Dear Valued Client:

Congratulations to the class of 2022. As Cat Steven's song goes, "Oh baby, baby it's a wild world, it's hard to get by just upon a smile...." The pandemic tested graduates now face a world like the one that their parents may have witnessed if they grew up in the 70's. In our office, we have a copy of Time Magazine, October 14, 1974, with a picture of Gerald Ford rolling up his sleeves with the headline "Trying to fight back- inflation, recession, oil." As Mark Twain said, "history does not repeat itself, but it often rhymes."

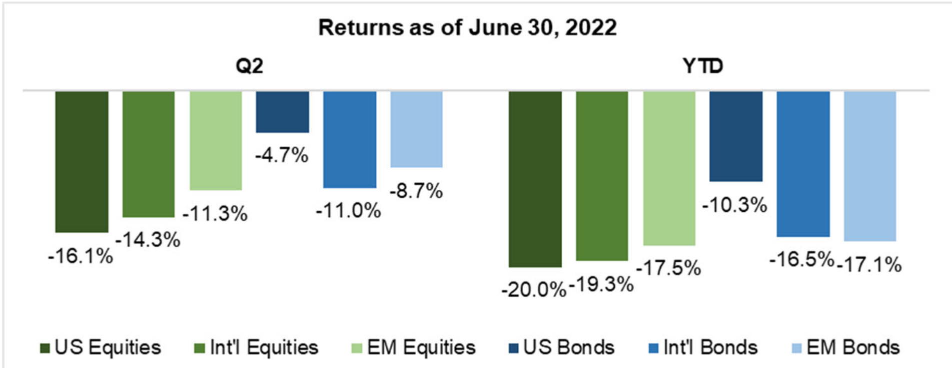
The good news for graduates is that the June employment report showed that, despite recession fears, the labor market remains strong. The net job gain of 372K was in line with the average job creation in the prior three months. Wage growth is moderating but the market remains tight- a factor that will likely support the Fed in its July 27th rate hike decision expected to be 75 basis points. While we expect an easing in demand as companies cope with cost pressures, the outlook for qualified workers is positive. It is also worth noting that, according to the Bureau for labor statistics, more Americans are self-employed than any time since the 2008 financial crisis.

The new entrants to the work force are receiving higher wages than ever before (we understand babysitters are making upwards of $25-30/hour in the Northeast!). Unfortunately, these wage increases force companies to raise prices while other input costs are high. As such, a moderation in inflation may be in the cards but we see a longer glide path to get to a manageable rate of inflationary growth. Supply chains will eventually fix themselves and a growth slowdown will curb demand so inflation will not remain at current elevated levels, but it could settle in above the 1-2% range we saw after the Global Financial Crisis due to tight labor markets, de-globalization and a commodity super cycle.

The most common question we receive is when will we hit bottom? Historically, getting to "the bottom" is a process. From a valuation standpoint, Stategas Research shared that the average P/E at "the bottom" of the bear market since 1942 has been 11.9. Today, the P/E ratio of the S&P 500 is around 15.5. They note that the composition of the index, among other variations (including profitability of firms in the S&P 500) over the years, should be considered when viewing this datapoint but it certainly allows for a further decline in equity prices on a pure valuation basis. In addition, they suggest that the Fed's ability to tame inflation will continue to come at a cost that may not have played out. Once we see a moderation in inflation, the market could be near a good inflexion point.

