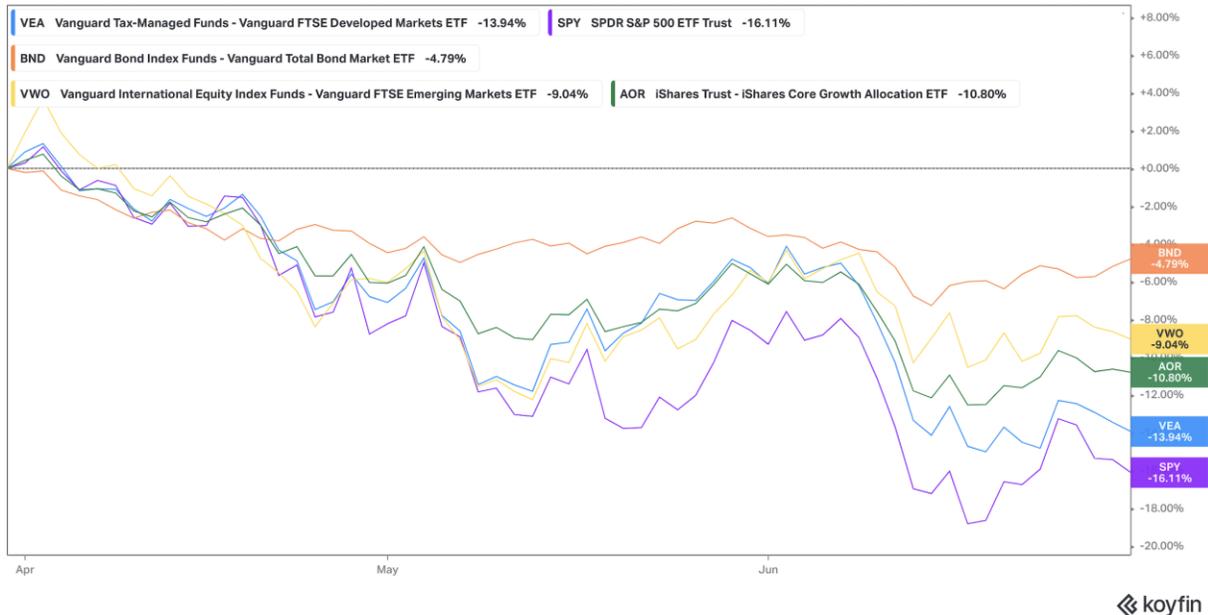


## 2nd Quarter 2022

The chart below shows last quarter's performance for five products. The first four, VEA, SPY, BND and VWO, represent four major asset categories and AOR represents a moderate-risk diversified portfolio. This chart provides a visual aid to help identify how major markets and a diversified portfolio performed last quarter.



- **VEA, FTSE Developed Markets Vanguard:** This product represents the developed international equity/stock market.
- **SPY, S&P 500 SPDR:** This product represents the US equity/stock market.
- **BND, Total Bond Market ETF Vanguard:** This product represents the US bond market.
- **VWO, Emerging Markets ETF MCSI Vanguard:** This product represents the emerging equity/stock market.
- **AOR, Growth Allocation Ishares Core ETF:** This product represents a moderate-risk diversified portfolio. This product does not necessarily match how your diversified portfolio is allocated. You can find your allocation within this report.

A terrible quarter across the board with few places to hide. The US equity market (SPY) was the worst performing major asset category finishing down 16.11%. Developed international markets (VEA) fell 13.94% while emerging international markets (VWO) fell 9.04%. Bonds (BND) continued their downward trend losing 4.79% and moderate risk diversified portfolios (AOR) lost 10.80%.

### Inflation, Inflation, Inflation

This quarter, our CIO, Chris Gauthier, spent two days in Boston with our research group Ned Davis Research to hear from both their economists and market strategists. When he returned, he summarized the meeting by saying, "inflation is everywhere." Let's look at a couple examples.

