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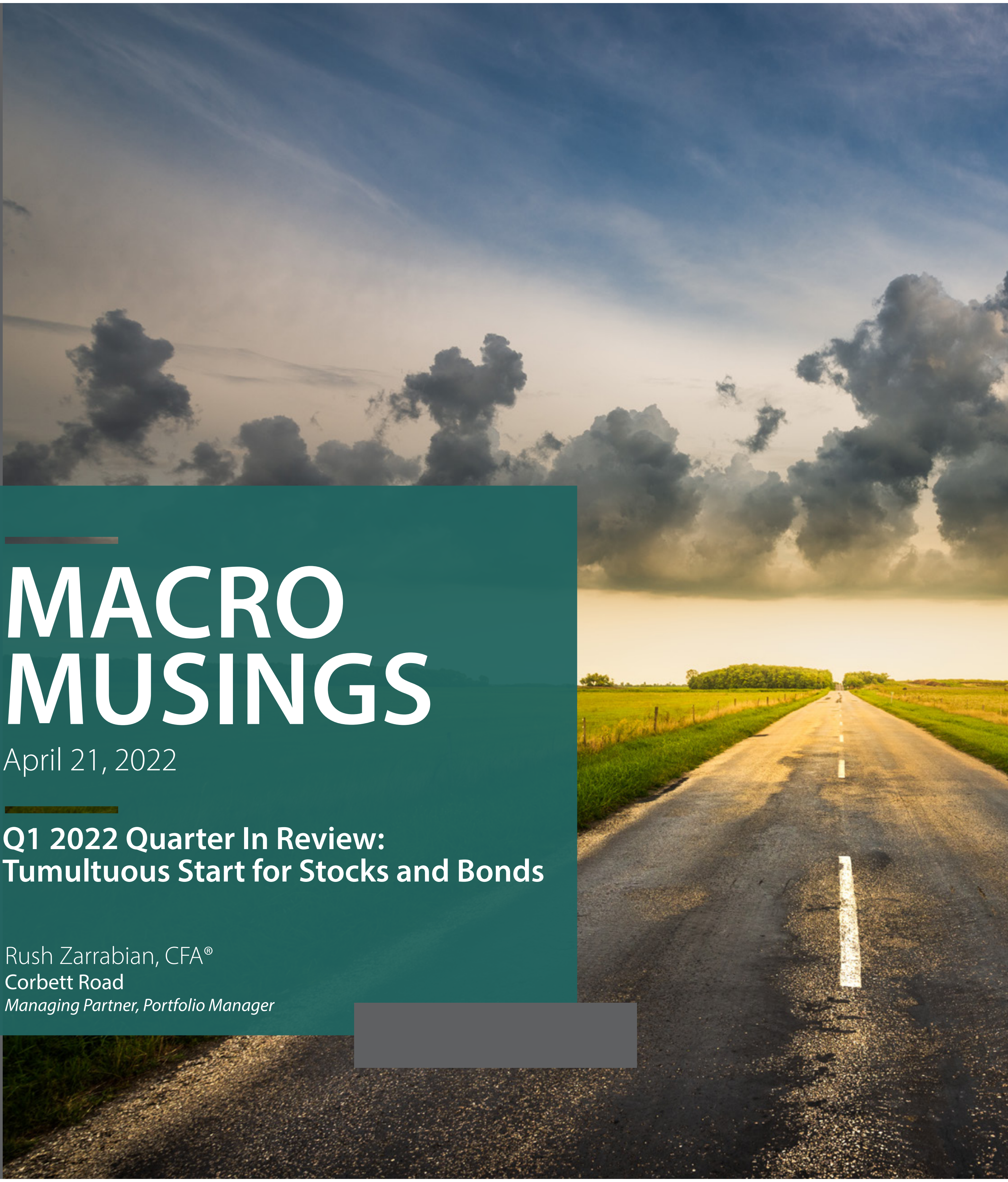


