OUTLOOK

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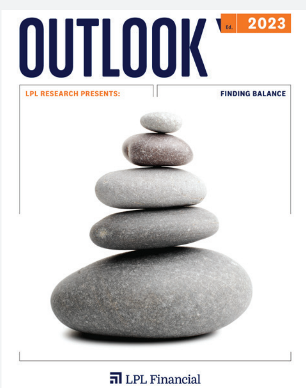
LPL RESEARCH PRESENTS

FINDING BALANCE

LPL Research's *Outlook 2023: Finding Balance* is our guide to how the readjustments in the economy and markets may impact you in the coming year. The disruptions may not be fully resolved and there may be more challenges to come, but progress toward finding balance is well underway.



OVERVIEW

Through all the challenges, newfound opportunities, and highs and lows we've experienced during the last couple of years, it's no surprise why we might be striving for more balance. Whether it's about the markets and global economy or what's happening in our local communities, the news we're hearing on a daily basis has the potential to disrupt the balance of our lives. But with resilience, perspective, and the support of close connections, we can navigate through it all and regain our sense of equilibrium—even after another dizzying year, as 2022 proved to be.

After two years of disruption due to the COVID-19 pandemic, we've been searching for some kind of return to normalcy while still experiencing the aftereffects of the pandemic. Some of those aftereffects included imbalances created by the fiscal, monetary, and public health policies put in place to address the pandemic—and the process of addressing those imbalances has been disorienting at times. If 2022 was about recognizing imbalances built into the economy and starting to address them, we believe 2023 will be about setting ourselves up for what comes next as the economy and markets find their way back to steadier ground—even if the adjustment period continues.

The Federal Reserve (Fed) spent 2022 aggressively fighting inflation by raising interest rates. In 2023, we expect the Fed to find that point where it can stop raising rates as inflation starts to come under control. The Fed's efforts to control inflation throughout 2022 pulled interest rates up from extremely low levels that were historically unprecedented. While that has been painful for bond investors, savers can now get an attractive yield for the first time since 2007, and 2023 will be more focused on how to potentially benefit from this significant shift. Stock market expectations may also see some realignment heading into 2023. The projections for certain market segments became too high in 2022 following a decade of low rates and a burst of extraordinary technology adoption. We expect 2023 will likely be more focused on the opportunities that may emerge from a market sell-off.

LPL Research's *Outlook 2023: Finding Balance* is our guide to how the readjustments in the economy and markets may impact you in the coming year. The disruptions may not be fully resolved and there may be more challenges to come, but progress toward finding balance is well underway. And when those disruptions hit the market, it can be hard to find our footing and stay the course. Those are the times when sound financial advice is more valuable than ever, as it helps us find our center, remember our plan, and stay focused on our goals.

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ECONOMY

The global economy will likely slow from above 3% to somewhere in the mid-2% range in 2023. An important aspect for investors is that the U.S. appears to have fewer headwinds to growth compared with Europe and other developed economies. The divergence between domestic and international economies is most obvious in the inflation regime. For example, in late 2022 Germany was experiencing accelerating rates of inflation, while at the same time the U.S. appeared to be moving past the peak. The longer inflation is uncontained, the riskier the growth prospects. If the U.S. falls into a recession, it is more likely to occur during the first half of 2023 and would probably not be as deep as the 2008 recession, which was initiated by a fundamentally flawed financial market.

INFLATION

We will likely enter 2023 with a slightly different trajectory for inflation—particularly services inflation. In recent months, durable goods prices have clearly decelerated—and in some cases, outright declined—but services prices have been stubbornly accelerating as rent prices and health services have risen. We could potentially be entering a new regime as rents across the country are showing signs of abating. During this transition period for services prices, the coming year could be the time when inflation is convincingly decelerating closer to the Fed's long-run target of 2%.

STOCKS

If stocks are going to go higher in 2023, a prompt end to the Fed's rate-hiking campaign will likely be a key component. The timing of the last rate hike of this cycle is uncertain and won't be clear for a while, but our view is that the Fed will pause during the first quarter of 2023 amid an improving inflation outlook and loosening job market. Should that occur, stocks will likely move higher, consistent with history. Stocks have tended to produce solid gains after hiking cycles end, including a 10% average gain one year later.

