ROCKBRIDGE INVESTMENT MANAGEMENT

FINANCIAL COMMON SENSE April 2022

The Fed Has Been Busy *by the Rockbridge Team*

The Federal Reserve has significantly altered their guidance in the last few months. The biggest change is the increase in the expected number of rate hikes this year. In December, the Fed was expecting three rate hikes in 2022. Three weeks ago, they increased that forecast to 7, and the market is now expecting 8. In 2022, that means short-term interest rates could increase from 0.12% to 2.12%.

The Federal Reserve has a “dual mandate.” The two things they are focused on are keeping the population at full employment and keeping inflation in check. Economists generally view full employment as an unemployment rate of 5% or lower and the Fed targets long-term inflation as 2%.

The rate hikes are expected to be modestly harmful to asset prices and represent action meant to cool an economy that is overheating. There is good reason for this; in March, the unemployment rate dropped to 3.6%. At the same time, the Federal Reserve is expecting inflation of 4.3% for 2022.

What does that mean for us?

Higher Short-Term Interest Rates: Remember a few years ago (2018) when you could actually get some return from a high-yield savings account or a 1-year CD? That’s expected to come back. A year from now we should see yields north of 2%. If the Fed’s longer-term expectations are realized, by the end of 2023 these numbers will be around 2.75%.

Higher Mortgage Rates: Much of this change has already happened. Six months ago, the average 30-year mortgage rate in the US was 3.0%; it now sits at 4.7%. We expect this to either reduce the rate at which home prices are increasing or cause a decrease in prices. This 1.7% increase means the annual mortgage cost of a $400,000 loan is now $4,700 higher.

Lower Realized Returns, but High Expected Returns: So far this year, we’ve seen stocks and bonds both decrease in value. The aggregate bond market is down 6.0%, and both US and International Stocks are down 5%. That’s the bad news, the good news is that expected returns are now higher! Over the last three months, the yield on bonds has gone from 1.5% to 2.5% - that’s a big deal! The math behind stocks isn’t as clean, but some of the price movement this year has come from higher discount rates which is another word for expected returns. Over the last quarter, our internal model has increased long-term expected equity returns by 0.50%. ◆

THE ROCKBRIDGE TEAM:

Craig Buckhout, CFA, CPWA
Anthony Farella, CFP®
Patrick Rohe, CFP®
Edward Barno, CPWA
David Carroll, CFP®
Ethan Gilbert, CFA, CFP®
Nicholas Stancato, CFP®
Kevin Sullivan, CFP®
Claire Kobylanski
Mike Antonacci, J.D., CFA
Zach DeBottis, CFP®
Robert Ryan, Ph.D.
Edward Petronio, Ph.D.
Patricia Edward
Julie Murfitt
Julia Conlan
Adam Underwood
Adam Gagas
Sharon Craig
Jodi DeAugustine

Our vision at Rockbridge is to provide our clients with unrivaled financial advice; building lifelong relationships and empowering them to fully enjoy their lives.

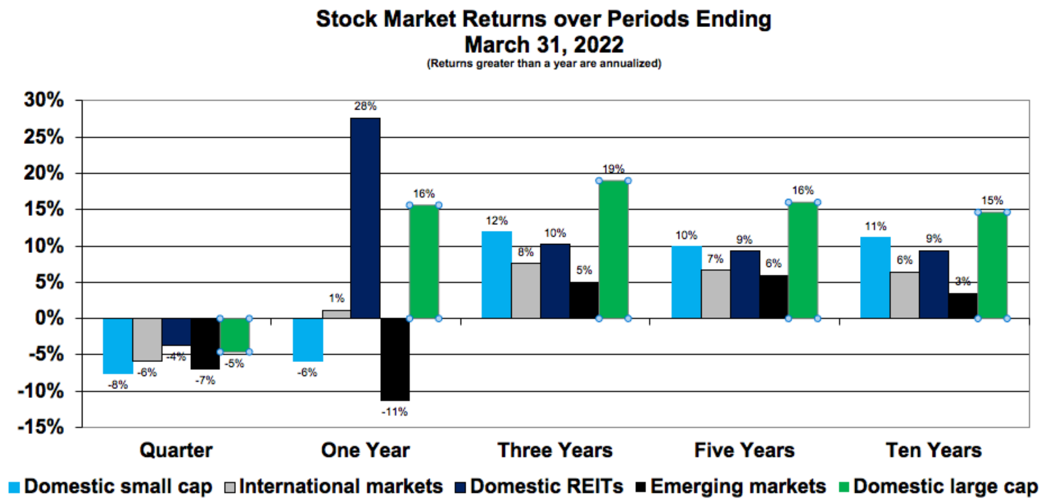
We believe the success we share with our clients is driven by a relentless focus on our culture and core values: Honesty, Curiosity, Discipline and Excellence.

