# Fundamentum
## 2023 Q1 Market Commentary

After one of the worst years on record for equities and fixed income, the 1st quarter of 2023 rebounded with major reversals. The S&P500's 2022 bottom decile of the worst-performing stocks jumped an average of 16.8% during the 1st quarter while the decile of best-performing stocks actually fell -1.5%[1]. Overall, the tone of the markets was generally favorable with large upside moves in January, a pullback in February, and a reacceleration in March. Although still delivering positive returns, March was a volatile month with the Federal Reserve's aggressive rate hike cycle contributing to stresses in the financial system resulting in the surprise failure of some regional banks led by Silicon Valley Bank, a forced takeover of Credit Suisse – a global investment bank, the institution of a governmental deposit backstop, and a new special lending facility for banks. However, at the same time financials were under stress, technology stocks rallied led by semiconductors – delivering their 2nd best quarterly performance in 22 years[2]. In its entirety, financial returns for the quarter were constructive for both equities and fixed income leading to positive returns in balanced portfolios during the quarter versus 2022's double-digit negative numbers.

**<u>Q1 Total Returns by Asset Class[3]</u>**

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|---|---|
| Dow Jones Industrials Index | 0.93% |
| S&P 500 Index | 7.48% |
| NASDAQ Composite | 17.05% |
| Russell 2000 Index | 2.73% |
| Russell 1000 Value Index | 0.99% |
| Russell 1000 Growth Index | 14.36% |
| MSCI EAFE Index | 8.65% |
| MSCI EM Index | 3.97% |
| Bloomberg/Barclay US Bond AGG | 2.96% |
| Bloomberg/Barclay US Corp. Index | 3.50% |
| Bloomberg/Barclay US HY Corp. Index | 3.57% |
| HFRX Global Hedge Fund Index | 0.00% |

Within S&P 500 sectors, outperformers for the quarter were Technology +21.5%, Communications Services +20.2%, and Consumer Discretionary +15.8% while sector underperformers were Financials -6.0%, Energy -5.6%, and Healthcare -4.7%[4]. The three best-performing S&P500 stocks were NVIDIA Corporation +90.1%, Meta Platforms +76.1%, and Tesla Inc. +68.4% with First Republic Bank -88.5%, Zions Bancorp -38.6%, and Charles Schwab -36.9%. being the three worst S&P500 stocks[5]. During the quarter as the markets began to fear a recession and hope for lower rates, the preferred investment style moved away from "value" into "growth". As a result, the Russell 1000 Growth index significantly outperformed the Russell 1000 Value index (14.36% vs 0.99%). In the S&P500, the 50 stocks with the highest P/E ratios at the start of the year gained 13% in the quarter, while the 50 stocks with the lowest P/E ratios actually fell -2.5%[6].

The Federal Reserve (Fed) rate hike cycle that began a year ago has been extraordinary: 475 bps of Fed rate hikes within four quarters is the most aggressive since the early 1980s, and could be framed as even more so given the low starting point in March of 2022.[7] During the 1st quarter, the bond market rallied due to its increasingly confident view that the cyclical peak in inflation had occurred and the end of the Federal Reserve's historic tightening campaign was near. Another contributing factor pushing bond yields lower was the concern that the aggressive Fed rate hike cycle had slowed the economy and led to a “mini” banking crisis - potentially putting the economy into a recession. The yield of 10-year U.S. Treasury fell from 3.88% at the end of December 2022 to 3.48% on March 31st. As a result of these potential issues, the markets are now expecting that the Federal Reserve is done raising interest rates and will quickly begin to cut them. However, with pockets of strength still in the economy, we believe the Federal Reserve has more work to be done, keeping interest rates “higher for longer”.

Going into the rest of the year, we continue to focus our attention on the direction of interest rates, sustainability of earnings, the potential for a recession, and now a new concern – the escalating debt ceiling debate in Washington D.C. Our expectation for inflation is to fall through the spring/summer but stabilize in the fall/winter with inflation ending the year around 3.0% - above the Federal Reserve’s target rate of 2.0%. As the effects of rising rates and tighter credit standards affect profits and the economy, uncertainty will continue for equity markets but be a positive backdrop for bonds. Given the earnings and interest rate uncertainties along with elevated valuations - the risk vs reward ratio for the equity markets is not optimistic. Therefore, we continue to encourage Advisors to build diversified portfolios with lower capital market returns into their client’s long-term financial plans and expectations.

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**Sources:**

1. BeSpoke Report, April 3, 2023
2. Nasdaq First Quarter 2023 Review and Outlook, March 31, 2023
3. Bloomberg Business News, March 31, 2023
4. FactSet StreetAccount, March 31, 2023
5. Goldman Sachs US Quarterly Chartbook, March 31, 2023
6. BeSpoke Report, April 3, 2023
7. FS Investments Q2 2023 Economic Outlook, March 31, 2023



The Russell 1000 Index consists of the 1,000 largest securities in the Russell 3000 Index, which represents approximately 90% of the total market capitalization of the Russell 3000 Index. It is a large-cap, market-oriented index and is highly correlated with the S&P 500 Index.

The Dow Jones Industrial Average is comprised of 30 stocks that are major factors in their industries and widely held by individuals and institutional investors.

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 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.

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

The NASDAQ Composite Index measures all NASDAQ domestic and non-U.S. based common stocks listed on The NASDAQ Stock Market. The market value, the last sale price multiplied by total shares outstanding, is calculated throughout the trading day, and is related to the total value of the Index.

The Russell 1000 Growth Index measures the performance of those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values.  Russell 1000 Value Index measures the performance of those Russell 1000 companies with lower price-to-book ratios and lower forecasted growth values.

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.