MACRO MUSINGS

April 21, 2022

Q1 2022 Quarter In Review: Tumultuous Start for Stocks and Bonds

Rush Zarrabian, CFA®
Corbett Road
Managing Partner, Portfolio Manager

SUMMARY

- **macro**cast™ indicates a recessionary bear market in 2022 is unlikely. Our current **micro**cast™ signal is recommending a neutral allocation. The lower **macro**cast™ score and neutral **micro**cast™ allocation suggest volatility has not yet subsided and the environment for equities remains challenging.
- The decline in **macro**cast™ reflects the deterioration in market conditions over the past few months. Besides the obvious inflationary pressure, valuations remain rich and technical indicators are mixed. Surprisingly, despite a hawkish Federal Reserve, our Liquidity indicators remain mostly positive.
- Most asset classes performed poorly in the first quarter. Equities around the globe and across market caps saw mostly negative returns, except for those with significant commodity exposure. In a repeat of the first quarter of 2021, the Bloomberg Aggregate Bond index suffered another major negative quarter.
- Although the market performed poorly in Q1, returns were much weaker before equities rebounded in March. Historically, when the market staged a strong rally following a double-digit decline, future returns a year later were excellent.

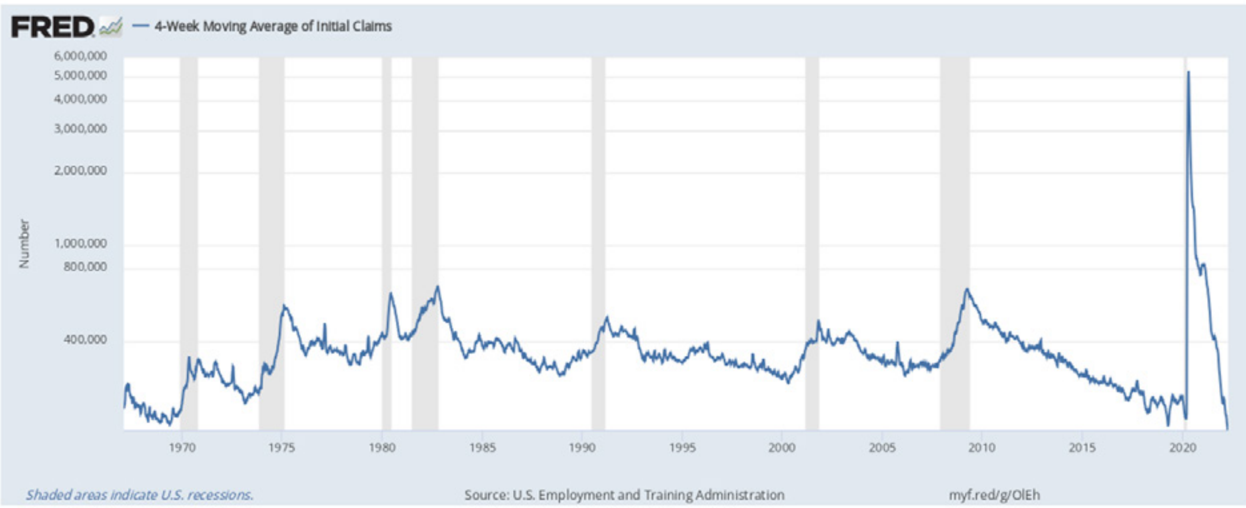
THE MESSAGE FROM MACRO**CAST™**

As a reminder, **macro**cast™ is Corbett Road's proprietary investment model. **macro**cast™ measures the appeal of risk assets by looking at the **VITALS** of the market—**V**aluation, **I**nflation, **T**echnical Analysis, **A**ggregate Economy, **L**iquidity, and **S**entiment. By looking at multiple factors, we seek to better gauge market conditions and the probability of a major, sustained market decline.

While **macro**cast™ remains positive, the current score reflects deteriorating market conditions and the increasing risk of a recessionary bear market.

