



# CHARTBOOK

## Market Comment

Prepared by OceanFront Investment Counsel Inc.

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# TABLE OF CONTENTS

## Chartbook Market Comment: August 2022

4. Market Comment
5. Energy versus Metals
6. Oil & Gas Returns
7. Inflation - US
8. Inflation - US
9. Interest Rates - US
10. Interest Rates - Canada
11. GDP - US
12. Treasury Yield Curve
13. S&P500 During Recessions
14. Bull & Bear Markets
15. Stock Returns & Drawdowns
16. Bond Returns & Drawdowns
17. Disclaimer

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# Market Comment

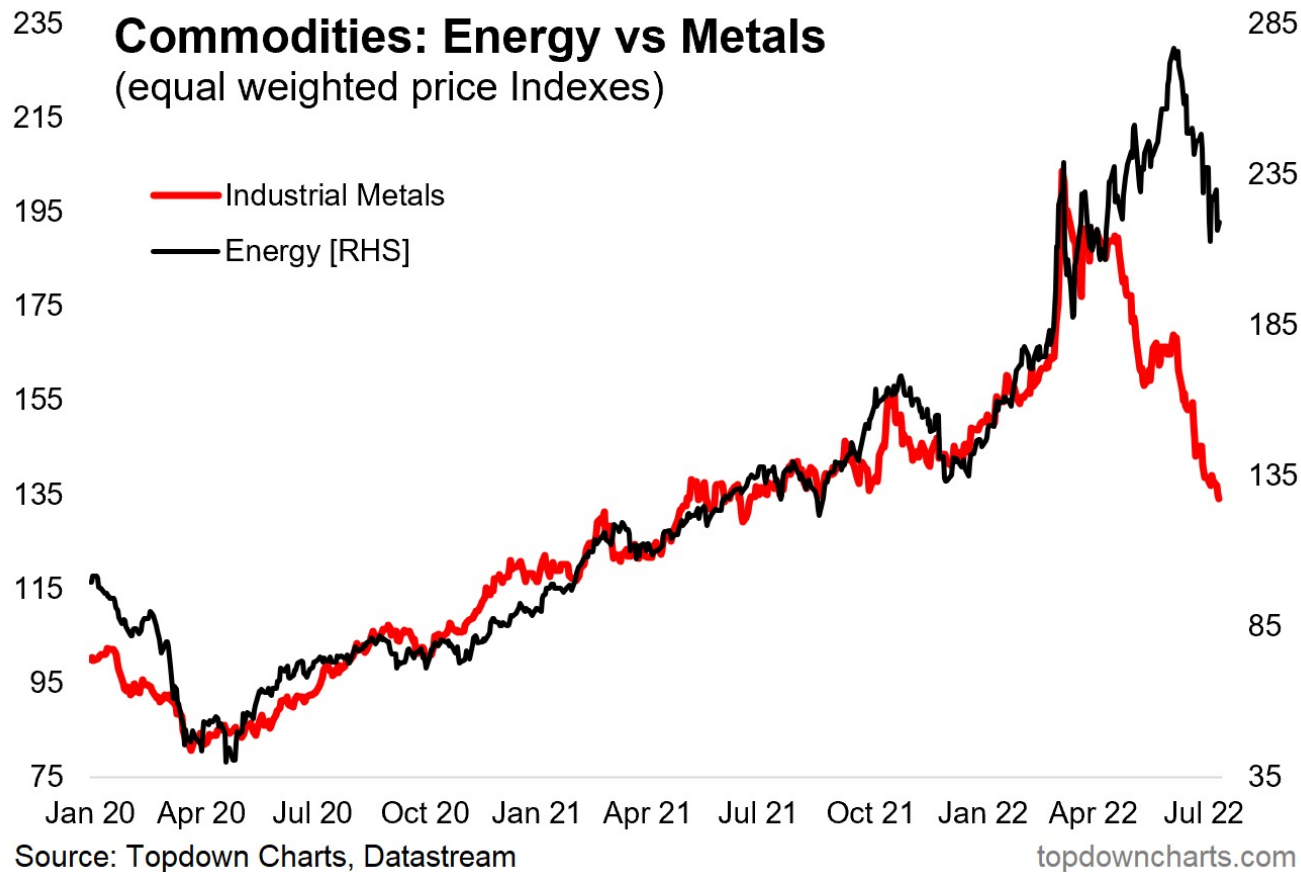
North American stock and bond markets bounced in July. The TSX, S&P500 and Nasdaq 100 stock indexes rose 4.4%, 9.1%, and 12.6% respectively, while the iShares Canadian Universe Bond Index ETF rose 3.7%. These returns came despite the headwinds from the Bank of Canada and the Federal Reserve, who raised their policy interest rates by 1% and 0.75% in July.

For the most part, global markets still show large losses year-to-date. Inflation is running high and central banks are reducing demand through interest rate hikes to attempt to bring it under control. When interest rates rise, the cost of servicing debt increases, thus reducing the amount of discretionary income that households and businesses have. In turn, this reduces the amount of credit and spending power in the economy, reduces demand for goods and services, and has a deflationary effect.

One person's spending is another's income, so when everyone is spending less there is a negative effect on economic output, GDP, and a heightened risk of an economic recession. One of the burning questions today is whether the central banks can calm inflation without pushing the economy into recession and, if they do, how bad the recession will be.

As unpleasant as bear markets are, we must remember that they are a natural part of the market cycle. Temporary declines from market volatility are the price of admission for equity and balanced investors who can expect a materially higher long-term return than they would otherwise earn in "safe," stable assets like GICs and cash.

# Energy versus Metals



Energy prices, shown here as a composite of crude oil, natural gas and other petroleum products, tend to be well correlated to industrial metals prices. While industrial metals have fallen into a deep correction, energy has held up much better. We will likely see either a departure from this correlation for a period of time or energy prices will “catch-down” to industrial metals.

