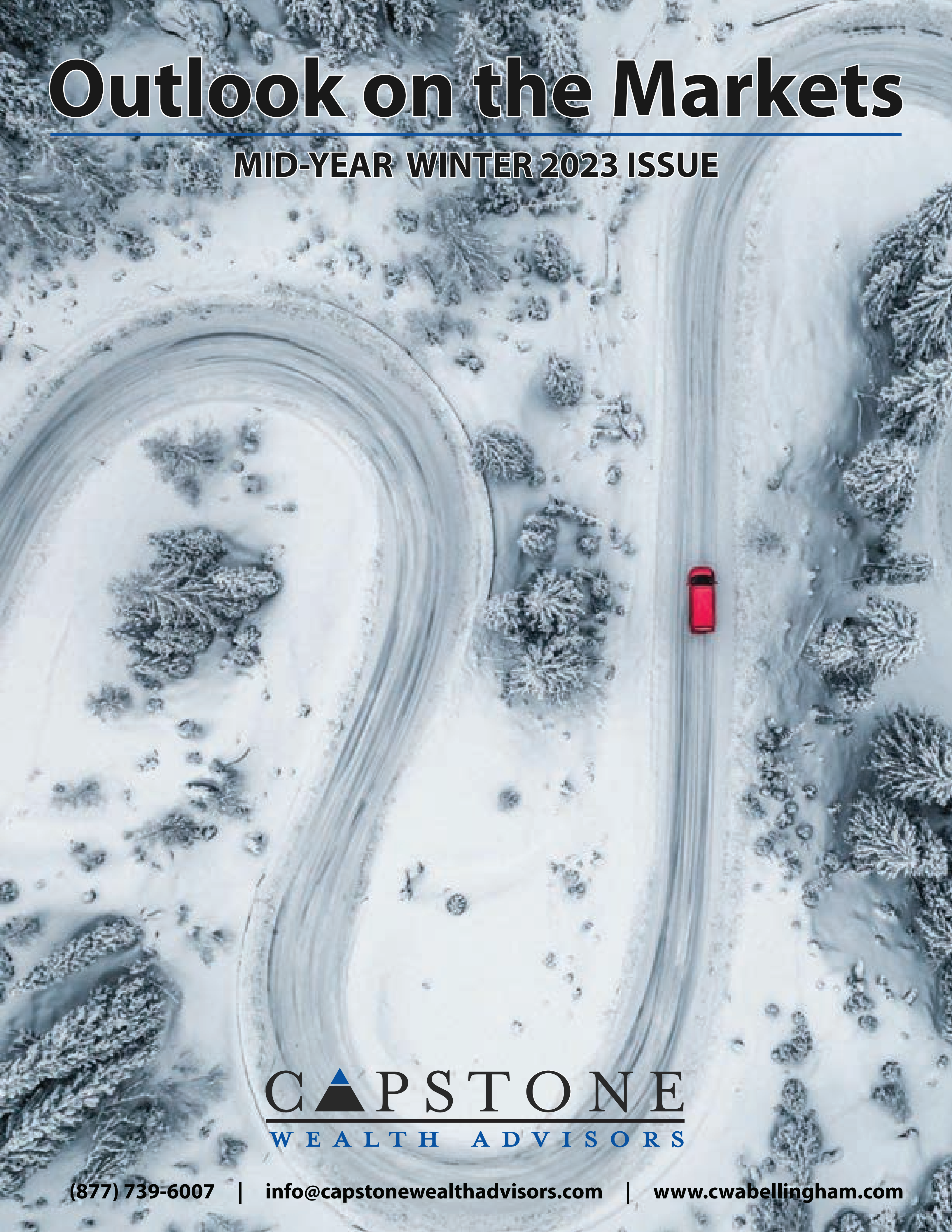

Outlook on the Markets

MID-YEAR WINTER 2023 ISSUE

CAPSTONE
WEALTH ADVISORS

(877) 739-6007 | info@capstonewealthadvisors.com | www.cwabellingham.com

Capstone Wealth Advisors is pleased to release our Mid-Year Outlook on the Markets written entirely by our advisory team. Our outlook is based on our views and philosophies as we see them impacting financial markets, and your money. Current trends, economic indicators and in-depth analysis is at the core of what we do. We monitor and analyze economic trends to help our clients have a clear understanding of the direction the economy is headed and how that impacts your portfolio strategies.

We have six offices throughout the Pacific Northwest, utilizing a team approach to provide continuity for your asset planning needs. Our investment committee meets weekly to discuss current economic events, market trends, asset allocations and more. By using a disciplined and methodical approach to investing, we remove the noise and emotion from your investment portfolio and allow you to focus on the things you love and enjoy most.

"As sure as the spring will follow the winter, prosperity and economic growth will follow recession."

