Birch Hill
INVESTMENT ADVISORS

Market View

April 2022

WAR AND FED RATTLE STOCKS

Most major US stock market indices ended the first quarter below the peaks achieved at the beginning of 2022. Concerns about high valuations and higher interest rates drove declines in late January. In February, markets fell more following Russia's invasion of Ukraine. After bottoming in early March, markets recouped a large part of their losses despite continued high uncertainty. Through March 31, the S&P 500 Index returned –4.6% after being down nearly 13% at its worst. The most speculative, high-priced growth stocks declined the most over the first three months of the year. The Nasdaq Composite, which is weighted toward growthier technology stocks, returned -8.9% after being down close to 21% at its lows.

LESS CERTAIN ECONOMIC PICTURE

US economic prospects looked relatively bright at the end of 2021, with gross domestic product (GDP) estimates calling for around +4% growth in the year ahead. Three months into 2022, this economic picture is much more mixed and uncertain due to Russia's invasion of Ukraine. Tough sanctions on the Russian economy are creating price spikes and supply disruptions across a number of commodities used to produce a wide variety of goods and services. Without a quick resolution to the war, an easing of sanctions, or finding new sources of supply, higher prices on commodities—including oil and gas—could weigh on global growth in the year ahead. US GDP forecasts have already been cut by almost a full percentage point to +3% growth in 2022. However, current estimates are uncertain and depend upon many moving parts, such as central bank policy and how consumers hold up amid higher prices.

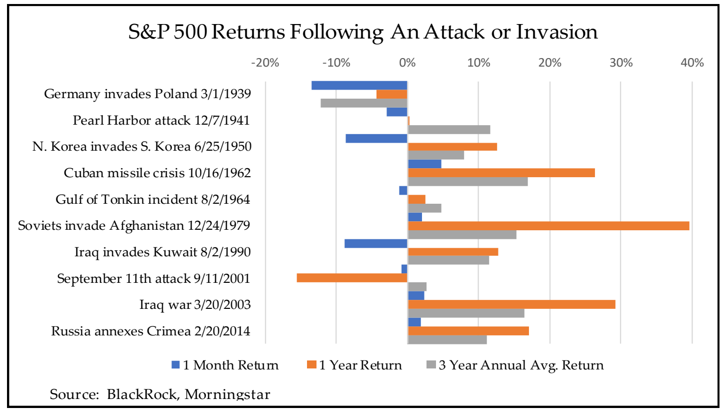
STOCK MARKETS IN TIMES OF WAR

The war between Russia and Ukraine is a tragedy. We sincerely hope it is resolved as quickly as possible and remains contained. How all of this unfolds and its overall impact on markets is impossible to know. However, if history is any guide, the stock market has generally moved higher in the years following an attack or invasion.

Market Indicators		3/31/2022
TOTAL RETURN		
US Stock Markets	12 Mos	1st Qtr 2022
S&P 500 Index	15.6%	-4.6%
S&P 400 Mid Cap	4.6%	-4.9%
Russell 2000 Small Cap	-5.8%	-7.5%
Int'l Stock Markets		
ETF Returns in US$		
EAFE Index (Europe, Australia, Asia, Far East)	0.3%	-6.5%
Japan (MSCI Index)	-8.2%	-8.0%
China (FTSE 50)	-30.5%	-12.6%
Emerging Mkts Index	-13.7%	-7.6%
US Fixed Income Yields	12/31/2021	3/31/2022
6 Mo US T-Bill	0.19%	1.06%
2 Yr US T-Note	0.73%	2.28%
10 Yr US T-Note	1.52%	2.32%

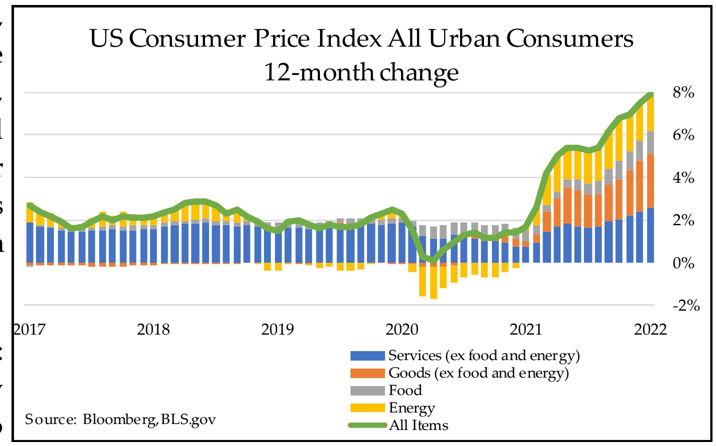
Birch Hill Investment Advisors LLC
One International Place, Suite 770
Boston, MA 02110
Phone: 617-502-8300
BHBoston.com

A BlackRock analysis of S&P 500 Index returns following an attack or invasion has been adapted by Birch Hill in the chart shown on the right. Across the chart's events, the index's return was -3% over a one-month period, +12% over a one-year period, and +9% annually over a three-year period. Of course, past performance is no guarantee of future returns, but the main takeaways here are that it usually pays to be patient and to stay invested, and that it is hard to time the market. The war will likely continue to weigh on the market and cause volatility, especially if the fighting escalates, but the market can also rebound quickly should it conclude more swiftly than expected.



INFLATION LIKELY TO WORSEN BEFORE IT IMPROVES

After a long period of relatively mild price increases, inflation has accelerated recently to levels not seen since the 1980s. In the decade preceding the pandemic, inflation, as measured by the Consumer Price Index for all urban consumers (CPI-U), averaged just under +2% per year. The most recent CPI-U numbers showed prices growing +7.9% over the 12-month period ended in February 2022.



The chart to the right shows the drivers of that inflation: energy, goods, and food, but with a broadening recently to services. Global supply chains, which helped keep prices for goods low before the pandemic, are now one of the main reasons for today's high inflation. Consumers have continued to buy goods while supply is struggling to catch up in areas like computer chips and vehicles.

The Russia-Ukraine war has further complicated the inflation picture. Russia and Ukraine are top suppliers of oil, gas, metals, and grains to the global economy. The supply of these commodities is now in question, which has fueled price surges. Therefore, inflation is likely to worsen as commodity price increases flow through to finished goods and supply shortages continue before eventually improving. The Federal Reserve has indicated it is ready to raise interest rates several times over the next year to combat high inflation. However, raising rates when the economy is experiencing commodity price shocks is tricky. Both higher interest rates and higher energy prices tend to dampen economic growth.

CONCLUSION: MIXED ECONOMIC BACKDROP WITH HIGH UNCERTAINTY

Stocks have had a volatile start to the year. The economic growth backdrop is much more uncertain due to the Russia-Ukraine war and a Federal Reserve set to raise rates to fight high inflation. We believe investors should be patient and continue to hold a portfolio of high-quality companies for the long-term. Industry-leading companies tend to have greater pricing power, allowing them to counteract inflating costs. The high level of uncertainty suggests investors should maintain adequate levels of cash to meet spending needs and take advantage of opportunities in what will likely continue to be volatile financial markets.

Gary R. Mikula, CFA   Robert A. O'Neil, Jr., CFA   Catherine M. Kennedy, CFP®   Timothy M. Malloy, CFP®

Brett A. Mirliani, CFA, CFP®, CPWA®   Adam J. Desjardins, CFA   G. Bowen Cook, Jr., CFA   Christopher P. Mikus, CFA