Vardhan Views: Week of October 10th, 2022

Periodic Returns

	Trailing Week			Quarter-to-Date			Year-to-Date		
	Value	Blend	Growth	Value	Blend	Growth	Value	Blend	Growth
U.S. Large-Cap	2.2%	1.7%	1.2%	-3.5%	-3.0%	-2.4%	-15.9%	-23.3%	-29.8%
U.S. Mid-Cap	2.3%	2.5%	2.8%	-2.7%	-1.0%	2.2%	-18.5%	-22.4%	-29.5%
U.S. Small-Cap	2.2%	2.3%	2.3%	-2.5%	0.0%	2.6%	-19.4%	-23.4%	-27.6%

	Trailing Week	Quarter-to-Date	Year-to-Date
S&P 500 Index	1.6%	-3.4%	-22.7%
NASDAQ Composite	0.7%	-3.2%	-31.5%
International Developed	1.9%	-7.6%	-25.7%
Emerging Markets	2.5%	-9.3%	-25.3%
U.S. Aggregate Bond	-0.3%	-5.0%	-14.8%
U.S. Municipals	0.8%	-2.7%	-11.4%
Corporate High Yield	1.4%	0.8%	-13.5%

Source: Morningstar, see 'Disclaimer' for details

U.S. Equity Markets

- U.S. equity markets finished higher for the first time in four weeks. That said, weakness late in the week handed back much of the rally sustained earlier in the week.
- Recent equity market performance has been heavily impacted by anticipated (and realized) central bank action. The rally earlier in the week reflected some downside surprises in data (bad news is good news) which could add to the argument for the Fed to not hike as aggressively going forward. An encouraging jobs market report later in the week (good news is bad news) almost fully reversed the rally.
- Despite substantial volatility, volumes were somewhat muted as investors awaited the third quarter earnings season and due to the observance of Yom Kippur.
- Within the S&P 500 Index, the energy sector was a standout performer – rising nearly 14%. This added to a 50%+ gain for the sector year-to-date. Interest rate-sensitive sectors, such as real estate and utilities, were notable laggards and ended up down for the week reflecting higher bond yields.

International Equity Markets

- International equity markets (both developed and emerging) also gained last week, although levels from mid-week were meaningfully higher than at Friday's close.
- European equities logged a small local market gain which converted to a small loss when converted to USD. The euro continues to be at its lowest level (0.974 euro/USD) since the early 2000s.
- Japanese equities rose in both local and USD terms recovering from a challenging September for most Asian markets.
- Chinese equity markets were shut for much of the week to celebrate the National Day (Golden Week) holiday.

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Credit Markets (Perspectives from our partners at Piton Investment Management)

- U.S. Treasury yields rose late in the week following the September jobs number. The curve flattened as the 2-year yield climbed to 4.31%, while the 10-year climbed to 3.88%.
- Corporate investment-grade spreads tightened modestly on the week.
- Corporate bond funds had continued outflows, although they were below levels reached last week. Investment-grade funds lost ~$3.5 billion while high yield funds were down ~$1.9 billion.
- Primary Issuance finished above dealer estimates. Recent corporate bond issues are coming in with higher concessions (4x the year-to-date average) and lower than average interest books. Borrowers are paying higher funding costs to issue new debt.
- Municipal yields led the treasury market this week. Despite slightly higher treasury yields in a volatile weak, municipal bonds yields fell on average by 7 basis points (0.07%) across the high-grade tax-exempt curve.
- The muni curve also flattened by 4 basis points to 83 basis points (between short and long duration bonds).
- The performance of muni bonds has left tax-exempt portfolios near historical fair value. Not expensive, but not cheap, versus government bond counterparts. Here are approximate historical muni valuations relative to Treasuries:
    - 2 year- 71%
    - 5 year- 75%
    - 7 year- 77%
    - 10 year- 83%
- Negative muni fund flows continued to build with tallies of over $100 billion in outflows for 2022.
- Trading in the secondary muni market totaled $97 billion in the past week, up 11% from the previous week.

U.S. Economic Data/News

- The change in nonfarm payrolls rose 263,000 last month, down from the prior 315,000 and slightly above the consensus. The unemployment rate came in at 3.5%, down from 3.7% last month. The important data points out of the labor market showed little signs of a serious economic slowdown, and support further aggressive tightening by the Fed.
- The market-implied expectation remains 75 basis points (0.75%) for November and will remain heavily influenced by data points in the coming month.
- The ISM manufacturing activity index fell to 50.9 in September, just slightly above the level indicative of a contraction in the space. Related but more positive, ISM also reported that pricing pressures for manufacturers were falling.
- OPEC+ announced a cut of 2 million barrels per day mid-last week which drove the price of oil meaningfully higher. In the U.S., a barrel of crude crossed the $90 mark for the first time since August.

