ECONOMIC AND MARKET COMMENTARY

2nd Quarter 2022

SMITH SHELLNUT WILSON
AN AFFILIATE OF b1BANK

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I. SECOND-QUARTER 2022 EQUITY MARKET RECAP

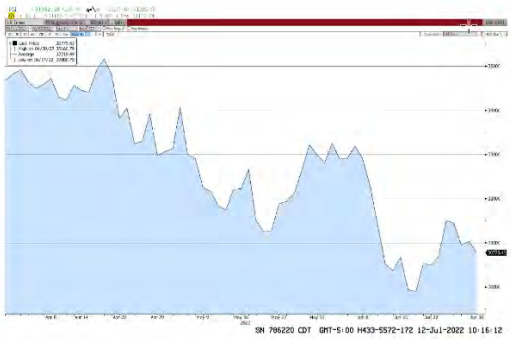
The equity market had a very difficult quarter with losses more than double those experienced in the 1st quarter of the year. The technology-heavy NASDAQ again took the largest decline falling 22.3%. The broader market, S&P 500, was down 16.1% while the Russell 2000 index fell 18.0%. For the second quarter in a row, Value stocks outpaced Growth stocks with Value falling 12.2% and Growth falling 20.9%.

European markets fell less than the U.S. with the UK's FTSE 100 Index down 3.8%, the French CAC 40 Index down 8.9%, and the German DAX off 11.3%. Japan's Nikkei-225 was off 5.0% while the Chinese Shanghai Composite Index was up 5.6% on hopes of expansion after further Covid-19 lockdowns.

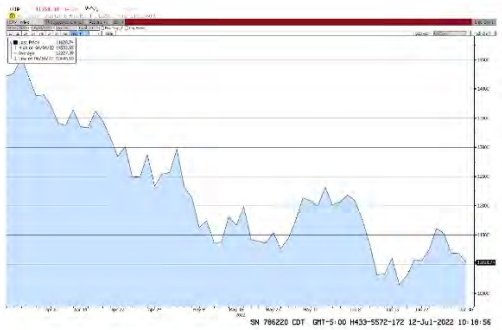
Investors have become very cautious with the confluence of many negative factors including consumer inflation hitting 40-year highs, the Russian invasion of Ukraine, The Federal Reserve increasing short-term interest rates, a contracting U.S. money supply, and fears of a recession in the future. The consumer, representing 70% of U.S. Gross National Product, has effectively lost purchasing power through both inflation and a decline in absolute wealth. Consumers have run up credit card balances this year after significant gains in debt reduction and increased savings during Covid-19.

Moving forward markets must adjust for corporate earnings declining while credit losses increase and credit availability declines. The U.S. is expected to experience disinflation in the 2nd half of the year with the inflation growth rate declining while GDP is expected to be flat to negative.

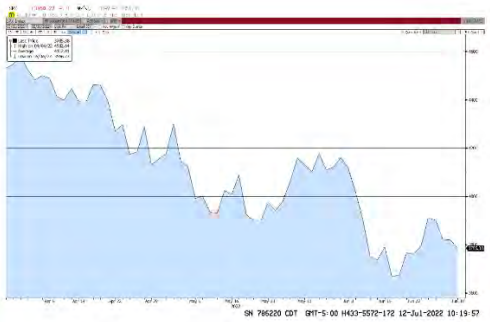
Dow Jones Industrial Index
03/31/2022 to 06/30/2022



NASDAQ Composite Index
03/31/2022 to 06/30/2022



S&P 500 Index
03/31/2022 to 06/30/2022



**Registration of an Investment Adviser does not imply any certain level of skill or training.*

II. SECOND-QUARTER 2022 BOND MARKET RECAP

Bonds were under pressure in the second quarter as investors priced in further rate hikes because of +40-year highs in inflation, global conflict, and growing signals regarding recession.

The Federal Reserve aggressively moved to tackle rising inflation even at the risk of slowing economic growth. The Fed hiked its overnight rate 125 basis points (50bp in May, 75bp in June), implementing its first 75bp rate hike since 1994. The 2-year Treasury rose sixty-two basis points and the 10-year Treasury yield finished sixty-eight basis points higher (see chart below). The Treasury curve inverted across multiple durations inside 10 years.

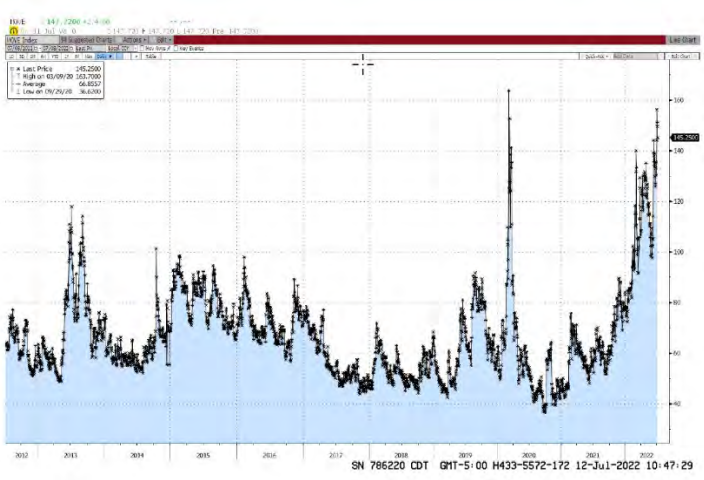
	March 31, 2022	June 30, 2022	Low/High
2yr Treasury	2.34	2.96	2.34/3.43
10yr Treasury	2.34	3.02	2.33/3.48
30yr Treasury	2.46	3.04	2.46/3.59
Bond Vol. (MOVE index)	107	136	98/144