The composite score is primarily being dragged lower by the indicators within two categories: **Technicals** and **Inflation**. The market's performance in the first quarter saw deteriorating breadth and a loss of momentum, weakening the technical indicators we follow. Our inflation indicators remain negative across the board, although there are signs that this could improve in the coming months (more on that below).

Reviewing the other VITALS, data in the Aggregate Economy category continues to show strength, particularly among the employment indicators. The 4-week average of Initial Claims for Unemployment recently touched an all-time low. Recessions typically do not occur when the labor market is this healthy:



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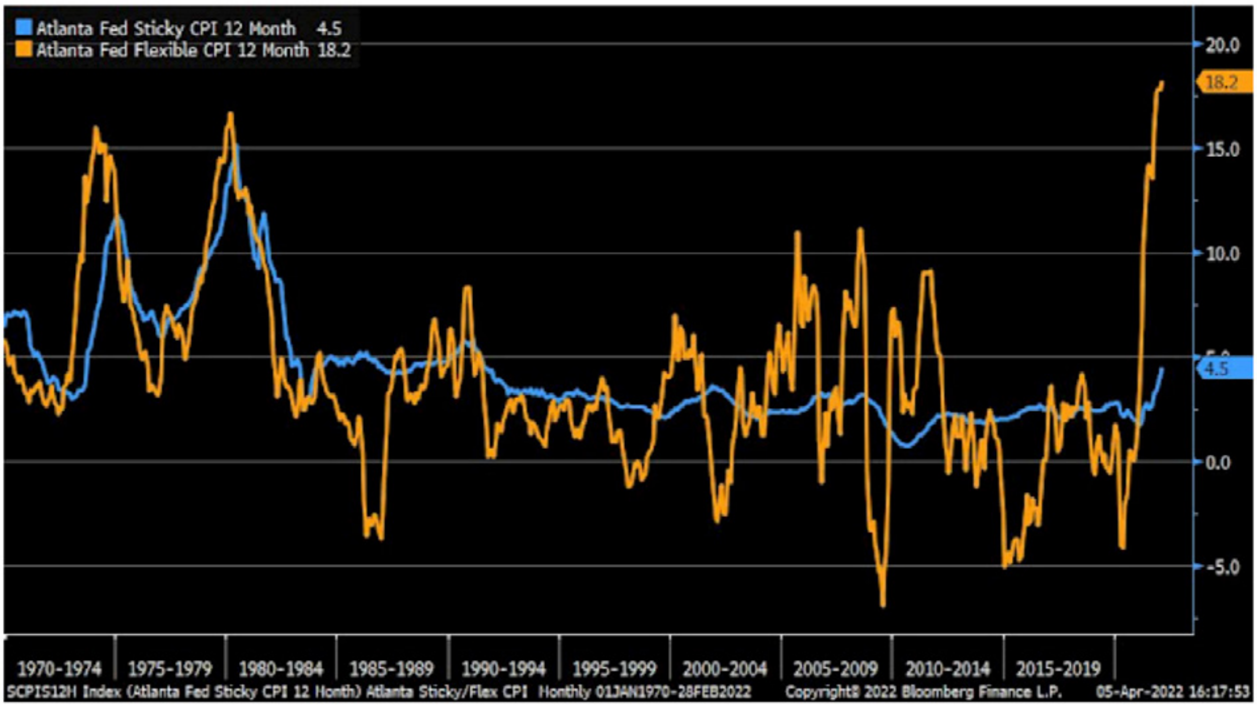
Inflation remains a problem, but there are signs it could be peaking. Notably, last month's Core CPI (excludes volatile food & energy prices) came in lower than expected as upward pressure from elevated categories like used cars and trucks continued to ease. Further, we don't think the current episode has yet led to long-term inflation concerns. The Atlanta Fed splits inflation into "flexible" and "sticky" classifications. While both categories have moved higher, only the flexible category is off the charts. In the high inflation period of the 1970s, both categories moved in tandem (chart from Bloomberg):



