

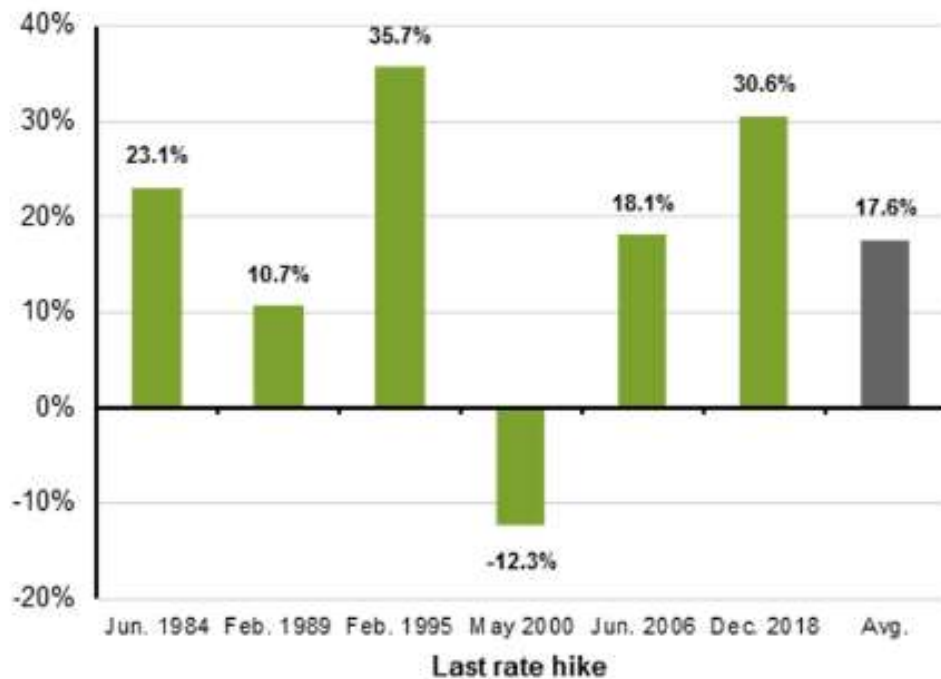
Monday, March 27, 2023

Good afternoon:

Ongoing angst in the banking sector last week was not enough to alter the Fed's plan to continue hiking rates as they announced another 0.25% increase at Wednesday's FOMC meeting. However, for the first time in this year-long tightening cycle, their forward-looking guidance was dovish and signaled a potential near-term conclusion to the rate hikes. By week's end, equity markets were again higher led by Communication Services, as well as rebounding Energy and Materials sectors. The S&P 500 added 1.41% and the NASDAQ gained 1.67% despite concerns about a growing banking contagion still swirling around among some investors.

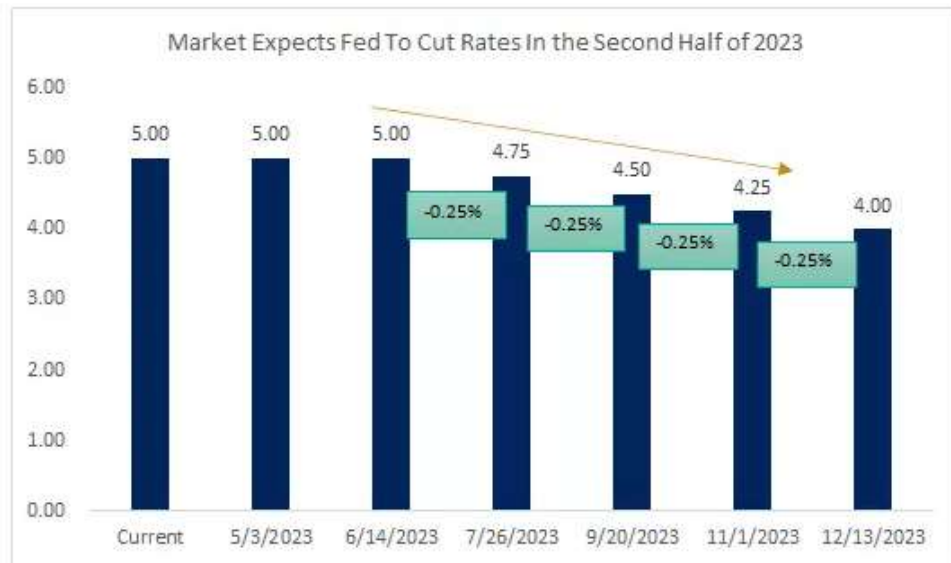
The response from many banks to this recent stress will likely be to tighten lending standards and ultimately write fewer loans. The economic impact will have a dampening effect on growth, adding to the statistical likelihood of a recession. The timing, duration, and severity of such a downturn remains to be seen. After the significant equity price declines of last year in anticipation of an economic contraction, further significant downside volatility may only result if the recession not only materializes but turns out to be far worse than a garden variety recession. History also has shown how equity markets bottom and start the next leg higher in the *early* stages of a recession and are often up *significantly* one year after a rate tightening cycle ends.

Equities have historically performed well after tightening cycles
S&P 500 price returns in the 12 months following past 6 hiking cycles



Source: FactSet, S&P 500, J.P. Morgan Asset Management

Additionally, now that short-term rates are no longer close to 0%, the Fed will have some ammunition to combat a future economic downturn by cutting rates again. Their main priority now, though, is to keep inflation trending lower. Once inflation is closer to the Fed's 2% target, it is likely they may adjust rates bank down anyway to normalize the inverted yield curve and remove some of the added costs to borrowers whose loans are tied to floating short-term rates. Bond futures markets have already started pricing in a series of rate cuts in the second half of this year.



Source: CME Fed Watch

With all the turmoil impacting the banking sector, particularly regional banks, a “flight to quality” led to large amounts of capital flowing into short-term treasuries. The result saw 2-Year treasury bond yields fall from a high of over 5.0% to now 3.8%. Corresponding short-term CD yields may also start to decline in response. If short-term rates on bonds and cash equivalents like money markets start to decline significantly, it could be a source of fuel to propel the next equity bull market as sidelined capital reenters the market seeking superior returns.

Despite a little profit-taking in some Tech and Communications sectors, the broader stock market averages are modestly higher this morning led by many of the largest banks and financial institutions signaling confidence is starting to return to that part of the sector. We expect markets to remain volatile and jittery as we await this week’s inflation and consumer sentiment reports.

Consumer Confidence



Have a great week!

Mark and Jeff

Mark S. Loftus, CFP®

Managing Partner & Founder, LPWP
Registered Principal, RJFS
CA Insurance License #0C83705

Jeffrey C. Preusser, CFP®

Senior Partner, LPWP
Registered Principal, RJFS
CA Insurance License #0E01600

O: 630.566.9200 // T: 844.890.8750 // F: 630.566.9292
1901 Butterfield Road, Suite 100, Downers Grove, IL 60515
www.loftus-preusser.com

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S&P 500 Index is an unmanaged, market value-weighted index of 500 stocks generally representative of the broad stock market. An investment cannot be made directly in a market index.

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The Russell 2000 Index measures the performance of the 2,000 smallest companies in the Russell 3000 Index, which represent approximately 8% of the total market capitalization of the Russell 3000 Index.

Investing in small cap stocks generally involves greater risks, and therefore, may not be appropriate for every investor.

The companies engaged in the communications and technology industries are subject to fierce competition and their products and services may be subject to rapid obsolescence.

Market return and statistical data obtained from: https://am.jpmorgan.com/blob-gim/1383452890099/83456/weekly_market_recap.pdf?segment=AMERICAS_US_ADV&locale=en_US

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