

Rick D. Moulton,  
CFA, Lead Portfolio Manager

The third quarter, and September specifically, lived up to its reputation as a challenging period of the year for investors. All major indices moved lower in the quarter and now formally sit in bear market territory.

Familiar culprits were at the heart of the market decline. Persistently high inflation and the Federal Reserve's efforts to thwart these pressures created turmoil in the financial markets – both domestically and globally. Investors are left to ponder how long inflation will persist and how much economic pain will be endured as the Fed continues their aggressive tightening path.

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Investors were guardedly optimistic during the first half of the third quarter. Against a backdrop of low expectations, corporate earnings were decent. Some broader indicators were providing signs that inflation may be at or near a peak. Consumer sentiment and spending remained robust, and investors were even willing to overlook European and Asian economic struggles.

This upturn was abruptly interrupted when Federal Reserve Chairman Jerome Powell delivered his annual Jackson Hole Symposium speech in late August, in which he stated that the Fed is resolutely committed to taming inflation even if it means “pain” for the economy and job market. The Fed's posture is that the risk of continued inflation outweighs the benefits of economic growth. Investors factored in several significant interest rate hikes and the ensuing selloff spared virtually no financial instrument. When the dust settled, the equity markets recorded their worst nine-month start to a year since 2002.

Inflation and Fed policy promise to be the primary market drivers for the fourth quarter. Investors will attempt to look ahead to discern which companies are best positioned in a slower global economy. The good news for investors, perhaps paradoxically, is that expectations have been lowered. Corporate earnings growth estimates have declined. Professional fund managers are holding abnormally high levels of cash in their portfolios. Pessimism amongst individuals has spiked to its highest level since early 2009. Low expectations and pessimism are an encouraging harbinger for equity markets.

The Riverbridge portfolios are well positioned regardless of what may transpire over the short term. Our portfolios hold companies that we believe can grow even if broader economic activity slows. Many of our companies offer their customers products or solutions that combat rising input costs by increasing their operating efficiency. Riverbridge portfolio companies are generally immune to rising borrowing costs as they are internally financed and not dependent on borrowing capital to grow their businesses. Our portfolios contain many fundamentally vibrant businesses that we expect to adapt or even thrive in more challenging operating environments.

Over our 35-year history, Riverbridge has witnessed many challenging market environments. Maintaining a long-term perspective has helped our clients do relatively well during these types of cycles. While difficult, these environments allow well-managed, strategically positioned companies to distinguish themselves. We greatly appreciate the trust that our clients place in Riverbridge.

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