SPRING 2023

As we began 2023, amid much uncertainty and facing the headwinds of inflation, higher interest rates and the threat of recession, investors might have reasonably expected continued struggles for the stock market. Add in the unexpected failure of Silicon Valley Bank and the yield on two-year Treasury Notes rising above 5.0% for the first time in 17 years and one might have expected the worst, particularly for technology stocks. As is so often the case in the short term however, stocks seemed to confound expectations by posting solid returns in the first three months of 2023.

In the first quarter of 2023, the Standard & Poor's 500 (S&P 500) advanced by 7.5% and the technology stock heavy NASDAQ composite rose 16.8%. This followed annual declines in 2022 of 18.1% for the S&P 500 and 33.1% for the NASDAQ. Foreign stocks also advanced in the first quarter with the MSCI developed markets index gaining 8.6% and the MSCI emerging markets index gaining 3.5%.

As evidenced by the performance of the NASDAQ composite index in 2023, growth stocks handily outperformed value stocks in the first quarter after significantly underperforming in 2022. In the first quarter of 2023, the Russell 1000 Growth ETF rose 14.3% while the Russell 1000 Value ETF rose only 0.9%. Some value stalwarts such as J.P Morgan, ExxonMobil and Johnson & Johnson declined in the first quarter of 2023 while growth stocks such as Apple, Microsoft and Tesla soared. Former growth index leader Meta (Facebook) declined in price so much in 2022 that its valuation placed it in the value index. Meta has recovered by over 70% year to date in 2023 and may be headed back to the growth index.

Some analysts attribute the rally in the technology stocks to the belief that the rise in interest rates is nearing an end. Others feel that as investors sold financial stocks in the wake of the Silicon Valley Bank collapse, the money was used to buy some of the large technology favorites. Certainly, long time market bellwether Apple, attracted buyers in the first quarter as the stock advanced by 27.1 % after declining by 26.4 % in 2022. As Apple is a major component of both the S&P 500 and the NASDAQ composite this surge helped lift both indices.

As shown in the very modest returns in the value index, all was not rosy across various industry groups in the first quarter. The crisis in the banking sector seems to have been limited to Silicon Valley Bank and a few others but the failure cast doubts across many smaller, regional banks. We believe these banks are well capitalized and can prosper barring a severe recession. However, the pall is likely to hover over these stocks for a while.

While the recovery in the NASDAQ and S&P 500 in the first quarter of 2023 has been encouraging, substantial challenges for the markets and the economy remain. The Federal Reserve will continue raising interest rates, perhaps modestly, as they try to tame inflation without forcing a severe recession. The yield curve remains inverted with short term interest rates higher than long term rates. The two-year Treasury Note currently yields just over 4% after reaching 5% in early March. Part of the rather sharp decline in the yield in March can be attributed to concerns over the isolated bank failures.

While higher yields have given investors more attractive options for investing short term cash, the impact of higher rates on borrowers like homebuyers is a potential negative for the economy. If yields could stabilize at current levels as inflation gradually declines without a significant slowdown in the economy, the Fed will have achieved the longed for "soft landing".

This may be wishful thinking and challenges remain, but the economy seems to be holding up reasonably well despite the dramatic headlines of the first quarter. While we are optimistic for the long term, it is important for investors to anticipate continued volatility and have a solid reserve of short-term assets to meet anticipated spending needs over the next few years. We wish you all the best as spring gradually, and always grudgingly, arrives in Maine.

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