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While the Fed is set to continue raising rates throughout 2022, our Liquidity indicators remain surprisingly constructive. Corporate bond spreads, a measure of credit risk, remain low by historical standards:

The **Sentiment** category is mixed. While consumer sentiment is depressed—thanks to higher gas and food prices and ongoing geopolitical conflict—investor sentiment is extremely negative. Even though the market is not that far off its all-time high, the latest sentiment survey from the American Association of Individual Investors (AAII) showed the lowest level of bullish investors since 1992—that's fewer investors reportedly bullish than there were during the dotcom bubble burst, the depth of the financial crisis, and the Covid crash!

Historically, the lack of bulls has been a positive contrarian indicator. The following table from Jefferies shows that when the number of individuals who are bearish on the market exceeds those who are bullish by 30%, future returns were strong, especially 6 and 12 months later:

SPX Perf. When AAII Bull-Bear Breaks Below -30				
Incident	+1M	+3M	+6M	+12M
2/1/1990	1.20%	1.05%	8.13%	4.34%
8/16/1990	-4.68%	-4.59%	11.03%	16.00%
10/15/1992	3.13%	6.73%	9.47%	14.62%
2/20/2003	4.61%	9.87%	19.50%	36.68%
7/20/2006	4.26%	9.56%	14.52%	22.81%
7/10/2008	3.43%	-28.26%	-28.96%	-29.86%
11/20/2008	18.00%	2.34%	20.07%	45.05%
1/1/2009	-8.57%	-10.20%	2.22%	23.45%
11/5/2009	3.69%	-0.04%	9.31%	14.93%
7/8/2010	4.80%	8.87%	18.81%	25.56%
4/11/2013	2.53%	5.12%	6.89%	13.95%
4/14/2022	-	-	-	-
Average	2.95%	0.04%	8.27%	17.05%
Pct. Pos.	81.8%	63.6%	90.9%	90.9%
Av.g ex-GFC	2.26%	5.23%	12.62%	19.14%
Pct. Pos.	85.7%	85.7%	100.0%	100.0%

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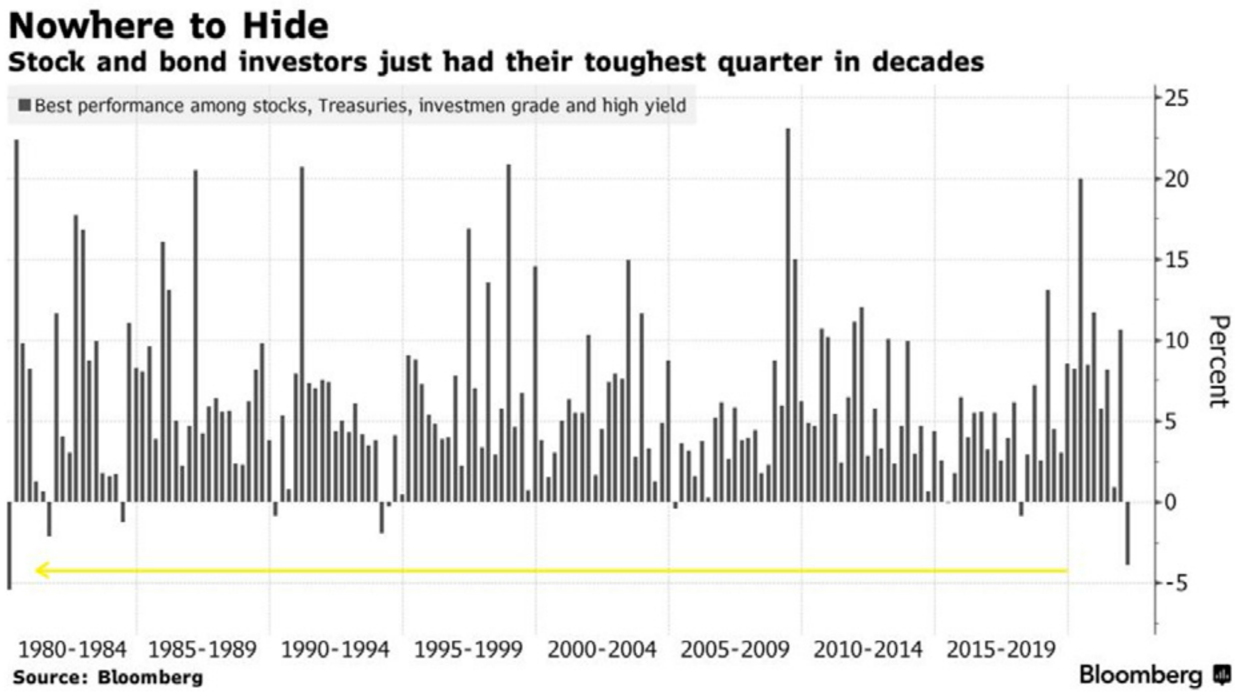
While this is just one indicator, the historical data suggests that when investors get this bearish on the stock market, much of the weakness has already been priced in.