# Oil & Gas Returns

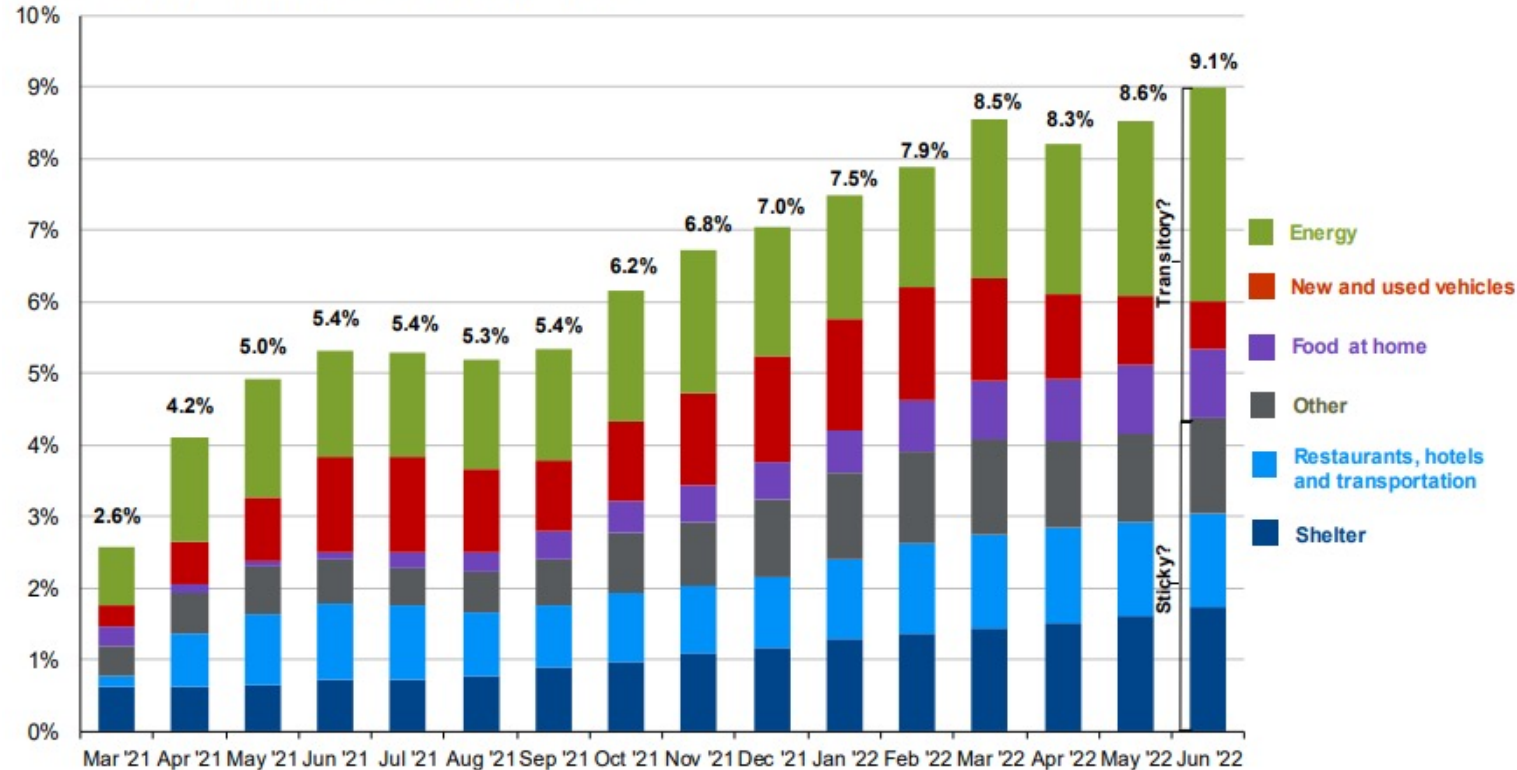


Crude oil and gasoline prices have seen huge gains over the past year but have fallen significantly from the recent highs. This is good news for prices at the pump and consumer budgets.