– Sen. Robert Foster Bennett

As US equity markets come off their worst year since 2008, investors may be wondering what lies ahead for 2023. Navigating the economic and stock market landscape can be a daunting challenge, full of unpredictable possibilities and a multitude of influencing factors. To make sense of this ever-changing puzzle, investors must stay informed, remain alert, and be prepared to adjust their strategies accordingly. With the right knowledge and tools, investors can make the most of the opportunities and avoid potential pitfalls.

Inflation, interest rate increases, corporate earnings, and geopolitical events are just a few of the factors shaping the outlook for stocks and bonds this year. And as we embark on 2023, the word "Recession" keeps being thrown around when talking about the US Economy. Recessions usually occur with little to no warning, but this time it's no secret there are increasing challenges facing the economic climate in the US. 2022 was a difficult year for financial markets but it appears that economic conditions in the US may continue to deteriorate, creating uncertainty surrounding what's ahead. Many, if not most economists have already penciled a recession into their forecasts for this year, but views differ on the timing and severity. Some remain hopeful that a "soft landing" is still possible, while others are pointing to the growing amount of economic data suggesting something more significant may be coming. Currently there are several very accurate historical indicators suggesting our economy will likely continue to weaken, leading to further market instability and a reduction in consumer spending. It is our team's opinion that investors should prepare themselves for what could potentially be another challenging investment climate in 2023.

The greatest headwinds for the US economy in 2023 mostly surround stubbornly high inflation levels and the Federal Reserve's response by aggressively raising interest rates. The Federal Reserve has been focused on driving down inflation with a series of interest rate increases, but inflation is still running near a 40-year high, eroding the value of the U.S. dollar and reducing the purchasing power of consumers. Rising prices of basic necessities such as food, housing and transportation have drastically outpaced wage growth, adding to the financial burden facing Americans. This is compounded by the Federal Reserve's decision to rapidly raise interest rates, causing borrowing costs to increase and business investments and consumer spending to slow down. Unemployment rates are beginning to rise, and wages are stagnating – a trend we expect to continue well into 2023.

The weakening housing market is another source of concern. Housing prices and transaction volume is widely expected to decline in 2023 due to mortgage rates sitting at levels not seen in decades. Housing market declines are generally considered a precursor to economic recessions. Rising mortgage costs decrease the affordably of homes for borrowers, causing housing prices to fall. This is already showing up in the real-estate data with the Case/Schiller National Home Price Index which recently posted its largest decline on record.

As the Fed increased interest rates at record speed starting in March of 2022, it brought us a bond market that experienced its worst performance since 1842 – that is not a typo. But now, it is possible that the Fed near the end of its interest rate hiking cycle, which makes Government issued bonds more attractive. Interest rates are currently at levels not seen since 2006, and with the increased likelihood of a recession, interest rates could start to come down at some point later in 2023. The important part for investors to keep in mind is that bond prices move inversely to interest rates - when rates go up, bond prices go down, the opposite is true when rates decrease, bond prices go up.

Facts to Consider

- **The S&P/Case-Shiller Home Price Index**, widely recognized as the gauge for home price movements, reported that national home prices peaked in June 2022 at 308.37 and have declined since. The index is currently sitting at 298.99 in October 2022. The current decline in home prices is the first decline seen since March 2012.

- **The Consumer Confidence Index®** increased in December following back-to-back monthly declines. The Index now stands at 108.3, up sharply from 101.4 in November. The Present Situation Index—based on consumers' assessment of current business and labor market conditions—increased to 147.2 from 138.3 last month. The Expectations Index—based on consumers' short-term outlook for income, business, and labor market conditions—improved to 82.4 from 76.7. However, Expectations are still lingering around 80—a level associated with recession.

- **The Purchasing Managers Index (PMI)®** for the manufacturing sector contracted in November for the first time since May 2020 after 29 consecutive months of growth. The November Manufacturing PMI® registered 49%, 1.2 percentage points lower than the 50.2% recorded in October and the lowest since May 2020, when it registered 43.5 percent. Customer demand is softening, yet suppliers are maintaining high prices and record profits. A PMI reading below 50 indicates economic contraction, which is a leading indicator of economic weakness to come.

- **The National Federation of Independent Business** reported labor quality as their top small business operating problem remains elevated at 21%, according to NFIB's monthly jobs report. Nine percent of owners reported labor cost as their single most important problem, down one point from October. "The small business economy is recovering, but owners continue to face ongoing labor troubles throughout the country," said NFIB Chief Economist Bill Dunkelberg. "Employment plans remain historically strong with 18% of owners planning to hire and create new jobs in the coming months, historically high but the lowest reading since February 2021.