ASSET CLASS REVIEW: **NOWHERE TO HIDE (EXCEPT SOME COMMODITIES)**

The following chart from Bloomberg summarizes just how challenging a quarter it was for investors:



Among stocks, Treasuries, corporate bonds, and high yield bonds, not a single group saw positive returns in Q1. Such broad weakness is rare, with only 8 quarters going back to 1980 seeing similar performance. The good news is universally negative quarters rarely follow through to the next quarter. Only one of the previous instances saw further declines in the following quarter (and the decline was minimal).

The following table highlights asset class performance for the first quarter:

Index	March % Chg	QTD % Chg	YTD % Chg
S&P 500 Index	3.58%	-4.95%	-4.95%
Dow Jones Industrial Avg.	2.32%	-4.57%	-4.57%
Nasdaq Composite	3.41%	-9.10%	-9.10%
Nasdaq 100 Index	4.22%	-9.08%	-9.08%
Russell 2000 Index	1.08%	-7.80%	-7.80%
S&P 1500	3.36%	-4.98%	-4.98%
S&P MidCap 400	1.21%	-5.22%	-5.22%
S&P SmallCap 600	0.18%	-5.93%	-5.93%
S&P 500 Equal Weight Index	2.39%	-3.15%	-3.15%
Russell 1000 Value	2.63%	-1.24%	-1.24%
Russell 1000 Growth	3.84%	-9.22%	-9.22%
Commodities, Currencies & Volatility			
Bloomberg Commodity Index	8.61%	25.45%	25.45%
Crude Oil	5.73%	34.56%	34.56%
Gold	2.17%	6.20%	6.20%
Natural Gas	28.42%	51.55%	51.55%
Copper	6.18%	5.97%	5.97%
U.S. Dollar Index (DXY)	1.66%	2.77%	2.77%
Euro	-1.31%	-2.62%	-2.62%
Japanese Yen	-5.50%	-5.43%	-5.43%
CBOE Volatility Index (VIX)	-31.81%	19.40%	19.40%
CBOE NDX Volatility Index (VXN)	-17.51%	27.31%	27.31%
International			
Toronto Stocks Exchange Comp.	3.74%	3.26%	3.26%
FTSE 100 Index	0.77%	1.78%	1.78%
Deutsche Boerse	-0.32%	-9.25%	-9.25%
CAC 40	0.02%	-6.89%	-6.89%
Nikkei 225	4.88%	-3.37%	-3.37%
Hang Seng Index	-3.15%	-5.99%	-5.99%
MSCI Emerging Markets Index	-1.88%	-6.71%	-6.71%
S&P 500 Sectors			
Consumer Discretionary	4.82%	-9.19%	-9.19%
Consumer Staples	1.41%	-1.63%	-1.63%
Energy	8.78%	37.66%	37.66%
Financials	-0.35%	-1.91%	-1.91%
Health Care	5.39%	-2.99%	-2.99%
Industrial	3.29%	-2.74%	-2.74%
Information Tech.	3.44%	-8.55%	-8.55%
Materials	5.82%	-2.84%	-2.84%
Real Estate	7.28%	-6.88%	-6.88%
Communication Services	0.93%	-12.11%	-12.11%
Utilities	10.08%	3.96%	3.96%

