

Delta Investment Management is a registered investment advisory firm. Delta welcomes discussions with individuals seeking investment advice and advisors seeking a new turnkey asset management solution.

Delta manages portfolios at TD Ameritrade and Schwab.

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October 7, 2022

2022: Year of the Interest Rate Bear

At the beginning of 2022, investors expected the Federal Reserve to raise the Fed Funds rate roughly 2-4 times with a single rate hike equating to 0.25%. Using 0.25% as our definition of a rate hike, the Fed has raised the Fed Funds rate 12 times this year. The Fed says there is more to come.

The cause for this historically rapid pace of rate hikes has been higher and more persistent inflation than expected. The single largest driver of inflation has been a 42% increase in the money supply in response to the Covid pandemic. Inflation caused by this huge increase in the money supply has been exacerbated by supply chain constraints, higher labor costs, expansionary federal government spending, the Russian invasion of Ukraine (biggest impacts on food/fertilizer and energy costs), China lockdowns and a reluctance of oil producers to invest in supply when the U.S. is rapidly transitioning away from carbon-based fuels.

The 10-year treasury rate has risen from 1.5% to as high as 4%. The chart below shows the rise in the 10-year treasury rate and the devastating impact on the S&P 500 P/E multiple. Even with earnings rising by 5.1% year-to-date, the price return of the S&P 500 (without dividends) is down nearly 25% on -29.9% multiple compression.

Interest Rates and P/E Multiple Compression



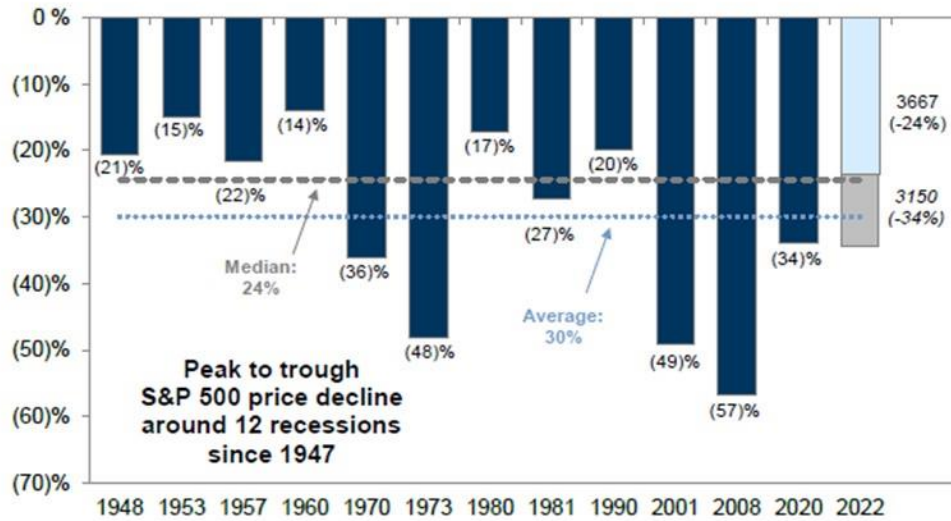
The real bear market this year has been in bonds more so than stocks. The total return for the Bloomberg U.S. Aggregate Bond Index reached a low of -15.2% in September. The second worst year on record dating back to 1976 was 1994 with a loss of -2.9%. The loss this year in bonds has no historic precedent in modern times.

On Monday and Tuesday of this week, there was a sharp rebound in equities. The 10-year treasury rate dropped to 3.56% briefly on a market perception that the Fed may stop its rate hike program sooner than expected. This is the same sentiment that helped drive a 19% bounce off the June stock market lows.

At some point (many expect in early 2023), the Fed will stop raising rates. The 1-year inflation expectation is 4.6%. The current S&P 500 P/E is about 15x. When we add the P/E to the expected inflation rate of 4.6%, the sum is roughly 20. There is a rule of thumb that has worked for years in the market called the "Rule of 20." When inflation and P/E are added, the market is fairly valued at 20.

Below is a history of peak to trough market declines since 1948. The decline we have experienced year-to-date is equal to the median decline. If the pace of rate hikes abates, it is possible we have seen the worst of this interest rate bear market.

S&P 500 Peak to Trough Declines in Recession Since 1947



Source: Goldman Sachs Global Investment Research

Let Us Help You Position Your Portfolio – Give Us a Call Today

We have unique and sophisticated investment methods that seek to capture the stock market's gains while minimizing drawdowns in bear markets. If you would like to learn more about how we manage money, we invite you to give us a call at **(415) 249-6337**, visit www.deltaim.com or email us at info@deltaim.com.



Delta Stock Market Dashboard

MARKET SENTIMENT IS

BEARISH

THIS WEEK'S NUMBER IS

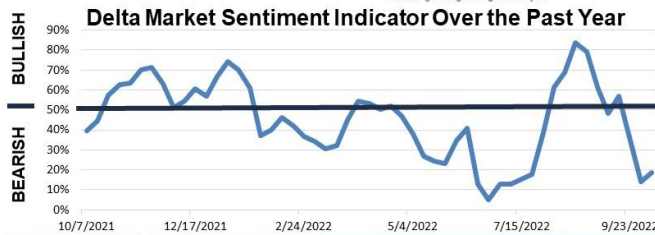
18.5

Our technical indicator increased from 14.3 to 18.5 this week

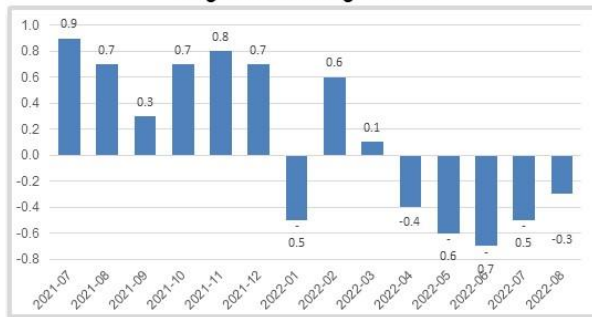
INDICATOR STATISTICS

Consecutive Bearish Weeks:	3
Cycle Inception Date:	9/23/2022
Range:	14.3 - 34.80
Mean:	22.5
Bullish Weeks YTD:	15
Bearish Weeks YTD:	26
*S&P 500	-0.2%
*DJIA	-0.4%
*NASDAQ	0.1%

* Percentage change during current cycle

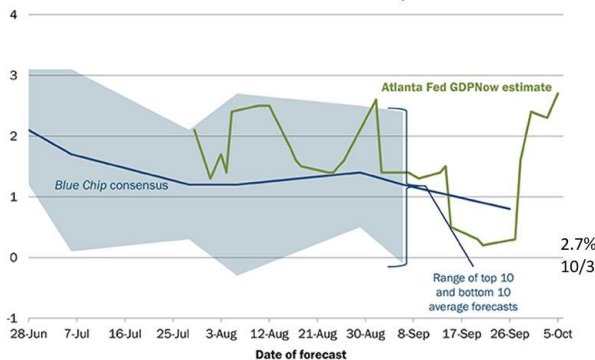


Leading Economic Index % Change Monthly August 2021 – August 2022



Source: The Conference Board – last update 9/22/2022

Atlanta Fed GDPNow Forecast Real GDP Estimate for Q3 2022



Sources: Blue Chip Economic Indicators and Blue Chip Financial Forecasts

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