# Inflation – US

## Contributors to headline inflation

Contribution to y/y % change in CPI, non seasonally adjusted



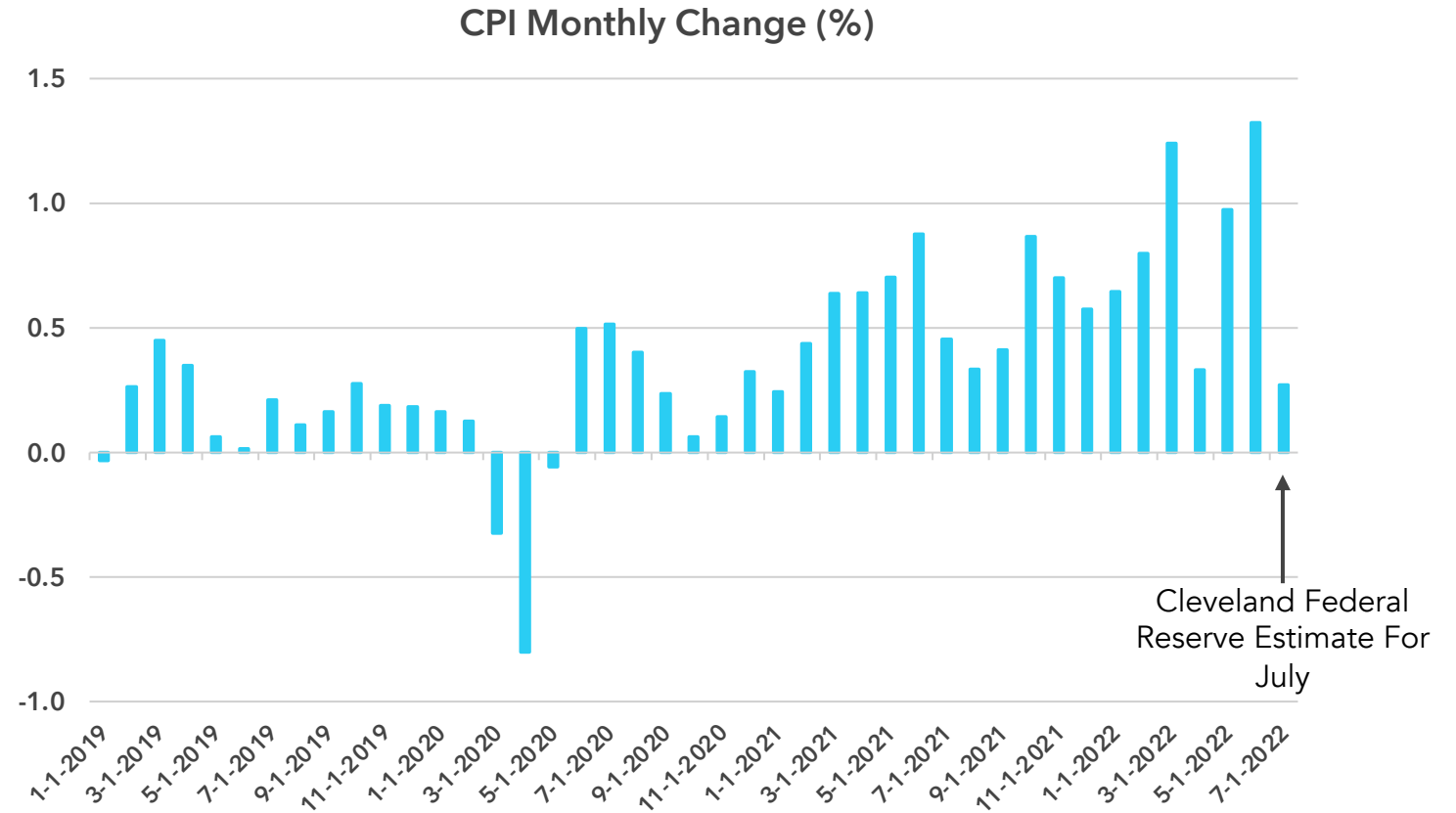
Source: BLS, J.P. Morgan Asset Management. Contributions mirror the BLS methodology on Table 7 of the CPI report. Values may not sum to headline CPI figures due to rounding and underlying calculations. "Shelter" includes owners equivalent rent and rent of primary residence. "Other" primarily reflects household furnishings, apparel, education and communication services, medical care services and other personal services.  
*Guideto the Markets – U.S.* Data are as of July 28, 2022.

In June, about a third of the total inflation measure was contributed by energy prices. After a big decrease from the recent highs in price, the contribution from energy to inflation in July should decrease significantly.

# Inflation - US

As measured by CPI, month-over-month increases in inflation have been consistently large in 2022. The latest estimate (as of August 2) for the July inflation number from the Cleveland Federal Reserve is 0.27%, which would be the smallest number since January 2021.

Cooling the overheated economy and high inflation has been the stated goal of central banks in raising interest rates. A sustained decline in monthly inflation data could signal central banks to back off the rate hikes.