A dominant storyline in the bond market has been the substantial increase in volatility and the resulting spread widening that has occurred in bond sectors with credit, option and/or liquidity exposure. An excellent gauge of bond market/interest rate volatility is the MOVE index (see right). It ended the second quarter up to 136. It has averaged 82 over the past fifteen years and has only been above that level twice (2008, 2020). The resulting spread widening has been very noticeable in bonds with embedded call options and credit exposure. For example, during the quarter, investment grade option adjusted credit spreads (LUACTRUU index) widened by 36%. Bond investors, with purchasing power, have been taking advantage of the opportunity. But bond investors that purchased bonds with extension risk or lower credit quality in 2020-2021, are experiencing higher unrealized losses.

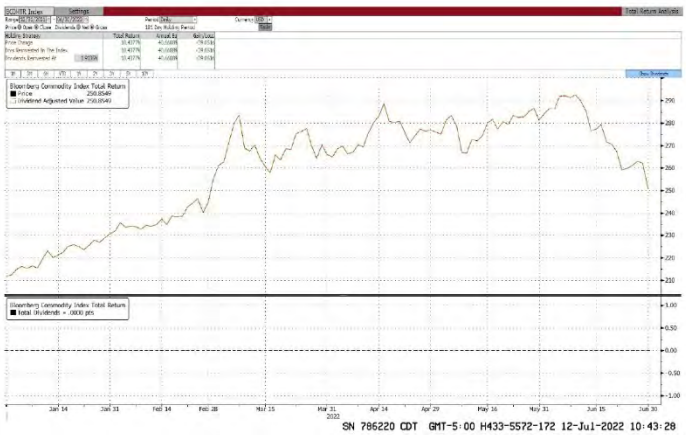
Looking forward, the market is beginning to settle into a peak in rates. The market is currently pricing in that the Fed funds rate will level off in March 2023 at 3.60% and in fact is now pricing in 50-75 basis points of rate cuts during the second half of 2023. The 10-year Treasury yield is priced to rise about 20-25 basis points more over the next year.

III. ALL EYES ON THE FED IN 2ND HALF 2022

Market volatility remained elevated throughout the first half of 2022 as the economy takes on headwinds on multiple fronts, and financial markets are facing great uncertainty. The current crisis began with inflation elevating to levels not seen since the early 1980's. Current inflation is believed to be a supply chain driven issue and has been exacerbated by the war in Ukraine and COVID lockdowns in China. Commodity prices increased dramatically in the first half of the year but have settled recently. Inflation expectations are forcing the hand of the Fed as Chairman Powell attempts to assure markets that he is willing to utilize the full power of the Fed to tame inflation.



The MOVE index (a measure of bond market volatility) indicates that bond market volatility is elevated.



The Bloomberg Commodity Index was up as much as 39% in early June but ended the quarter at a gain of 18%.

The Fed has increased the Fed funds rate from a range of 0.00% to 0.25% at the start of the year to 1.50% to 1.75%, currently. As stated above, the market is pricing in that the Fed funds rate will increase to 3.60% by March of 2023. Secondly, the Fed has begun to reduce its historically large balance sheet by no longer reinvesting all principal cashflow. Chairman Powell continues to present a hawkish tone even as fears of recession begin to loom over Fed decisions.



Fed fund futures have the implied rate at year end is 3.47%.

It remains uncertain if the Fed can manage to tame inflation without pushing the economy into a recession. There are some indications that the Fed may be able to pull it off, for example, employment data continues to surprise to the upside. There are also some warning signs being revealed like the steep drop in mortgage applications and the flat-to-inverted yield curve. Current consensus economic forecasts have GDP growth slowing throughout the year and into 2023 and place the likelihood of recession at 33%. However, there is more uncertainty around all economic forecast than normal as economists have consistently missed on economic data in recent weeks. What is certain is that markets will remain volatile until future Fed actions are more certain.

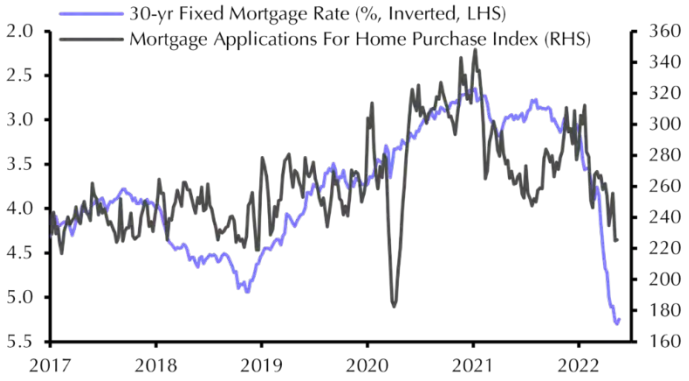
IV. THE NOT-SO-GOOD, THE BAD AND THE UGLY: THE OUTLOOK FOR THE WORLD'S BIG THREE ECONOMIES

Written By: Neil Shearing, Group Chief Economist
Date: May 31, 2022

We've spent a long time arguing that the global economy faces a more difficult outlook than most expect. The consensus is now moving towards our view as evidence of weakness mounts. But, amid the pervasive gloom, it's worth noting that the three largest economic blocs – the US, euro-zone and China – face challenges that are very different in nature and scale. This has important implications for the size and duration of their downturns – and for the extent of their recoveries.