Rockbridge Investment Management, LLC
220 South Warren Street, 9th Floor, Syracuse, NY 13202
Phone: 315-671-0588
www.rockbridgeinvest.com

Market Commentary *by Bob Ryan*

Stock Markets

Not surprisingly, stock markets were volatile this quarter. Faced with a myriad of issues ranging from renewed inflation, historically high equity valuations, winding down the Fed's "Quantitative Easing", capped by Russia's invasion of Ukraine. The largest tech companies held up reasonably well, with Facebook as the only notable exception. Returns from stocks traded in international and emerging markets are in negative territory. However, value stocks in both international and domestic markets traded at a premium over the quarter. The ups and downs of stock prices reflect the market's continued incorporation of the ongoing news associated with our uncertain environment.



Inflation is a concern. Over the past twelve months the Consumer Price Index (CPI) is up 8% - levels not seen since the early 1980's. It's not clear whether this spike reflects government stimulus spending, or shortages due to global supply chain disruptions; likely a combination of both. The Fed is beginning to increase interest rates in response. Its success at balancing the need to bring down inflation without triggering a recession is uncertain. While the concern of continued inflation seems to be heightened, market signals continue to indicate that inflation will be relatively short lived.

Stock returns in various markets over the past twelve months differ significantly from one another. Some differences in returns are offsetting performance from earlier periods, as the variability across market segments is less pronounced over the three-year period (shown above). Returns from domestic large-cap stocks remain well above long-term averages.

Over longer periods, we continue to see stocks in domestic markets doing better than those in non-domestic markets indicating generally more positive responses to uncertainty. Ten years is not a long period in financial markets. While these relative returns are useful to understanding recent performance in diversified portfolios, these results shouldn't be used to predict the future.

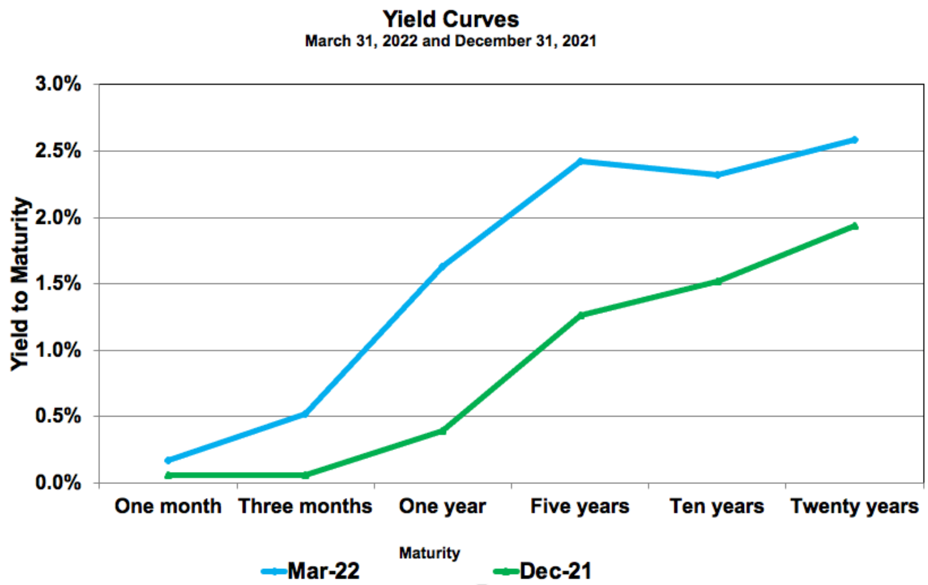
Bond Markets

A Yield Curve exhibits the pattern of observed returns from holding bonds to term across several maturities. It provides a sense of where interest rates are heading. Shifts help explain short-term bond returns as bond prices/returns move inversely to yield changes. The longer the period to maturity, the greater the effect. Today's upward sloping Yield Curve implies increasing yields going forward. The upward shift explains this quarter's negative bond returns.

Yields are driven by interest rates, risk premiums and expected inflation. These factors change over time resulting in moving yields and volatile bond market returns. If we isolate interest rate and risk by looking at Treasury yields of like maturities, then we have a view of expected inflation. Five-year yields have increased to levels above the ten-year numbers, reflecting increased short-term inflation expectations. Five-year yields imply 3.8% inflation over that period while ten-year yields imply 2.8% inflation. While these numbers are up since December, they are well below the 8% experienced over the past twelve months.

