CAPITAL MANAGEMENT GROUP

The Hefter Report – January 2022

The major US stock market indices have not seen a 10% decline since April 2020. We think that we are seeing that correction now.

The catalysts for the pullback and rapid rise in interest rates are elevated inflation levels, tightening monetary policy and higher labor costs. Fed Chairman Powell's comments and aggressive plans to curb inflation are weighing on the financial markets. The market is currently anticipating the first rate hike with the possibility of 3 additional increases later in the year.

This adjustment in Fed policy, we believe, is causing a shift in investor allocation, primarily out of small, mid and large cap growth stocks and into value and cyclicals as well as some international securities and commodities. We favor more value-oriented ETFs and funds that invest in companies that can pass on rising costs to consumers.

Historically, during periods of Fed tightening, equities have outperformed bonds and have still delivered positive returns. While the S&P 500 is currently down about 10%, many companies in the index have corrected even more (especially those with high price earnings ratios). That's true for the NASDAQ as well, with some companies already down more than 20%. That's a healthy correction and may be a little overdone.

Right now the entire market is getting hit and it is painful. However, we believe the bull market is still intact. As omicron subsides, the positive growth effects of the economy reopening will lead to declines in supply chain issues, a reduction in inflation and an increase in earnings. This, we hope will allow for another positive year for the stock market with indices ending the year up more than bonds, cash and inflation.

We do not believe it is a sign of a near-term recession or a bear market.

We therefore still favor large cap, well capitalized companies, especially over fixed income securities.

We believe that this trend will prevail during the first half of the year but may revert to outperformance in growth during the second half of the year. This is because once the Fed hikes take effect, cyclical economic growth could slow and investors may once again seek out the companies that can grow despite the overall economy.

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S&P 500 Index: The S&P 500 Index consists of 500 stocks chosen for market size, liquidity, and industry group representation. It is a market value weighted index with each stock's weight in the Index proportionate to its market value.

Stocks are subject to market risk which means their value may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors. Investments in equity securities are generally more volatile than other types of securities. There is no guarantee that dividend-paying stocks will return more than the overall stock market. Dividends are not guaranteed and are subject to change or elimination.

Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability, and different accounting standards. This may result in greater share price volatility. Investing in emerging markets accentuates these risks.

Investments that are concentrated in a specific sector or industry may be subject to a higher degree of market risk than investments that are more diversified.

Investments in fixed-income securities are subject to market, interest rate, credit and other risks. Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in interest rates can result in the decline in the bond's price. Credit risk is the risk that an issuer will default on payments of interest and/or principal. This risk is heightened in lower rated bonds. If sold prior to maturity, fixed income securities are subject to market risk. All fixed income investments may be worth less than their original cost upon redemption or maturity.

There are special risks associated with an investment in real estate, including credit risk, interest rate fluctuations and the impact of varied economic conditions.

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