



## IMPACT

FINANCIAL STRATEGIES

**April 1, 2022**

### **The World is Different**

On Thursday, Feb 24, 2022, Russia invaded Ukraine. The attack came from the ground, from the sea, and by air. It was the largest invasion in Europe since WWII. Outside of loss of life, one of Ukraine's biggest fears was a cyber-attack, loss of communication, electronics, and Internet.

- Feb 26<sup>th</sup> at 5:06 AM, Ukrainian minister of digital transformation, Mykhailo Federov, tweeted the following: "@elonmusk , while you try to colonize Mars — Russia try to occupy Ukraine! While your rockets successfully land from space — Russian rockets attack Ukrainian civil people! We ask you to provide Ukraine with Starlink stations and to address sane Russians to stand"
- Hours later Elon Musk replied: ""Starlink service is now active in Ukraine. More terminals en route."
- \*\*Source: Washington Post\*\*

As of my writing this newsletter, and to my knowledge, the Starlink service has held up, and delivered, and Ukraine has been able to fight a war with the aid of technology that was no more than science fiction just two decades ago. Whether you are a fan of Elon Musk, or not. Whether you think he is a genius, or a crackpot, your opinion is okay; we are privileged to live in a country where we can disagree. However, the implications of one company and one person being able to make technology work in the face of such a human and global crisis is simply incredible. It is one small example of the truly "magical" times we are living in. This is not to say that technology, and the pace of rapid advancement is all good. This is an example of how quickly things can change, and how things imaginable just a few years ago, can be accomplished in mere hours.

While the tragedy and suffering of the Ukrainian people is heartbreaking, we are also witnessing something that is unbelievably inspiring. We are witnessing, in real time, how a former comedian turned politician, can become a hero to the world! My heart, my prayers, and the thoughts and well wishes of our entire team go out to the brave citizens of Ukraine, and we wish them all the success in the world. Russia (and especially Putin) has become a global pariah for the first time in decades. The world has changed.

Normally, I use this intro section as a personal note about what is going on with us here at IFS, or some sort of personal update, but I feel it is more important to focus you on the global and market shifts we are seeing and what we are watching closely as we guide you. Taken as a whole, (barring the human tragedy, of course) they are neither good or bad for the future. They just **are**; and all we can do is prepare, adjust, and make changes where we can, and most importantly, control our response.

I wish you joy, peace, health, and moments that matter with those you care about most.

I hope you enjoy this newsletter, please reach out if you have any questions or comments,

Justin

## Quarterly Insights – April 2022

### Inflation, Geopolitics and Rising Rates Weigh on Markets in the First Quarter

After a historically calm 2021, volatility returned in the first quarter of 2022, as inflation surged to 40-year highs, the Federal Reserve promised to raise interest rates faster than previously thought, and Russia surprised the world with a full-scale military invasion of Ukraine, marking the first major military conflict in Europe in decades. Those factors fueled a rise in volatility and pushed stocks lower in the first three months of the year.

Broad market volatility began to pick up during the first few days of 2022 as inflation readings hit multidecade highs, confirming that price pressures were still accelerating. That prompted multiple Federal Reserve officials to signal that interest rates will rise faster than markets had previously thought, including a possible rate hike in March. The prospect of sooner-than-expected interest rate hikes weighed on the sectors with the highest valuations, specifically growth-oriented technology stocks. The steep declines in the tech sector exacerbated market volatility in January. Additionally, while the fourth-quarter earnings season was solid, there were several large, widely held technology companies that posted disappointing results or forecasts, and that also contributed to general market volatility. Finally, in late January at the FOMC meeting, Fed Chair Powell clearly signaled that the Fed would be raising rates at the next meeting (in March) confirming to investors that interest rates were going to rise much more quickly than had been assumed just a few months prior. The S&P 500 ended January with the worst monthly return since March 2020 (the onset of the pandemic).