As it happens, the turmoil in US financial markets over the past month stands in contrast to the strength of the latest hard activity data from the US. We expect that tighter monetary conditions will eventually cause growth to slow over the second half of this year, but this slowdown is likely to be concentrated in the most rate-sensitive areas of the economy. This includes durable goods, business equipment investment and, most notably, housing. Indeed, the increase in mortgage rates over the past couple of months is already consistent with a sharp fall in mortgage applications. (See Chart 1.)

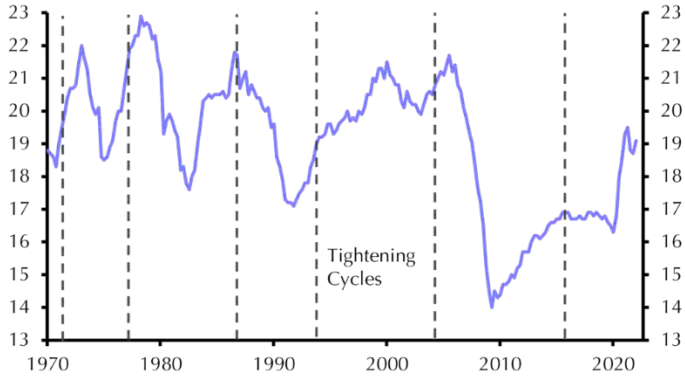
Chart 1: US Mortgage Applications and Mortgage Interest Rates



Sources: Refinitiv, Capital Economics

Admittedly, interest rate-sensitive expenditure by consumers and businesses has declined as a share of GDP over the past decade (see Chart 2), and household balance sheets remain in good shape. We therefore expect the economy as a whole to skirt recession. But the US economy is nonetheless likely to slow as the Federal Reserve continues to tighten, and we anticipate a period of below-trend growth over the second half of this year and into 2023.

Chart 2: Interest Rate-Sensitive Expenditure in US (% of GDP)



Sources: Refinitiv, Capital Economics

By the same token, however, the slowdown in the US is likely to be relatively mild compared to other advanced economies. Those in Europe are facing much larger headwinds. This is due in part to the fact that Europe's economic ties to Russia are deeper than those of the US. But another key difference is that, while the US is no longer a large net importer of energy, the euro-zone is. Accordingly, it has experienced a severe deterioration in its terms of trade as global energy prices have surged. (See Chart 3.) Put another way, the price of its imports has increased sharply compared to the price of its exports, meaning the economy as a whole is worse off.

Chart 3: US and Euro-zone Terms of Trade (2020 = 100)



Sources: Refinitiv, Capital Economics

This means a much larger squeeze on real household incomes in the euro-zone. The latest survey data suggest that the region's economy is holding up a bit better than we had anticipated, but consumer spending is nonetheless likely to contract across most of the region over the next quarter or so. This will pose a major challenge to policymakers: *should they focus on providing support to the real economy or reining in inflation?*

In truth, there's little that monetary policy can do to mitigate the effects of such a large terms of trade shock and, with core price pressures now building, policymakers must focus on bringing inflation to heel. The European Central Bank will not have to tighten by as much as the Fed. But just getting policy back to a more neutral setting will add to the headwinds facing households and business in the euro-zone.

If the situation facing European policymakers is challenging, China's problems are even more complex. Most immediately, efforts to quash the continuing Omicron outbreak have resulted in tightened restrictions across some of the country's biggest and most economically-important cities. In a meeting last week, Chinese Premier Li Keqiang warned officials about signs of contraction in May, urging them to ensure that the economy grows in the second quarter.

China is also facing mounting cyclical headwinds. While its recovery from the first wave of COVID in early 2020 was aided by a surge in construction activity, property developers are now struggling to finance existing projects. They won't launch new ones until there has been a marked pick-up in sales. China's recovery two years ago was also underpinned by a surge in global demand for consumer goods that benefitted local producers. But this too is fading as global spending on services rebounds. China's goods exports are more likely to fall than rise further over the rest of this year.

Finally, beyond these near-term problems, China's structural economic problems are deepening as many of its long-term challenges come into sharper focus.

Economic activity is likely to rebound in the third quarter as the government gets on top of Omicron and lockdowns are lifted. The package of policy support measures announced last week will also help the recovery, although this too was small by past standards. The rebound, when it comes, is likely to stand in contrast to weakness in the US and euro-zone and could be interpreted as evidence of the relative health of China's economy. This would be the wrong take: China's recovery from Omicron is likely to be muted compared to previous downturns and GDP will remain on a weaker track post-COVID.

Clouds are gathering over the global economy. But compared to other major economies, particularly the US, China's economic problems look more intractable.

