



## FULLEN FINANCIAL GROUP

### Quarterly Market Summary – Q2 2022

#### Market Results as of the Second Quarter of 2022

##### Selected Index Results for Q2 – 2022

<u>Index<sup>(1)</sup></u>	<u>%Growth For FY 2021</u>	<u>%Growth For YTD 2022</u>	<u>%Growth For Q2 2022</u>
DJIA	18.73%	-15.31%	-11.25%
Core U.S. Aggregate Bond Index (U.S. multi-sector bond)	-3.48%	-10.87%	-5.06%
S&P 500 (large cap)	26.89%	-20.58%	-16.45%
S&P 400 (mid cap)	23.21%	-20.16%	-15.77%
Russell 2000 (small cap)	13.69%	-23.93%	-17.49%
MSCI EAFE Index (developed international)	7.84%	-20.58%	-15.10%
iShares MSCI Emerging Market Index	-5.46%	-17.91%	-11.18%
iShares Dow Jones US Home Construction	48.60%	-36.69%	-11.41%
MSCI US REIT Index	38.61%	-21.52%	-17.67%
Amex Oil Index	48.67%	26.69%	-5.22%
Barclays Global Agg ex-US Corp Bond Index	-8.73%	-18.88%	-12.02%

(1) These results do not include reinvestment of dividends.

#### Q2 Quick Summary

- Global forecasts for economic growth were revised downward in the second quarter, due primarily to the ongoing supply shock from the war in Ukraine. Geopolitical uncertainties underlying supply chain and commodity pressures are unlikely to be fully resolved soon.
- The U.S. inflation rate reached 9.1% in June, the highest year-over-year inflation reading since November 1981. Although supply chain pressures have eased somewhat in the U.S., inflation has proved to be more persistent than expected.
- The U.S. labor market continues to perform better than expected, and labor demand remains near historic highs. The U.S. economy added 372,000 non-farm payroll jobs in June versus a forecast of 250,000.
- Global consumer sentiment has taken a negative turn as surging costs for essentials (food, energy, and shelter) have combined with rapidly tightening financial conditions. The U.S. Federal Reserve raised the benchmark borrowing rate by 0.75% in June and is expected to continue to raise rates aggressively.
- In China, Covid continues to dictate the economic trajectory as the country's zero-Covid policy led to lockdowns in multiple cities this spring. The risk of another wave of infections, and resultant supply chain disruptions, remains as the virus continues to circulate globally.