Volatility remained elevated in February with the market's primary concern shifting from monetary policy to geopolitics as Russia amassed troops on the Ukrainian border, prompting warnings from the United States and other Western countries of an imminent invasion. The rising threat of a major military conflict in Europe for the first time in decades further weighed on stocks in early February. That additional uncertainty, combined with still-stubbornly high inflation readings and continued warnings from Fed officials about future interest rate increases kept markets volatile throughout most of the month. Then on February 24<sup>th</sup>, Western warnings of a Russian invasion of Ukraine were fulfilled as Russia invaded in the early morning hours. The conflict sent essential commodity prices such as oil, wheat, corn, and natural gas surging as commodity producers and end users feared production disruptions and reduced supply. As one would expect, markets dropped in response to the invasion, and not just because of rising geopolitical concerns, but also as investors realized higher commodity prices will only add to existing inflation pressures, and in turn, possibly pressure corporate earnings and consumer spending. Geopolitical uncertainty combined with lingering inflation concerns and anxiety over the pace of Fed rate hikes weighed on stocks again in February, and the S&P 500 declined for a second straight month.

Markets remained volatile in early March, as hopes for a relatively quick ceasefire in Ukraine faded and commodity prices stayed elevated. Shortly after Russia's invasion, the developed world united in a never-before-seen way against Russia, imposing crushing economic sanctions on the Russian economy. But while that demonstrated important unity against Russian aggression, it became clear that the sanctions would also have a negative impact on Western economies, especially in the EU, and that raised concerns about a global economic slowdown. However, stocks did mount a strong rebound in late March thanks to incrementally positive geopolitical and monetary policy news. First, the Ukrainian resistance stalled the Russian advance, and while the situation devolved into an intense humanitarian tragedy in Ukraine, fears of the conflict extending beyond Ukraine's borders faded over the course of the month. Then, on March 16<sup>th</sup>, the Federal Reserve raised interest rates by 25 basis points, the first rate hike in over three years. But the rate hike was no worse than markets feared, and that provided a spark for a "relief rally" in stocks that produced a solidly positive monthly return for the S&P 500 and carried the major indices to multi-week highs by the end of the quarter.

In sum, the first quarter of 2022 was the most volatile quarter for markets since the depths of the pandemic in 2020, as numerous threats to economic growth emerged. As we start the second quarter, investors will need to see incrementally positive progress across geopolitics, monetary policy expectations, and the outlook for inflation if the late-March rally is to continue.

### First Quarter Performance Review

All four major equity indices posted negative returns for the first quarter of 2022, although the S&P 500 and the Dow Industrials saw only mild losses compared to the Nasdaq and Russell 2000. Investors rotated out of growth-oriented, high-P/E technology stocks and into sectors that were more exposed to the traditional economy which, generally speaking, trade at a cheaper valuation relative to the tech sector. That rotation benefitted the Dow Jones Industrial Average primarily while the Nasdaq Composite badly lagged both the S&P 500 and the Dow.

By market capitalization, large-cap stocks outperformed small-cap stocks in the first quarter, and that was to be expected given the geopolitical uncertainty and rising interest rates. Small-cap stocks typically are more reliant on debt financing to sustain their businesses, and therefore, rising interest rates can be a headwind on small-cap stocks. Additionally, investors flocked to the relative safety of large caps amid the rise in volatility over the course of the quarter.

From an investment style standpoint, value massively outperformed growth in the first quarter as select value ETFs registered positive returns over the past three months. Elevated volatility, geopolitical uncertainty, and the prospect of quickly rising interest rates caused investors to flee richly valued, growth-oriented tech stocks and rotate to more fairly valued sectors of the market.

On a sector level, only two of the eleven sectors in the S&P 500 finished the first quarter with a positive return. Energy was the clear standout as the sector benefitted from the increase in geopolitical uncertainty and subsequent surge in oil and natural gas prices in response to the Russia-Ukraine war. Utilities, a traditionally defensive sector, logged a modestly positive return as investors rotated to defensive sectors in response to elevated market volatility and geopolitical uncertainty. Finally, financials relatively outperformed the S&P 500 and saw only a small loss as the sector has historically benefited from rising interest rates, although concerns about exposure to the Russian economy weighed on many financial stocks in February and early March.