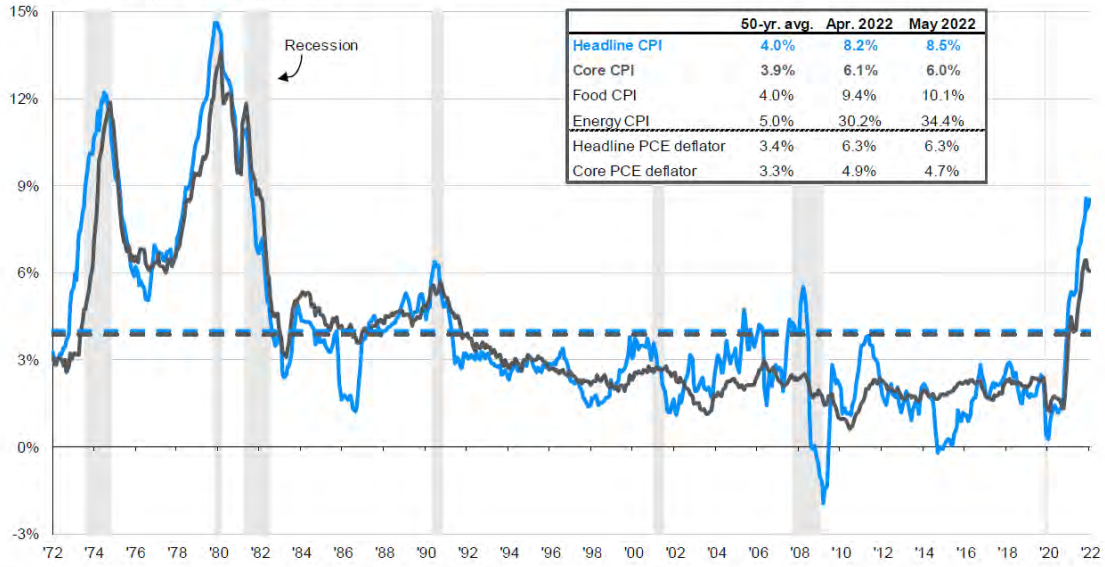
The source of the information in this commentary is SSW, Neil Shearing (Group Chief Economist), and Bloomberg.

Economy

Inflation

CPI and core CPI

% change vs. prior year, seasonally adjusted



	50-yr. avg.	Apr. 2022	May 2022
Headline CPI	4.0%	8.2%	8.5%
Core CPI	3.9%	6.1%	6.0%
Food CPI	4.0%	9.4%	10.1%
Energy CPI	5.0%	30.2%	34.4%
Headline PCE deflator	3.4%	6.3%	6.3%
Core PCE deflator	3.3%	4.9%	4.7%

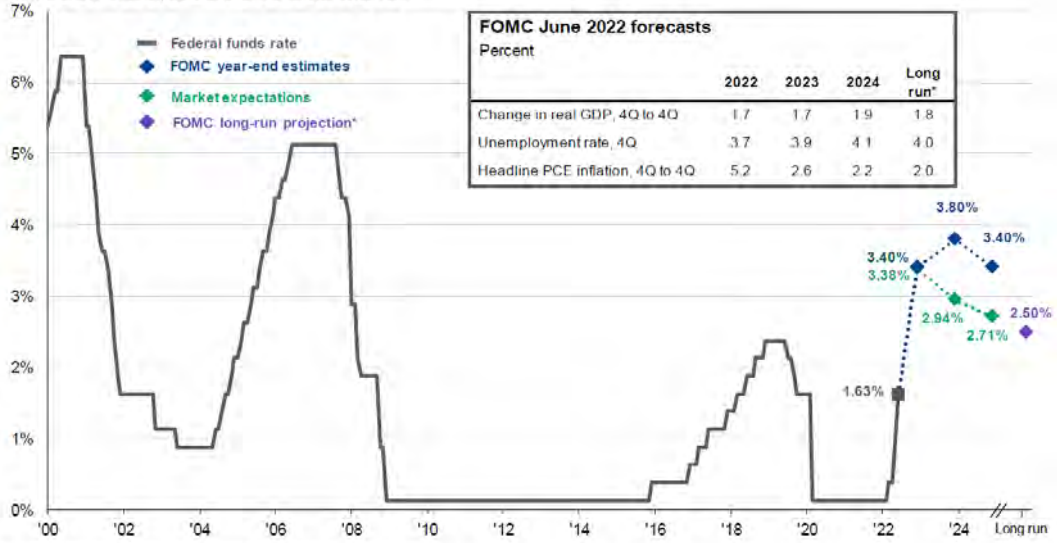
Source: BLS, FactSet, J.P. Morgan Asset Management.
CPI used is CPI-U and values shown are % change vs. one year ago. Core CPI is defined as CPI excluding food and energy prices. The Personal Consumption Expenditure (PCE) deflator employs an evolving chain-weighted basket of consumer expenditures instead of the fixed-weight basket used in CPI calculations.
Guide to the Markets – U.S. Data are as of June 30, 2022.

