Comprehensive Investment Management, LLC
Fee Only Personal Financial Planning
Fall 2022

A Review of the Financial Markets at September 30, 2022

When the stock market is going up you often hear: "Trees don't grow to the sky". Obviously a warning that don't expect stock prices to continue to go up forever. When the markets are going down you may hear: "Groundhogs don't dig to China." Or maybe not. I haven't, but the sentiment is the same. The market is like a pendulum and spends very little time at the midpoint. Since 1970 just three times has the annual return of the S&P500 been within 2% of its long time average of 10%. Over the five years 2017 through 2021 the S&P return for each year respectively was 21.8%, -4.4%, 31.5%, 18.4% and 28.5%. As you can see, if you want consistency you're going to have to look elsewhere. If you invested $100,000 in the S&P in 2017, your account would now be more than doubled to $215,000, and that includes the –24% over the last nine months.

Recent market and economic activity is newsworthy. However most of it can be dismissed as "noise" and not indicative of a trend. Investment performance over longer periods, while not predictive, is significantly more meaningful.

Unfortunately, it's unlikely the S&P is going to end 2022 anywhere close to its average. It very well may go lower before it goes higher. Each week seems to bring bad news. However, news coverage is by its nature short term and often tilted towards the negative. Studies show that financial news is 22% more likely to be covered if it is negative. That brings to mind another expression: "No news is good news." From a psychological standpoint, humans are hardwired to respond more strongly to the negative rather than the positive.

The market decline deepened in the third quarter as a false hope faded among traders. Federal Reserve Chairman Powell had repeatedly said the Reserve was not going to ease monetary tightening until infla

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Average Annual Returns of CIM Select Mutual Funds

At September 30, 2022	QTR	YTD	1 Year	3 Years	5 Years	10 Years	15 Years
Large Cap Stocks	-5.7	-20.9	-15.1	6.7	7.8	12.1	8.8
Mid Cap Stocks	-3.8	-29.2	-27.2	4.5	6.1	11.6	8.6
Small Cap Stocks	-2.7	-32.1	-30..5	2.0	6.0	10.8	8.7
Healthcare Stocks	-2.7	-15.4	-12.4	11.1	8.5	13.5	11.8
Foreign Stocks	-9.3	-34.6	-35.0	-.1	-.1	4.9	3.1
Short Term Bonds	-2.0	-7.0	-7.8	-.9	.5	1.0	2.1
Intermediate Bonds	-4.9	-15.1	-14.7	-1.9	.1.0	1.1	3.3
High-Yield Bonds	-.9	-13.3	-12.8	-1.0	1.3	3.5	4.9
Wellesley Fund 65/35 bonds/stocks	-5.2	-14.8	-12.2	.9	3.2	5.0	5.6
Wellington Fund 35/65 bonds/stocks	-4.9	-20.2	-14.6	3.4	5.4	7.7	6.4

On a deposit of $100,000, over the past 15 years, Wellesley's balance would grow to $231,185, Wellington $260,504.

tion was brought under control. But some investors didn't believe him, or didn't want to believe him. Others used the volatility to profit from short term trades. By mid August the S&P was down 9%, which was a big improvement from -22% in June. As the Reserve raised interest rates (there have been three consecutive 75 basis point increases) the S&P dropped back into a bear market, down at the end of the quarter by 24%.

Interest rates have been kept artificially low since the financial crisis of 2008 and were taken even lower due to the Covid pandemic. Raising rates closer to historic norms is the right thing to do. What is good for the economy is not necessarily good in the short term for the markets. To combat recent high inflation, interest rates are being raised faster than what would otherwise be desirable and that can be quite disruptive. Mortgage rates a year ago were 3.1% and are now 6.9%, a twenty year high. That's disruptive.

A hazy outlook has weighed on investor spirits, with surveys showing individual investors are the most pessimistic in years and mutual fund mangers are holding unusually high levels of cash. In September a survey of global fund managers found that average cash balances jumped to the highest level since October 2001, in the aftermath of the 9/11 terrorist attacks. Vanguard's Wellington fund for the first time in a long time has a higher than normal cash position. That doesn't necessarily mean the fund has been selling stocks to raise cash. It's more likely they are holding off on the investment of new deposits and dividends.

LOOKING AHEAD

The persistence of inflation and the moves by central banks around the world to lift interest rates have slammed overseas markets. Russia's invasion of Ukraine and China's Covid-19 lockdowns continue as negatives. Britain sent its bond values, pension plans and the pound into a downward spin when the Bank of England raised rates to slow the economy at the same time the government lowered taxes which spurs an economy. A major part of the tax reduction that was to benefit the rich was rescinded and other damage control steps have been taken.

One particularly disorienting twist in 2022 is that instead of providing a steading ballast to our portfolios, bonds values have fallen alongside stocks, giving investors few if any places to hide. Our US investment-grade bonds lost 5.3% during the quarter and are down 15% year to date. Bond markets are on pace for their worst year since 2004. Yields are rising so a consensus is starting to build that the worst for bonds may be behind us.

In June CIM issued a Special Bear Market Edition newsletter. In it CIM assigned a Scale of Concern of 3 on a scale of 1 to 10. In other words not a high concern compared to the 2008 financial crisis and the Covid pandemic in 2020. That assessment has not changed, not because things right now are looking up necessarily, but because the current market conditions, at least here in the US, are well understood. In fact the reason the Federal Reserve is aggressive in taking steps to lower inflation is because of lessons learned in the 1970's and 80's.

