Alexis Investment Partners, LLC

Practical ✧ Tactical

Summary

Famed Investor Peter Lynch once said, **"Everyone has the brainpower to make money in stocks. Not everyone has the stomach."** Stocks staged a powerful rally in October. **The Dow Jones Industrial Average** (DIA) **surged 14%, its best monthly gain since 1976.** This, as inflation continues to soar, the war in Ukraine rages and the Fed tightens policy even as housing activity slumps and recessionary pressures mount. The S&P500 index gained 8.1%, MSCI All Country World index rose 6.4%, and tech heavy Nasdaq 100 (QQQ) was up 4%.

This may be another bear market bounce similar to this summer, but it is also possible (and we believe increasingly probable) that expectations were so low in September that bad news is no longer a surprise, and therefore has limited impact on markets. **Fear and pessimism pushed many investors to the sidelines. If stocks continue to climb after the November Fed meeting and mid-term elections, the pain of missing gains having endured declines has the potential to build momentum.**

One of the better decisions we have made over the last few years has been to minimize exposure to ultra-low yielding bonds. **As yields climb, bond prices have been decimated. The Bloomberg Aggregate Bond index** (AGG) **is down -15.5% in 2022,** LQD, the iShares ETF that holds investment grade corporate bonds fell -21.8%, TLT (iShares 20-year US treasury ETF) plunged -34.1%. The silver lining to rising rates is that **yields are now at levels that make sense for long-term investors looking to earn a return above inflation with less volatility than stocks.**

As difficult as 2022 has been, our **discipline and long-term optimism has helped us add value** by minimizing exposure to lagging areas like foreign and emerging markets and unprofitable tech companies, diversifying beyond mega-cap leaders, tactically trimming exposure into rallies and significantly adding stock exposure into declines. Still, it's been far from smooth sailing, and **we appreciate your continued confidence** as we work through this challenging time. When we look back, **we expect this will be another example of the long-term wealth that is both created and destroyed by the choices investors make in bear markets.**

It's not too late to do year-end planning. We encourage you to schedule some time to check in, update us on your plans, goals, and any concerns, and review performance. And finally – **Don't forget to vote!**

What to Expect in Portfolios

Last month we wrote: "**It is likely to take several weeks to confirm if the bear market is over** or the bottoming process fails which would imply a continuation of the downtrend. **We tactically added to stocks into the decline and will continue to adjust our allocation…"**

Markets surged in October as described above.

We remain tactically overweight stocks. As we incrementally rebalance portfolios, we expect to increase exposure to short-term investment grade bonds and T-bills. **The pace of rebalancing will be based in part on our assessment of the market's reaction to the Fed and mid-term elections.**

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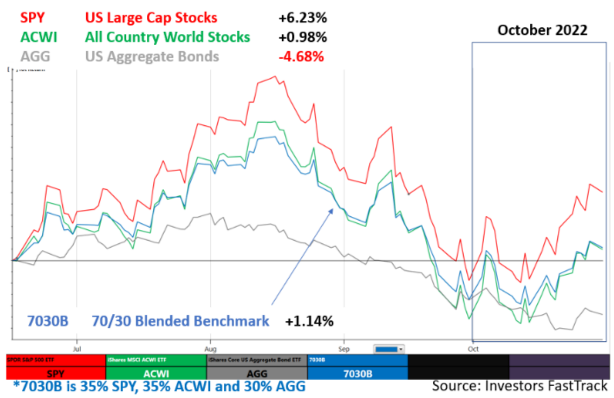
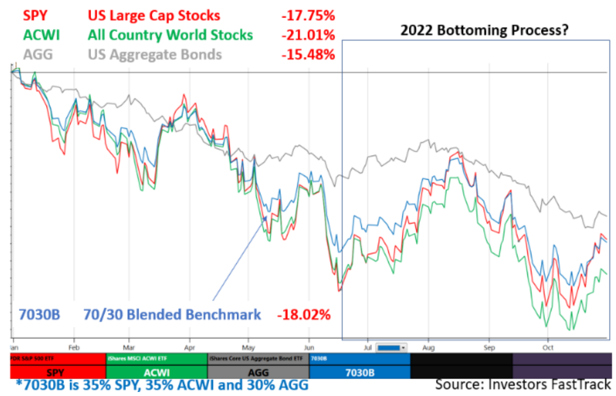
The chart below shows that **the September swoon** to new lows **failed to push stocks meaningfully lower and a strong rally has kept the bottoming process in play.** Bonds remain weak, but **yields are more attractive.** We were tactical buyers of stocks into the drop, which worked well in October.