Fixed Income

The Fed and interest rates

Federal funds rate expectations

FOMC and market expectations for the federal funds rate



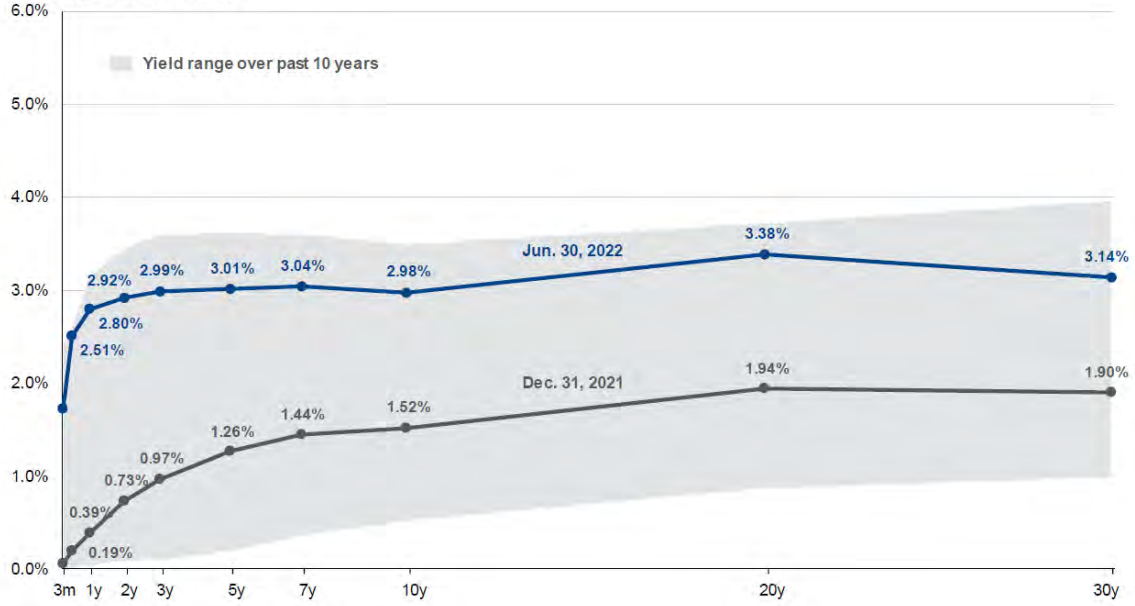
FOMC June 2022 forecasts Percent	2022	2023	2024	Long run*
Change in real GDP, 4Q to 4Q	1.7	1.7	1.9	1.8
Unemployment rate, 4Q	3.7	3.9	4.1	4.0
Headline PCE inflation, 4Q to 4Q	5.2	2.6	2.2	2.0

Source: Bloomberg, FactSet, Federal Reserve, J.P. Morgan Asset Management.
Market expectations are based off of the respective Federal Funds Futures contracts for December expiry. *Long-run projections are the rates of growth, unemployment and inflation to which a policymaker expects the economy to converge over the next five to six years in absence of further shocks and under appropriate monetary policy. Forecasts are not a reliable indicator of future performance. Forecasts, projections and other forward-looking statements are based upon current beliefs and expectations. They are for illustrative purposes only and serve as an indication of what may occur. Given the inherent uncertainties and risks associated with forecasts, projections or other forward-looking statements, actual events, results or performance may differ materially from those reflected or contemplated.
Guide to the Markets – U.S. Data are as of June 30, 2022.

Fixed Income

Yield curve

U.S. Treasury yield curve



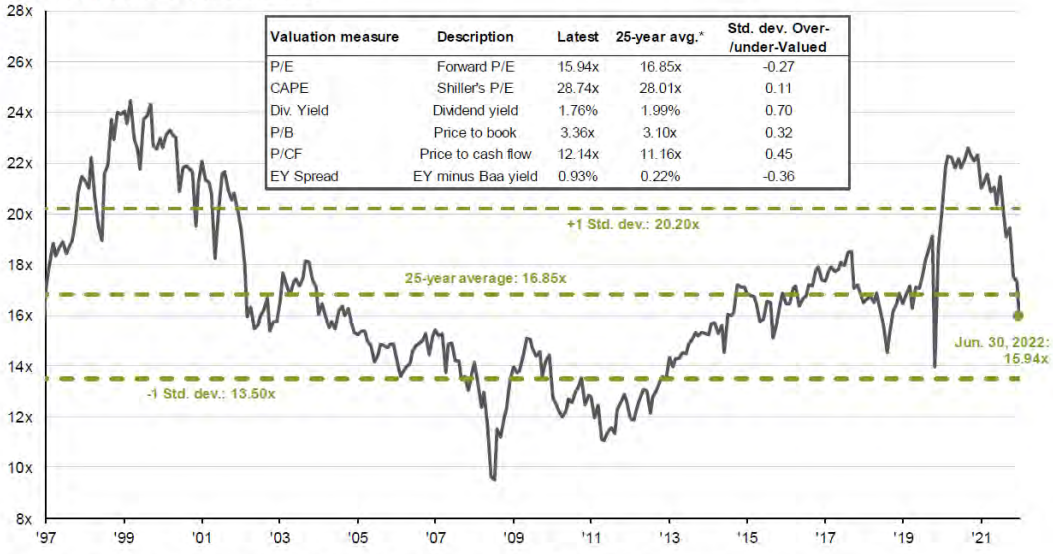
Source: FactSet, Federal Reserve, J.P. Morgan Asset Management.
Guide to the Markets – U.S. Data are as of June 30, 2022.

