LSAM LIFESTYLE ASSET MANAGEMENT

Market Commentary

May 2022

Equity and Bond Market Update

(as of May 4, 2022)

Index	YTD	1-Year
Dow Jones Industrial Average TR	-5.7%	+1.7%
S&P 500 Total Return Index	-9.4%	+4.0%
Russell 2000 Total Return Index	-12.8%	-13.5%
MSCI EAFE Index (net)	-13.2%	-8.9%
MSCI Emerging Markets Index (net)	-13.1%	-18.5%
Barclays US Aggregate Bond TR	-9.4%	-8.5%

Recent Economic Indicators

	Statistic	Data as of
Unemployment Rate	3.6%	Mar 2022
Gross Domestic Product (GDP)	-1.4%	Q1 2022
Consumer Price Index (CPI)	+1.2%	Mar 2022
Consumer Confidence (1985=100)	107.3	Apr 2022
30-year fixed mortgage rate	5.42%	4/29/2022
Housing Starts (single family)	1,200,000	Mar 2022
10-Year Treasury Yield	2.97%	5/3/2022

Both stock and bond markets continued their theme of volatility over the last month, with almost all of the major indices (both equity and fixed income) trading down between -9% and -13% year-to-date. We experienced a short-lived relief rally yesterday when the Fed announced a 50 bp short-term rate hike, and transmitted the message during their post-meeting press conference that 75 bps hikes are off the table for now. One item to note is that the Fed did somewhat broadcast its expectations at this time to hike rates by 50bps at least at their next meeting in June, and possibly again in July, and then pull back to the customary 25bp hike at the remaining three meetings this year. This would leave the fed funds rate at a range of 2.50% to 2.75% by year's end. The 2-year Treasury is already currently trading with a yield of 2.73%. In addition, the Fed laid out it's plan to divest its balance sheet of the bonds it has purchased over the last two years.

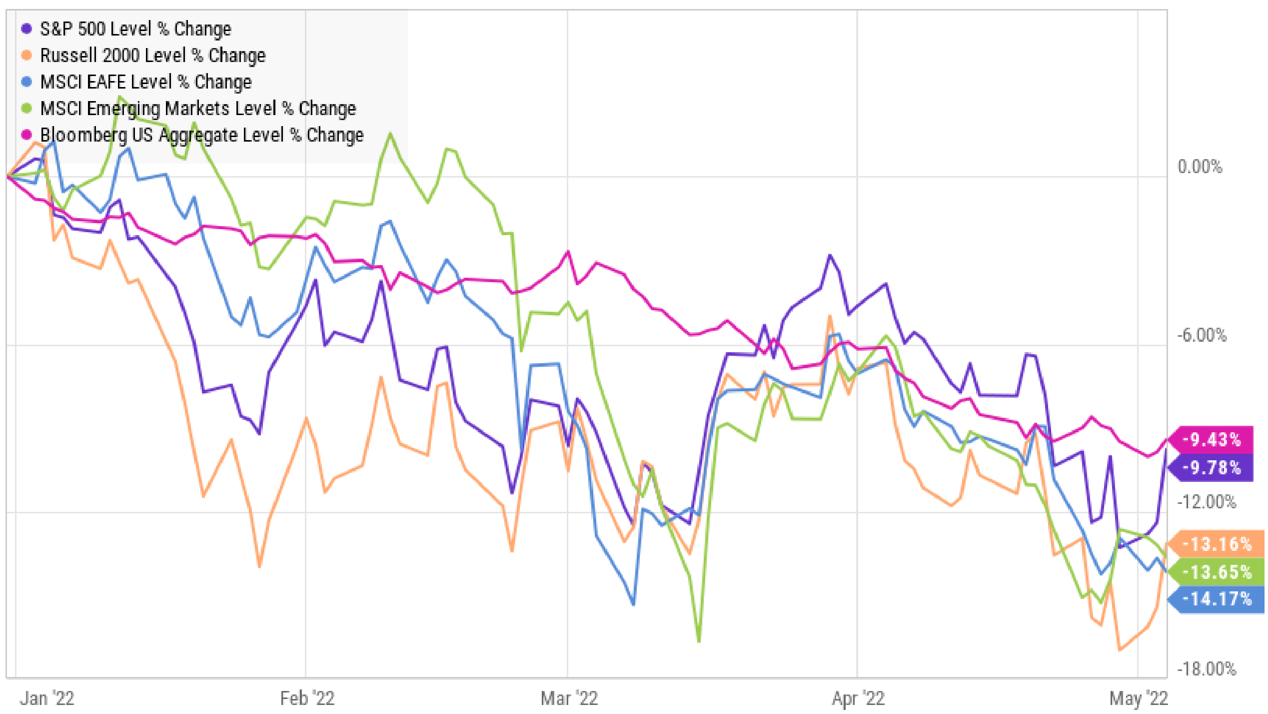
Barring any additional unforeseen damaging event, it is tough at this time to forecast seeing the 2-year Treasury trading with a yield too much higher than its current 2.73%, but we can't completely rule that out. Last time we saw the 2-year Treasury trade with a yield this high was back in the fourth quarter of 2018, where it maxed out around 2.92%; and before that all the way back to mid -2008 right in the middle of the financial crisis bear market. Currently, the only portion of the yield curve that is slightly inverted is past the 20-year Treasury, where there is a slight spread of -20bps between the 20-year and 30-year Treasury. As we have discussed previously, we have not experienced a recession (and associated bear market) over the last 30 years that was NOT preceded by an inversion of the 3-month to 10-year treasury spread. Currently this spread is at +204bps, so we have a long way to go before this factor comes into play.