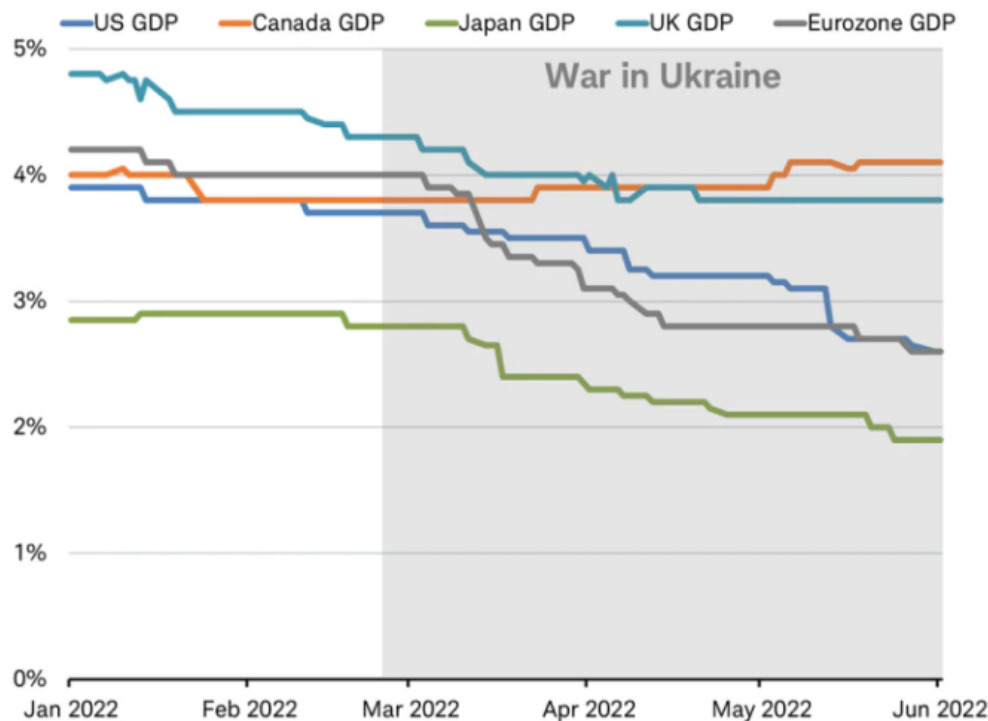


## Economic Uncertainty Is High

Stocks around the world slumped during the second quarter as economic uncertainty surged with the war in Europe, a lockdown-induced recession in Asia's biggest economy, stubbornly high inflation, and several major central banks pursuing the most aggressive series of policy rate increases in decades. Only the more commodity-based economies of Canada, Australia, and the U.K. fared noticeably better than others, when measured in U.S. dollars.

It's often said that markets hate uncertainty. In the first half of 2022, economic uncertainty in Europe was higher than during the height of the COVID-19 pandemic. Also, it was higher than any other time in the past two decades, except right after the Brexit referendum in June 2016, according to the Economic Policy Uncertainty indexes developed by Baker, Bloom and Davis, a well-respected economic research team from Northwestern, Stanford and the University of Chicago.

Concerns over a global economic recession have grown this year, due primarily to high inflation, further boosted by the war in Ukraine, and central bankers' efforts to tamp down inflation through tighter monetary policy. Economists' 2022 GDP forecasts have slumped in the first half of the year for most major countries with growth estimates cut by 1% or more, as you can see in the chart below. Canada is the exception, thanks to strong demand for its natural resources.



Source: Charles Schwab, Bloomberg data as of 6/1/2022

In contrast to this weaker economic outlook, analysts have been raising earnings per share estimates, and most countries have seen earnings estimates climb meaningfully since the start of the year. It is rare to see a divergence in the direction of the economic and earnings forecasts but it does have positive implications for stock values.



While investors have been focused on the slowdown in the economic outlook for much of the first half of the year, the direction of earnings may be more important to stock prices than GDP for the second half. If earnings remain solid, stocks may rebound. But should we begin to see the earnings outlook deteriorate, low valuations may not protect against further declines.

### **No Inflation Relief Yet**

The U.S. economy remains under significant pressure from inflation. The Consumer Price Index (CPI), driven largely by surging food and energy prices, accelerated at a 9.1% annual rate in June—the highest since November, 1981. Energy spending as a percentage of total consumer spending has grown over the past year and is approaching 1%, a level that heightens stress for consumers—particularly lower-income consumers, who spend a greater share of their household income on items like gasoline.

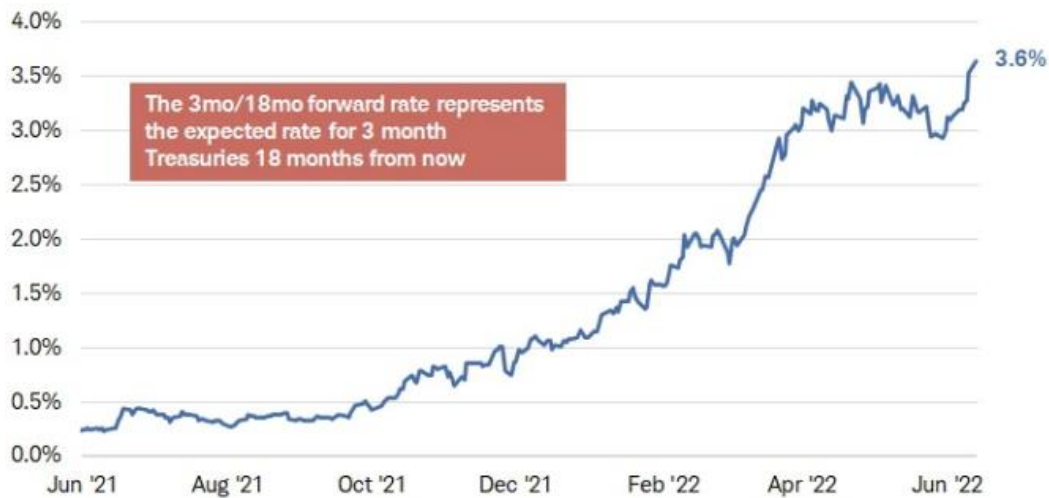
That said, food and energy aren't solely to blame for inflation. At this point, prices are up across many categories. Alternative measures that attempt to deliver a less "noisy" read on inflation (by screening out volatile categories or focusing on the median) are also rising at their fastest rates on record. The Dallas Fed excludes the most extreme price changes in consumer goods and services each month, while the Cleveland Fed excludes all price changes except for the one in the center of the distribution of price changes. These measures' acceleration suggests that taming inflation in food and energy alone won't solve the problem.