Equities

S&P 500 valuation measures

S&P 500 Index: Forward P/E ratio

Valuation measure	Description	Latest	25-year avg.*	Std. dev. Over-/under-Valued
P/E	Forward P/E	15.94x	16.85x	-0.27
CAPE	Shiller's P/E	28.74x	28.01x	0.11
Div. Yield	Dividend yield	1.76%	1.99%	0.70
P/B	Price to book	3.36x	3.10x	0.32
P/CF	Price to cash flow	12.14x	11.16x	0.45
EY Spread	EY minus Baa yield	0.93%	0.22%	-0.36

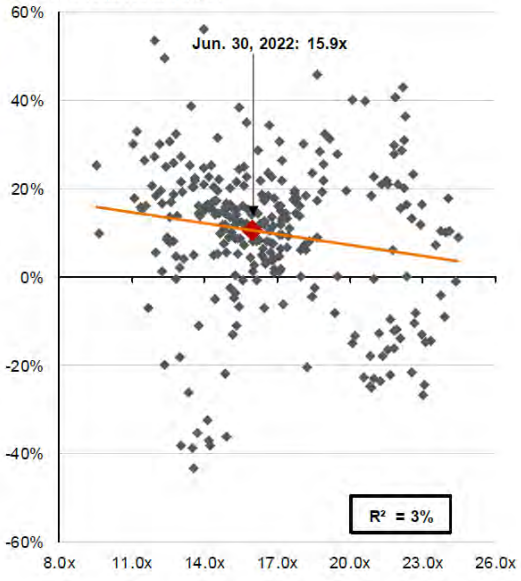


Source: FactSet, FRB, Refinitiv Datastream, Robert Shiller, Standard & Poor's, Thomson Reuters, J.P. Morgan Asset Management.
Price-to-earnings is price divided by consensus analyst estimates of earnings per share for the next 12 months as provided by IBES since June 1997 and by FactSet since January 2022. Current next 12-months consensus earnings estimates are $240. Average P/E and standard deviations are calculated using 25 years of history. Shiller's P/E uses trailing 10-years of inflation-adjusted earnings as reported by companies. Dividend yield is calculated as the next 12-months consensus dividend divided by most recent price. Price-to-book ratio is the price divided by book value per share. Price-to-cash flow is price divided by NTM cash flow. EY minus Baa yield is the forward earnings yield (consensus analyst estimates of EPS over the next 12 months divided by price) minus the Moody's Baa seasoned corporate bond yield. Std. dev. over-/under-valued is calculated using the average and standard deviation over 25 years for each measure. *P/CF is a 20-year average due to cash flow availability.
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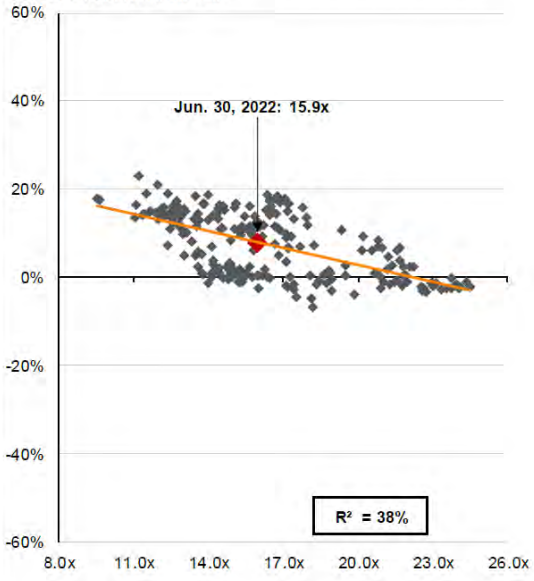
P/E ratios and equity returns