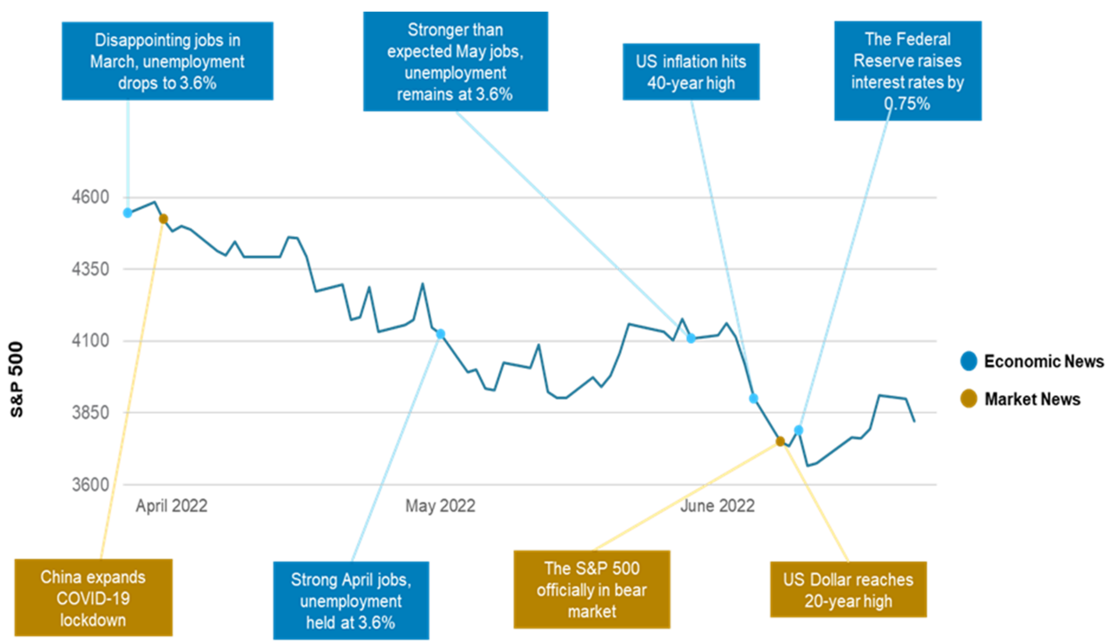
We expect the summer to remain challenged with elevated volatility. Many of the moves may be further exaggerated by machine trading, leverage, and rules-based programs that are part of today's investment landscape. On the plus side, fixed income may now be at a point where it can provide some of the ballast it has traditionally offered. Municipal bonds in particular look attractive currently. Below we discuss more of our outlook and thoughts on how we are approaching this environment.

Second Quarter Market Review



Source: Zephyr StyleADVISOR

- **Record high inflation, rising interest rates, and recession fears led stocks and bonds lower in the second quarter of 2022 (2Q22)**. For just the second time in 40 years, bonds and stocks both posted losses for two consecutive quarters.[i] US equities ended the quarter at -16.1% and entered an official bear market (defined as a drop of 20% from last peak). Despite the pain from the first half of 2022, US equities are still up an average of 8.4% per year over the last three years.[ii]



Source: Zephyr StyleADVISOR, Standard & Poor's, FactSet, CNBC, MarketWatch

[i] Source: Morningstar. 14 Charts on Market's Second-Quarter Performance

[ii] Source: FactSet

- **Within US equities, all 11 sectors suffered losses in Q2 22.** Amid recession fears, Consumer Staples and Utilities, often considered defensive sectors, suffered the least at -4.6% and -5.1% respectively. On the other hand, growth-oriented technology-related sectors like Communication Services and Consumer Discretionary, were the worst performers at -20.7%and -26.2% respectively. Energy is the only sector with positive returns of 31.8% for the year despite losses of 5.2% in the quarter. [i]

- **Rising interest rates continued to hurt growth stocks.** Growth stocks are often synonymous with the high-flying companies in the markets like technology while value stocks are often considered undervalued, steady, and sometimes even boring. The gap in performance between value and growth stocks across size and style was stark and was significantly in favor of larger and value-oriented segments as investors have sought safety amid looming uncertainties. Large cap value stocks outperformed large cap growth by 8.7% for the quarter and over 15% for the year. [i]

- **International equities fared better than US equities in Q2 22 despite the ongoing war in Ukraine and China's economic toll from zero COVID policy.** Developed international and emerging markets ended 2Q22 at -14.3 % and -11.3% respectively. A strong dollar also had a significant impact. Generally speaking, a stronger dollar translates to lower returns for international investments. This can be seen in its local currency returns for developed international, emerging markets which ended 2Q22 at -7.6% and -8.0% respectively. [i]

- **Bonds extend their losses in Q2 22.** US bonds fell 4.7% in the quarter led by the Fed's aggressive interest rate increases. After raising the rate by 0.25% in March, the Fed amped up its effort with a 0.5% increase to the funds rate in May followed by a 0.75% increase in June. Despite higher inflation, TIPS also fell 6.1% due to rising rates. Longer-term Treasuries, which have the greatest sensitivity to interest-rate changes, were the hardest hit and fell 11.9%. US high yield bonds fell 9.8% due to the flight to quality stemming from recession fears. Lastly, a stronger dollar and inflation woes also led international bonds lower for the quarter.[i]