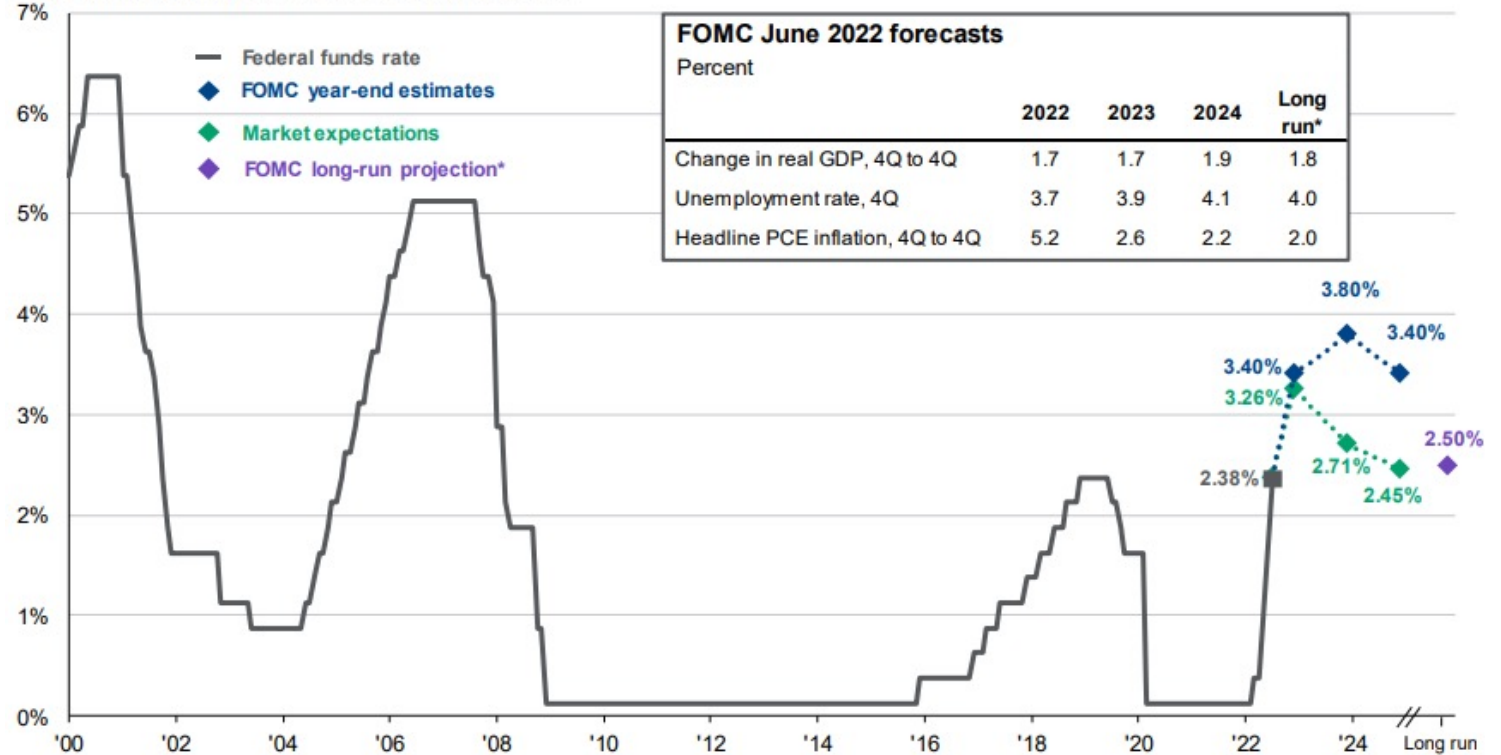
# Interest Rates - US

The Federal Reserve has increased its Federal Funds rate to a range of 2.25%-2.5%. The Fed projects that it will raise the rate to a high of 3.8% and then begin to reduce it, with the long-run rate projection at 2.5%. This projection is based on their assumption that they will "win" the battle with inflation in the short run which will allow them to cut rates. They expect inflation of 2.6% in 2023 and 2.2% in 2024.

The stakes are very high here because if the Fed is wrong about inflation coming down in the short run, they will probably have to keep hiking rates to bring it down, which will put economic growth at serious risk.

## Federal funds rate expectations

FOMC and market expectations for the federal funds rate



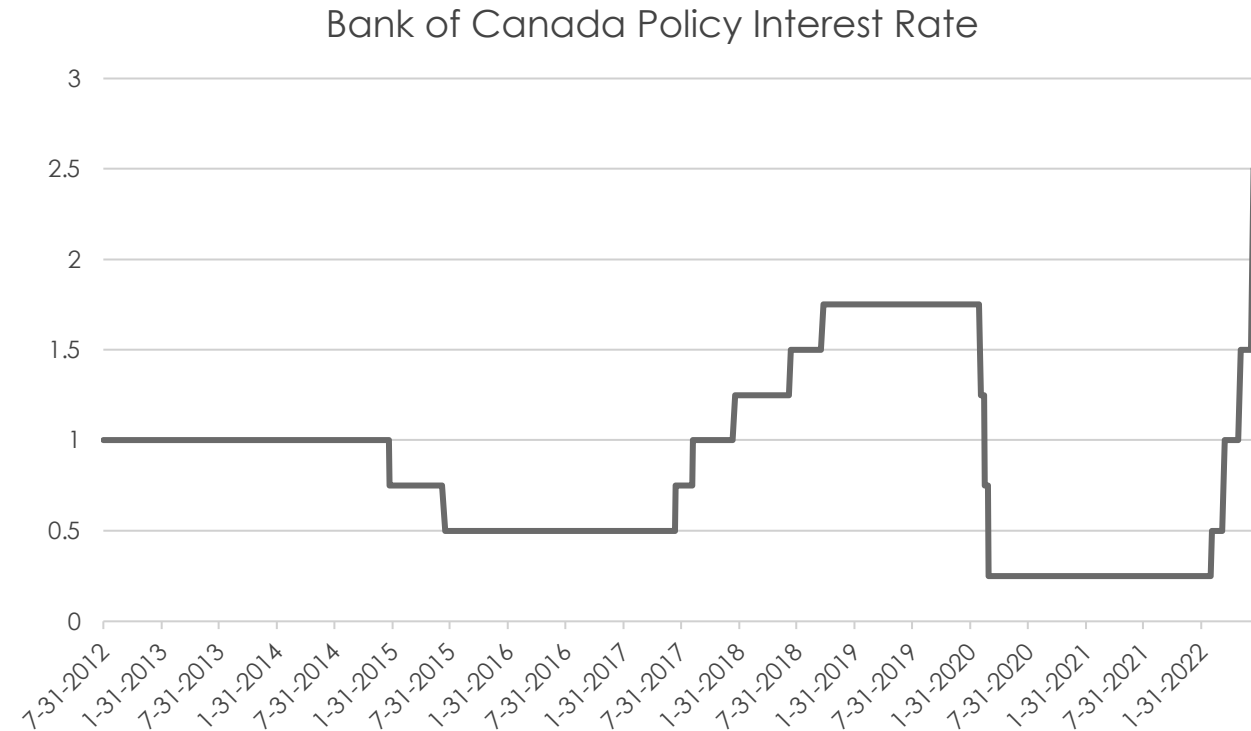
Source: Bloomberg, FactSet, Federal Reserve, J.P. Morgan Asset Management

Market expectations are based off of the respective Federal Funds Futures contracts for December expiry. \*Long-run projections are the rates of growth, unemployment and inflation to which a policymaker expects the economy to converge over the next five to six years in absence of further shocks and under appropriate monetary policy. Forecasts are not a reliable indicator of future performance. Forecasts, projections and other forward-looking statements are based upon current beliefs and expectations. They are for illustrative purposes only and serve as an indication of what may occur. Given the inherent uncertainties and risks associated with forecasts, projections or other forward-looking statements, actual events, results or performance may differ materially from those reflected or contemplated.

GuidetotheMarkets - U.S. Data are as of July 28, 2022.