Equities

Forward P/E and subsequent 1-yr. returns
S&P 500 Total Return Index



Forward P/E and subsequent 5-yr. annualized returns
S&P 500 Total Return Index

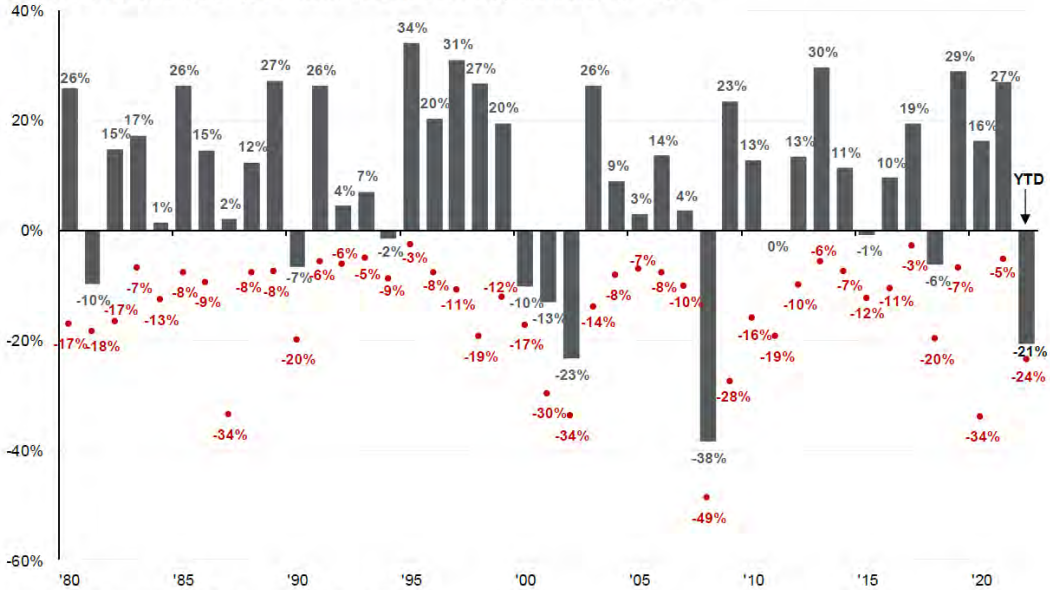


Source: FactSet, Refinitiv Datastream, Standard & Poor's, Thomson Reuters, J.P. Morgan Asset Management.
Returns are 12-month and 60-month annualized total returns, measured monthly, beginning 5/31/97. R^2 represents the percent of total variation in total returns that can be explained by forward price-to-earnings ratios. Price-to-earnings is price divided by consensus analyst estimates of earnings per share for the next 12 months as provided by IBES since January 1997 and by FactSet since January 2022.
Guide to the Markets – U.S. Data are as of June 30, 2022.

Annual returns and intra-year declines

Equities

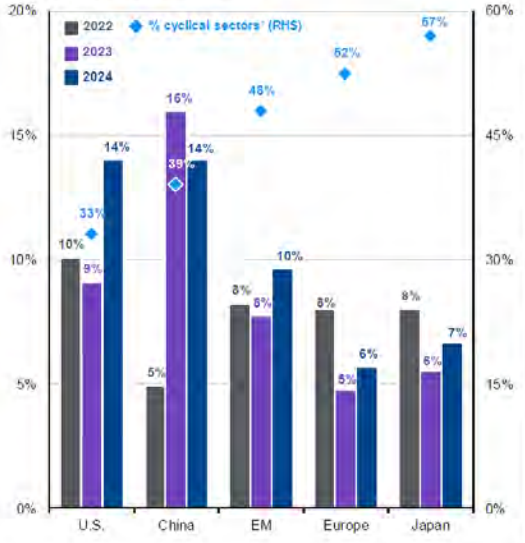
S&P intra-year declines vs. calendar year returns
Despite average intra-year drops of 14.0%, annual returns were positive in 32 of 42 years



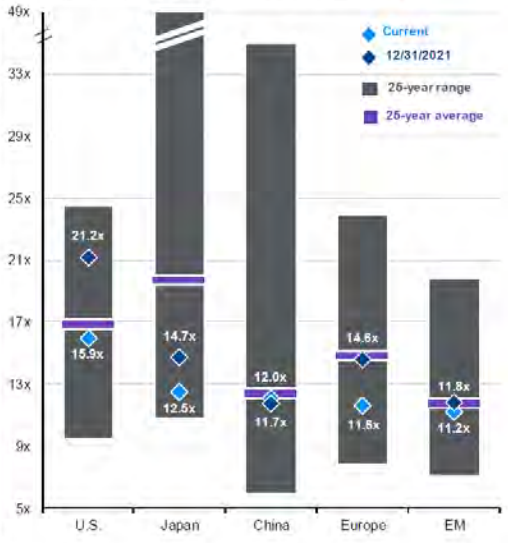
Source: FactSet, Standard & Poor's, J.P. Morgan Asset Management.
Returns are based on price index only and do not include dividends. Intra-year drops refers to the largest market drops from a peak to a trough during the year. For illustrative purposes only. Returns shown are calendar year returns from 1980 to 2021, over which time period the average annual return was 9.4%.
Guide to the Markets – U.S. Data are as of June 30, 2022.

International equity earnings and valuations

Global earnings growth
Calendar year consensus estimates



Global valuations
Current and 25-year next 12 months price-to-earnings ratio

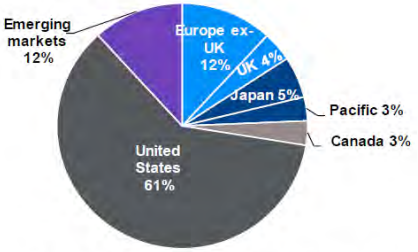


Source: FactSet, MSCI, Standard & Poor's, Thomson Reuters, J.P. Morgan Asset Management.
*Cyclical sectors include consumer discretionary, financials, industrials, energy and materials. The Internet and direct marketing subsector has been removed from the cyclicals calculation. In our judgement, companies in this space do not yet fit into the cyclical category, as they are still in a transitional growth phase and are not being directly impacted by the business cycle. Valuation and earnings charts use MSCI indices for all regions/countries, except for the U.S., which is the S&P 500. All indices use IBES aggregate earnings estimates, which may differ from earnings estimates used elsewhere in the book. MSCI Europe includes the eurozone as well as countries not in the currency bloc, such as Norway, Sweden, Switzerland and the UK (which collectively make up 44% of the overall index). Past performance is not a reliable indicator of current and future results.
Guide to the Markets – U.S. Data are as of June 30, 2022.