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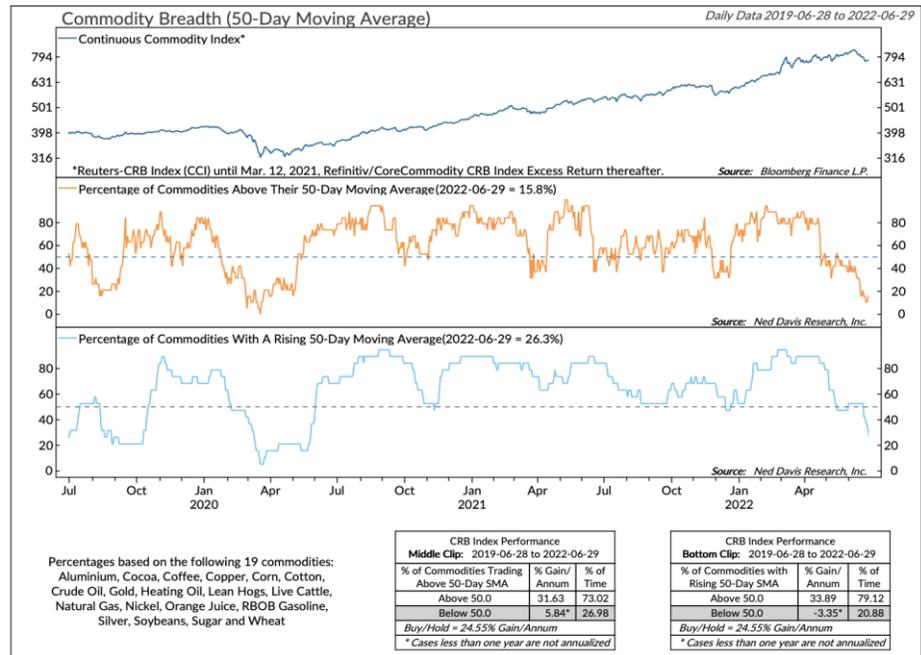
Through April 30, 2022, the Case Shiller US National Home Price Index is reporting a 1-year increase of 20.39%. This means that one year ago a \$500K home is now worth over \$600K. And if you need a mortgage, it gets worse. Thirty-year fixed mortgage rates have doubled over the last year and now stand at close to 6%. Assuming a buyer puts 20% down and finances the balance, what used to cost \$1,686/month now costs \$2,887/month, a **71% increase**.

The good news is that the frothy housing market appears to be subsiding, especially over the last couple of months. Peak values are likely behind us, at least for this cycle anyways. Sellers still have the upper hand (thanks to low inventories), but buyers are gaining ground.

Commodity prices have been a thorn in everyone's side. Record high fuel prices were the result of recovering demand, limited supplies, and tight inventories. Fortunately, recent data (see chart to the right) shows that most commodities are trending downward.

This should result in lower inflationary pressures in the weeks and months ahead.

### Commodity breadth weak and worsening



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### Federal Reserve

The Federal Reserve is on a mission to lower inflation. The primary way they do this is by raising short-term interest rates which influences borrowing costs. As rates go up, families and businesses are less likely to borrow money. If they don't borrow money, then consumption falls and the economy slows. If the economy slows too much we could tip into a recession. I suspect that the Federal Reserve will turn their attention to avoiding a recession once they see signs of inflation receding. The question is whether or not it will be too late?

### Fork in the Road

Are we headed for a recession OR are we experiencing a moderate slowdown? There is no shortage of opinions, but the truth is that no one knows. Only when we have the luxury of hindsight will we know for sure. The chart below might help explain why it matters, especially for your portfolio.

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	<b>Bear Market During Non-Recession</b>	<b>Bear Market During Recession</b>
<b>% Change</b>	-23.30%	-32.80%
<b># Months</b>	6.9	17.4

Source<sup>1</sup>: (Clissold, 2022)

Bear markets (aka 20% correction) that overlap with recessions are more severe and last longer than non-recession bear markets. If we avoid a recession, then the lows are probably in for this cycle (SPY is down 19.98% year-to-date). Plus, we are right there at about seven months since the selloff began. If a recession is here, then we have about 10-15% more downside ahead and about 12 more months to go. If we avoid a recession, then the second half of the year *should* be good. We will see. Please remember, past performance is not indicative of future results.

### **Hedging Protocol (Risk Management Tool)**

Our hedging protocol looks at 49 different indicators that have been selected based on their historical track record at identifying market risk (*past performance is not indicative of future results*). 34 of these indicators come from Ned Davis Research (NDR), an independent research group, and the remaining 15 were chosen by Stonehearth's Investment Committee to complement NDR's indicators. Together they provide us the ability to observe risk as it unfolds to help us determine if trades are needed to manage risk within your diversified portfolio.

Some of our risk indicators turned "red" (sell signal) during the quarter, which resulted in our decision to cut your stock exposure by 5% to help reduce risk in your portfolio. Below is our current stock/equity exposure for each risk profile:

- Conservative: Began the quarter at 27.0% and ended the quarter at 22% (benchmark = 30%)
- Moderate: Began the quarter at 58.5% and ended the quarter at 53.5% (benchmark = 60%)
- Aggressive: Began the quarter at 85.5% and ended the quarter at 80.5% (benchmark = 85%)

We continue to monitor each of the indicators for guidance on how much risk we should be taking within your portfolio. We will be sure to let you know if/when we make changes to our hedged exposure, but for the time being, we are happy with how we have your portfolio positioned.

## **Upcoming Events**

CIO's Corner: Quarterly Update Webinar with  
Chief Investment Officer, Chris Gauthier, CFA

Monday, August 15<sup>th</sup> at 12:00 PM EST

**[Register Now!](#)**

<sup>1</sup> Clissold, B. E. (2022, June 14). *Ndr Bear Market Criteria met. back to step 1*. NDR. Retrieved July 1, 2022, from [https://www.ndr.com/web/ndr/publications/-/c/SSF22\\_24\\*PDF/ndr-bear-market-criteria-met-back-to-step-1](https://www.ndr.com/web/ndr/publications/-/c/SSF22_24*PDF/ndr-bear-market-criteria-met-back-to-step-1)