- **With the exception of oil prices, broad commodities and gold also fell in Q2 22.** Oil prices extended their climb due to Russia's war against Ukraine. At the same time, key commodities including gold, wheat, and copper declined over concerns of a global economic slowdown. Gold prices fell 7.6% for the quarter and are down 1.5% for the year and gold has failed to meet expectations as an inflation hedge in 2022**.** Expectations for higher interest rates in the US led the dollar to rally 6.3% for the quarter and 9.1% for the year. Finally, US REITs lost 14.7% over concerns of rising costs due to higher interest rates. [i]

i Assetmark - June 2022 Quarterly Market Revuew

Stagflation

The World Bank recently announced their concern of a possible slowdown in global economic growth and a corresponding elevated risk of stagflation[1]. Inflation has stubbornly refused to decline, despite the Federal Reserve raising rates and promising to do more. This has placed concerns of stagflation back in the consciousness of investors, prompting questions as to what stagflation even is and whether or not we should be concerned about it.

Stagflation is a term used to describe periods of high inflation accompanied by declining GDP, and increased unemployment. This is a difficult place to be for your average consumer as their spending power erodes from high inflation coupled with high levels of unemployment, effectively decreasing overall consumer spending power. Before the 1960s, stagflation was widely thought impossible among economists who believed there is always an inverse relationship between inflation and unemployment. Until that time, economists had never documented periods of economic stagnation coupled with high inflation, hence the term "stagflation"[2].

The last time the US economy wrestled with stagflation was the 1970s when increases in international competition, decreases in manufacturing jobs, and an expensive war in Vietnam made inflation and unemployment soar[3]. This led President Nixon to institute a series of policy actions, known by many as the "Nixon Shock" to remedy inflation and protect jobs[4]. These policies were largely ineffective and served as the primary catalyst for 1970s stagflation which was only worsened by OPEC's series of oil embargos on the US. The spiraling inflation and increasing unemployment eventually forced Fed chair Paul Volker to trigger a recession to try to stop the momentum in inflation.

Fast forward to 2022 and we are experiencing soaring inflation primarily due to persistent global supply-chain disruptions, a war in Ukraine, Covid-19 lockdowns in China, and soaring wage growth. As the Fed continues to raise interest rates investors and consumers are wary of the dampening effect this could have on economic growth. This worry was only cemented by the World Bank's announcement on June 7th. According to the World Bank, global growth is expected to decelerate by 2.8 percent from 2021[5]. The outlook for global growth remains cloudy as the war in Ukraine continues to constrict global oil and grain supplies which put upward pressure on gas and food prices.

However, there are reasons to be optimistic that stagflation is not inevitable. Our current economic situation starkly diverges from the conditions of the 1970s: the dollar remains strong relative to other international currencies, the price increases in commodities are thus far much less than those seen in the 1970s, employment is strong, and the balance sheets for major global financial institutions remain robust[6]. Additionally, and most importantly, central banks across the world now have strict price and employment mandates that they have a three-decade-long track record of achieving their growth and inflation targets. Although the momentum of inflation is expected to be felt well into 2023, we believe that the actions of the Fed, an easing of supply chains, and inflation itself will help to reduce inflation well below its current levels.

[1] https://www.worldbank.org/en/news/press-release/2022/06/07/stagflation-risk-rises-amid-sharp-slowdown-in-growth-energy-markets
[2] https://www.investopedia.com/terms/s/stagflation.asp
[3] https://www.businessinsider.com/personal-finance/stagflation
[4] ibid
[5] https://www.worldbank.org/en/news/press-release/2022/06/07/stagflation-risk-rises-amid-sharp-slowdown-in-growth-energy-markets
[6] ibid

Outlook

In our last few commentaries, we have discussed the conundrum facing the Federal Reserve. The challenge of monetary normalization after years of easy money and the significant distortions it created is quite daunting. Unfortunately, the Fed has moved at a turtle's pace while inflation (NOT transitory), has raced ahead like a hare. The past quarter had investors sitting on edge as persistent high inflation reports suggested faster and higher rate hikes that the market quickly and painfully factored into prices. The result- the worst start to a year since 1950.