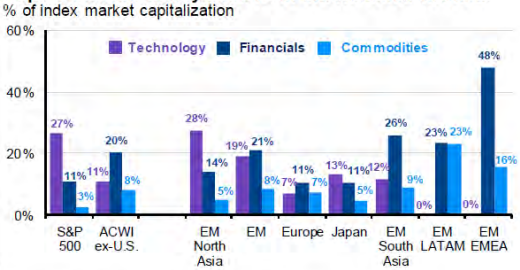
Global equity markets

Returns	2022 YTD		2021		15-years	
	Local	USD	Local	USD	Ann.	Beta
Regions						
U.S. (S&P 500)	-	-20.0	-	28.7	10.7	0.90
AC World ex-U.S.	-11.6	-18.2	13.5	8.3	4.2	1.07
EAFE	-10.9	-19.3	19.2	11.8	4.1	1.04
Europe ex-UK	-17.3	-23.6	24.4	16.5	4.8	1.18
Emerging markets	-13.5	-17.5	0.1	-2.2	4.8	1.18
Selected Countries						
United Kingdom	1.7	-8.8	19.6	18.5	2.3	1.02
France	-14.8	-21.7	29.7	20.6	4.7	1.22
Germany	-21.8	-28.1	13.9	5.9	4.7	1.31
Japan	-5.7	-20.1	13.8	2.0	3.4	0.72
China	-9.9	-11.2	-21.6	-21.6	5.8	1.10
India	-9.8	-15.1	28.9	26.7	6.7	1.26
Brazil	-3.4	2.9	-11.2	-17.2	0.9	1.50
Korea	-21.7	-28.3	0.8	-7.9	5.9	1.49

Weights in MSCI All Country World Index
% global market capitalization, float adjusted



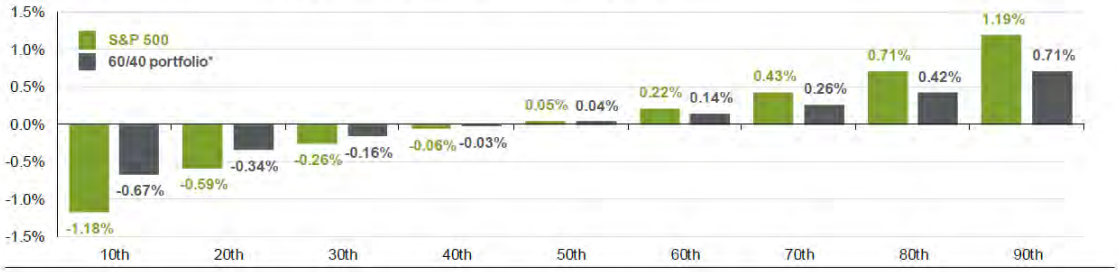
Representation of key sectors in international markets
% of index market capitalization



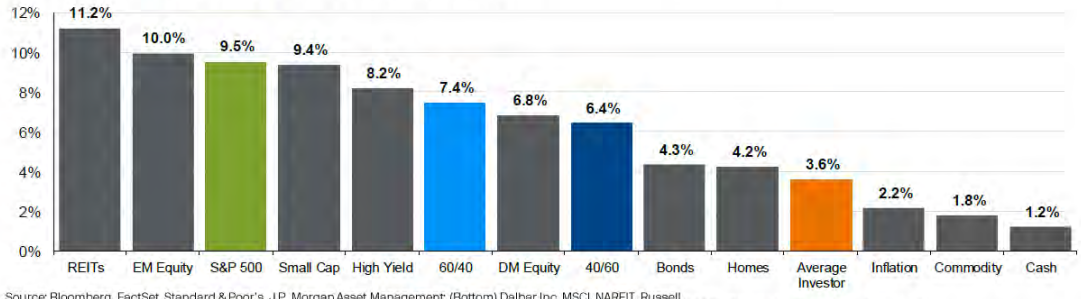
Source: FactSet, Federal Reserve, MSCI, Standard & Poor's, J.P. Morgan Asset Management. All return values are MSCI Gross Index data. 15-year history based on USD returns. 15-year return and beta figures are calculated for the time period 12/31/2006 to 12/31/2021. Beta is for monthly returns relative to the MSCI AC World Index. Annualized volatility is calculated as the standard deviation of quarterly returns multiplied by the square root of 4. Chart is for illustrative purposes only. Please see disclosure page for index definitions. Past performance is not a reliable indicator of current and future results. EM North Asia includes China, Taiwan and South Korea. EM South Asia includes India, Indonesia, Malaysia, Pakistan, Philippines, Taiwan and Thailand.
Guide to the Markets – U.S. Data are as of June 30, 2022.

Diversification and the average investor

Equities vs. 60/40 portfolio: Last 20 years' daily market performance by decile



20-year annualized returns by asset class (2002 – 2021)



Source: Bloomberg, FactSet, Standard & Poor's, J.P. Morgan Asset Management; (Bottom) Dalbar Inc, MSCI, NAREIT, Russell.
Indices used are as follows: REITs: NAREIT Equity REIT Index, Small Cap: Russell 2000, EM Equity: MSCI EM, DM Equity: MSCI EAFE, Commodity: Bloomberg Commodity Index, High Yield: Bloomberg Global HY Index, Bonds: Bloomberg U.S. Aggregate Index, Homes: median sale price of existing single-family homes, Cash: Bloomberg 1-3m Treasury, Inflation: CPI. *60/40: A balanced portfolio with 60% invested in S&P 500 Index and 40% invested in high-quality U.S. fixed income, represented by the Bloomberg U.S. Aggregate Index. The portfolio is rebalanced annually. Average asset allocation investor return is based on an analysis by Dalbar Inc., which utilizes the net of aggregate mutual fund sales, redemptions and exchanges each month as a measure of investor behavior.
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Investing Principles