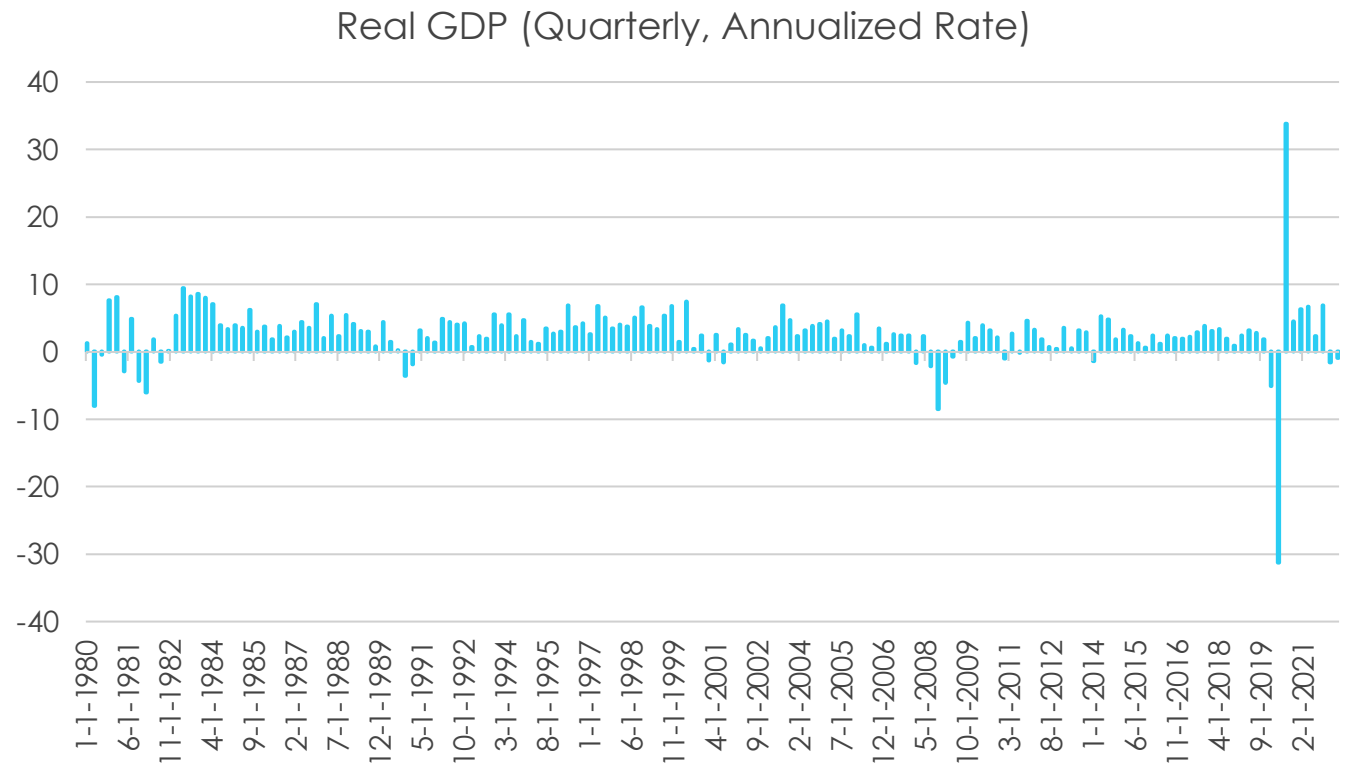
# Interest Rates - Canada

Similarly, the Bank of Canada has raised its policy rate to 2.5%, with a 1% increase in July alone.



