

Markets hit their highs for the year in January and struggled to regain momentum over the next 12 months. What's in store for investors in the new year — and will we see a recession in 2023?

## A YEAR TO FORGET

Like most of 2022, the fourth quarter had a small share of ups — and more than its share of downs.

Markets hit new lows to start the quarter, then pulled off a huge comeback in October. The rally snapped a two-month losing streak for markets, especially the Dow, which had its best month since 1976.<sup>1</sup>

Equity Performance as of Dec. 31, 2022				
Equity Index	Q4	1 YR	3 YRS	5YRS
S&P 500:	7.08%	-19.44%	5.92%	7.51%
NASDAQ:	-1.03%	-33.10%	5.27%	8.68%
DJIA:	15.39%	-8.78%	5.12%	6.04%

Source: Morningstar. Index Performance: Return (%). [https://www.morningstar.com/markets?CustId&CLogin&CType&CName&\\_LPAGE=%2FFORBIDDEN%2FCONTENTARCHIVED.HTML&\\_BPA=N](https://www.morningstar.com/markets?CustId&CLogin&CType&CName&_LPAGE=%2FFORBIDDEN%2FCONTENTARCHIVED.HTML&_BPA=N). Accessed Jan. 3, 2023.

Markets were buoyed by positive economic data, with third-quarter gross domestic product (GDP) rising by 2.9% and avoiding three consecutive quarters of loss.<sup>2</sup> The positive economic growth came even as the Federal Reserve made aggressive efforts to slow it through a series of interest rate increases. The Fed hiked rates seven times in 2022, including four consecutive increases of 75 basis points (0.75%).<sup>3</sup>

The economy continued to hang in there despite the rate hikes. Unemployment — a crucial indicator of an economic slowdown — hovered around 3.7%. We even saw significant (and unexpected) employment growth in the fourth quarter, adding 263,000 nonfarm payroll jobs in November.<sup>4</sup>

November also brought midterm elections and a divided government. Markets liked the idea of no additional government spending being likely for the next two years, as well as the idea that the Fed might slow or even pause rate hikes altogether — even as inflation remained stubbornly high. The latest numbers showed inflation increased 7.1% year-over-year in November, far above the Fed's target rate of 2%.<sup>5</sup> (Still, inflation is slowly ticking down from its high of 9.1% in June.<sup>6</sup>)

Strong employment numbers and slightly decreased inflation played into the Fed's decision to increase interest rates by 50 basis points during its mid-December meeting, bringing the federal funds rate to its highest level since 2007 at 4.25%–4.5%.<sup>7</sup> Markets initially dropped on the news, especially when Federal Reserve Chairman Jerome Powell wouldn't commit to pausing future rate hikes. "While it was good to see inflation come down these last two months, the Fed will need to see a few more signs over a longer time frame that inflation is under control



before a full pivot,” Powell said in his post-meeting news conference.<sup>8</sup> In other words, the Fed is committed to staying the course in its pursuit of 2% inflation — dashing markets’ hopes that a rate pause or even cut would happen soon.

## RECESSION — OR NO RECESSION?

The potential for recession continued to dominate the conversation in the fourth quarter, much as it did throughout the entirety of 2022. So is a recession looming in the early months of 2023? Possibly. The yield curve — the gap between the yield on 10-year and 2-year Treasuries — has remained inverted, a sign that recession could still be on the way.<sup>9</sup>

Additional signs also point to recession. Third-quarter GDP growth was more about the drop in gas and energy prices than real economic growth. Higher prices mean consumers are spending more on essentials such as gas and groceries, and rising interest rates have increased the cost of loans and credit card debt. These factors all make it difficult to see how we could avoid a recession, although it’s still unclear how long or how deep it could go.

## LOOKING AHEAD

The events of the past few years have reminded us that anything can happen — and it’s important to be prepared. Market volatility will likely continue over the next several months, especially as the Federal Reserve continues its pursuit of lower inflation.

If you haven’t done so lately, we recommend scheduling an appointment with your advisor to review your financial plan and make sure your investments are aligned with your goals. Short-term events may continue to rattle markets, especially in the first half of 2023. If these events become distracting or discouraging, turn to your advisor for support. He or she can help you stick to the plan and continue working toward your long-term goals.



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4TH QUARTER - 2022

<sup>1</sup> Samantha Subin, Jesse Pound. CNBC. Oct. 31, 2022. "Dow closes lower on Monday, but still posts best month since 1976." <https://www.cnbc.com/2022/10/30/stock-market-news-futures-open-to-close.html>. Accessed Dec. 14, 2022.

<sup>2</sup> Bureau of Economic Analysis. Nov. 30, 2022. "Gross Domestic Product (Second Estimate) and Corporate Profits (Preliminary), Third Quarter 2022." <https://www.bea.gov/news/2022/gross-domestic-product-second-estimate-and-corporate-profits-preliminary-third-quarter>. Accessed Dec. 14, 2022.

<sup>3</sup> CBS News. Dec. 14, 2022. "Fed hikes key interest rate for seventh time this year." <https://www.cbsnews.com/news/federal-reserve-hikes-interest-rates-seventh-time-2022/>. Accessed Dec. 16, 2022.

<sup>4</sup> Bureau of Labor Statistics. Dec. 2, 2022. "The Employment Situation – November 2022." <https://www.bls.gov/news.release/pdf/empsit.pdf>. Accessed Dec. 14, 2022.

<sup>5</sup> Bureau of Labor Statistics. Dec. 13, 2022. "Consumer Price Index Summary." <https://www.bls.gov/news.release/cpi.nr0.htm>. Accessed Dec. 14, 2022.

<sup>6</sup> U.S. Inflation Calculator. "Current US Inflation Rates: 2000-2022." <https://www.usinflationcalculator.com/inflation/current-inflation-rates/>. Accessed Dec. 14, 2022.

<sup>7</sup> Trading Economics. "United States Fed Funds Rate." <https://tradingeconomics.com/united-states/interest-rate>. Accessed Dec. 14, 2022.

<sup>8</sup> Fred Imbert. CNBC. Dec. 14, 2022. "Full recap of the Fed's rate hike and Chair Powell's news conference." <https://www.cnbc.com/2022/12/14/live-updates-fed-rate-hike-december.html>. Accessed Dec. 14, 2022.

<sup>9</sup> Simon Moore. Forbes. Nov. 18, 2022. "Yield Curve Inversion Deepens, Increasing Likelihood of 2023 Recession." <https://www.forbes.com/sites/simonmoore/2022/11/18/yield-curve-inversion-deepens-increasing-likelihood-of-2023-recession/?sh=c42849534eb4>. Accessed Dec. 14, 2022.

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