Weekly Market Update

October 16, 2023

by David A. Smith, CFP®, MSFS, AIF® and Michael Cozad, CFP®, MSFS

"All the magic I have known
I've had to make myself."

~ Shel Silverstein
from
"Where the Sidewalk Ends"

Market Watch

Week Ending Oct. 13, 2023

(Source: Briefing.com)

• DJIA: *2023 YTD 1.60%*	33,670.20	262.70
• NASDAQ: *2023 YTD 28.10%*	13,407.20	-24.10
• S&P 500: *2023 YTD 12.70%*	4,327.78	19.28
• Russell 2000: *2023 YTD 2.40%*	1,719.71	-25.85
• 10 Year Treasury:		4.63%

SMITH, MOSES & COZAD

Beavercreek Office:
2149 N. Fairfield Rd., Suite B
Beavercreek, OH 45431
ph: 937.431.8010

smithmosesandcozad.com

Dave's Weekly Commentary

Hello everyone, I hope everyone had a pleasant week and weekend. The office had a busy week last week, and looking at my calendar, another busy week is in store for us. Later this week Nancy and I will be heading to Phoenix to attend our annual multi-firm educational conference (called ConnectEd). The rest of the team will follow on Sunday as the conference begins Sunday evening. On Sunday morning, we will have the last FSC Advisory Board meeting, as the firms transition under one umbrella – Osaic. I have thoroughly enjoyed and was honored to be an advisor board member for the past five years and am humbled to be part of such a talented and dedicated group of financial professionals.

Remember the saying "when one door closes another door opens"? Michael and I received some exciting news late Friday. Osaic (formerly Advisor Group) formalized a "Teams Council," comprised of teams like ours, to help Osaic develop processes, focused services, and tools. The council is comprised of 18 members. Michael and I applied to be members of the council and were notified Friday we were selected to be 2 of the 18 council members.

As council members, a primary mission will be to collaborate, challenge, and provide feedback to Osaic for the benefit of the 11,000+ financial professionals across the country. While volunteering to serve takes time away from the office it helps us become better financial advisors and hopefully through our contributions and experience helps other advisors and firms become better. I think I can speak for Michael on this subject this is an investment in our and our clients future to keep forging ahead to stay and be a first in class firm.

One last point before I move on to some economic and market commentary. Moving from FSC Securities Corporation to Osaic means our email address will change. Shortly, you'll receive separate email communications from us notifying you of our new email addresses. Our fscadvisor.com emails will be forwarded for several months, the details are on page 2 of this newsletter and we'll cover them in a separate correspondence.

When is there a Return to Normal?

Interest Rate When the Federal Reserve started raising its policy rate in March 2022, the yield on of 10-yr note was about 2.15%. Not that long ago, it was knocking at the door of 5.00% and today it sits at 4.63%. That is a big move in a short amount of time. Where things sit today looks and feels abnormal for a lot of investors who have only known the low and ultra-low interest rate environment that had become entrenched in the post-financial crisis period. Well, that period is over, and a new period has arrived. The new period is going to be accented with higher rates, or at least higher than the low rates that were the norm for the past 15 years +/-.

Inflation Still Inflated Things don't feel normal today because the inflation rate doesn't feel normal. It is higher than it was the last time rates were "normal." Inflation is getting better, but core-PCE inflation is still well above the Fed's 2.0% target rate. Some think that the inflation rate might not get much lower than 3.0% for some time given the structural shifts in the economy that include, among other things, de-globalization, baby-boomers aging out of the workforce, and higher budget deficits.

Deficit Concerns By the end of 2022, the federal deficit as a percent of GDP stood at -5.3%, much improved from the -14.7% seen in 2020 COVID year, but worse than anything seen between 1998 and 2008. The budget deficit remains a growing problem for the U.S., which must contend with growing entitlement spending and demographic challenges that include lower birth rates and retiring baby boomers enjoying longer life expectancies. A pressing concern today is that the deficit is as large as it is when the economy is growing. What happens, then, if the lag effect of prior rate hikes, and higher market rates, ends up driving the economy into recession and tax receipts dwindle at a time when more social assistance is needed, and possibly at a time, too, when defense spending may need to be increased?

This return to normal is perhaps the most uncomfortable for the generation that came of financial age after the financial crisis. That is an age that grew accustomed to quantitative easing, not the quantitative tightening we are experiencing now. It is an age that only knew a core-PCE inflation rate that vacillated between 1.0-2.0%. It is an age when we thought a mortgage rate under 5.0% was normal. It is an age that saw the effective fed funds rate barely get above 2.0% while spending most of its time closer to the zero bound until now. It is an age that was inclined to think that a 10-yr note yield between 1.0% and 3.0% was the norm. We may be seeing today is more normal, even if the way we got here is not. The latter is understandably making investors of all ages feel uncomfortable knowing that things are different from when we last saw normal.