At the beginning of July, Chairman Powell indicated that the market had "gotten it right" with the current rate hike expectations. This assuaged the markets on the rate hike front leaving open the earnings season to provide signs on the health of corporate American. While we noted that the current price/earnings ratio of the S&P 500 has fallen to a level near the 25-year average, it could have further to fall if the expected earnings do not materialize as forecasted.

Below we have shared a view on earnings from Oxford Economics that is in line with many we have reviewed and makes sense to us as we feel that analysts have been slow to update their forecasts. They recently wrote that "the upcoming earnings season could prove challenging for US equities. Expectations for the second quarter itself have been revised lower in recent months and look achievable (at -2% ex-Energy), but the focus will be on company guidance for Q2 and beyond. We think the current consensus forecast for near 10% earnings growth over the next 12 months is too optimistic and is likely to be revised lower.

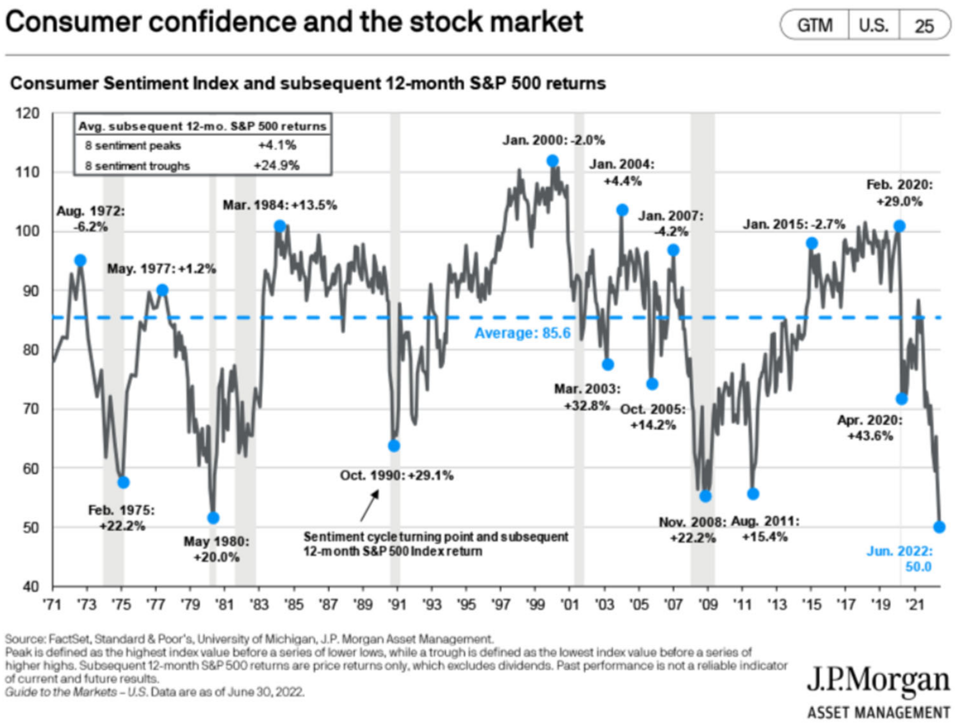
Although we agree with the consensus view that revenue growth will remain relatively healthy in the context of our soft-landing view, we are less sanguine on the outlook for profit margins. The bottom-up consensus forecast would suggest that we have already seen the entirety of the margin squeeze, but this seems unrealistic in the context of slowing economic activity and fading corporate pricing power. Indeed, our profit margin leading indicators have continued to deteriorate and now point to a much more marked decline in margins than bottom-up analysts expect. Falling profitability is likely to offset revenue growth and could drive a modest decline in US earnings over the next 12 months, even if a recession is avoided."

Rising interest rates, shrinking money supply, persistent inflation, and a potentially challenged earnings season implies more volatility as we move through the summer. On top of these concerns, we face policy uncertainty with the mid-term elections, the continued effects from the pandemic and the war in Ukraine, and the growing chorus of economist predicting an oncoming recession. We expect we will see many fits and starts throughout driven in part by some of the worst consumer sentiment and investor confidence readings we've seen in years- on a positive note, a contrarian indicator. Managing through this volatility has been and will continue to be difficult. So what are doing to adjust to this environment?

