Third Quarter 2022

GALECKI FINANCIAL MANAGEMENT — FINANCIAL SENSE

	LAST MONTH	LAST 3 MONTHS	YTD
S & P 500 Index	-8.25%	-16.10%	-19.96%
Russell Midcap Index	-9.98%	-16.85%	-21.57%
Russell 2000 Index	-8.22%	-17.20%	-23.43%
Dow Jones Industrial Average	-6.56%	-10.78%	-14.44%
Morgan Stanley EAFE Index	-9.28%	-14.51%	-19.57%
DJ US Real Estate Index	-6.87%	-14.46%	-20.02%
S&P Commodity Index	-7.64%	2.01%	35.80%
Barclays Aggregate Bond Index	-1.57%	-4.69%	-10.35%

INDEX RETURNS

Stocks continued to slide in the second quarter after a rough start to the year. The S&P 500 dropped 16.10% in the quarter and officially entered Bear Market territory with a decline of more than 20%. The Russell Mid-cap index was down 16.85% and small-cap stocks were down 17.20%. Both Mid-Cap and Small-Cap growth stocks outperformed their value counterparts during June but still trailed for the quarter and the entire year.

International stocks also struggled as the MSCI EAFE Index declined 14.51%. Australia and Germany were down around 18%. Emerging Markets held up relatively well with a quarterly decline of 11.45%. China led the way with a gain of 3.5% while India was only down 13.52%.

Bond markets have seen rates move higher this year as the Fed has been raising rates. The Barclays Aggregate Bond index correspondingly dropped 4.69% in the first quarter and is now down 10.35% on the year. Global bonds were hit even harder with a decline of 12.09% in Q2 and are now down 20.82% on the year.

ECONOMIC REVIEW AND OUTLOOK

A recession is defined as a business cycle contraction when there is a general decline in economic activity. The National Bureau of Economic Research (NBER) is the entity tasked with defining when a recession officially began and when it ended. A recession timeframe is typically identified 1-2 years after it ends. The media often defines a recession as two consecutive quarters of negative GDP growth. However, that is not the official definition. It is important to note that Q1 GDP was -1.4% and Q2 GDP is expected to be in the -1% to 1% range. If it does come in negative, look for a lot of headlines about the economy being in a recession already.

Going back to 1941, recessions last an average of 14 months while economic expansions last roughly four years. It is also important to remember that the market is a leading economic indicator. It tries to look ahead to what the economy will be doing 6-9 months from now. If we are indeed in a recession today, and the recession lasts a year, then the market could start to move higher in anticipation of better economic growth in 2023.

We have seen a shift of consumer spending from goods to services. Restaurant traffic is now down only 1% from pre-pandemic levels. Hotel occupancy is down 4% and TSA Traffic is down about 5%. We continue to see these areas of the economy trending positively while spending on things like exercise equipment, TVs, etc. have slowed.

The Leading Economic Index declined 0.4 percent in May to 118.3 following a 0.4 percent decline in April. Industrial Production increased 0.2% in May and has increased every month this year. The Capacity Utilization rate (which measures how much slack is in the economy) was up 0.5 percentage points to 79.0.

Non-farm payrolls rose by 372,000 in June and the unemployment rate remained at 3.6 percent. Weekly unemployment claims were 235,000 for the week ending July 2, 2022. There are currently 1.9 jobs available for each job seeker. The labor market is still very robust. The demand for labor should prove helpful if the economy is in recession territory.

Manufacturing decreased to 53% on the ISM PMI index in June. This was a drop of 3.1% from May. The New Orders Index came in at 49.2% which is now in contraction territory. The ISM Services index was at 55.3% in June. This marks the 25th straight month of growth for the services sector. The Business Activity Index came in at 56.1% and New Orders were at 55.6%. This further shows what we stated previously regarding a change in consumption from manufacturing to services.

Global economies are still growing…barely. The JPM Global Manufacturing PMI was at 51.4 in June which was down from 51.5 in May. The European zone was at 51.9.