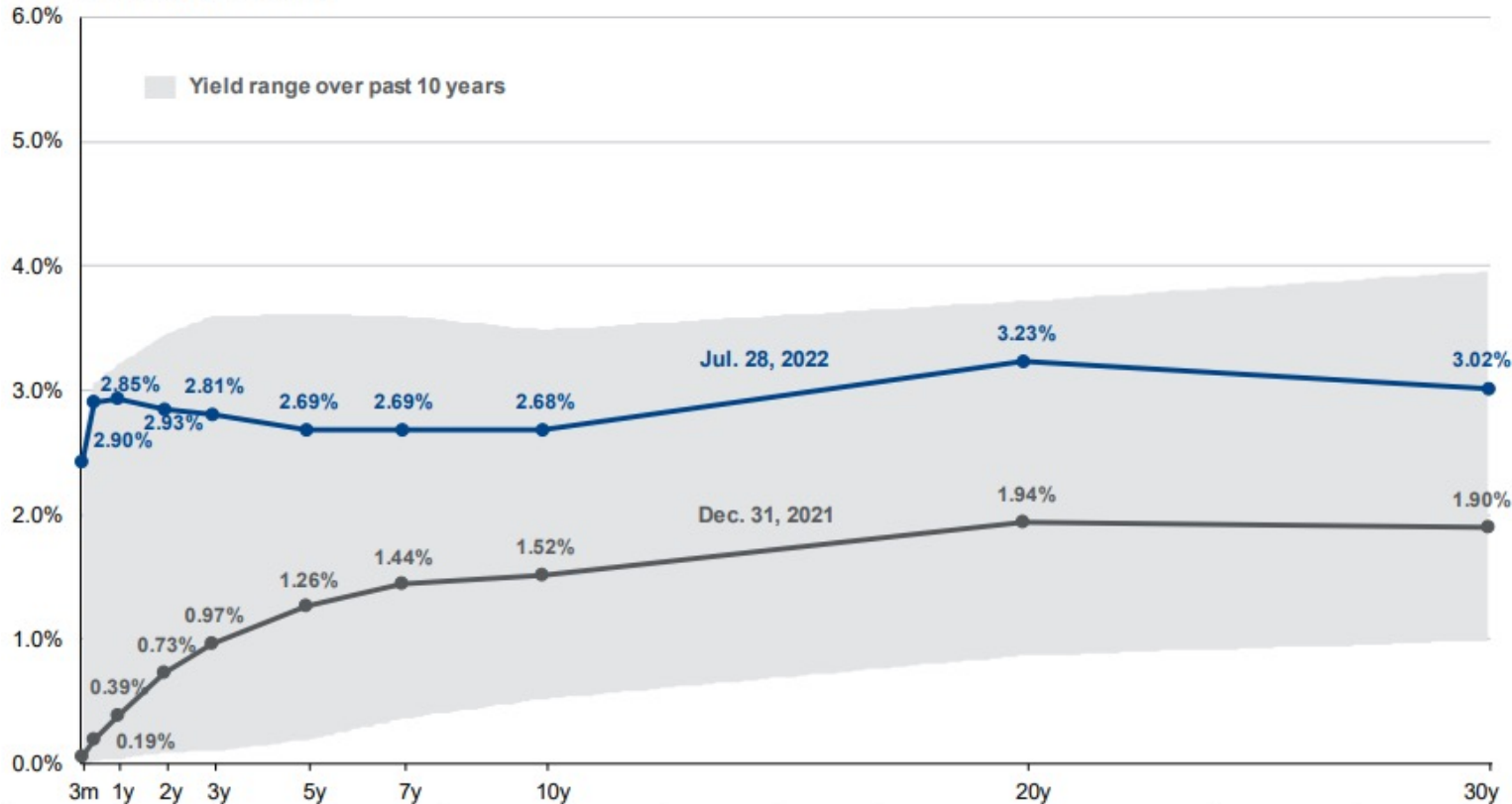
# GDP - US

The US has now seen two consecutive quarters of negative Real GDP growth, which is a common rule of thumb that a recession is underway, but a recession is yet to be formally declared by the authorities. Real GDP growth is net of inflation; hence the US economy is still growing at a fast nominal pace, just slightly slower than inflation.



# Treasury Yield Curve

U.S. Treasury yield curve



Source: FactSet, Federal Reserve, J.P. Morgan Asset Management. *Guide to the Markets – U.S.* Data are as of July 28, 2022.

The chart shows the US Treasury yield curve, the market yield offered on US Treasury securities at various maturities, as of July 28, 2022 (blue line) and Dec. 31, 2021 (gray line).

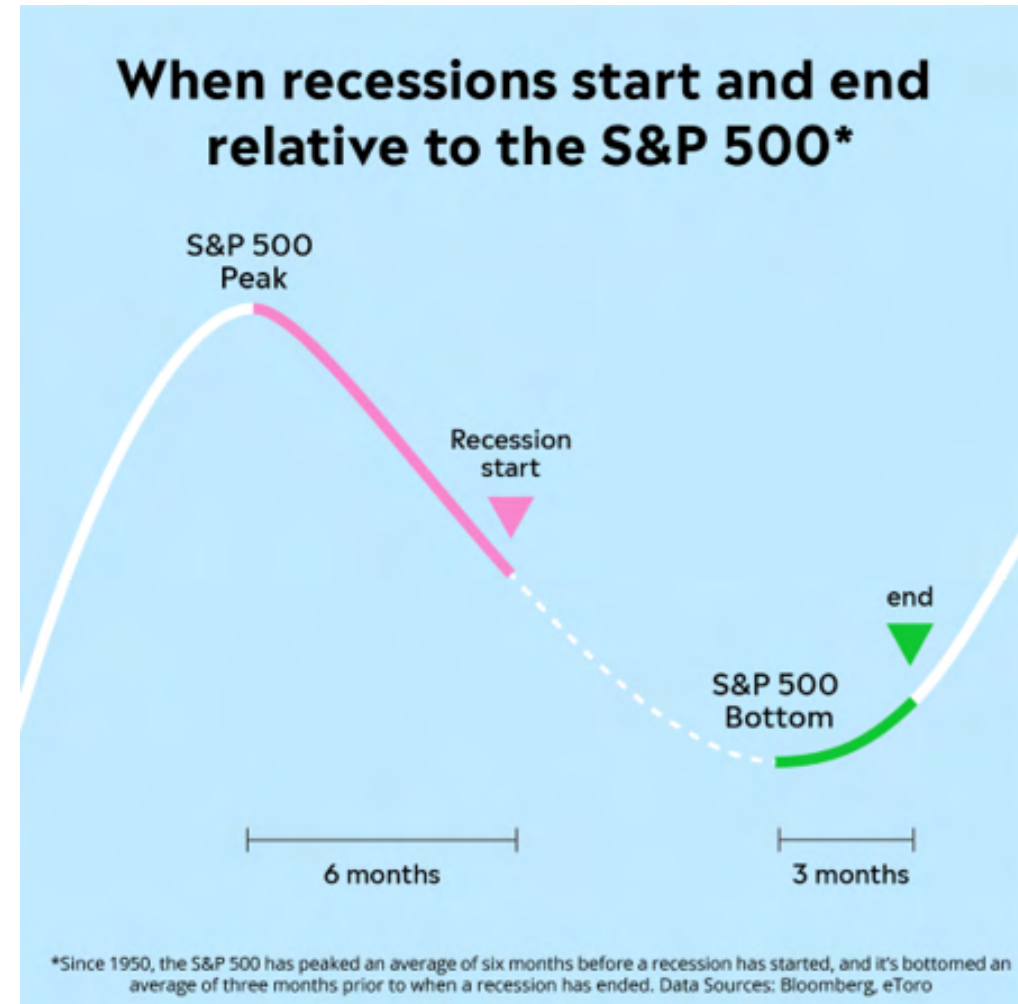
Typically, short-term Treasuries yield less than long-term Treasuries because they carry less risk. This was the case in Dec. 2021. As of July 28, 2022, several shorter dated yields were higher than corresponding longer-term yields. The yields on the 1-7 year Treasuries are all higher than the yield on the 10 years.