Sector laggards included the communication services, tech, and consumer discretionary sectors as they saw material declines in the first quarter thanks primarily to the broad rotation away from the more highly valued corners of the market. Specifically, internet stocks weighed on the communications sector, while online retail stocks were a drag on the consumer discretionary sector. Away from tech and techrelated sectors, most other sectors in the S&P 500 saw modest declines that did not stray too far from the performance of the S&P 500.

US Equity Indexes	Q1 Return	YTD
S&P 500	-4.60%	-4.60%
DJ Industrial Average	-4.10%	-4.10%
NASDAQ 100	-8.91%	-8.91%
S&P MidCap 400	-4.88%	-4.88%
Russell 2000	-7.53%	-7.53%

Source: YCharts

Internationally, foreign markets declined in the first quarter. Geopolitical uncertainty hit foreign markets early in the quarter, erasing what was moderately positive performance until that point. Emerging markets slightly lagged foreign developed markets due to a stronger U.S. dollar and rising geopolitical risks, but the underperformance was modest.

International Equity Indexes	Q1 Return	YTD
MSCI EAFE TR USD (Foreign Developed)	-5.79%	-5.79%
MSCI EM TR USD (Emerging Markets)	-6.92%	-6.92%
MSCI ACWI Ex USA TR USD (Foreign Dev & EM)	-5.33%	-5.33%

Source: YCharts

Commodities registered massively positive returns in the first quarter primarily thanks to rising geopolitical risks. Oil, wheat, natural gas, corn, and other essential commodities surged on a combination of actual production outages related to the Russia-Ukraine war (which reduced current supply) and buyers locking in supply for fear of any future production disruptions should the war continue for months or spread beyond Ukraine's borders.

Commodity Indexes	Q1 Return	YTD
S&P GSCI (Broad-Based Commodities)	33.13%	33.13%
WTI Crude Oil	34.42%	34.42%
Gold Price	6.61%	6.61%

Source: YCharts/Koyfin.com

Switching to fixed income markets, bonds registered some of the worst performance in years during the first quarter with most major bond indices declining as investors exited fixed income holdings in the face of high inflation and as the Federal Reserve consistently signaled that it was going to raise interest rates faster than investors had previously expected.

Looking deeper into the bond markets, shorter-term Treasury Bills outperformed longer-duration Treasury Notes and Bonds as high inflation and the threat of numerous future Fed rate hikes weighed on fixed income products with longer durations.

In the corporate debt markets, investment-grade bonds saw materially negative returns and underperformed lower-quality but higher-yielding corporate debt, which also declined but more modestly so. This underperformance in investment-grade debt reflected the impact of rising Treasury yields, while the outperformance of high-yield corporate bonds served as a reminder of the still-positive outlook for the U.S. economy and corporate America, despite the macroeconomic headwinds of inflation, geopolitical unrest, and rising interest rates.

US Bond Indexes	Q1 Return	YTD
BBgBarc US Agg Bond	-5.93%	-5.93%
BBgBarc US T-Bill 1-3 Mon	0.03%	0.03%
ICE US T-Bond 7-10 Year	-6.54%	-6.54%
BBgBarc US MBS (Mortgage-backed)	-4.97%	-4.97%
BBgBarc Municipal	-6.23%	-6.23%
BBgBarc US Corporate Invest Grade	-7.69%	-7.69%
BBgBarc US Corporate High Yield	-4.84%	-4.84%

Source: YCharts

## Second Quarter Market Outlook

As we start a new quarter, markets are facing the most uncertainty since the pandemic, as headwinds from inflation, less-accommodative monetary policy, and geopolitics remain in place.

Inflation still sits near a 40-year high as we start the second quarter and with major commodities such as oil, wheat, corn, and natural gas surging in response to the Russia-Ukraine war, it's unlikely that key inflation indicators like the Consumer Price Index will meaningfully decline anytime soon. Until there is a definitive peak in inflation, the Federal Reserve is likely to continue to aggressively raise interest rates, and over time, higher rates will become a drag on economic growth.