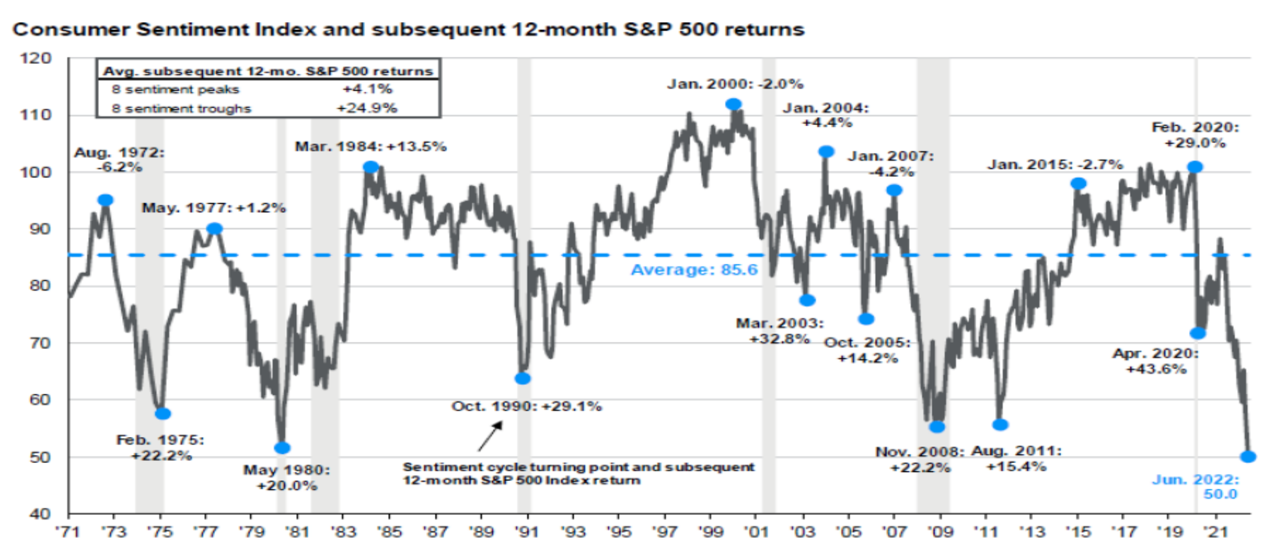
EQUITY AND BOND MARKETS

Equity markets experienced a brutal second quarter with the S&P 500 declining 16% and is now in Bear Market territory on the year. The NASDAQ 100 and the Russell 2000 are both down roughly 30%. In fact, the average stock in each of those indexes is down roughly 50% from the 52-week high.

Major indexes and maximum drawdowns

	Year-to-date				Past 52 weeks		
Index	YTD return	Index maximum drawdown from YTD high	Average member maximum drawdown from YTD high	Index return from YTD low	Index maximum drawdown from 52w high	Average member maximum drawdown from 52w high	Index return from 52w low
S&P 500	-23%	-24%	-28%	N/A	-24%	-31%	N/A
NASDAQ	-32%	-33%	-42%	3%	-34%	-51%	3%
Russell 2000	-27%	-27%	-42%	1%	-32%	-50%	1%

Source: Charles Schwab, Bloomberg, as of 6/16/2022. Indexes are unmanaged, do not incur management fees, costs and expenses and cannot be invested in directly. Past performance is no guarantee of future results. Some members excluded from year-to-date return columns given additions to indices were after January 2022.



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

Consumer Sentiment came in at 50 at the end of June. Going back to 1971, subsequent returns for the S&P 500 off sentiment troughs have been more than 24% over the next twelve months. These troughs also tended to occur during recessions. We won't know for a while if this is indeed a trough, but the contrarian nature of this indicator could provide some reassurance that the market may have more upside potential over the next year than downside risk. In addition, the Ned Davis Research Investor Sentiment indicator is in the Extreme Pessimism zone, which has also been a good contrarian indicator.

