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SUMMARY

- Tough quarter once again for stocks and bonds
- Tactical outlook remains challenging
- Valuation reset gives us hope for the future

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Q3 2022 Recap: A Broken Record Stuck on a Terrible Song

CHALLENGING NEAR-TERM OUTLOOK AND A CASE FOR LONGER-TERM OPTIMISM

Quarterly Recap: Inflation Remains the #1 Issue; Rates Are Higher, But Earnings Hang On

While it may seem like a faint memory, Q3 2022 began on a somewhat optimistic note. Inflation – especially gasoline prices – appeared to have peaked and there was a hope that inflation would moderate quickly, appeasing the Fed and avoiding a recession. Q2 earnings were lower than the previous year but still strong – making the case for a soft landing and providing hope the market might look through the economic slowdown. This prevailing view from July through mid-August created a short-lived bear market rally for equity and credit markets.

Then came Fed chair Jerome Powell's speech at the annual Jackson Hole conference. He used it to place a clear emphasis on reducing inflation to 2%, even at the cost of a recession. The clarity of this message brought this calm to a halt. Shortly thereafter, the August Consumer Price Index (CPI) report was more elevated than expected. The realization that inflation is still in the windshield and not the rear-view mirror, so to speak, coupled with Powell's crystal-clear determination, effectively ended what has been known for years as the "Fed Put". The Fed Put is a widely held belief that the Fed will step in to buoy the markets with monetary accommodation. The equity market's response was a complete reversal, a lower low for the year and levels not seen since 2020. For both stock and bond investors, Q3 probably felt like a broken record stuck on a terrible song.

Bond investors faced similar challenges in the quarter. Interest rates across the yield curve have risen both directly as the Fed raised the Fed Funds rate, and indirectly through the Fed's strong rhetoric against inflation. The rate increases sent shock waves through the bond and equity markets at the same time, roiling balanced investors, who are used to some measure of downside protection from their bond portfolio in down markets. The ten-year Treasury bond yield briefly went over 4% in overnight trading before closing the quarter at 3.83%. The effects of the dramatic increase in rates will affect housing, the consumer, and the US economy broadly in Q4 and beyond.

Not only are US interest rates rising domestically, but also relative to the rest of the world. This resulted in a strengthening dollar in our view, which jolted non-US markets as many foreign currencies hit multi-decade lows vs. the dollar. Europe faces additional challenges with the annexation of Ukrainian territory by Russia and the stoppage of the Nord Stream Pipeline – the primary supply of natural gas from Russia to Europe. This will prove a challenge to their fight against inflation in the 4th quarter.

Returns Recap: Nowhere to Hide in Q3, Just Like Q2

From a returns perspective, the Q3 seemed to largely be a continuation of challenges of the previous three quarters. Two of the assets most commonly used to hedge equities – bonds and gold – both performed poorly as rising rates have harmed bonds at the same time as stocks in our view. The shifting perception of the Fed as an inflation fighter and the lack of any yield has also weighed on gold. While cash appears to be a haven, that is somewhat illusory against increasing inflation. In the long run, the loss of purchasing power is an important risk to guard against, since lost purchasing power can often be permanent, while stock market losses are often temporary.

Returns Of Major Asset Classes

Market	Q3 2022	Q2 2022	YOY
CASH (Bloomberg US Treasury Bill 1-3 M TR USD)	0.4%	0.1%	0.5%
HIGH YIELD (ICE BofA US High Yield TR USD)	-0.7%	-10.0%	-14.1%
US SMID CAP (S&P 1000 TR)	-3.3%	-15.0%	-16.4%
US LARGE-CAP (S&P 500 TR)	-4.9%	-16.1%	-15.5%
DEVELOPED INT'L EQUITIES (MSCI Eafe Total Return Net)	-3.5%	-7.6%	-10.7%
TREASURY BONDS (Bloomberg US Treasury TR USD-1987)	-4.3%	-3.8%	-12.9%
FIXED INCOME INV GRADE (Bloomberg US Agg Bond TR USD)	-4.8%	-4.7%	-14.6%
GOLD	-8.2%	-6.7%	-5.8%
EMERGING MARKET EQUITIES (MSCI Emerging Markets Total Return Net)	-8.2%	-8.1%	-21.5%

Source: Bloomberg.. Data as of 09.30.2022. Chart shown for illustrative purposes only. Past performance is no guarantee of future results. Not indicative of RiverFront portfolio performance.

