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Markets enjoyed a brief summer rally, echoing faded hopes that monetary tightening would ease. Approaching the end of the third quarter, turmoil in the markets intensified. Bond yields were soaring, and stocks were on track for their worst year since the 2008 financial crisis. The S&P 500 ended Q3 with a 4.9% loss, bringing its year-to-date decline to 23.9%. The Dow Jones Industrial Average lost 6.2% in Q3, and has fallen 19.7% year to date. The Nasdaq declined 3.9% in Q3 and incurred a loss of 32.0% year to date.

The Dow Jones Industrial Average has fallen into a bear market, down over 20% from its record high set January 4th, 2022. The decline marked the index's first bear market since the pandemic-fueled selloff in early 2020. The S&P 500 has been in a bear market since June 2022, while the Nasdaq entered one in March 2022.

At the beginning of the final quarter of the year, it is necessary for investors to take a moment to reflect on how the current bear market compared to previous downdrafts. The last bear market was in early 2020 due to the outbreak of Covid-19. The Dow briefly stayed in the bear market and bounced back sharply to a bull market in less than three months. The S&P 500 took just a little over four months to swing back to a new record high. In contrast, the bear market in the S&P 500 during the Great Financial Crisis spanned more than 500 days. The bear market started during the tech bubble lasted more than 900 days. The current bear market differs from previous ones and has been triggered by a mix of factors, with inflation the most critical driver. Strong demand and supply chain disruptions during the pandemic had driven higher prices across consumer goods and services. The war in Ukraine sent prices for energy and agricultural commodities soaring. To tame inflation, the Federal Reserve has been raising interest rates rapidly. This has led to fears that the Fed's actions could drive the economy into a recession. Bear markets have often proceeded recessions, yet there have been several bear markets that did not coincide with recessions. Since the Great Depression, there have been 17 bear markets, nine of which were accompanied by a recession.

Turbocharged volatility has rattled various asset classes including stocks, bonds, currencies, and commodities recently. Central banks around the world are trying to play catch up by tightening monetary policy. These actions have propelled investors to reckon with the end of a multi-decade era of low interest rates.

Bonds have fallen along with stocks. The iShares Core US Aggregate Bond Index have declined 15% year to date, on pace for their worst year in history. In the final trading days of Q3, global government bond markets saw mounting volatility. Such wild swings in the world's safest assets could further destabilize already rocky financial markets. Concerns about a potential for a spiraling crisis in the global debt markets carried the 10-year US Treasury note above 4% for the first time in over a decade. This was followed by a historic reversal of the benchmark yield after the surprise announcement by the Bank of England that it would buy longer-term UK bonds

Third Quarter Market Watch

	Date	YTD		1 Year Ago	
	9/30/2022	12/31/2021	% chg	9/30/2021	% chg
DJIA	28,725.51	36,338.30	-19.7%	33,843.92	-13.4%
S&P 500	3,585.62	4,766.18	-23.9%	4,307.54	-15.5%
NASDAQ Composite	10,575.62	15,644.97	-32.0%	14,448.58	-26.3%
Russell 2000	4,137.24	5,580.17	-25.1%	5,478.42	-23.5%

	Date	YTD		1 Year Ago	
	9/30/2022	12/31/2021	% chg	9/30/2021	% chg
Japan Nikkei 225	25,937.21	28,791.71	-28.3%	29,452.66	-32.6%
MSCI EM (Emerging Markets)	875.79	1,232.01	-26.9%	1,253.10	-27.8%
MSCI EAFE	1,661.48	2,336.07	-26.8%	2,281.29	-24.7%
MSCI AC World	553.37	754.83	-25.3%	709.51	-20.3%
FTSE 100	7,045.57	7,313.56	-20.6%	6,982.44	-6.8%
SSE Composite Index	3,024.39	3,639.78	-25.3%	3,568.17	-19.7%

US Equity Sectors

	YTD	1-yr ret.
Consumer Discretionary	-29.9%	-20.9%
Consumer Staples	-11.8%	-0.5%
Energy	34.9%	38.0%
Financials	-21.2%	-19.8%
Health Care	-13.1%	-2.5%
Industrials	-20.7%	-15.5%
Information Tech	-31.4%	-20.4%
Materials	-23.7%	-13.9%
Communication Services	-39.0%	-39.8%
Utilities	-6.5%	4.4%

US Equity Styles

	YTD	1-yr ret.
RUSSELL 1000 VALUE	-17.8%	-12.7%
RUSSELL 1000 GROWTH	-30.7%	-22.7%
RUSSELL 2000 VALUE	-21.1%	-19.3%
RUSSELL 2000 GROWTH	-29.3%	-29.4%

Commodity Prices

	Sep 2022	Dec 2021	Sep 2021
Gold	1,672.00	1,828.60	1,828.60
Crude Oil	79.49	75.21	75.21
UD Dollar Index	112.08	95.59	95.59
Commodity Index	111.49	99.17	99.17

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to keep the debt market afloat. Global bond markets briefly rallied on the BoE announcement. Yields on global government bonds, which rise when their prices fall, have been climbing all year as central banks try to fight the worst inflation in decades by raising short-term interest rates. In the recent weeks, however, yields have risen at an alarming rate, resulting in a fresh sell-off for bonds. In recent months, rising treasury yields have ratcheted up borrowing costs for households, businesses, and the government. The 10-year US treasury yield has climbed nearly 2.5 percentage points this year, the largest increase since 1981.