International Economic Data/News

- Eurozone inflation rose to 10% in September. Producer prices also surprised to the upside, largely driven by surging energy costs.
- Minutes from the ECB's recent policy meeting showed continued concerns about rising inflation and support for additional monetary tightening. There is growing support for a 75-basis point hike at their next meeting whereas a 50-basis point hike seemed more likely in prior weeks.
- The yen remained in focus for Japanese policymakers. Despite a short-lived rally earlier in the week, the yen is next to its lowest level relative to the USD since 1990. Japan's foreign reserves are also declining because of the government's intervention in their currency markets.
- In China, Beijing has increased measures to support its debt-strapped property sector ahead of the Communist Party congress. President Xi is assumed to assert a third term while there's some hope for the relaxation of the government's zero-COVID policy.

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Odds and Ends

- Many large U.S. businesses say they have been able to increase prices this year with limited pushback from customers. Not all the changes are leading to higher corporate profits. Prices are sticky, economists like to say. Once they go up, customers get used to it, and they rarely come down quickly. If companies' costs then fall, they can pass along even a little of the savings and keep the rest, customers get a bit of a break and margins still widen. Corporate profit margins or the difference between expenses and revenue, reached historically high levels in recent quarters, helped by strong consumer demand for a range of goods and services. But as more companies prepare to report third-quarter results, there are signs that profits might be under pressure, at least relatively speaking. Excluding the volatile energy sector, analysts expect third-quarter earnings to decline 2.6% from the third quarter of 2020, Refinitiv said.
- Rapidly rising interest rates are squeezing the flow of private capital to the world's poorest countries. The problem is that the preferred alternatives such as the International Monetary Fund(IMF) and World Bank, are getting quickly committed. Lending by the pair has reached a record as they help poor and emerging countries cope with the pandemic, soaring energy costs, and the fallout from Russia's invasion of Ukraine. The IMF has committed $258 billion to 93 countries since the onset of the pandemic, and an additional $90 billion to 16 countries since Russia's invasion of Ukraine. Not all committed funds have been lent out. At the end of September, the IMF had a record $135 billion of loans outstanding, up 45% from 2019, and more than double the amount in 2017.
- The Nobel Prize in Economic Sciences was awarded to former Federal Reserve chief Ben Bernanke and two other U.S. academics whose work helped governments and central bankers navigate the global financial crisis and avoid an economic depression of the kind seen during the 1930s. Bernanke, who served as chairman of the Fed during the crisis, is currently a distinguished senior fellow at the Brookings Institution. His fellow recipients are Douglas Diamond, an economist at the University of Chicago, and Philip H. Dybvig, an economist at Washington University. Announcing the prize, Stockholm University economist John Hassler said their research had proved invaluable during the 2008 crisis, which brought the global financial system to the brink of collapse.

Resource of the week:

- This episode of *Invest Like the Best* features Scott Wilson. Scott is the CIO of Washington University (Wash U) in St. Louis' Endowment, which manages over $13 billion. In this conversation, Patrick (host) and Scott discuss Wash U's non-traditional endowment model and cover a variety of asset classes and geographies. They talk about the quality Scott looks for in managers, lessons from investing in Asia and emerging markets, and red flags in the venture space. Please enjoy this conversation with Scott Wilson.
- **Podcast link**: https://www.joincolossus.com/episodes/43243284/wilson-global-endowment-investing?tab=transcript

