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BALANCED INVESTMENT MANAGEMENT

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Archer 2nd Quarter 2022 Outlook:

Inflation has been the word of the year so far in 2022 and shows few signs of easing any time soon. As you are likely aware, gas prices are higher, the cost of groceries has increased and just about everything you can purchase has risen in price. This increase in inflation is relatively simple to explain; more money chasing fewer goods and services. It has everything to do with the government passing out free money to every type of entity available (PPP money to businesses, ARPA money to local governments, individual checks, loan forgiveness, etc.) All of this money in the system has a cost and now it is time to start paying for it in the way of higher prices for goods and services.

This does not mean the stock market will falter, although we do believe returns will be muted going forward. If you look at the following chart of historical Federal Funds rates, you will see that often, increases or decreases in rates are quickly reversed by the Federal Open Market Committee. It will not surprise you that often, the hard-working government officials are behind the curve when it comes to raising rates or reducing rates. This interest rate manipulation is an effort to control employment, earnings power, inflation, and a myriad of other items.

Our attention is on the stock and bond market as we navigate these rate hikes and what actions we should take in investor portfolios. The shaded areas above are the periods of recession. Some of these recessions were caused by the Fed raising rates too many times. However, some of them were not Fed induced. The COVID-19 closing of the global economy in 2020 led to a sharp, but brief recession before governments around the world turned on the spigots and flooded the world with liquidity.

If we focus on 1970 to present, we can see in the following table where the Fed Funds Rate started and ended and what the stock market did during the same time frame. We can see stocks held up reasonably well during these past hiking cycles.

Dates	Fed Funds Rate Starting Rate	Fed Funds Rate Ending Rate	S&P 500
1971-1974	3.75%	13.00%	-7.52%
1976-1981	5.50%	20.00%	68.38%
1983-1984	9.50%	11.50%	8.05%
1985-1988	6.00%	9.75%	52.42%
1994-1995	3.25%	6.00%	4.45%
1999-2000	5.00%	6.50%	10.48%
2004-2006	1.25%	5.25%	17.74%
2015-2018	0.00%	2.50%	28.37%

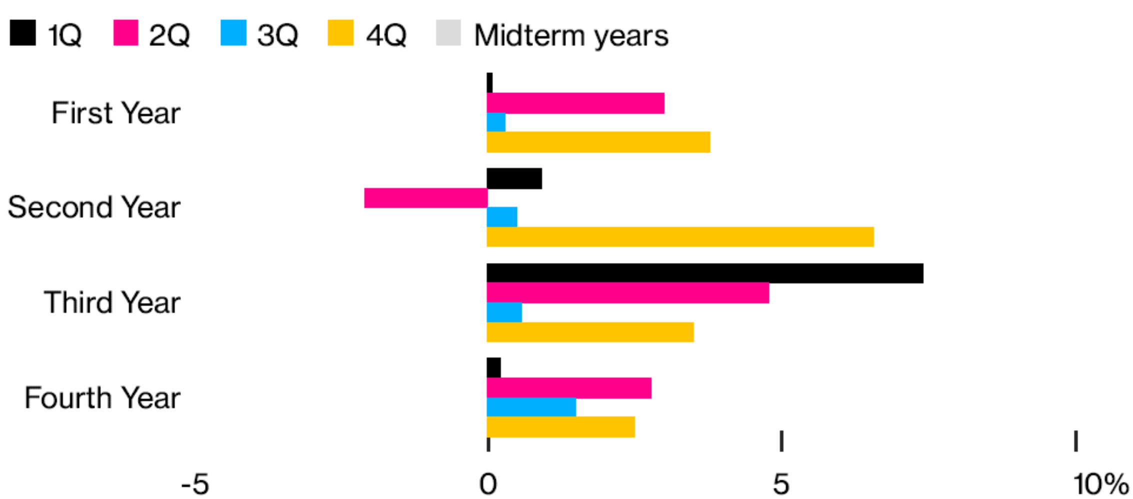
Source: FRED

According to Morningstar, the average US Stock and bond performance 12 months following the first Fed hike from 2/4/94 – 12/31/21 was a return of 7.3% for stocks and 3.2% for bonds. We are not as confident on the returns for the bond side of the equation. We will likely make some adjustments to our portfolios to protect against further increases in interest rates, as we have done for the last few years to lower interest rate risk.

For 2022, one of the most impactful variables on the markets may be the impending mid-term elections. Generally, the mid-term weakness starts in May and ends in October, with the majority of the weakness in the 2nd Quarter. This is normally followed by a solid rally in late November and December. We do not expect this year to be any different.

