CAPITAL INVESTMENT SERVICES, LLC

Finding Balance in 2023
Q1 Quarterly Commentary

Happy New Year! As we look forward into 2023, Capital Investment Services (CIS) will be celebrating 15 years in business. Since the beginning in 2008, our focus has been “Client First” and building relationships with our clients that goes far beyond the world of finance. The core values of CIS have been in place from the beginning and remain our foundation.

I am grateful for the confidence that you place in my team as we navigate complicated markets while working to grow your overall net worth. As we begin this new year, please allow me to say thank you for allowing our team the opportunity to serve as your trusted advisor. We stand ready to serve in 2023.

When I think about 2022, the word that continues to come to mind is “noisy”. In summary, the Fed raised interest rates at the fast pace in history, Russia invaded Ukraine, China’s continuation of its zero COVID policy and the US political division, all markets were operating in a very noisy environment with the backdrop of recessionary pressures and slowing economic momentum. These issues developed a grind through the year that resulted with the constant repricing of assets in all markets. Amid all the noise, the financial markets remained healthy with a record amount of activity and trading volume. Throughout 2022, the quest to find balance in a portfolio seemed almost impossible.

Q4 and Full Year 2022 Performance Review

Unlike the first three quarters of 2022, when all four major indices saw quarterly declines, performance was mixed during the fourth quarter as the Dow Jones Industrial Average rose sharply, while the S&P 500 and Russell 2000 were solidly higher. However, like most of 2022, the Nasdaq lagged and fell slightly in the fourth quarter. Expectations for higher rates, slowing economic growth and underwhelming earnings weighed on the tech sector in the fourth quarter, which was the case for much of 2022. Conversely, less economically sensitive companies that trade at lower valuations than tech stocks outperformed. On a full-year basis, all four major indices posted negative returns. With the NASDAQ being the worst performer with a 2022 return of -32.38%.

S&P 500 Total Returns by Month in 2022											
Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
-5.17%	-2.99%	3.71%	-8.72%	0.18%	-8.25%	9.22%	-4.08%	-9.21%	8.10%	5.59%	-5.90%

Source: Morningstar

US Equity Indexes	Q4 Return	2022 Return
S&P 500	7.56%	-18.11%
DJ Industrial Average	16.01%	-6.86%
NASDAQ 100	-0.04%	-32.38%
S&P MidCap 400	10.78%	-13.06%
Russell 2000	6.23%	-20.44%

Source: YCharts

International Equity Indexes	Q4 Return	2022 Return
MSCI EAFE TR USD (Foreign Developed)	17.40%	-14.01%
MSCI EM TR USD (Emerging Markets)	9.79%	-19.74%
MSCI ACWI Ex USA TR USD (Foreign Dev & EM)	14.37%	-15.57%

Source: YCharts

Switching to fixed income markets, the leading benchmark for bonds (Bloomberg Barclays US Aggregate Bond Index) realized a positive return for the fourth quarter but declined sharply for the full year of 2022, due to aggressive Fed rate hikes combined with decades-high inflation.

Looking deeper into the fixed income markets, longer-duration bonds outperformed those with shorter durations in the fourth quarter, due to bond investors reacting more favorably to economic data. For the full year, shorter-term bonds handily outperformed longer-duration bonds as they were less impacted by Fed rate hikes and spiking inflation.

US Bond Indexes	Q4 Return	2022 Return
BBgBarc US Agg Bond	1.87%	-13.01%
BBgBarc US T-Bill 1-3 Mon	0.89%	1.52%
ICE US T-Bond 7-10 Year	0.98%	-14.90%
BBgBarc US MBS (Mortgage-backed)	2.14%	-11.81%
BBgBarc Municipal	4.10%	-8.53%
BBgBarc US Corporate Invest Grade	3.63%	-15.76%
BBgBarc US Corporate High Yield	4.17%	-11.19%

Source: YCharts

In sum, 2022 was a difficult year for investors from a return and volatility standpoint. It required decisive action within the portfolios regularly to navigate the evolving landscape. Multi-decade highs in inflation combined with historically aggressive Fed rate hikes led to growing concerns about economic state pressured both stocks and bonds. The S&P 500 posted its worst performance since 2008 while major benchmarks for both stocks and bonds declined together for the first time since the 1960s, punctuating just how disappointing the year was for investors.

2023 Market Outlook

Our focus must be on finding balance as it appears the Fed will begin slowing its pace of raising rates in early 2023. The losses in stocks and bonds were driven by decades-high inflation and geopolitical unrest. While those factors were clear negatives for asset prices in 2022, it's important to note that as we enter 2023, the market is approaching an important transition period that could see each of these headwinds ease in the months ahead.

First, inflation has shown definitive signs of peaking and declining. The Consumer Price Index has fallen from a high of 9.1% in June to 7.1% in November, while other metrics of inflation have registered similar declines. Now, to be clear, inflation remains much too high in an absolute sense, but if price pressures ease faster than expected, this will present a positive surprise for markets in the first several months of 2023.

Second, after a historically aggressive rate hiking campaign in 2022, the current Fed hiking cycle is likely nearly complete. In December, the Federal Reserve signaled that it expected the peak interest rate to be just 75 basis points higher than the current rate. That level could easily be reached within the first few months of 2023 and the Fed ending its rate hike campaign will remove a significant headwind from asset prices.

Finally, while both economic growth and corporate earnings are expected to decline in 2023, those negative expectations have been at least partially priced into stocks and bonds at current levels. As such, if the economy or corporate America proves to be more resilient than forecasts, it could provide a positive spark for asset markets in early 2023.

As we start the new year, we should expect financial media commentary to be focused on the 2022 losses and current market risks, including earnings concerns and recession fears. However, the market is a forward-looking instrument. While there are undoubtedly economic and corporate challenges ahead in 2023, some of those best-known risks are partially priced into markets already, and there are positive catalysts in place as we start a new year.

My Commitment to You

1. We are prepared for continued volatility and are focused on managing both risk and return potential.
2. We understand that finding a balance between income producing investments and stocks is the most appropriate way to address the new year.
3. We understand the risks facing both the markets and the economy.
4. We are committed to helping you effectively navigate this challenging investment environment.

Remember, successful investing is a marathon, not a sprint. Therefore, it’s critical for you to stay invested and remain patient as we’ve worked with you to establish a unique, personal allocation target based on your financial position, risk tolerance, and investment timeline.

Thank you for your ongoing confidence and trust. Please rest assured that my team will remain dedicated to helping you successfully navigate this market environment, and do not hesitate to contact us with any questions, comments, or to schedule a portfolio review.

Sincerely,

Bobby Lumpkin
President, CIS
Founder, *investingsimply*
Financial Advisor, RJFS