This suggests that the bond market is expecting interest rates to be lower in the future than they are now, which commonly happens when the Federal Reserve cuts interest rates in a recession. This phenomenon has been a reliable indicator of an upcoming recession in the past.

# S&P500 During Recessions

If a recession does occur or has already begun, the stock market will most likely bottom before the end of the recession when the prospects for the economy appear bleak.

Historically on average, the S&P500 peaks six months before the recession begins and bottoms three months before it ends. With the decline in stock markets we have experienced this year, it's possible the market has already anticipated and priced in a recession or at least priced in a significant slowdown in economic growth.



# Bull & Bear Markets

Bull markets			Bear markets		
Bull begin date	Bull return	Duration (months)	Market peak	Bear return*	Duration (months)*
Jul 1926	152%	37	Sep 1929	-86%	32
Mar 1935	129%	23	Mar 1937	-60%	61
Apr 1942	158%	49	May 1946	-30%	36
Jun 1949	267%	85	Aug 1956	-22%	14
Oct 1960	39%	13	Dec 1961	-28%	6
Oct 1962	76%	39	Feb 1966	-22%	7
Oct 1966	48%	25	Nov 1968	-36%	17
May 1970	74%	31	Jan 1973	-48%	20
Mar 1978	62%	32	Nov 1980	-27%	20
Aug 1982	229%	60	Aug 1987	-34%	3
Oct 1990	417%	113	Mar 2000	-49%	30
Oct 2002	101%	60	Oct 2007	-57%	17
Mar 2009	401%	131	Feb 2020	-34%	1
Mar 2020	114%	21	Jan. 2022**	-24%	5
<b>Averages</b>	<b>162%</b>	<b>51</b>	<b>-</b>	<b>-41%</b>	<b>20</b>

In data dating back to the 1920's, bear markets have averaged a decline of 41%, while bull markets have returned an average of 162%. Bear markets are unpleasant, but a new bull market always follows them.

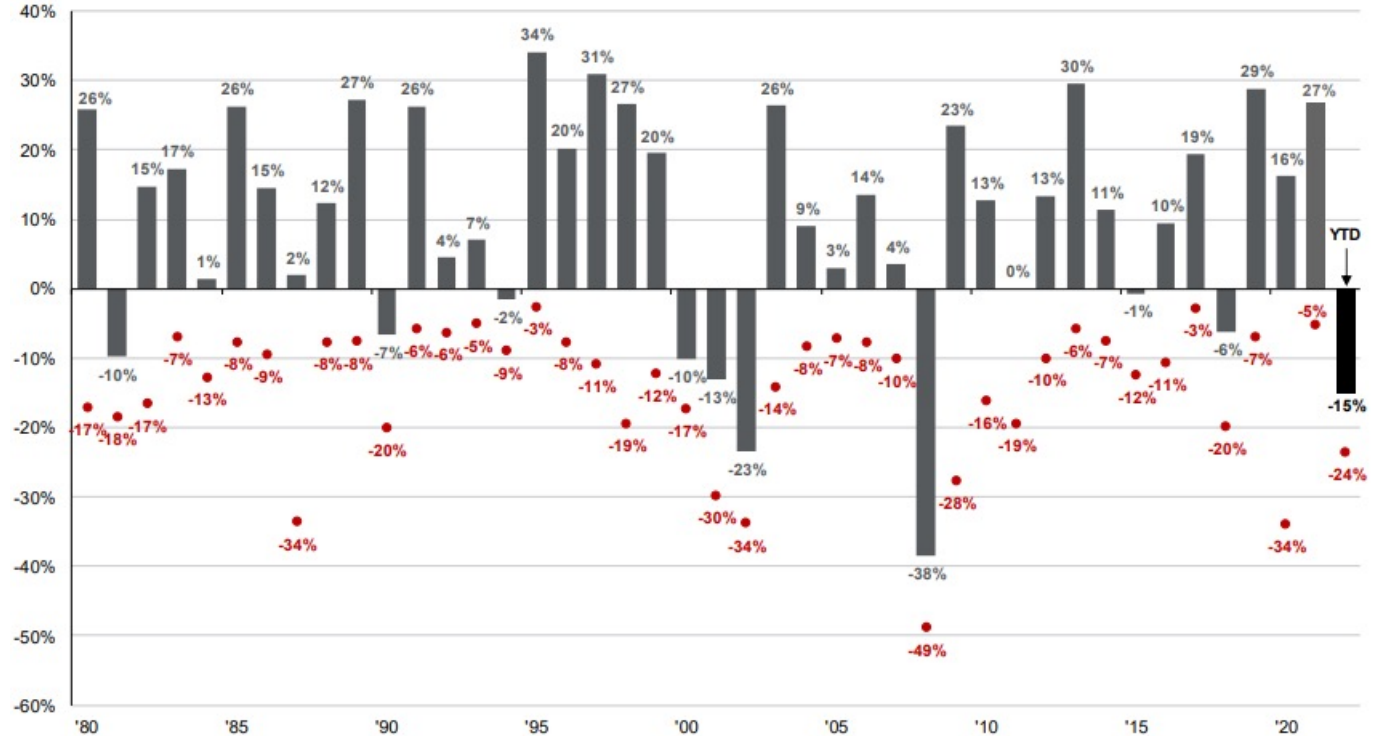
Source: FactSet, NBER, Robert Shiller, Standard & Poor's, J.P. Morgan Asset Management. (Right) The current peak of 4797 was observed on January 3, 2022. The current market level as of July 28, 2022 is 4072. (Left) \*A bear market is defined as a 20% or more decline from the previous market high. The related market return is the peak to trough return over the cycle. Bear and bull returns are price returns. \*\*The bear market beginning in January 2022 is currently ongoing. The "bear return" for this period is from the January 2022 market peak through the current trough. Averages for the bear market return and duration do not include figures from the current cycle. *Guide to the Markets* – U.S. Data are as of July 28, 2022.