- **The Bureau of Economic Analysis (BEA)** reported personal income increased $80.1 billion (0.4%) in November. Disposable personal income (DPI) increased $68.6 billion (0.4%) and personal consumption expenditures (PCE) increased $19.8 billion (0.1%). The increase in current-dollar personal income in November primarily reflected increases in compensation and personal income receipts on assets. The increase in compensation reflected increases in private wages and salaries in both services-producing industries and goods-producing industries.

- **The Official Unemployment Rate** in the US, known as "U-3", stands at a seasonally adjusted 3.7% in November according to the Bureau of Labor and Statistics. The U-6 unemployment rate, a more comprehesive measure of unemployment, was at 6.7% in November which has been an improvement from the November 2021 rate of 7.7%.

- **Gross Domestic Product (GDP)** increased at an annual rate of 3.2% in the third quarter of 2022, according to the "third" estimate released by the Bureau of Economic Analysis. The increase in exports reflected increases in both goods and services. Within exports of goods, the leading contributors to the increase were industrial supplies and materials (notably nondurable goods), "other" exports of goods, and nonautomotive capital goods. Within exports of services, the increase was led by "other" business services and travel.

- **CBOE Volatility Index (VIX)** has continued to experience moderate volatility year to date. Its highest level over that period was 36.45 on March 7th, 2022. The index sits at 21.71 as of the end of December.

Globally, the world has been plagued with a multitude of geopolitical issues. The ongoing war in Ukraine has had an unmistakable impact on global financial markets, as investors have remained concerned about the impacts the prolonged conflict will have on economic conditions in Europe. The war has caused downward pressure on markets, however, if a resolution is achieved and the war ends, markets could move higher.

While Developed International stocks appear to face the same challenges US stocks face in 2023, this year may also be quietly setting the stage for Emerging Market stocks to outperform those of developed markets. This is largely due to a weakening US dollar and the re-opening of China after its COVID-19 lockdowns. As the US dollar weakens, Emerging Markets will benefit from stronger local currencies and more favorable exchange rates, making it an attractive option for US based investors. Additionally, as China re-opens and its economy starts to recover, Emerging Markets will benefit from increased demand for goods and services, potentially leading to positive returns. While we do believe there is opportunity in this segment of investing, it also carries a heightened risk level due to the potential of geo-political instabilities that can occur with little to no forewarning.

What does all this mean to you and your portfolio?

We believe investors should continue to remain focused on forward-looking economic data for indications as to when our currently choppy economic situation may begin to turnaround. For the time being, we anticipate an environment of market turbulence to continue in 2023 as it did in 2022. For client portfolios, we have proactively raised the levels of cash in client accounts as a means of reducing risk as well as keeping some "dry powder" ready to deploy once stock prices have fallen to levels where renewed optimism is warranted. For the equity portion of your portfolio, we believe that maintaining a focus on high quality, dividend paying US companies, will provide investors some reprieve from additional market turbulence. And for the forementioned reasons above, we are beginning to add exposure to areas like Emerging Markets and Government Bonds. Economic conditions are rapidly changing, and the possibility of a continued downturn is real but during these challenging times, investors should remind themselves that every recession, bear market, and economic downturn in history has always ended and was subsequently followed by a long-term sustained bull market, lasting far longer than the downturn. We believe this situation will ultimately show that it is no different.

To our valued clients, your investment portfolios already reflect our investment philosophy. As market conditions change, we will continue to proactively implement portfolio adjustments as part of our investment process. For those of you who are not currently a client and would like to learn how we can help assist you in your retirement planning and investment management during these challenging times, we invite you to schedule a complimentary consultation with our team. We can discuss our current economic outlook in greater detail and specifically how it might affect your existing portfolio. If you would like to schedule, please call our office directly at (877) 739-6007 or email us at info@capstonewealthadvisors.com.

Schedule Your Consultation Today!

References:
- S&P/Case-Shiller Home Price Index https://fred.stlouisfed.org/series/CSUSHPINSA
- The Consumer Confidence Index https://www.conference-board.org/data/consumerconfidence.cfm
- The Purchasing Managers Index https://www.ismworld.org/supply-management-news-and-reports/reports/
- ism-report-on-business/
- The National Federation of Independent Business https://www.nfib.com/foundations/research-center/month
- ly-reports/jobs-report/
- The Bureau of Economic Analysis http://www.bea.gov/newsreleases/national/pi/pinewsrelease.htm
- The Bureau of Labor and Statistics https://www.bls.gov/news.release/empsit.t15.htm
- Gross Domestic Product http://www.bea.gov/
- CBOE Volatility Index http://finance.yahoo.com/echarts?s=%5EVIX+Interactive#symbol=%5EVIX;range=6m

CAPSTONE
WEALTH ADVISORS

(877) 739-6007 | info@capstonewealthadvisors.com | www.cwabellingham.com