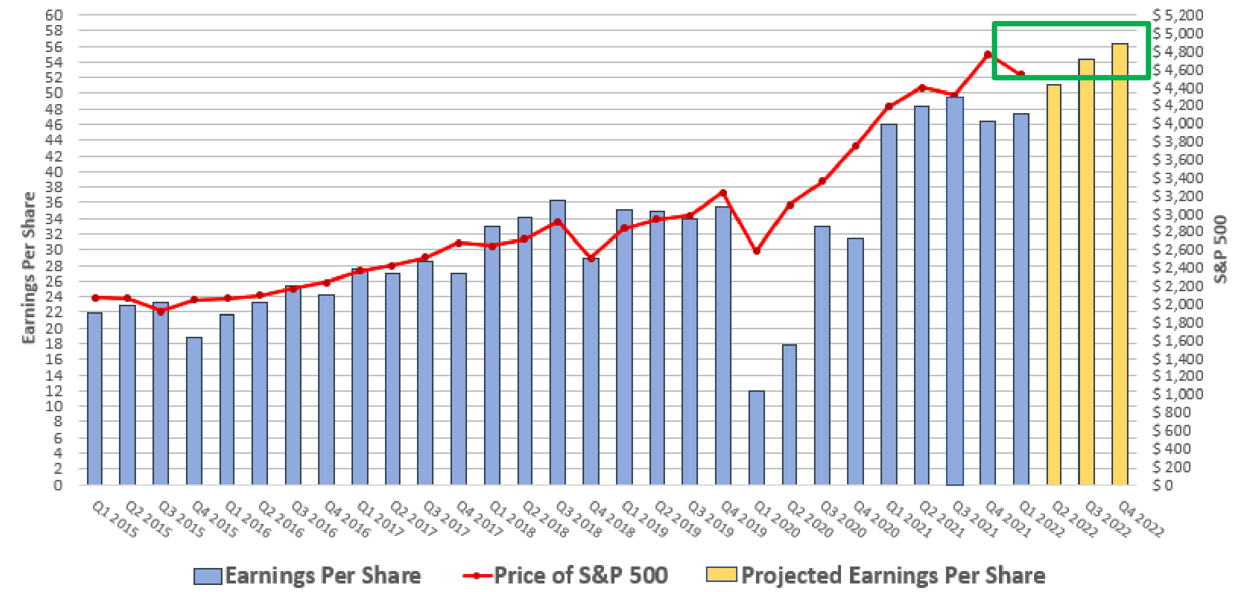
Midterm Weakness

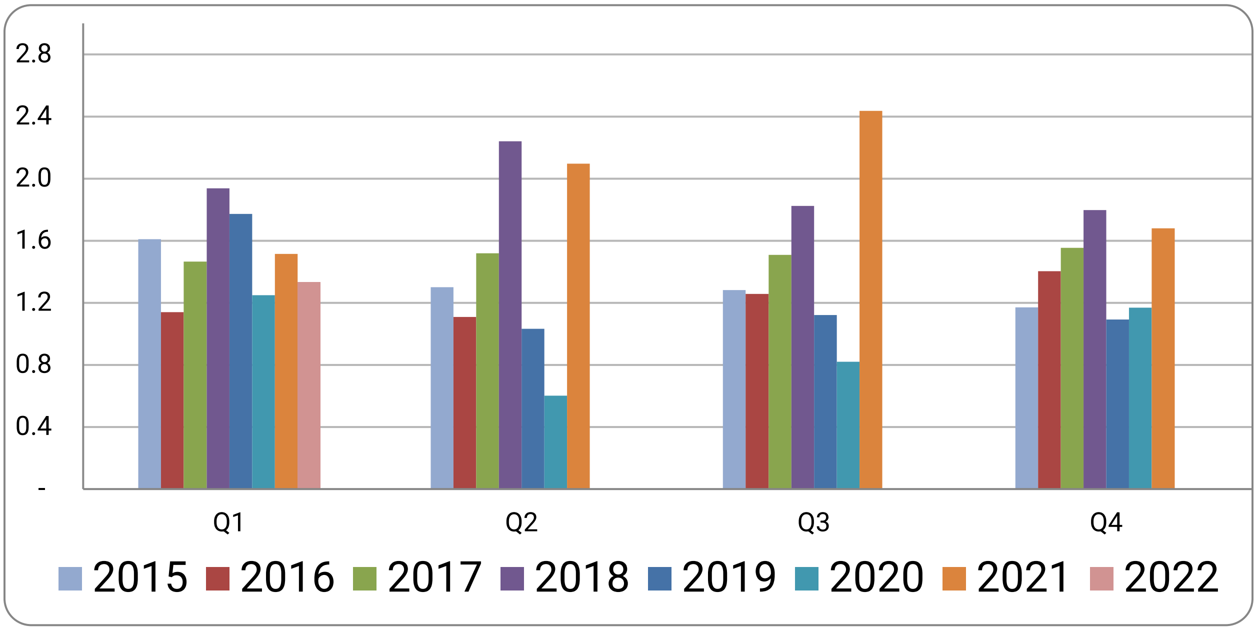
S&P 500 quarterly performance by presidential cycle from 1950-2021



As always, regardless of the change in politics, administrations, the Fed, or any other factor, the bottom line is if earnings are rising, then the stock market will generally rise with it. Below is the chart with the actual earnings and the expected earnings over the next 3 quarters. As you can see, the expectation is for earnings to continue to increase. This should result in further market gains.

Quarterly earnings continue to come in higher than last year, even with the prior year's earnings showing large increases thanks to pent up demand from COVID. In fact, retail sales were nearly 25% higher than prior to COVID, while manufacturing production was up only low single digits. This continues to be a catalyst for the market as inventories attempt to keep up with demand (thus inflation). The inflation should continue to subside once supply chains are repaired and inventories rise to the level of demand.





We continue to see positive returns for 2022, given an increase in corporate profits, inflation getting in check and the labor market remaining positive. We do see the returns being much lower than the previous three years, but positive, nonetheless. We will continue making adjustments to portfolios as rates gyrate and possibly move higher.

Regards,

The Archer Team