We continue to introduce structured credit and hedged investments into our portfolios and have added additional exposure to real assets in both public and private real estate. During the first half of the year, we were more conservative in our fixed income positioning and held higher levels of cash but have recently begun to add to fixed income, particularly municipal bonds where the valuations have become more compelling. We are neutral on growth vs value at this point as a compelling case can be made for either depending on one's view of the world over the coming months. As an example, the recent change in expectations suggesting that the Fed could be less aggressive and even accommodative later next year boosted growth stocks for a few day run while signs of a stronger economy (via the latest labor report) could mean faster tightening, a potential blow to growth stocks. The strong dollar has been a headwind for international stocks whose returns have been better than US returns when viewed in local currency. We continue to favor the US where we see better opportunities but will watch the dollar while we assess international investments. From a tax standpoint, the gyrations in the market continue to provide loss-harvesting opportunities that we are taking advantage of where possible.

Fund flows have not been supportive for markets as conviction remains elusive. The "buy the dip" mentality of years past is not in vogue. The good news is that according to Hartford Financial, the average length of a bear market is 289 days, or about 9.6$months. That's significantly shorter than the average length of a bull market, which is 991 days or 2.7 years. They also point out that "A bear market doesn't necessarily indicate an economic recession. There have been 26 bear markets since 1929, but only 15 recessions during that time" Bear markets often go hand in hand with a slowing economy, but a declining market doesn't necessarily mean a recession is looming. This topic will continue to be debated but the odds are growing that recession will hit within the next 18 months. The key will be the severity of the recession.

If history holds, we may be stuck in this morass for the remainder of the year owing to many of the factors cited above. As we look for bright lights, we remind ourselves that the markets have already discounted a good deal of economic and earnings slowdown (how much is still unclear of course), that markets have often done quite well following times when consumer confidence was extremely low (see below), and that markets have also, often, gotten a boost from mid-term elections. Private equity, flush with cash, may also be poised to step in and purchase companies whose valuations have come down and may be quite attractive.



Our headwinds/tailwinds summary is below.

<u>Headwinds</u>

- Federal Reserve tightening aggressively
- Inflation (commodity prices) staying high in a decelerating economy
- Supply chain issues and declining labor participation hampering economic growth
- Equity and fixed income valuations remain high on an historical basis despite the recent pullback
- Elevated corporate and government debt levels offset in part by healthier consumer balance sheets.
- Geopolitical risks are escalated with the war in Ukraine showing no signes of abating
- Covid still impacting the world with China potentially instituting more economically hurtful lockdowns.

Tailwinds

- Strong labor market
- Corporate buybacks are likely to be supportive
- Significant cash on the sidelines- hedge funds are holding a ton of cash!
- Healthy consumer and corporate balance sheets and continued consumer spending
- Earnings expectations are still positive in 2022

PRW News

PRW's Chief Investment Officer, Elliot Herman was quoted in the fortune.com article **The Fed just raised rates by half a point. Here's what financial advisers think you should do with your money**[i] by Megan Leonhardt and also in the cnbc.com article **Here's who should consider filing a tax extension and how to do it**[ii] by Kate Dore.

We look forward to connecting with you over the coming months. Enjoy the summer.

William A. Payne   Richard A. Renwick   Elliot B. Herman

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[i] The Fed just raised rates by a half point. Here's what financial advisers think you should do with your money – Fortune

[ii] Here's who should consider filing a tax extension and how to do it (cnbc.com)

Asset classes are represented by the following indexes:

