MARKET UPDATE

What's happened?

- Global equities have fallen into correction territory, defined as a decline of more than 10%.
- Bond markets have been even more challenged. The Bloomberg US Aggregate Bond Index has declined more than 10% since August 2020, its worst drawdown since 1980. The Bloomberg 1-10yr Blend (1-12) Municipal Bond Index lost -6.3% year-to-date.

Why have markets sold off?

- Market participants now expect the Fed to hike 9 more times this year, including 50bps hikes in May, June, and July. Federal Open Market Committee members have validated these expectations in their speeches.
- The 10-year Treasury Bond yield increased from 1.95% in early March to 2.93% last week.
- Financial conditions are tightening. For example, the Bankrate 30 Year Mortgage Rate National Average has increased from 3.2% to 5.4% this year.
- We've seen some high-profile earnings season misses, including Netflix, which declined 30% after its earnings release.
- China has doubled and quadrupled down on its zero-COVID policy, resulting in a rapidly slowing economy. The MSCI China Index (Mill Creek position: underweight) is down 25% year-to-date and 43% over the last 12 months.

Our Perspective

- We're concerned that equity prices and bond yields have begun to decline together. Earlier equity declines this year were "growth sell-offs" – equity prices declined in response to higher bond yields. We're now seeing the opposite – a risk-off flight to safety.
- Even so, sentiment has become too negative. Investor and consumer sentiment measures have fallen to levels not seen since the depths of the financial crisis. The probability of a US recession continues to increase, but it is still not the most likely outcome over the next 12 months.
- Real economic growth in the US is gradually slowing — as it needs to — but remains above trend. We are watching housing and aggregate household income as leading indicators of growth and inflation, respectively.
- Earnings season is off to a good start. 79% of the firms that have reported so far have surprised to the upside.
- Following the Russian invasion of Ukraine, we suggested investors accelerate equity dollar-cost-averaging programs. Equities recovered during March, but have now returned to late-February levels. Investors that missed the late-February entry point should consider accelerating a tranche. Investors dollar-cost averaging into fixed income should also consider accelerating a tranche at this point as well.

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