Economic Update & Asset Allocation (David Lynch)
The US economy is in the late cycle. This phase can last some length of time before a recession fully arrives and is not necessarily cause for immediate doom and gloom. However, financial conditions have deteriorated since the start of the year and the consensus is now agreeing that a recession is coming, and perhaps already underway.
S&P 500 Short-Term Recovery (top)...

...Forward Valuation Mid-Range (bottom)

Source: Bloomberg, 8/9/22
Earnings Could Have More Correcting to Do

Source: Morgan Stanley

Earnings Leading Indicator Now in Negative Territory

Source: FactSet, Bloomberg, Morgan Stanley Research as of June 1, 2022.
Note: The LEI is a top down macro indicator consisting of the dollar, manufacturing PMI survey data, consumer confidence, housing related data, and credit spreads.

Source: Morgan Stanley
Stock Market Lively Nearly Every Day

NEARLY 90% OF DAYS WITH > 1% RANGE THIS YEAR

Source: Strategas as of 8/10/22
Stocks Calmer Than Covid Onset...Bonds Still Volatile

BOND & FX VOL PROVING STICKIER THAN EQUITY VOL

The VIX is below where it traded pre-June CPI print, but Bond and FX vol are not.

Source: Strategas, 8/7/22
The Treasury yield curve shows investors expecting more interest rate hikes by the Federal Reserve. This outlook has inverted parts of the normally upward sloping curve.
The bellwether 10-year Treasury bond has recovered some recently as concerns of recession have grown. Overall, bond returns have been negative year-to-date, though the higher yields are now more attractive for income-focused investors.
Credit spreads have widened in sympathy with the growing odds of recession as well as the ongoing stock market volatility. However, credit markets remain orderly thus far and indicate that companies remain in generally good financial health and that defaults should remain subdued.
Historically the tightening cycles have ended only after the Fed Funds rate gets above CPI. On this basis, the Fed Reserve still has more hiking to do. However, if growth and inflation start to moderate on their own, then the Federal Reserve might ultimately need fewer rate hikes (and/or move at a less aggressive pace).
Mortgage Rates Up, Housing To Cool More?

Source: FreddieMac.com, data as of 8/4/22
Gasoline Prices Cooling Rapidly
Volatility is Inevitable, Don’t Lose Sight of the Big Picture

DYNAMIC ASSET ALLOCATION TIMELINE

HORIZONS

Secular
(10–30 years)

Business Cycle
(1–10 years)

Tactical
(1–12 months)

Portfolio Construction
Asset Class | Country/Region | Sectors | Correlations

Source: Fidelity Investments (AART)
Stock Market Overview
(Stig Zarle)
U.S. Equities: A Difficult First Half of the Year

S&P 500 Price Index

Source: CT Research, FactSet Research Systems; Data as of 8/3/22

S&P 500 Sectors (1/1 - 6/16)

- Energy: 41.8%
- Utilities: -7.9%
- Staples: -10.1%
- Health Care: -14.6%
- Materials: -16.9%
- Industrials: -18.6%
- Financials: -20.7%
- S&P 500: -22.5%
- Real Estate: -24.7%
- Technology: -29.2%
- Comm. Svs: -32.1%
- Discretionary: -34.4%

Source: Wolfe Research
Q2 Earnings Results Have Been Pretty Good

Source: FactSet Research Systems, 8/5/22
‘22 & ‘23 Corporate Profit Estimates Slowly Coming Down

Source: FactSet Research Systems, 8/5/22
Bank Loan Growth Among the Best in Decades …

Source: Evercore ISI
... While Other Lines of Business Under Pressure

Core fee revenue saw a meaningful decrease (-12%) in 2022, with IB, and mortgage the worst performers YoY...

Source: Goldman Sachs Investment Research
Few Signs of Stress Among Borrowers/Loan Groups

Delinquency Rates by Loan Category
(%, All Commercial Banks by Qtr)

Source: Board of Governors of the Federal Reserve System
YTD Bankruptcy* Filings Well Below Historical Norms

US bankruptcy filings by year


Source: S&P Global Market Intelligence

*Note: Bankruptcy data from S&P is limited to public/private companies with assets or liabilities greater than $2B/$10B at time of filing.
Consumer Sentiment Pressured

Consumer Sentiment Index and subsequent 12-month S&P 500 returns

- Avg. subsequent 12-mo. S&P 500 returns
  - 8 sentiment peaks: +4.1%
  - 8 sentiment troughs: +24.9%

- Average: 85.6

- Sentiment cycle turning point and subsequent 12-month S&P 500 Index return

Source: J.P. Morgan
Risks Signals From Lower-Income Consumer Cohorts

Low-Income Consumers Are the Worst Affected by High Prices of Energy, Food, and Shelter

Share of Disposable Income Spent on Essential Items In 2020 (Groceries, Shelter, Utilities, Gasoline)

1st: 94%
2nd: 49%
3rd: 36%
4th: 29%
5th: 21%

Source: KKR, Bureau of Labor Statistics
Quick Check on Consumer Activity

1. TSA - 7D Avg % Chg From 2019 Year Avg
   - Source: RBC

2. MTA Subway % Change From Pre-Pandemic Trend

3. MTA Bus % Change From Pre-Pandemic Trend

4. OpenTable United States Seated Diners YoY (7D Avg)

5. Johnson Redbook Index Same Store Sales Weekly (YoY & 4Wk Avg)

6. Kastle Back to Work Barometer Average

Source: RBC
Higher Income Consumer Spending Remains Robust

Source: American Express

G&S vs. T&E

<table>
<thead>
<tr>
<th></th>
<th>Q2'22</th>
<th>G&amp;S</th>
<th>T&amp;E</th>
<th>Total</th>
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<tbody>
<tr>
<td>YoY</td>
<td>18%</td>
<td>70%</td>
<td>31%</td>
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Billed Business Growth by Age Cohort

<table>
<thead>
<tr>
<th></th>
<th>Q2'22</th>
<th>Millennials + Gen-Z</th>
<th>Gen-X</th>
<th>Baby Boomer +</th>
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<tbody>
<tr>
<td>YoY</td>
<td>48%</td>
<td>30%</td>
<td>19%</td>
<td></td>
</tr>
<tr>
<td>% of Total</td>
<td>30%</td>
<td>38%</td>
<td>31%</td>
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$ in Billions

<table>
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<tr>
<th></th>
<th>Q2'19</th>
<th>Q3'21</th>
<th>Q4'21</th>
<th>Q1'22</th>
<th>Q2'22</th>
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</thead>
<tbody>
<tr>
<td>Pre-Pandemic</td>
<td>$139</td>
<td>$153</td>
<td>$174</td>
<td>$164</td>
<td>$187</td>
</tr>
</tbody>
</table>

% Increase(decrease) vs. Prior Year (FX-adjusted):

Source: American Express