Source: Bloomberg/Canaccord Genuity

Some additional insights:

1. Weak returns across all major equity markets. The S&P 500 declined ~5% during the first quarter. It was the index's first negative quarter since 1Q 2020 and the fourth worst quarterly return since 1Q 2013. The negative return was a significant change from 2021 when the S&P 500 registered a +28.6% annual total return. Other equity markets did not fare any better, with small caps down roughly 8% (Russell 2000) and the tech-heavy Nasdaq down over 9%.

2. The S&P 500's performance was uneven. While the -4.6% return may seem shallow, it hides the S&P 500's roller coaster ride during the first quarter. U.S. large-cap stocks saw significant selling pressure in January and the S&P 500 suffered its largest monthly selloff since March 2020. The declines continued into February, and by early March, the S&P 500 was down -12.5% since the end of 2021. The index then proceeded to rebound in the second half of March, rallying ~9% off the lows and ending the quarter only 5% below its prior high in January.

3. Value stocks significantly outperformed Growth stocks. The Russell 1000 Growth index returned -9%, underperforming the Russell 1000 Value's -0.7% return. Within the S&P 500, Energy was the top-performing sector, climbing +39% as oil prices soared +30%. On the opposite end of the spectrum, Communication Services, Consumer Discretionary, and Technology were the three worst performing sectors due to their large Growth-factor exposures.

4. International stocks underperformed U.S. stocks. The MSCI EAFE Index, a benchmark for developed international stocks, declined -6.5%, while the MSCI Emerging Market Index

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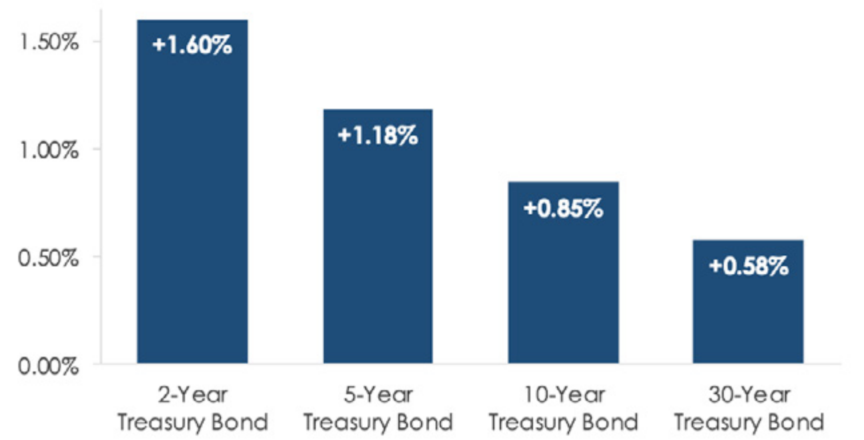
produced a -7.6% return. A strengthening U.S. dollar was a headwind for international equities, as foreign exchange effects were a drag on returns.

5. Rising Treasury yields led to steep losses in the bond market. The speed and magnitude of the rise in Treasury yields caused bonds to underperform equities during the first quarter (see chart from MarketDesk below). Corporate investment grade bonds produced a -8.4% total return, underperforming corporate high yield bonds' -4.7% total return. Why are these returns notable? Bonds have two primary risks: (1) interest rate risk, which is the risk interest rates rise and the bond's price declines, and (2) credit risk, which is the risk a borrower defaults on the loan. In general, investment grade bonds have more interest rate risk, because investors lend money for a longer period. In contrast, high yield bonds have more credit risk. Year-to-date bond returns indicate investors are more concerned about interest rate risk rather than credit risk.