Even with the negative GDP number we received last weak (-1.4% in Q1), we do not see this as a precursor to a follow-up negative GDP quarter, and would much rather combine this number with the fourth quarter of 2021 GDP of +6.9% to smooth out economic growth to +2.7% to +2.8% over the last six months, a more realistic statistic. It is no doubt that economic activity over the last 2 years has been volatile, and therefore believe it prudent to not segregate each quarter on its own, but smooth out consecutive quarters to get a better feel of the direction in which we are moving.

With stock values down over -10% this year, we are seeing attractive valuations we haven't seen since the beginning of the pandemic, when we were in the middle of the COVID recession. At that time, we were either just starting or in the middle of unprecedented economic shutdowns that decimated our economy for months to come at that time. Now we are not facing this. In fact, analysts are still forecasting close to 10% growth in corporate earnings this year over 2021, and another 10% growth in 2023 over this year. Couple this with a declining market, and stock values start to look more and more attractive. When things look bad, it is a ripe time to take action and establish long-term positions in investments that only just recently looked too overvalued. You may not realize the return benefits right away, but over the long-term, right now is the time to take action.

When perception and reality get decoupled like they are today, volatility and risk spike. We just briefly went through some fundamentals of why many stocks are good values today (or at least better than they were six months ago), so why isn't the market moving higher from here and why are we seeing all of this volatility? One historical trend in which we are currently is the mid-term election cycle. According to the Capital Group, year-to-date performance of the S&P 500 Index during a mid-term election year up to early November is around +2%,

Major Market Indices Price Return (YTD through May 4, 2022)



while all other years average around +7%. It is not until right after election day during these mid-cycle years does the S&P 500 index tend to start catching up to the norm, far outperforming all other years during those last two months of the year.

Of course, in addition to this mid-term election phenomenon, we also have all of the headline risks we have been fighting through since earlier this year: inflation, rising interest rates, the Russia-Ukraine conflict, etc. But we have seen all of these negative similar factors before in the past and have eventually come out just fine on the other side. Currently, we feel that inflation is in the process of peaking and will subside in the second half of this year, and that the negative feelings and effects of a rising rate environment have already been baked into stock and bond prices. No one can predict what will happen in Ukraine, so we can only keep a mindful eye for any positive progress.

Never forget that working with your advisor and planning your portfolio structure based on your specific financial situation before we get into periods of stress like we are now, are by far the most important inputs to successfully navigating through these volatile periods. By doing so, you are aware of what to expect ahead of time, and only need to stay on track and not deviate from your plan. Your risk tolerance (and associated portfolio construction) should not be affected by your current emotions regarding market conditions.

Always keep in mind that fear, panic, and optimism are not investment strategies, but rather emotions that drive short-term markets.

Please contact Lifestyle Asset Management, Inc. at (281) 612-2035 or by email at **pjackson@lsaminc.com** should you have any questions or comments.

Sources:

S&P Dow Jones Indices website (us.spindices.com)
MSCI Barra website (http://www.mscibarra.com)
The Conference Board (www.conference-board.org)
Bureau of Economic Analysis (www.bea.gov)
JP Morgan Guide to the Markets
FTSE Russell (www.ftserussell.com)
Bankrate.com (www.bankrate.com)
Bureau of Labor Statistics (www.bls.gov)
United States Census Bureau website (www.census.gov)