The Federal Reserve, meanwhile, has consistently warned markets that aggressive interest rate hikes are coming in the months ahead, and this quarter we expect the Fed will reveal its balance sheet reduction plan, which will detail how the Fed plans to unload the assets it acquired via the Quantitative Easing program over the past two years. If the details of this balance sheet reduction plan are more aggressive than markets expect, or the Fed commits to more rate hikes than are currently forecasted by markets, that could weigh on stocks and bonds alike.

Finally, the Russia-Ukraine war continues to rage on, and the geopolitical implications have spread beyond the battlefield, as relations between Russia and the West have hit multi-decade lows. Meanwhile, crippling economic sanctions against Russia remain in place, while commodity prices are still very elevated, and the longer those factors persist, the greater the chance we see a material slowdown in the global economy.

But while clearly there are risks to portfolios as we start the new quarter, it's also important to note that the U.S. economy is very strong and unemployment remains historically low, and that reality is helping support asset markets. Additionally, interest rates are rising but remain far below levels where most economists forecast that they will begin to slow the economy. Finally, consumer spending, which is one of the main engines of growth for the U.S. economy, is robust, and corporate and personal balance sheets are healthy.

In sum, the outlook for markets and the economy is uncertain, and we should all expect continued volatility across asset classes in the short term. But core macroeconomic fundamentals remain very strong while U.S. corporations and the U.S. consumer are, broadly speaking, financially healthy. So, while risks remain, as they always do, there are also multiple positive factors supporting markets, and it is

important to remember that a well-executed and diversified, long-term financial plan can help overcome bouts of even intense volatility like we saw in the first quarter.

At Impact Financial Strategies, we understand the risks facing both the markets and the economy, and we are committed to helping you effectively navigate this challenging investment environment. Successful investing is a marathon, not a sprint, and even temporary bouts of volatility like we experienced over the past three months are unlikely to alter a diversified approach set up to meet your long-term investment goals.

Therefore, it's critical for you to stay invested, remain patient, and stick to the plan, as we've worked with you to establish a unique, personal allocation target based on your financial position, risk tolerance, and investment timeline.

Rest assured that our entire team will remain dedicated to helping you successfully navigate this market environment.

Please do not hesitate to contact us with any questions, comments, or to schedule a portfolio review.

Sincerely,

Justin

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# IMPACT

## FINANCIAL STRATEGIES

<b>A Game of Multiples (Updated 4/4/22)</b>			
<b>Market Influence</b>	<b>Current Situation</b>	<b>Things Get Better If...</b>	<b>Things Get Worse If...</b>
<b>Russia/Ukraine War</b>	The Russia/Ukraine war has stalemated but importantly hasn't spread to a larger conflict between NATO and Russia. Sanctions remain in place and will be a headwind on the EU and, to a lesser degree, the U.S.	Russia and Ukraine declare a sustainable ceasefire.	The war remains a stalemate, keeping commodity prices elevated for months ahead.
<b>Oil Prices</b>	Oil has dropped from the recent highs but remains above \$100/bbl.	Oil retreats back to, and through, \$100/bbl.	Oil rallies on continued geopolitical uncertainty and moves back towards \$120/bbl.
<b>Fed Tightening</b>	Markets expect the Fed to tighten by 250 basis points through year-end, and for balance sheet reduction to begin this summer.	Rate hike expectations stay at 250 bps of total hikes for 2022, while balance sheet reduction isn't over \$100 bln/month.	The Fed gets more hawkish, and markets start to price in more than 250 bps of total tightening, or the Fed announces plans to reduce the balance sheet by more than \$100 bln/month.
<b>Inflation</b>	Inflation remains at multi-decade highs although there are some potential hints that inflation pressures may be peaking.	Inflation begins to back off the recent highs and politicians begin to lose focus on the issue.	Inflation pressures continue to accelerate higher, fueled by surging commodity prices and more supply chain disruptions.
<b>Economic Growth</b>	Growth remains strong and there are no hints of a slowdown.	Economic growth remains resilient through Fed tightening.	Growth begins to slow, causing stagflation concerns.
<b>Expected 2022 S&amp;P 500 EPS</b>	\$226	\$226	\$215
<b>Multiple</b>	19X-19.5X	19.5X-20X	17X-18X
<b>S&amp;P 500 Range</b>	4,294 - 4,407	4,407 - 4,520	3,655 - 3,870
<b>S&amp;P 500 Target (Midpoint)</b>	4,351	4,463	3,763
<b>Change from today</b>	-5.0%	-2.4%	-17.6%