FIGURE 2 – Year-to-Date Change in U.S. Treasury Bond Yields



Source: MarketDesk, U.S. Treasury. Data as of 3/30/2022.

A 10% RALLY AFTER A 10% DECLINE **HAS HISTORICALLY BEEN BULLISH**

While the market finished the quarter down almost 5%, it could have been a lot worse. It was down 13% at one point and had to stage a major rally to limit the decline.

From its lowest point in the quarter, the market rallied over 11% (before dropping 2% to end the quarter). A 10% drop and subsequent 10% rally have historically been very bullish for the S&P 500 (table from Bespoke):

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S&P 500 10% Down and Up Quarters: 1945 - 2022

	S&P 500 Performance (%)				
Quarter	Max Drawdown During Quarter (%)	Max Gain From Intra Quarter Low (%)	Entire Quarter	Next Quarter	Next Year
Q2 1970	-23.1	13.3	-18.9	15.8	37.1
Q4 1974	-13.6	10.1	7.9	21.6	31.5
Q4 1987	-31.7	14.9	-23.2	4.8	12.4
Q4 1997	-10.8	12.2	2.4	13.5	26.7
Q3 1998	-19.3	11.4	-10.3	20.9	26.1
Q3 2002	-19.4	20.7	-17.6	7.9	22.2
Q1 2003	-14.1	11.9	-3.6	14.9	32.8
Q4 2008	-35.5	21.4	-22.6	-11.7	23.5
Q1 2009	-27.6	23.1	-11.7	15.2	46.6
Q1 2016	-10.5	12.8	0.8	1.9	14.7
Q1 2020	-33.9	17.6	-20.0	20.0	53.7
Q1 2022	-13.0	11.1	-3.6		
		Average	-10.6	**11.3**	**29.7**
		Median	-11.7	**14.9**	**26.7**
		% Positive	**27.3**	**90.9**	**100.0**

S&P 500 trades up 10%+ from an intra-quarter low after trading down 10%+ from an intra-quarter peak.

Over the next quarter, the S&P was positive 10 out of 11 times, with a median gain of almost 15%. The market was higher every time a year later, and in some cases, the gains were substantial. Again, we are not suggesting that this will repeat, but we can't ignore similar patterns that preceded strong forward returns.

In summary, the **macro**cast™ score suggests the risk for a recessionary bear market is increasing but not necessarily imminent. The first quarter saw poor returns for risk assets across the globe, and bonds did not provide the ballast they normally do thanks to rising interest rates. The market's strong rally after being down double digits has historically led to further gains. While we believe a lot of investors' concerns are reflected in the market's recent performance, the current environment remains challenging.

APRIL SHOWERS…

Don't waste those rainy days. Take the opportunity to review your financial budget. You may find a few easy items you could trim and save money or apply to an upcoming summer vacation!

Contact your Wealth Manager today to discuss any thoughts or questions you may have.

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CORBETT ROAD
WEALTH MANAGEMENT

Washington, D.C.
7901 Jones Branch Dr
Suite 800
McLean, VA 22102
Local: 703.748.5836

Boston, MA
101 Arch St
8th Floor
Boston, MA 02110
Local: 617.600.7930

Los Angeles, CA
10100 Santa Monica Blvd
Suite 300
Los Angeles, CA 90067
Local: 310.591.5674

Fort Lauderdale, FL
2598 E. Sunrise Blvd
Suite 2104
Ft. Lauderdale, FL 33304
Local: 954.507.6028

Knoxville, TN
800 S. Gay St
Suite 700
Knoxville, TN 37929
Local: 865.444.4520

Phoenix, AZ
2375 E. Camelback Rd
Suite 600
Phoenix, AZ 85016
Local: 602.807.1145

St. Louis, MO
7777 Bonhomme Ave
Suite 1800
Clayton, MO 63105
Local: 314.463.0132

Toll Free: 844.688.4955
info@corbettroad.com
www.corbettroad.com
linkedin.com/company/corbettroad