The forward P/E ratio for the S&P 500 has dropped down to 15.9 times earnings, which is now below the 25-year average. Stocks have gone from expensive in December of last year, to relatively inexpensive today. In fact, if the S&P 500 returns to it's January peak in two years, it would equate to a 14.3% annualized return. If it takes three years, it would be a 10% annualized return.

What could turn the tide for the market? If Russia and Ukraine have a cease-fire, global equity markets would experience a rally. When inflation data begins to slow, and the Federal Reserve slows tightening, global equity markets will benefit. Since the market is a leading indicator, waiting for the economic data to turn higher would be too late for investors. On the bond side of the market, it might be time to extend out to some intermediate bonds in case the Fed does slow down their tightening Monetary policy.

PORTFOLIO MANAGEMENT

The Investment Committee continues to monitor the performance of our portfolios and the underlying funds and ETFs. So far this year, performance has been holding up relatively well. Our passive ETFs are getting us index returns at a low cost and the active funds are performing well versus their corresponding benchmarks. We continue to look at ways to reduce costs and maximize performance.

International markets are outperforming U.S. markets for the first time in 14 years. The surge in the U.S. Dollar has weaken that performance, but we believe that international markets could continue to outperform domestic markets over the next ten years.

Timing the market is nearly impossible. You can't be right once; you need to be right twice. Since nobody can do this consistently, we must rely on "Time in the market" and not "Timing the market". Over the last 20 years, the S&P 500 has averaged 9.5% per year. However, if you missed the best 30 days out of those 20 years, then the annualized return dropped to less than 1%. We must keep a long-term focus and ignore the short-term volatility.

The 10-year Treasury yield is around 3%. Inflation is running around 8%. Investing only in fixed income will give you a guaranteed real rate of return loss of around 5% per year. This is not a good investment strategy. We must own equities in our portfolio to stay ahead of inflation. International valuations are cheap, domestic valuations are significantly cheaper today than in December. Investor Sentiment is in extreme pessimism territory. The market is pricing in a recession and more rate hikes. Any good news at all could be the catalyst for the next bull market.

FINANCIAL PLANNING

Estate Planning is an area of Financial Planning that can occasionally be overlooked. Estate documents are drafted and forgotten about for many years. We review estate documents every few years for our clients as way to keep those documents top of mind. Situations change over the years and a brief review can bring to light areas of the plan that need to be adjusted by an attorney.

Below is a brief overview of the basic types of estate planning documents and their function:

Last Will:

This is a public document that is presented to the county Judge whereby your appointed Executor (Personal

Representative) of your Estate is approved and Guardianship of any minor children is granted. The Executor works in conjunction with the Court to handle tangible property distributions, bequests, gifts, payment of debts, and the distribution of all residual estate assets in accordance with the terms your Will.

Revocable Trust:

This is a private document that details exactly how you'd like certain assets handled during life and distributed at death. All terms of the trust are shielded from public records. This is shell document that is used to protect assets from the probate process.

Power of Attorney

This document appoints an Attorney-in-Fact. This is the individual who conducts financial affairs while you are still alive but unable to do so yourself.

Health Care Representative / Health Care Power of Attorney

This document appoints a Health Care Representative. The representative makes health care decisions on your behalf if you are incapacitated. This power includes decisions on artificially supplied nutrition and hydration (life support). We recommend having these end-of-life conversations, explaining your wishes, with the representative you choose.

Living Will

This is a non-legally binding document that indicates in writing your desires surrounding artificially supplied nutrition and hydration. The actual decision on your care is still made by your Health Care Representative.

COMPANY NEWS

In April, Senior Staff Financial Planner, Nicole Thieme, welcomed her son Jayton into the world! We love watching our Galecki family continue to grow. Congratulations to Nicole and her family on their newest addition.

Please be sure to "Like" us on [Facebook]() and follow us on [Linkedin]() for more insights into our firm, our team, and our thoughts on the economy and markets.

- Galecki Financial Management Investment Committee

If you would like to schedule an appointment with a Certified Financial Planner™ Professional, please visit www.galecki.com