## DISCLOSURES

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The S&P 500 is an unmanaged index of 500 widely held stocks that is generally considered representative of the U.S. stock market.

The Dow Jones Industrial Average (DJIA), commonly known as "The Dow" is an index representing 30 stocks of companies maintained and reviewed by the editors of the Wall Street Journal.

The NASDAQ Composite Index is an unmanaged index of securities traded on the NASDAQ system.

The S&P MidCap 400® provides investors with a benchmark for mid-sized companies. The index, which is distinct from the large-cap S&P 500, measures the performance of mid-sized companies, reflecting the distinctive risk and return characteristics of this market segment. Russell 2000 Index measures the performance of the 2,000 smallest companies in the Russell 3000 Index, which represent approximately 8% of the total market capitalization of the Russell 3000 Index.

The S&P GSCI is a composite index of commodities that measures the performance of the commodity market. S&P GSCI Gold is an index tracking changes in the spot price for gold bullion. S&P GSCI Crude Oil is an index tracking changes in the spot price for crude oil. GLD is a gold index fund based on gold and holds gold and/or cash as its only assets, but shareholders are not guaranteed to receive physical gold in exchange for their shares.

The MSCI EAFE (Europe, Australasia, and Far East) is a free float-adjusted market capitalization index that is designed to measure developed market equity performance, excluding the United States & Canada. The EAFE consists of the country indices of 22 developed nations.

The MSCI Emerging Markets is designed to measure equity market performance in 25 emerging market indices. The index's three largest industries are materials, energy, and banks.

The MSCI ACWI (All Country World Index) is a free floating-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets.

The Barclays US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market.

The Barclays US T-Bill index measures the performance of public obligations of the U.S. Treasury that have a remaining maturity of greater than or equal to 1 month and less than 3 months.

The ICE U.S. Treasury 7-10 Year Bond Index is market value weighted and is designed to include U.S. dollar denominated, fixed rate securities with minimum term to maturity greater than or equal to seven years and less than ten years. Barclays Capital U.S. MBS Index measures the performance of investment grade fixed-rate mortgage-backed pass-through securities of GNMA, FNMA, and FHLMC.

The Barclays Capital Municipal Bond is an unmanaged index of all investment grade municipal securities with at least 1 year to maturity. The Bloomberg Barclays US Corporate Bond Index measures the investment grade, fixed-rate, taxable corporate bond market. It includes USDdenominated securities publicly issued by US and non-US industrial, utility and financial issuers.

The Bloomberg Barclays U.S. Corporate High Yield Bond Index is composed of fixed-rate, publicly issued, non-investment grade debt, is unmanaged, with dividends reinvested, and is not available for purchase. The index includes both corporate and non-corporate sectors. The corporate sectors are Industrial, Utility and Finance, which include both U.S. and non-U.S. corporations.

Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance. Individual investor's results will vary. Diversification and asset allocation do not ensure profit or protect against loss. Holding investments for the long term does not insure a profitable outcome. Investing involves risk and you may incur a profit or loss regardless of the strategy selected. Links are being provided for information purposes only. Raymond James is not affiliated with and does not endorse, authorize or sponsor any of the listed websites or their respective sponsors. Raymond James is not responsible for the content of any website or the collection or use of information regarding any website's users and/or members.

\*\* Washington Post link: <https://www.washingtonpost.com/technology/2022/03/19/elon-musk-ukraine-starlink/>