Sources: The WSJ, T. Rowe Price Global Markets Weekly Update

DISCLAIMER

This commentary was written by Craig Amico, CFA®, CIPM®, Associate Director of Investment Management, Noreen Brown, CFA®, Deputy Chief Investment Officer and Steven Melnick, CFA®, Associate Director of Investment Management at Summit Financial, LLC., an SEC Registered Investment Adviser ("Summit"), headquartered at 4 Campus Drive, Parsippany, NJ 07054, Tel. 973-285-3600. It is provided for your information and guidance and is not intended as specific advice and does not constitute an offer or solicitation to buy any securities mentioned. Summit is an investment adviser and offers asset management and financial planning services. Indices are unmanaged and cannot be invested into directly. The periodic returns are represented by the following indices: large-cap value by Russell 1000 Value TR Index, large-cap blend by Russell 1000 TR Index, large-cap growth by Russell 1000 Growth TR Index, mid-cap value by Russell Mid Cap Value TR Index, mid-cap blend by Russell Mid Cap TR Index, mid-cap growth by Russell Mid Cap Growth TR Index, small-cap value by Russell 2000 Value TR Index, small-cap blend by Russell 2000 TR Index, and small-cap growth by Russell 2000 Growth TR Index, international developed by the MSCI EAFE NR USD Index, Emerging Markets by the MSCI EM NR USD Index, U.S. Aggregate Bond by the Bloomberg US Agg Bond TR USD Index, U.S. Municipals by the Bloomberg Municipal TR USD Index, and Corporate High Yield by the Bloomberg US Corporate High Yield TR USD Index. The S&P 500 Index is a market capitalization-weighted Index of 500 widely held stocks often used as a proxy for the stock market. It measures the movement of the largest issues. Standard and Poor's chooses the member companies for the 500 based on market size, liquidity, and industry group representation. Included are the stocks of eleven different sectors. The Nasdaq Composite Index is a large market capitalization-weighted index of more than 2,500 U.S.-domiciled stocks. The index's composition is heavily weighted to the information technology sector, with consumer services, health care, and financials the next most prominent industries. The Russell 2000 Index measures the performance of the small-cap segment of the U.S. equity universe. It is a subset of the Russell 3000 Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2,000 of the smallest securities based on a combination of their market cap and current index membership. The Russell 1000 Index measures the performance of the large-cap segment of the U.S. equity universe. It is a subset of the Russell 3000 Index representing approximately 90% of the total market capitalization of that index. It includes approximately 1,000 of the largest securities based on a combination of their market cap and current index membership. The Russell 3000 Index measures the performance of the largest 3,000 U.S. companies representing approximately 98% of the investable U.S. equity market. It is constructed to provide a comprehensive, unbiased, and stable barometer of the broad market and is completely reconstituted annually to ensure new and growing equities are reflected. The MSCI EAFE Index (Europe, Australasia, Far East) captures large- and mid-cap representation across developed markets countries around the world, excluding the U.S. and Canada. The index covers approximately 85% of the free float-adjusted market capitalization in each country. The MSCI Emerging Markets Index captures large- and mid-cap representation across emerging markets countries across the world. The index covers approximately 85% of the free float-adjusted market capitalization in each country. The MSCI Europe Index captures large- and mid-cap representation across developed markets countries in Europe. The index covers approximately 85% of the free float-adjusted market capitalization across the European developed markets equity universe. The MSCI China Index captures large- and mid-cap representation across China A-shares, H shares, Red chips, P chips, and foreign listings. The index covers about 85% of the China equity universe. The Nikkei 225 Index is a stock market index for the Tokyo Stock Exchange which is price-weighted operating in Japanese Yen. The index measures the performance of 225 large, publicly owned companies in Japan from different industry sectors. The Bloomberg U.S. Aggregate Bond Index is a broad-based flagship benchmark that measures the investment-grade, U.S. dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, MBS (agency fixed-rate pass-throughs), ABS, and CMBS (agency and non-agency. The Bloomberg Municipal Bond Index covers the U.S. dollar-denominated long-term tax-exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds, and pre-refunded bonds. The Bloomberg U.S. Corporate High-Yield Index measures the U.S. dollar-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch, and S&P is Ba1/BB+/BB+ or below. Bonds from issuers with an emerging markets country of risk, based on the EM country definition, are excluded. The Consumer Price Index (CPI) is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. CPI is often used as a barometer to measure inflation. The Caixin China General Services PMI (Purchasing Managers' Index) is based on data compiled from monthly replies to questionnaires sent to purchasing executives in over 400 private service sector companies. The index tracks variables such as sales, employment, inventories, and prices. A reading above 50 indicates that the services sector is generally expanding; below 50 indicates that it is generally declining. The 2s30s spread is the difference between the yield on the 30-year Treasury bond and the yield on the 2-year Treasury note.

Data in this newsletter is obtained from sources that we, and our suppliers believe to be reliable, but we do not warrant or guarantee the timeliness or accuracy of this information. Consult your financial professional before making any investment decision. Past performance is no guarantee of future results. Diversification/asset allocation does not ensure a profit or guarantee against a loss. The attached materials, URLs, or referenced external websites are created and maintained by a third party, which is not affiliated with Summit Financial LLC. or its affiliates. The information and opinions found within have not been verified by Summit, nor do we make any representations as to its accuracy and completeness. Summit Financial, LLC, and affiliates are not endorsing these third-party services, or their privacy and security policies, which may differ from ours. We recommend that you review these third-party's policies and terms. Investment advisory and financial planning services offered through Summit Financial, LLC ("Summit"), an SEC Registered Investment Advisor, doing business as Vardhan Wealth Management (2755 Executive Drive, Suite 190, Farmington Hills, MI 48331-3550; Telephone: 248.365.4440; Fax: 248-365-4446).