US Equities	**S&P 500** – is an unmanaged index that is generally considered representative of the US equity market, consisting of 500 leading companies in leading industries of the US economy (typically large cap companies) representing approximately 75% of the investable US equity market.
International Equities	**MSCI EAFE** – is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of countries considered to represent developed markets, excluding the U.S. and Canada.
Emerging Markets Equities	**MSCI Emerging Markets** – is a free float-adjusted, market capitalization index that is designed to measure the equity market performance of countries considered to represent emerging markets.
China	**MSCI China -** measures the performance of small-cap equities in developed market countries around the world, excluding the U.S. and Canada. The index covers approximately 14% of the market cap in each country.
US Small Cap Growth	**S&P 600 Growth -** measures the performance of the small cap growth segment of the US equity market.
US Small Cap Value	**S&P 600 Value -** measures the performance of the small cap value segment of the US equity market.
US Mid Cap Value	**S&P 400 Value** – measures the performance of the mid cap value segment of the US equity market.
US Mid Cap Growth	**S&P 400 Growth** – measures the performance of the mid cap growth segment of the US equity market
US Large Cap Value	**S&P 500 Value** – measures the performance of the large cap value segment of the US equity market
US Large Cap Growth	**S&P 500 Growth** – measures the performance of the large cap growth segment of the US equity market
US Bonds	**Bloomberg US Aggregate** — measures the market of USD-denominated, investment grade, fixed-rate taxable bond market of SEC-registered securities, including bonds from the Treasury, government-related, corporate, mortgage-backed securities (agency fixed-rate and hybrid ARM passthroughs), ABS and CMBS sectors. US Agency Hybrid Adjustable Rate Mortgage (ARM) securities were added to the US Aggregate Index on April 1, 2007.
International Bonds	**Bloomberg Global Aggregate ex USD** - is a flagship hard currency Emerging Markets debt benchmark that includes fixed and floating-rate US dollar-denominated debt issued from sovereign, quasi-sovereign, and corporate EM issuers. Country eligibility and classification as Emerging Markets is rules-based and reviewed annually using World Bank income group and International Monetary Fund (IMF) country classification.
Emerging Markets Bonds	**Bloomberg Emerging Markets USD Aggregate** - is a flagship hard currency Emerging Markets debt benchmark that includes fixed and floating-rate US dollar-denominated debt issued from sovereign, quasi-sovereign, and corporate EM issuers. Country eligibility and classification as Emerging Markets is rules-based and reviewed annually using World Bank income group and International Monetary Fund (IMF) country classification.
TIPS	**Bloomberg US TIPS** - measures the performance of inflation-protected securities issued by the US Treasury.
US Long Treasuries	**Bloomberg Long Treasuries** - measures the performance of long-term US Treasury bonds, including all publicly issued securities that have a remaining maturity of ten or more years, are: non-convertible, denominated in US dollars, rated investment-grade, fixed-rate and have $250 or more of outstanding face value.
High-Yield Bonds	**Bloomberg US Corporate High Yield** - measures the market of USD-denominated, non-investment grade, fixed-rate, taxable corporate bonds. Securities are classified as high yield if the middle rating of Moody's, Fitch, and S&P is Ba1/BB+/BB+ or below. The index excludes emerging market debt.
Utilities	**S&P 500 Sector Utilities -** measures the performance of companies that product, generate, transmit or distribute electricity, water or natural gas, and also includes power producers & energy traders and companies that engage in generation and distribution of electricity using renewable sources.
Consumer Staples	**S&P 500 Sector Consumer Staples** - measures the performance of companies involved in the development and production of consumer products including: food and drug retailing, beverages, food products, tobacco, household products and personal products.
Communication Services	**S&P 500 Sector Communication Services -** measures the performance of companies from the media, retailing, and software & services industries in the U.S.

Consumer Discretionary	**S&P 500 Consumer Discretionary Sector** - measures the performance of companies involved in industries such as: automobiles and components, consumer durables, apparel, hotels, restaurants, leisure, media and retailing.
Real Estate	**S&P 500 Sector Real Estate** - measures the performance of companies from the following industries: real estate management & development and REITS, excluding mortgage REITS.
Energy	**S&P 500 Sector Energy -** measures the performance of companies involved in the development and production of crude oil, natural gas and provide drilling and other energy-related services.
US REITs	**FTSE NAREIT All Equity REIT -** measures the price of physical commodities futures contracts traded on US exchanges, except aluminum, nickel and zinc, which trade on the London Metal Exchange. Weightings are determined by rules designed to insure diversified commodity exposure.
Gold	**Bloomberg Sub Gold** - measures the price of gold futures contracts, reflecting the return of underlying commodity futures price movements quoted in USD.
Commodities	**Bloomberg Commodity** - dynamically rebalances exposure to maintain a 10% volatility target and represents portfolios consisting of the S&P 500 index and a cash component accruing interest. Uses S&P 500 methodology and overlays algorithms to control the index risk at specific volatility targets.
US Dollar	**US Dollar Index** - measures the value of the US dollar relative to the value of a 'basket' of currencies of the majority of the U.S.'s most significant trading partners. Factors the exchange rates of six major world currencies: euro, Japanese yen, Canadian dollar, British pound, Swedish krona and Swiss franc.

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