Last Week's Markets... Market participants entered the week with news that Israel declared war on Hamas after a surprise attack launched by Hamas last weekend. The potential for a wider regional clash weighed on sentiment this week but reports so far give the impression that the Israel-Hamas war is still a two-party conflict. The stock market still fared okay this week, aided by a decline in Treasury yields. Oil prices climbed this week in another manifestation of geopolitical worries. WTI crude oil futures jumped 6.0% to $87.80/bbl. Eight of the S&P 500 sectors registered a gain with energy (+4.5%) leading by a wide margin. The consumer discretionary sector (-0.7%) saw the largest decline. Source: Briefing.com

Newsletter continues on the next page.

Updated SMC Team Emails

We have updated our SMC Team email addresses to reflect our website. This change will help us better serve you and ensure the security of our communications.

Beginning today, all communications will be sent from the new email addresses:

Dave Smith:
dsmith@smithmosesandcozad.com

Michael Cozad:
mcozad@smithmosesandcozad.com

Daniel Griffith:
dgriffith@smithmosesandcozad.com

Kailee Hiss:
khiss@smithmosesandcozad.com

Maddie Cook:
mcook@smithmosesandcozad.com

Megan Cyrus:
mcyrus@smithmosesandcozad.com

Cole Fisher:
cfisher@smithmosesandcozad.com

Please take note that our old email address will be phased out over the next few months to allow for a smooth transition.

We kindly ask that you update your records with our new email address to ensure that you continue to receive important emails and information.

Thank you for your continued support.

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Beavercreek, OH 45431
ph: 937.431.8010

smithmosesandcozad.com

Planning Points, Part 1 of 2 *To read the article in it's entiirety, visit https://www.smithmosesandcozad.com/blog*

Investing Has Been Ugly. Stick With It Anyway.

This is one of those stretches when you may want to avoid looking at your investments.

Performance reports for the three months that ended in September are arriving now, and they are ugly. The vast majority of mutual funds and exchange-traded funds — the vehicles used by most Americans for their investments — fell. There were losses in most markets and in nearly all asset classes.
If you've lost money, take some deep breaths, practice yoga, watch a ballgame, enjoy time with family and friends — whatever works. But don't make abrupt changes in your investments. A good plan is better than an emotional response when markets fall.

I say all that assuming you already have a solid investment portfolio set up — a simple one, ideally, containing cheap funds, preferably index funds that mirror the total market.

If you don't have a solid plan yet, a downturn is a great time to start. Most basically, stock and bond prices will be lower than they were just a short time earlier.

But invest for the long term. Hold diversified stock funds for higher returns and bond funds for income and stability (although bonds haven't been paragons of stability lately), and stick with them. Stash the money you need to pay the bills in money-market funds, short-term savings accounts and Treasury bills.

Keep your costs low and hold broadly diversified investments for years to come. For most people, that's a much better bet than stock-picking and frequent trading, numerous studies show.

This approach requires the ability to withstand losses, though, and that ability is being tested now.

Nasty Numbers

The average domestic stock fund in the Morningstar database declined 3.5% for the quarter. The average taxable bond fell 1.1%. The average municipal bond fund fell 3.3%. As a group, internationally oriented stock funds fared even worse. They declined 4.7%.

Furthermore, core stock and bond indexes that function as benchmarks — and, in some cases, are the foundation — for many mutual funds and ETFs. fell during the quarter.

Dividends included, the S&P 500 stock index lost 3.3% for the three months through September.

These numbers aren't shocking in themselves. What makes them painful, however, is that they come after the markets had begun recovering from the steep declines of last year.

It shouldn't be terribly surprising when the stock market falls. Such declines have made headlines for decades. But bonds are different. They have a reputation for steady, even stodgy performance. The latest returns undercut those assumptions.

For the last quarter, the Bloomberg Aggregate Bond Index (it was once the Lehman Brothers Aggregate Index) lost 3.2%, including dividends, nearly as much as the S&P 500. What's worse, over three years, this core bond index lost nearly 15%, including interest paid out in dividends, while the S&P 500 gained about 34%.

Those returns understate the bond market carnage. The Bloomberg U.S. Treasury 20+ Year Index, which tracks long-term Treasurys, lost 13% for the quarter — and about 42% for the three years through September, including dividends.

You don't need to worry about individual, high-quality bonds if you hold them to maturity. But if you trade them while market interest rates rise, you can incur serious losses.

What Causes the Losses?

A major shift in interest rates caused the pain in the bond market and hurt stocks, too.

Recall that during the first stage of the pandemic, the Federal Reserve dropped the short-term federal funds rate to nearly zero in a bid to support the ravaged economy. Then, after inflation became red-hot, it began raising short-term rates early last year in an effort to put out the inflation fire. It isn't done yet.

Longer-term rates in the bond market didn't rise as much or as quickly at first — perhaps signaling an eventual recession — but longer-term bond rates have been shooting up lately.

Article continues next week.