Most International Markets Performed Similarly to US, Dollar Strength Was Real Pain Point

The table below shows that local markets in developed markets have largely moved consistently with US Markets, and that the underperformance of international markets has largely come from the currency – China is a notable exception, as they face issues with rapidly slowing growth and continued COVID-19-related lockdowns, which has dragged down overall Emerging Market returns.

	In USD		In Local		Currency Impact	
MSCI Total Return Net	**Q3 2022**	**Year Over Year**	**Q3 2022**	**Year Over Year**	**Q3 2022**	**Year Over Year**
China	-22.5%	-35.4%	-21.7%	-33.9%	-0.8%	-1.5%
United Kingdom	-10.8%	-14.1%	-2.9%	3.8%	-7.8%	-17.9%
Emerging Markets	-11.6%	-28.1%	-8.2%	-21.5%	-3.4%	-6.6%
Europe	-10.1%	-24.8%	-4.1%	-11.8%	-6.0%	-13.0%
EAFE	-9.3%	-24.7%	-3.5%	-10.7%	-5.8%	-14.1%
Canada	-7.9%	-13.1%	-1.9%	-5.7%	-6.0%	-7.4%
Japan	-7.7%	-29.3%	-1.6%	-8.3%	-6.0%	-21.0%
United States	**-4.9%**	**-15.5%**	**-4.9%**	**-15.5%**	**0.0%**	**0.0%**

Source: Bloomberg, RiverFront. Chart shown for illustrative purposes only. Data as of 09.30.22. Past performance is no guarantee of future results. Not indicative of RiverFront portfolio performance.

Outlook: Q4 is Looking Challenging, But There is a Case for Longer-Term Optimism

Given the short-term uncertainties discussed in this piece, we are cautious on equities across all balanced portfolios versus our benchmarks. Indeed, last week we reduced equity weightings. As a result, in our shorter-horizon portfolios, we are close to our COVID-19-level lows in equities, and our fixed income strategy still favors corporate bonds with shorter maturities.

Our longer-horizon portfolios are also below the equity weighting in their benchmarks, but less so. In these portfolios, we have sought out high yield bonds and other alternative yield-oriented securities in an effort to increase expected yields across the portfolio, as well as favoring energy-related and technology companies versus cyclical consumer themes. The reason we are not at historically high levels of cash is that stocks and bonds have already fallen significantly, making them both attractive to us on a longer-term basis. Given this, there is a case for longer-term optimism even as the shorter-term tactical outlook remains fraught with uncertainty.

Risk Discussion: All investments in securities, including the strategies discussed above, include a risk of loss of principal (invested amount) and any profits that have not been realized. Markets fluctuate substantially over time, and have experienced increased volatility in recent years due to global and domestic economic events. Performance of any investment is not guaranteed. In a rising interest rate environment, the value of fixed-income securities generally declines. Diversification does not guarantee a profit or protect against a loss. Investments in international and emerging markets securities include exposure to risks such as currency fluctuations, foreign taxes and regulations, and the potential for illiquid markets and political instability. Please see the end of this publication for more disclosures.

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Index Definitions

Standard & Poor's (S&P) 500 Index TR USD (US Large Cap) measures the performance of 500 large cap stocks, which together represent about 80% of the total US equities market.

S&P 1000 Index TR USD (US SMID Cap) is a combination of the S&P Mid Cap 400 Index TR USD & S&P Small Cap 600 Index TR USD.

MSCI EAFE Index NR USD (Developed International Equities) is designed to represent the performance of large and mid -cap securities across approximately 21 developed markets, including countries in Europe, Australasia and the Far East, excluding the US and Canada. Net total return indices reinvest dividends after the deduction of withholding taxes, using (for international indices) a tax rate applicable to nonresident institutional investors who do not benefit from double-taxation treaties.

MSCI Emerging Markets Index NR USD (Emerging Market Equities) is an equity index that captures large and mid cap representation across approximately 25 emerging markets (EM) countries.

MSCI Europe Index represents the performance of large and mid-cap equities across approximately 15 developed countries in Europe.