Despite a great October - **2022 returns remain dismal across stocks and bonds (global and domestic)**. Conservative investors with balanced portfolios enjoyed little reprieve. As stocks continue to trace out a bottoming process, it is still **too soon to declare the bear market over.**

2022 Bottoming Process? (6/16/2022-10/31/2022)

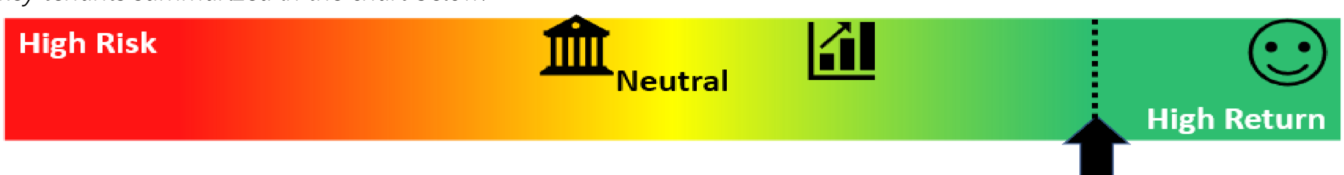


2022 Year-to-Date (12/31/2021-10/31/2022)



Insights and Commentary

Investing can be an emotional roller coaster leading to costly mistakes. To navigate effectively as we seek greater participation in advances than declines, we have found it helpful to monitor a series of indicators and models based on 3 key tenants summarized in the chart below:



Summary of Current Conditions

Monetary conditions have tightened considerably as the Fed raises rates and drains reserves. **Stock downtrends have stalled and breadth looks increasingly constructive. Stocks still face several hurdles to break downtrends.**

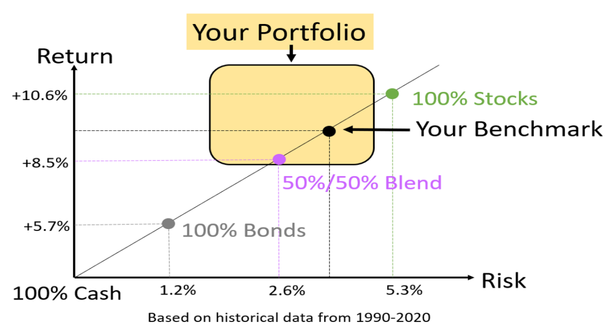
Near-term, the most positive indicators we see are based on extreme negative sentiment, seasonal strength in the 4th quarter of mid-term election years and oversold conditions (each of which are better as trading indicators and can provide false comfort in severe bear markets).

The combination of slower growth and signs that we are past peak inflation is consistent with past bear market lows and above average forward returns.

We have been tactically overweight stocks and recently sold REITs and Gold to add to stocks, and also boost exposure to cash and treasury bills.

As we rebalance to a more neutral posture in the months ahead, **we expect to increase exposure to short-term ...**

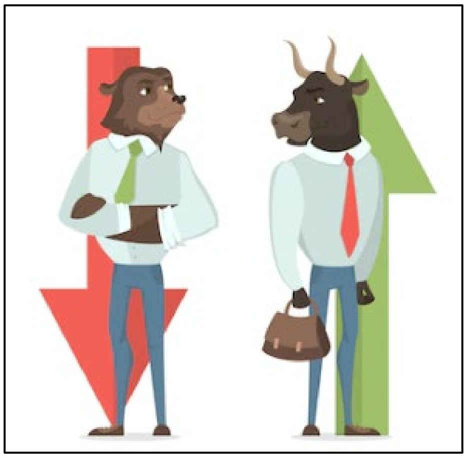
Risk/Return Expectations



We kept this graphic as an important reminder that our goal is to add value (generate higher risk-adjusted returns) through full market cycles by allowing our portfolios to deviate from benchmarks. **We base allocation decisions on an assessment of both risk and return potential.**

... investment grade bonds and T-bills to take advantage of attractive yield opportunities and manage volatility.