It takes time for the full effects of higher interest rates to filter through the economy, so naturally investors are concerned about how the Fed's sequence of rate increases will eventually affect the behavior of businesses and consumers. Given the pace of the Reserve's monetary tightening, many suspect that an economic slowdown will dent corporate earnings, eroding the attractiveness of company shares.

Higher interest rates mean a higher discount rate in the calculation of company future cash flows and therefore a potential reduction in their perceived stock value. A discount rate brings in line a comparison between cash flows and the risk free return from US Treasuries. Again, nothing new or surprising there.

The markets generally look ahead about six months to two years at the most. Projections run high that the US will be in a recession within the next six months. But it's not expected to be severe or to last long.

An investor's time horizon for their stock portfolio should be at least five years. The horizon for bonds can be shorter, because they are not as volatile as stocks, although their values have not held up so far in 2022. If bonds could talk they would say: "Don't blame us. We're not the ones that kept interest rates so low for so long."

1972 to 2022 — INFLATION AND THEN SOME

For a lot of young adults, they see being able to buy their own home while still in their twenties as a fantasy. According to a recent Pew Research report the percentage living with their folks has more than doubled to 17% up from 8% in 1972. Many have student debt. But a more pervasive issue is that real wages in America (real meaning after inflation) have generally stagnated since the 1970's. Worker productivity has grown three times more than wages. Economist offer several reasons for that, for example, technological advancements, which have generally raised living standards for a great majority of the population. Especially in the lower paid tiers, hourly wages have the same purchasing power as they did 40 or 50 years ago.

The annual inflation average since 1972 is 4%. Cumulatively, if inflation was the only factor, an item that cost a dollar in 1972 should now cost $7. But in many cases that is a gross over simplification. Some examples are shown in the table below. All amounts have been adjusted to 2022 dollars, so it compares what an item in 1972 should cost in 2022 based on inflation versus what it does cost. For example, the median price for a home in 1972 was just $26,800. Increasing that for inflation takes it to the $189,500. The additional $250,800 to get to $440,300 is the increase beyond inflation. Of course, there are caveats. Home buyers now expect more in a home than folks did in 1972. And cars today are not your grandfather's Oldsmobile, if there was such a thing today as an Oldsmobile.

All amounts are in 2022 dollars	1972	2022
A HOME	$189,500	440,300
PUBLIC 4 YEAR COLLEGE	$10,000	20,700
PRIVATE 4 YEAR COLLEGE	$24,000	56,100
MEDICAL EXPENSES	$915	1,350
A NEW CAR	$26,100	48,200
4 PEOPLE 4 DAYS DISNEY WORLD	$1,170	2,670

FUN FACTS ABOUT BEAR MARKETS

(Well, all right, maybe not fun, but facts that may help keep the current bear market in perspective.)
A bear market is one where the market has declined by 20% or more.
Since 1960 there have been 12 bear markets.
The average bear market bottomed out at 34.5% and lasted 333 days .
The worst bear market was 51.9%, 2007 to 2008, and lasted 408 days.
The current bear market is at 24% and has lasted 105 days.
The two longest bear markets were 1973-74 and 1980-1982. They were marked by high inflation that had been entrenched for years.
The average time between bear markets is 3.5 years.
There was no bear market for 11 years from March 2009 until February 2020.
The shortest bear market was 33 days starting in February 2020. The quick end was a direct result of unprecedented actions by Congress and the Federal Reserve.
Despite 12 bear markets, since 1960 the S&P has an annual return of 10%, 6.1% after inflation.

Comprehensive Investment Management, LLC

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ADV and Privacy Notice available on request. The one ADV change in 2022 was the registration of Mercedes Petrellis with the PA Dept. of Banking & Securities.

Q&A

Q< Over the last few weeks on several TV investment shows I hear mention of investing in alternatives. What is alternative investing?

A> Quite literally alternative investing simply means investing in assets other than stocks, bonds and cash. Typically, but by no means exclusively, examples are bitcoins, commodity futures (energy, metals, livestock and agriculture), real estate, antiques, art work, venture capital, and derivatives. You may remember mortgage derivatives as the main component that led to the 2008 financial crisis.

Once the exclusive domain of the rich and sometimes famous, alternative investing is now available to retail investors. As you can imagine the investment instruments vary, and usually have high fees, are risky, complex, volatile and illiquid. There is often little information about them available to the public. They are not for everybody.

The argument for alternative investments is that they don't correlate with the stock market. Art work, for example, tends to hold its value during periods of high inflation. Venture capitalist often invest in start up companies or just in business concepts that aren't expected to hit their targeted markets for several years.

Vanguard has four funds that can be categorized as alternative. Alternative Strategies (VASFX), Commodity Strategies (VCMDX), Global Capital Cycles (VGPMX) and Market Neutral (VMNFX). The four are as varied as alternative investing itself. The most intriguing is the Commodity Strategy Fund. Its prospectus says it invests in agriculture, livestock, precious and industrial metals and energy, with some treasury bonds included to reduce risk . But the current portfolio is 100% short term inflation protected treasury bonds. It opened in 2019, so presumably it has not yet launched its intended portfolio. Minimum initial investment is $50,000. Year to date the fund's return is 9%, reflecting well timed purchases.