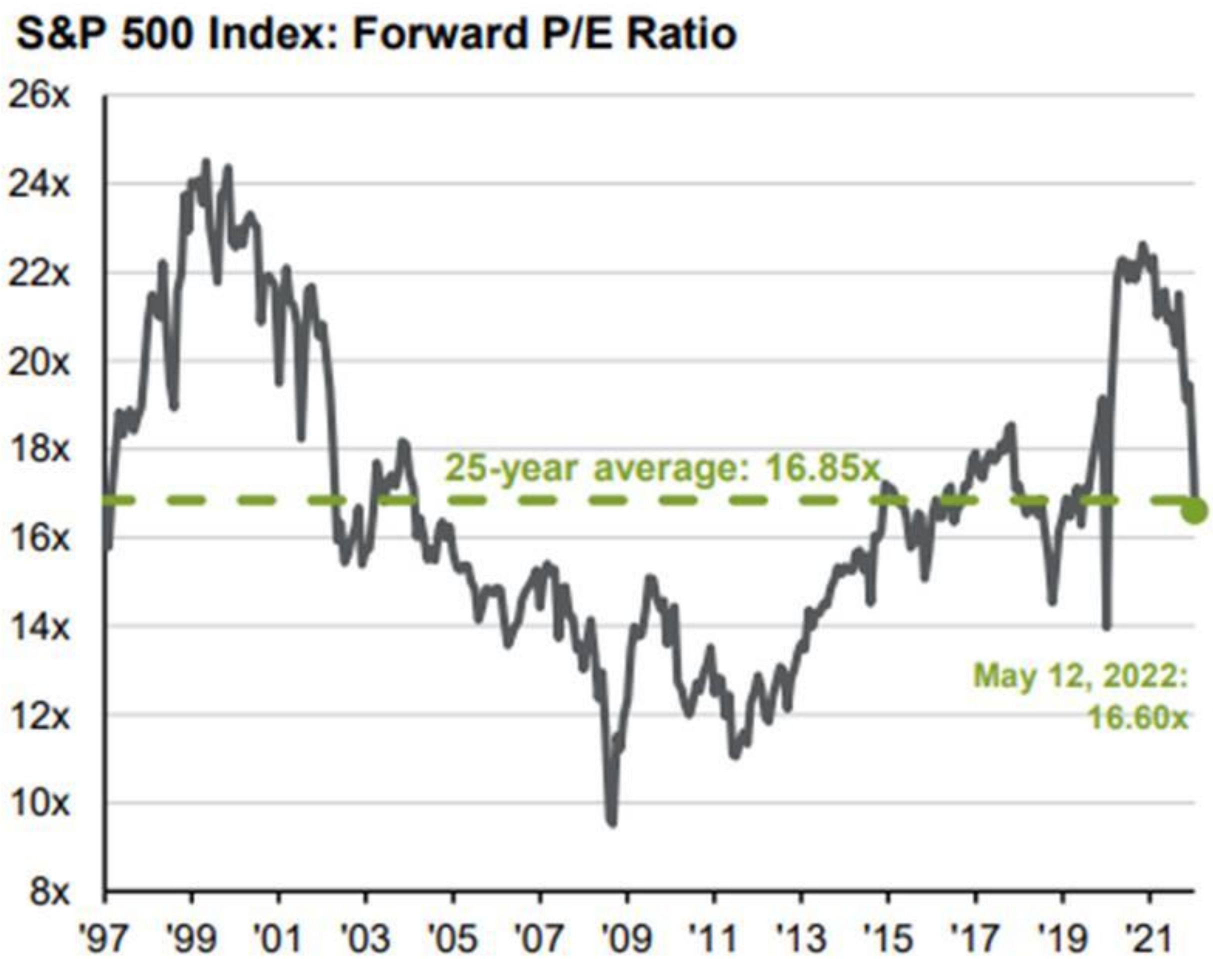
Monday, May 16, 2022

Good afternoon:

Hope for a significant drop in the rolling annual inflation rate did not materialize last week as the April CPI report showed inflation is still running hot. While the rate did drop from 8.5% to 8.3%, the decline was less than the 8.1% anticipated rate. As a result, fears of more aggressive Fed action in the coming months prompted another round of selling in the stock market. However, as small as the decline in the CPI was, it still may indicate that inflation has peaked. As we discussed on one of our recent client calls, inflation merely measures the *rate* of price increases. Therefore, even when inflation declines more significantly, prices generally may remain at current elevated levels.

All areas of the market were hard hit for most of last week before Friday's bounce managed to recover about half of the decline. Major averages posted weekly declines of about 2½% as traders and investors now try to determine whether the market may have found a bottom. Clearly, uncertainty and concern about the impact of inflation and rising rates on the economy will be with us for quite some time. Markets try to price-in as much of the potential consequences to equity earnings and valuations, but often overshoot. Just like valuations can get very frothy on the upside, stock prices can become very oversold on the downside, irrespective of company fundamentals. As a result, we remain in very challenging and volatile markets with many traders and hedge funds opting to sell every bounce the market can muster.

Today's modest declines at the open illustrate the market's inability to build on Friday's recovery. The negative investor sentiment is also starting to reflect in the latest drop in consumer sentiment. University of Michigan's Consumer Sentiment Index fell from 65.2 to 59.1 this month, its lowest level in more than a decade – even lower than the worst of the great financial crisis in 2009. It's clearly rising consumer prices perhaps coupled with declining markets that are behind these results. Ironically, declines in both consumer and investor sentiment may actually serve to *help* in the Fed's effort to cool inflation as declines in portfolios may cause some to curtail spending in the near term.



Let's not lose sight of the big picture. As a result of recent volatility in this market correction, equity valuations have declined to much more reasonable levels. History suggests that periods of high investor angst or even gloom have been great times to invest when others are exiting stocks out of fear. Indeed, following 8 rather obvious troughs in consumer sentiment over the last 50 years, subsequent 12-month S&P 500 returns averaged almost 25%. The problem is that *logic* and *emotion* oppose each other in our minds creating uncomfortable cognitive dissonance for many as we go through difficult periods like this in the market. We encourage our clients to keep their emotions in check and consider this correction in the context of the past couple years of strong market performance. Remember, market bottoming is a *process*, where increased volatility and choppy trading is the norm.

We will continue to watch the earnings and fundamental underpinnings of companies within the funds we manage while we wait for further indications of moderating inflation. Although fund managers have been adjusting their portfolios to address current conditions, a broad-based correction such as this impacts all sectors. Companies with growing earnings and dividends will likely continue to fare better, but patience will be necessary to get through this period.

Have a great week!

Mark and Jeff

Mark S. Loftus, CFP®
Managing Partner & Founder, LPWP
Registered Principal, RJFS

Jeffrey C. Preusser, CFP®
Senior Partner, LPWP
Registered Principal, RJFS

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

The Dow Jones Industrial Average (DJIA), commonly known as “The Dow” is an index representing 30 stocks of companies maintained and reviewed by the editors of the Wall Street Journal.

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.

The NASDAQ Composite Index is a broad-based capitalization-weighted index of stocks in all three NASDAQ tiers: Global Select, Global Market and Capital Market.

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.

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

Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance. Individual investor's results will vary.