Portfolios are based on client needs, goals and preferences.



Update, Observations, Indicators and Outlook:

Based on current patterns and mounting signals from several of our historically reliable models and indicators, **we believe the market is working through a bottoming process that began with the June lows.**

In the last few months, we have shared examples of what past bottoming processes have looked like. In addition to sharing similar chart patterns, another commonality is that most **bear markets bottom while news and sentiment remain bleak.**

Testing is a frustrating and sometimes scary part of a bottoming process as **pundits** label the prior move a "bear market bounce" and **predict lower lows based on the same news that drove us to the prior trough.** That news, however, is widely known and beginning to improve.

The Fed has made significant progress tightening monetary conditions. They continue to stress their commitment to fighting inflation and **we expect further rate increases but that we are nearing the end of this tightening cycle.**

From an economic perspective, job openings remain strong even as we see increasing layoffs. One reason is that our economy is 70% services and services are still understaffed having cut back during COVID as demand rebounds.

There is real economic pain from both inflation and higher interest costs. It will take time for inflation to slow and for consumers to get used to higher interest rates.

Bond interest rates have been suppressed by the Fed for years. At this point, rates have risen to levels consistent with more normal **market driven prices**. As investors, this **offers opportunities in fixed income that make it easier to manage risk while preserving purchasing power.**

Over time, market driven interest rates leads to more thoughtful capital allocation, improved loan underwriting and innovation.

Our tactical portfolio has been actively shifting between neutral and overweight stocks and remains broadly diversified.

We continue to expect volatility as we pursue attractive long-term opportunities. If you have any questions or concerns about your portfolio, we encourage you to send us an email or schedule a call.

Market Pulse:

We try to avoid jargon, but a few terms are helpful when describing financial conditions.

Bull Market: markets trending up (making higher highs on rallies and higher lows in periods of decline).

Consolidation: after a period of strong gains or steep declines sometimes markets become range bound, moving up and down by 3-5% over several weeks. After consolidation, the prior trend resumes.

Pullback: a decline of 3-5% that generally happens at least twice per year. Pullbacks often resolve within a few weeks.

Correction: a decline of 5% to 10% that typically happens once per year. Like pullbacks, markets recover quickly after corrections, generally within 3-6 months.

Bear Market: a decline of 20% or more. Many bear markets are fully recovered within 18- 24 months, but severe bear markets like 2000-2003 and 2007-2009 can take 5-7 years or longer to recover from. **Despite an impressive October rally, it is premature to declare the bear market over. The maximum loss has (so far) been -25% from peak to trough.**

Bottoming Process: After a correction or bear market, stocks often bounce and re-test lows multiple times before recovery. **The market continues to trace out a bottoming process that appears to have started with the June lows and September re-test.**

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Closing Comments:

Several clients have recently been speaking with friends who are looking to make a change either because they are nearing a life transition or have been unhappy with their current advisor.

We appreciate your referrals and are pleased that our company continues to enjoy steady growth. Our focus is always on providing exceptional service and performance and we are very grateful for your confidence and support!

Although our focus is on financial planning and investments, we also have relationships and resources to help with life and LTC insurance and annuities.

As an Accredited Investment Fiduciary (AIF), Jason acts as a 3(38) Fiduciary Advisor to 401k plans and has been able to help several small business owners reduce costs, significantly improve their plans and offload some of their liability as plan sponsors while creating a better experience for employees.

Please call and/or email me personally for most of your account servicing needs and especially when you have questions or concerns.

Disclosures

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