MSCI Japan Index designed to measure the performance of the large and mid cap segments of the Japanese market.

MSCI China Index captures large and mid cap representation across China A shares, H shares, B shares, Red chips, P chips and foreign listings (e.g. ADRs).

MSCI United Kingdom Index (USD) is designed to measure the performance of the large and mid cap segments of the UK market.

The MSCI Canada Index is designed to measure the performance of the large and mid cap segments of the Canada market.

Precious Metals Buying gold, silver, platinum or palladium allows for a source of diversification for those sophisticated persons who wish to add precious metals to their portfolios and who are prepared to assume the risks inherent in the bullion market. Any bullion or coin purchase represents a transaction in a non-income-producing commodity and is highly speculative. Therefore, precious metals should not represent a significant portion of an individual's portfolio.

Bloomberg Capital US Treasury Index TR USD (Treasury Bonds) measures the performance of the US Treasury bond market.

Bloomberg US Aggregate Bond Index TR USD (Fixed Income Investment Grade) is an unmanaged index that covers the investment grade fixed rate bond market with index components for government and corporate securities, mortgage pass-through securities and asset-backed securities. The issues must be rated investment grade, be publicly traded and meet certain maturity and issue size requirements.

ICE BofA High Yield Index TR USD (High Yield) tracks the performance of US dollar denominated below investment grade rated corporate debt publicly issued in the US domestic market. Index constituents are capitalization-weighted based on their current amount outstanding times the market price plus accrued interest.

Bloomberg Capital 1-3 Month US Treasury Bill Index TR USD (Cash) includes all publicly issued zero-coupon US Treasury Bills with a remaining maturity between one and three months, are rated investment-grade and have an outstanding face value of $250 million or more.

The Consumer Price Index (CPI) is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services.

The yield curve is a line that plots yields (interest rates) of bonds having equal credit quality but differing maturity dates. The slope of the yield curve gives an idea of future interest rate changes and economic activity.

In a rising interest rate environment, the value of fixed-income securities generally declines.

Stocks represent partial ownership of a corporation. If the corporation does well, its value increases, and investors share in the appreciation. However, if it goes bankrupt, or performs poorly, investors can lose their entire initial investment (i.e., the stock price can go to zero).

Bonds represent a loan made by an investor to a corporation or government. As such, the investor gets a guaranteed interest rate for a specific period of time and expects to get their original investment back at the end of that time period, along with the interest earned. Investment risk is repayment of the principal (amount invested). In the event of a bankruptcy or other corporate disruption, bonds are senior to stocks. Investors should be aware of these differences prior to investing.

High-yield securities (including junk bonds) are subject to greater risk of loss of principal and interest, including default risk, than higher-rated securities.

Investing in foreign companies poses additional risks since political and economic events unique to a country or region may affect those markets and their issuers. In addition to such general international risks, the portfolio may also be exposed to currency fluctuation risks and emerging markets risks as described further below.

Changes in the value of foreign currencies compared to the U.S. dollar may affect (positively or negatively) the value of the portfolio's investments. Such currency movements may occur separately from, and/or in response to, events that do not otherwise affect the value of the security in the issuer's home country. Also, the value of the portfolio may be influenced by currency exchange control regulations. The currencies of emerging market countries may experience significant declines against the U.S. dollar, and devaluation may occur subsequent to investments in these currencies by the portfolio.

Foreign investments, especially investments in emerging markets, can be riskier and more volatile than investments in the U.S. and are considered speculative and subject to heightened risks in addition to the general risks of investing in non-U.S. securities. Also, inflation and rapid fluctuations in inflation rates have had, and may continue to have, negative effects on the economies and securities markets of certain emerging market countries.

Technology and internet-related stocks, especially of smaller, less-seasoned companies, tend to be more volatile than the overall market.

Small-, mid- and micro-cap companies may be hindered as a result of limited resources or less diverse products or services and have therefore historically been more volatile than the stocks of larger, more established companies.

Buying commodities allows for a source of diversification for those sophisticated persons who wish to add this asset class to their portfolios and who are prepared to assume the risks inherent in the commodities market. Any commodity purchase represents a transaction in a non-income-producing asset and is highly speculative. Therefore, commodities should not represent a significant portion of an individual's portfolio.

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