# Stock Returns & Drawdowns

## S&P intra-year declines vs. calendar year returns

Despite average intra-year drops of 14.0%, annual returns were positive in 32 of 42 years

The chart shows the calendar year returns of the S&P500 (gray bars) and the intra-year drawdown (red dots), the largest correction from high to low during the year. As you can see, it is common for stocks to have a significant correction during the year, often recovering most or all of the loss by year-end. The S&P500 has lost 15% so far in 2022, after falling as much as 24%.



Source: FactSet, Standard & Poor's, J.P. Morgan Asset Management.

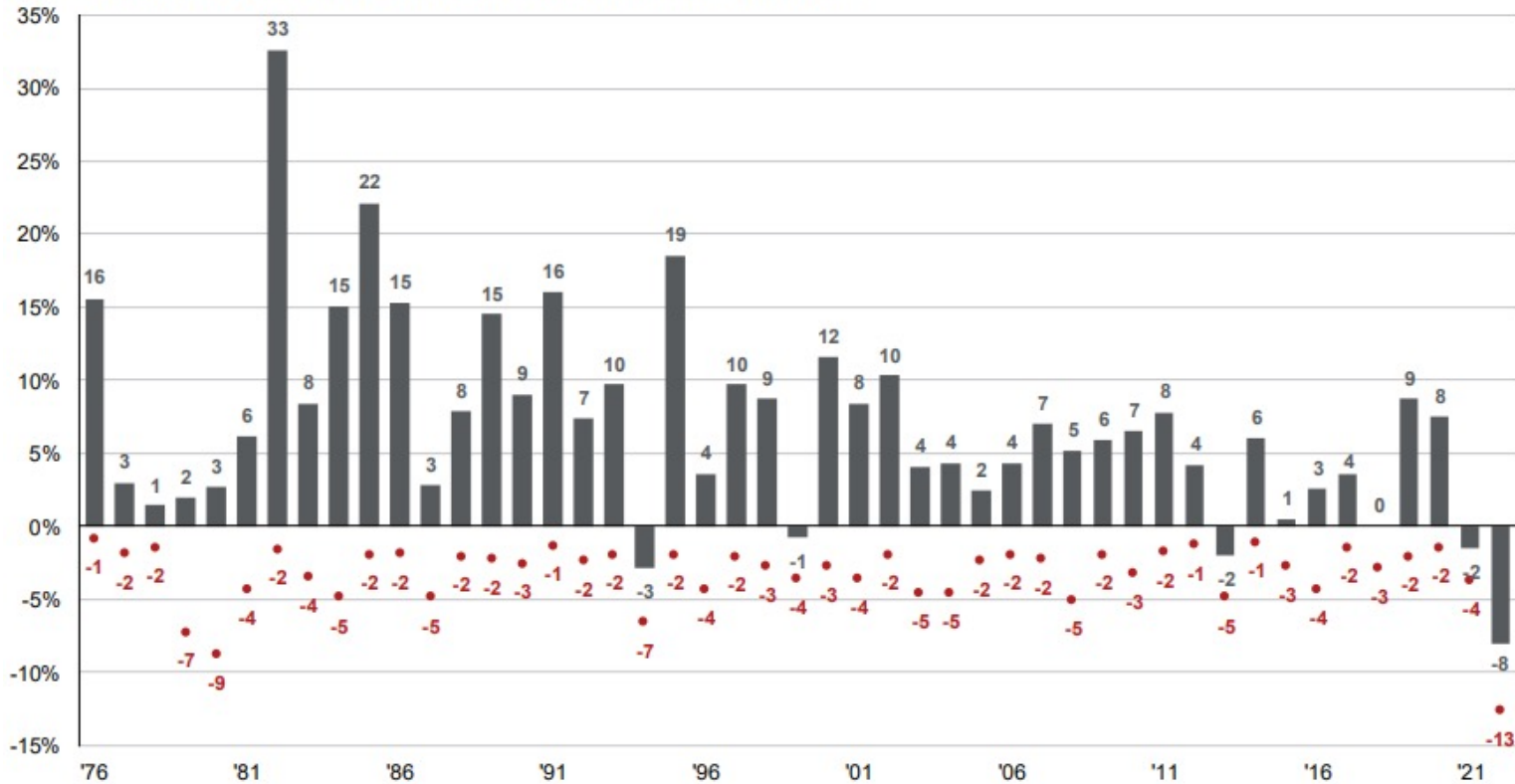
Returns are based on price index only and do not include dividends. Intra-year drops refers to the largest market drops from a peak to a trough during the year. For illustrative purposes only. Returns shown are calendar year returns from 1980 to 2021, over which time period the average annual return was 9.4%.

Guide to the Markets – U.S. Data are as of July 28, 2022.

# Bond Returns & Drawdowns

## Bloomberg U.S. Aggregate intra-year declines vs. calendar year returns

Despite average intra-year drops of 3.1%, annual returns positive in 42 of 46 years



Source: Bloomberg, FactSet, J.P. Morgan Asset Management.

Returns are based on total return. Intra-year drops refers to the largest market drops from a peak to a trough during the year. For illustrative purposes only. Returns shown are calendar year returns from 1976 to 2021, over which time period the average annual return was 7.1%. Returns from 1976 to 1989 are calculated on a monthly basis; daily data are used afterwards.

Guideto the Markets – U.S. Data as of July 28, 2022.

The chart shows calendar year returns and intra-year drawdowns for the Bloomberg US Aggregate Bond Index. As you can see, this year's drawdown of 13% is the worst on record in this data, while the index is now down 8% on the year.



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**E&OE**

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