Market Commentary *Continued*

Uncertainties associated with the Fed's activities include (1) how fast and by how much it will increase interest rates to contain inflation and (2) how it will deal with the massive amount of government securities on its balance sheet. The Fed increased interest rates by ¼% at its last meeting, expecting several more rate hikes going forward with a goal to bring down inflation without triggering a recession. The Fed has $9.0 trillion of government securities on its balance sheet, well above anything seen in the past. How aggressively the Fed brings this amount back to historical levels will likely impact bond markets. ◆



Rockbridge Spotlight

Please join us in welcoming Rockbridge's newest advisor, Adam Underwood. After spending 4 years with Equitable, Adam wanted to partner with an Investment Advisory Firm that was free from conflicts of interest. With his prior firm, Adam struggled with the moral dilemma of making financial recommendations that were in his client's best interests versus his own. Adam was looking for a firm like Rockbridge where he could be successful while truly putting his client's interests first. Adam lives in East Syracuse with his girlfriend Lindsey. They are looking forward to purchasing their first home in the near future and getting a dog (much to Lindsey's delight!). Outside of work, Adam enjoys a round of golf, trying new local brews and cheering on his sport's teams. ◆

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Returns from Various Markets

The following table shows the returns from various markets over periods ending March 31, 2022:

Market/Asset Class	Quarter	1 Year	3 Years	5 Years	10 Years	20 Years
FIXED INCOME						
3-Month US Treasury Bills	0.04%	0.06%	0.81%	1.13%	0.63%	1.27%
Bloomberg US Agg Bond	-5.93%	-4.15%	1.69%	2.14%	2.24%	4.00%
Bloomberg 1-5 Yr Credit	-3.65%	-3.63%	1.61%	1.95%	2.08%	3.59%
DOMESTIC STOCKS						
S&P 500	-4.60%	15.64%	18.92%	15.99%	14.64%	9.25%
S&P 500 Value	-0.16%	12.58%	14.12%	11.14%	11.90%	7.87%
S&P 500 Growth	-8.59%	18.16%	22.47%	19.91%	16.81%	10.28%
Russell 2500	-5.82%	0.34%	13.79%	11.57%	12.09%	9.76%
Russell 2500 Value	-1.50%	7.73%	12.99%	9.20%	11.05%	9.23%
Russell 2500 Growth	-12.30%	-10.12%	12.97%	13.21%	12.69%	9.80%
MSCI US REIT	-4.06%	26.20%	11.14%	9.65%	9.74%	10.07%
INTERNATIONAL STOCKS						
MSCI EAFE	-5.91%	1.16%	7.78%	6.72%	6.27%	5.98%
MSCI Emerging Markets	-6.97%	-11.36%	4.94%	5.98%	3.36%	8.61%
U.S. Consumer Price Index	1.76%	7.11%	3.73%	3.08%	2.15%	2.34%

Note: These results were developed by simulating past returns in the various markets included in each benchmark, assuming the reinvestment of dividends and other earnings. The BofA Merrill Lynch 3-Month U.S. Treasury Bill Index represents money market/cash; the Bloomberg US Aggregate Bond Index represents the total U.S. bond market; the Bloomberg 1-5 Yr Credit Index represents the U.S. corporate bond market; the S&P 500, S&P 500 Value Index and S&P 500 Growth Index represent the domestic large-cap market; the Russell 2500, Russell 2500 Value Index and Russell 2500 Growth Index represent the domestic small-cap market; the MSCI U.S. REIT Index represents the U.S. real estate market; the MSCI EAFE Index represents the developed international equity market; the MSCI Emerging Markets Index represents international emerging markets. Benchmark Portfolio returns include Real Estate and Emerging Markets allocations beginning in July 2011. Benchmark Portfolio returns do not include allocations to these asset classes prior to June 30, 2011. Benchmark portfolio returns include Corporate Bond Market as of January 1, 2019 and do not include an allocation to this asset class prior to this. This data is presented to show the long-term relationship between returns at various levels of investment risk. It is not intended to present performance results experienced by clients of Rockbridge Investment Management, but is intended to provide a benchmark against which actual performance might be judged. Also, readers should recognize that future investments would be made under different economic conditions. It should not be assumed that future investors would experience returns, if any, comparable to those shown above. The information given is historic and should not be taken as any indication of future investment results.

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