Mortgage rates rose to their highest level in 15 years, a new record since the 2008 financial crisis. This adds pressure to the already cooling housing market. The average rate on a 30-year fixed mortgage climbed to 6.7%. A year ago, rates were 3.0%. The surge in mortgage rates follows the aggressive interest rate increases from the Federal Reserve. Mortgage rates usually rise or fall in tandem with the benchmark 10-year Treasury yield, which has surged this year during the broad bond market turmoil. There has been a large dispersion in mortgage rates among lenders, making it important for home buyers to shop around. With rates rising so much, some would-be buyers have now decided to rent. Meanwhile, some existing homeowners are reluctant to sell, as they are unwilling to take on new mortgages at significantly higher rates.

Core consumer prices, excluding food and energy items, increased 4.9% from a year ago. Spending on durable goods slipped 0.4% and services spending rose 0.3% from a month earlier. Some of that shift can be explained by people cutting back on stay-at-home categories after the pandemic and returning to activities such as travel and entertainment. Including the more volatile energy prices, inflation is stalling. The temporary retreat of energy prices is already having a positive impact on consumer confidence. Meanwhile, the US manufacturers continue to show resiliency. Leading indicators like the purchasing managers index (PMI) are still in expansionary territory. In addition, US industry will likely benefit the growing trend of re-shoring.

So far, corporate earnings growth has remained healthy, as companies have been able to push through price increases. Prices for goods sold by manufacturers, wholesalers and retailers increased 15% year-over-year. This begs the question how sustainable their pricing power will be going forward. Not only is the Fed raising rates to tame inflation, but consumers are also increasingly reluctant to pay up.

Interest Rates

	Sep '22	Dec '21	1 Yr. Ago
USD Prime Rate (TPI)	6.25	3.25	3.25
USD Federal Funds (TPI)	3.09	0.09	0.09
US 2Y T-Note Yield (TPI)	4.20	0.73	0.29
US 10Y T-Note Yield (TPI)	3.80	1.51	1.53
30YR FIXED MORTGAGE	6.70	3.11	3.01

Exchange Rates

	Sep 2022	Dec 2021	Sep 2021
Euro per U.S. Dollar	1.021	0.879	0.863
British Pounds per U.S. Dollar	0.896	0.738	0.742
China Renminbi per U.S. Dollar	7.091	6.373	6.462
Indian Rupee per U.S. Dollar	81.351	74.336	74.228
Japanese Yen per U.S. Dollar	144.745	115.155	111.575

Economic Sentiment

	Sep 2022	Dec 2021	Sep 2021
Unemployment Rate	3.70	3.90	4.70

US Bond Performance

	Q3	YTD	1-Year Return
BAR CAP Govt. Interm. TR	-3.1%	-8.6%	-9.2%

Further, weakening overseas demand and the dollar's strength are only becoming more pronounced, creating additional headwinds for multinational corporations that dominate the S&P 500. In addition, rising labor costs, the most significant cost for most US corporations, are making it more difficult for companies to maintain profit margins. Excluding the energy sector, which benefited significantly from surging oil prices, earnings at companies in the S&P 500 reported 2% year-over-year earnings decline in the second quarter. We are just at the beginning of the third quarter earnings reporting season. Currently, the consensus forecast provided by Wall Street analysts is calling for a 2.6% year-over-year earnings growth for the quarter - a notable decline from the 9% in Q2. This more pessimistic forecast reflects pressure on profit margins due to weaker pricing power.

For those nearing retirement, the year-to-date market decline does have significant implications. However, over the long history of the financial markets, bear markets eventually go away. Solid returns are made by investing when markets are near their lows. After the great financial crisis in 2008, equities entered a bull market for 11 years. However, timing the market bottom or peak is extremely difficult. For investors, panic selling is among some of the common mistakes. While corrections can be worrisome, they are a normal part of market cycles. Corrections have occurred periodically. Bear markets can give investors serious pause. However, missing the top days of market performance can have a significant impact on long-term returns. Staying invested through bear markets has been rewarding historically. On average, one-year returns following 20% declines of the S&P 500 are more than 12%. Here at the 1911 Trust Company, our investment professionals remain focused on how to re-balance your investment accounts by revisiting your return expectations and risk tolerance, use tax-loss harvesting to reduce your tax liability, or take advantage of the market downturn to buy securities with good fundamentals and attractive valuation.

Kevin Kavanaugh
President and Chief Investment Officer

Lei Qin, CFA, CFP®, FRM, CAIA
Director of Equity Research and Portfolio Management