BONDS

The path of interest rates will certainly be largely influenced by the Fed's behavior, which will be guided by economic growth and inflation data. Equally important is the level of non-U.S. developed government bond yields, as foreign investors play an important role by purchasing U.S. Treasuries. Higher foreign market yields, all else equal, generally dissuade foreign investment into our markets. There are a range of scenarios we think could play out over the next year. However, given our view that the U.S. economy could eke out slightly positive economic growth next year, we think 10-year Treasury yields could end the year around 3.5%.

POLICY

The 2022 midterm election was closer than many expected but, in the end, voters chose to rebalance the power dynamic in Washington. As expected, Republicans gained enough seats to win a narrow majority in the House, while Democrats held on to their slim majority in the Senate. Despite Republicans' narrow House majority, their victory in the House significantly shifts the balance of power, since only legislation with broad bipartisan support will get passed once the new Congress is sworn in on January 3, 2023.

GEOPOLITICS

Uncertainty surrounding the course of the Ukraine-Russia conflict has thwarted diplomatic attempts to reach a negotiated settlement. The intense military campaign involves a significant contribution from NATO toward the Ukrainian war effort, specifically from the United States. Depending on how long the fighting continues, it is expected that many NATO countries, including the U.S., may debate the financial burden. Markets historically have navigated regional conflicts fairly well despite the human toll. The largest market vulnerability remains the war's impact on inflation.

COMMODITIES

This year the global economy adjusted to a higher interest-rate campaign initiated by most central banks in order to tackle inflationary pressures. As such, expectations are rising that several regions may face a recession or a significant economic slowdown will unfold, which would weigh on demand. Unless there are severe shortages, commodity prices typically tend to ease until there are signs that central banks are nearing the end of the rate-hike cycle.

CURRENCIES

To say the U.S. dollar has vaulted higher during the Fed's rate-hike cycle would be an understatement. Whether it is the result of the interest-rate differential (that is, that the Fed has been more aggressive than other central banks) or that U.S. markets have been attracting more investments from foreign investors, the result has been staggering. The strong dollar, while making imports less expensive, has put pressure on many of the large multinational companies with a global footprint.

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The opinions, statements and forecasts presented herein are general information only and are not intended to provide specific investment advice or recommendations for any individual. It does not take into account the specific investment objectives, tax and financial condition, or particular needs of any specific person. There is no assurance that the strategies or techniques discussed are suitable for all investors or will be successful. To determine which investment(s) may be appropriate for you, please consult your financial professional prior to investing.

Any forward-looking statements including the economic forecasts herein may not develop as predicted and are subject to change based on future market and other conditions. All performance referenced is historical and is no guarantee of future results.

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Alternative investments may not be suitable for all investors and should be considered as an investment for the risk capital portion of the investor's portfolio. The strategies employed in the management of alternative investments may accelerate the velocity of potential losses.

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All index data from FactSet.

All information is believed to be from reliable sources; however, LPL Financial makes no representation as to its completeness or accuracy.

General Risk Disclosures

Investing involves risks including possible loss of principal. No investment strategy or risk management technique can guarantee return or eliminate risk in all market environments. There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not protect against market risk. Investing in foreign and emerging markets' debt or securities involves special additional risks. These risks include, but are not limited to, currency risk, geopolitical risk, and risk associated with varying accounting standards. Investing in emerging markets may accentuate these risks.

General Definitions

Gross Domestic Product (GDP) is the monetary value of all the finished goods and services produced within a country's borders in a specific time period, though GDP is usually calculated on an annual basis. It includes all of private and public consumption, government outlays, investments and exports less imports that occur within a defined territory.

The PE ratio (price-to-earnings ratio) is a measure of the price paid for a share relative to the annual net income or profit earned by the firm per share. It is a financial ratio used for valuation: a higher PE ratio means that investors are paying more for each unit of net income, so the stock is more expensive compared to one with lower PE ratio.

