

Investment Themes In 2023 and Beyond

Below are some of the top investment themes we expect investors to focus on in 2023 and beyond. The list is in no particular order:

- **An Economic Slowdown and Increasing Recession Risks**
  The economy is on a slowing path and the risk of a recession in 2023 is increasing. The biggest risks to the economy stem from the ongoing central bank tightening process. Fed tightening affects the economy with a lag, and persistent inflation threatens to keep the Fed in a position where it sees the need to tighten to

slow the economy more sharply. These risks are well known to market participants, however, if the Fed over-tightens and pushes the economy into a severe recession, there is additional risk to asset prices.

- **Geopolitical Tensions**
  We expect the secular rise in geopolitical risks to continue due to great power rivalry, hypo-globalization, and rising nationalism across the globe. Tensions are likely to remain high and confidence around the world regarding the US willingness and ability to protect them has been shaken. This likely leads to greater defense spending and strong demand global demand for the aerospace and defense industries.

- **The Value vs. Growth Debate Continues**
  Value stocks won the debate in 2022 (so far) and have outperformed growth stocks by roughly 20% YTD. The long-term case for value stocks still looks strong, however, relative performance doesn't happen in a straight line. In the near term, if interest rates continue to fall and economic growth falters there may be a strong case for growth stocks to outperform for a stretch. However, the chart to the right from GMO makes a strong case that value stocks are still trading at a significant discount which should bode well for long-term relative performance.

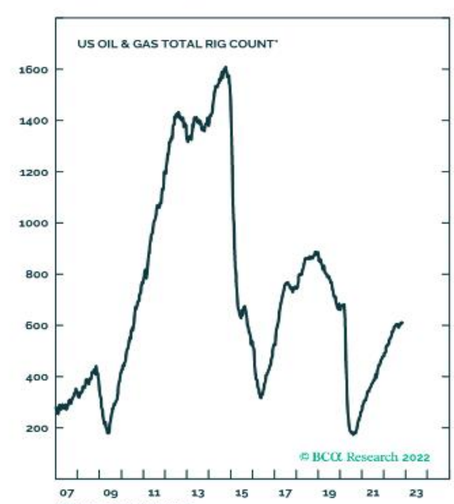
EXHIBIT 1: WHERE ARE WE ON RELATIVE VALUATIONS?

As of 9/30/2022 | Source: GMO
Composite Valuation is composed of price/sales, price/gross profits, price/book, and price/economic book.

- **Onshoring, Automation, and Fiscal Spending**
  The US is going through an industrial boom and there is an ongoing focus on bringing an industrial base back to the US, huge investments in robotics and automation, and fiscal spending will support those efforts. A good example is the recent fiscal commitments and investments being made to bring semiconductor capacity back to the US. With industrial capacity utilization relatively high the earning power for the industrial and capital goods sectors should be strong, leading to good investment opportunities.

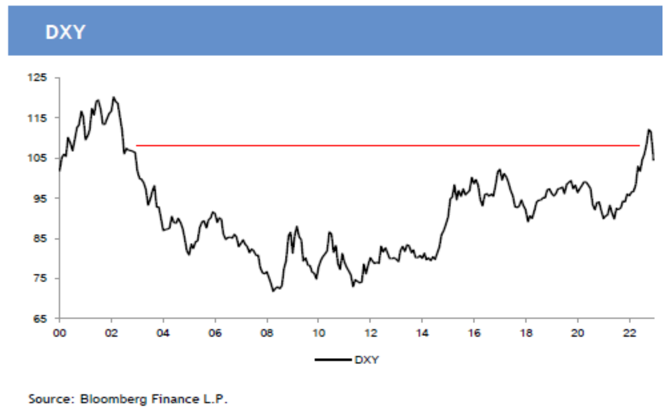
- **New Energy Capital Expenditure Cycle**
  The world is moving towards alternative energy sources, however, the reality is it will take years before they can replace traditional oil and gas. The chart to the right illustrates the lack of investment the past few years and the need for additional capital expenditures to meet the ongoing need for traditional energy sources. We remain advocates of investing in both new and

New Energy Cap Ex Cycle



traditional energy sources and believe investors can benefit from both sources as we transition to new energy alternatives.

- **Dollar Dominance**
  The US dollar reached 20-year highs in 2022. In general, the dollar is a contra-cyclical currency, meaning that in difficult times (economic, geopolitical, etc.) investors gravitate towards the dollar and in risk on periods the dollar often declines. Historically, the dollar fluctuates between periods of over and undervaluation, with today being a time of overvaluation relative to other currencies. Should the dollar revert to lower levels, we would expect global stocks to rally and foreign stocks to outperform.



- **Other Themes**
  We've written about other themes in the past year and believe those trends are still in place.
  - **TINA to TARA**- the term TINA refers to the process of the Federal Reserve driving interest rates so low after the crisis that investors had no alternative but to turn to stocks for income and growth. With the federal reserve increasing rates this year there are reasonable alternatives to stocks.
  - **Cybersecurity-** we continue to believe the trend of increased spending on cybersecurity-related technologies is firmly in place and will continue for years to come.
  - **Clean Energy**- we touched on this above, and continue to be investors in this space on a secular basis. We expect the performance to be volatile but expect long-term investors to be rewarded.

There are other themes that we could have touched on but will save those for another time. If you have any questions about your portfolio or investment strategy don't hesitate to give us a call.

Best regards,

Steve Giacobbe, CFA, CFP®