Earnings per share (EPS) is the portion of a company's profit allocated to each outstanding share of common stock. EPS serves as an indicator of a company's profitability. Earnings per share is generally considered to be the single most important variable in determining a share's price. It is also a major component used to calculate the price-to-earnings valuation ratio.

The Standard & Poor's 500 Index is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The Bloomberg U.S. Aggregate Bond Index is an index of the U.S. investment-grade fixed-rate bond market, including both government and corporate bonds.

Equity Risk

Investing in stock includes numerous specific risks including the fluctuation of dividend, loss of principal and potential illiquidity of the investment in a falling market. Because of their narrow focus, sector investing will be subject to greater volatility than investing more broadly across many sectors and companies. Value investments can perform differently from the market as a whole. They can remain undervalued by the market for long periods of time. The prices of small and mid-cap stocks are generally more volatile than large cap stocks.

Equity Definitions

Cyclical stocks typically relate to equity securities of companies whose price is affected by ups and downs in the overall economy and that sell discretionary items that consumers may buy more of during an economic expansion but cut back on during a recession. Counter-cyclical stocks tend to move in the opposite direction from the overall economy and with consumer staples which people continue to demand even during a downturn.

A growth stock is a share in a company that is anticipated to grow at a rate significantly above the average for the market due to capital appreciation.

A value stock is anticipated to grow above the average for the market due to trading at a lower price relative to its fundamentals, such as dividends, earnings, or sales.

Large cap stocks are issued by corporations with a market capitalization of $10 billion or more, and small cap stocks are issued by corporations with a market capitalization between $250 million and $2 billion.

Fixed Income Risks

Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and bonds are subject to availability and change in price. Bond yields are subject to change. Certain call or special redemption features may exist which could impact yield. Government bonds and Treasury bills are guaranteed by the U.S. government as to the timely payment of principal and interest and, if held to maturity, offer a fixed rate of return and fixed principal value. Corporate bonds are considered higher risk than government bonds but normally offer a higher yield and are subject to market, interest rate, and credit risk, as well as additional risks based on the quality of issuer coupon rate, price, yield, maturity, and redemption features. Mortgage-backed securities are subject to credit, default, prepayment, extension, market and interest rate risk.

Fixed Income Definitions

Credit Quality is one of the principal criteria for judging the investment quality of a bond or bond mutual fund. As the term implies, credit quality informs investors of a bond or bond portfolio's credit worthiness, or risk of default. Credit ratings are published rankings based on detailed financial analyses by a credit bureau specifically as it relates to the bond issue's ability to meet debt obligations. The highest rating is AAA, and the lowest is D. Securities with credit ratings of BBB and above are considered investment grade. The credit spread is the yield of the corporate bonds less the yield on comparable maturity Treasury debt. This is a market-based estimate of the amount of fear in the bond market. Base-rated bonds are the lowest quality bonds that are considered investment-grade, rather than high-yield. They best reflect the stresses across the quality spectrum.

The Bloomberg Aggregate U.S. Bond Index represents securities that are SEC-registered, taxable, and dollar denominated. The index covers the U.S. investment-grade fixed-rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities.

High yield/junk bonds (grade BB or below) are not investment grade securities, and are subject to higher interest rate, credit, and liquidity risks than those graded BBB and above. They generally should be part of a diversified portfolio for sophisticated investors.

Municipal bonds are subject to availability and change in price. They are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise. Interest income may be subject to the alternative minimum tax. Municipal bonds are federally tax-free but other state and local taxes may apply. If sold prior to maturity, capital gains tax could apply.

The fast price swings in commodities will result in significant volatility in an investor's holdings. Commodities include increased risks, such as political, economic, and currency instability, and may not be suitable for all investors.

Currency risk is a form of risk that arises from the change in price of one currency against another. Whenever investors or companies have assets or business operations across national borders, they face currency risk if their positions are not hedged.

For a list of descriptions of the indexes and economic terms referenced in this publication, please visit our website at lplresearch.com/definitions.

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