Even wealthier consumers, who can often rely on greater savings or a stronger stock market, could be feeling the pinch as stocks have fallen. The annual change in the S&P 500® Index has dipped into negative territory and is down 12.7% from one year ago—the worst annual return since the global financial crisis. While that may not translate into actual losses for investors who haven't sold investments, even paper losses can hurt households' confidence.

### **The Fed Gets Serious About Inflation**

Heading into this year, many economists predicted interest rates would rise gradually to meet the challenges of inflation. But the war in Ukraine sent energy prices spiking, and supply-chain problems were more prolonged than expected, causing inflation to spike sharply higher. The resulting message from the Fed was loud and clear: It will tighten policy "expeditiously" until inflation comes down. The Fed Funds target rate is now expected to reach 3% or more by the end of 2022. After that, it's likely that the pace of rate hikes will slow, as tightening financial conditions should lead to a slower economy and lower inflation. The market is pricing in a fed funds rate of as high as 3.6% by the end of 2023.

As with any tightening cycle, the risk of recession is rising. Based on past tightening cycles, the chances of the Fed achieving a "soft landing" for the economy are not great. There have been six Fed tightening cycles since the early 1980s, and over that period there have been only two tightening cycles (1994 and 1984) that avoided a decline into recession.



Source: Bloomberg

Even with the rising risk of recession, it's worth noting that each one is unique. The current environment seems most similar to the early 1980s. Inflation was high in large part due to oil price spikes. In response, the Fed raised nominal and real interest rates aggressively. The economy was otherwise relatively healthy, with a solid banking system and consumers who weren't overextended on debt. Nonetheless, there were two steep back-to-back recessions during that time period, from January to June 1980, and from July 1981 to November 1982. Housing and manufacturing experienced sharp declines and the unemployment rate soared to double-digit levels.

While the Fed is determined to push inflation lower, there's a good chance it won't have to go to the extremes of the early 1980s. Demographic trends are far different with the U.S. population aging. That tends to result in slower growth and inflation. Another key difference in policy this time around is the use of "forward guidance" by the Fed. In the 1980s the Fed provided very little information about its plans to the markets. Consequently, rate hikes often surprised investors, consumers, and businesses—increasing volatility. This time around the markets should be able to anticipate changes, mitigating some of the surprise factor that can create added volatility.

### Supply Chain Uncertainties Remain

Severe lockdowns in response to the latest COVID-19 outbreaks resulted in a sharp economic slowdown in China—the world's second largest economy—but as restrictions began to lift, economic data began to sharply rebound. As people were able to leave their homes in major cities and economic stimulus accumulated, the surprisingly big gains in China's May Purchasing Managers' Index suggest the worst of the economy's slump may be over. Covid continues to be a wild card, however, as the pandemic is still with us, and the emergence of new variants could result in renewed restrictions that hamper the supply chain.



While supply chains remain stretched and delivery times are still lengthy, they have shown some signs of improvement. Inventories have been rebuilding, with some retailers such as Walmart, Kohl's, and Target reporting excess inventories in some products in May.

## **Conclusions**

Economic uncertainty may be reaching a peak, but we believe it will remain high for the remainder of this year. Having a well-balanced, diversified portfolio, with a risk profile consistent with your goals, and being prepared with a plan in the event of an unexpected outcome are keys to successful investing.

Projecting stock market direction is always rife with problems, doing so in such an environment can quickly make even the most thoughtful projections irrelevant. In a rapidly growing economy with rising inflation, assets with exposure to high nominal growth rates, including value stocks and commodities, may hold up well, whereas bonds could struggle. Should tightening Fed policy, higher inflation or a change in consumer sentiment start to weigh heavily on the economy, however, bonds will be seen as a safe-haven alternative to equities. This highlights the benefits of a well-diversified portfolio and a consistent investment strategy to navigate through the volatility.

Fundamentally, stock valuations are based on long-term expectations for dividend payments and price appreciation. Assuming continued success in combatting the virus and returning the economy to more “normal” levels of activity, the long-term impact on economic growth and equity values should not be significant. However, as we have stated previously, the ongoing and unprecedented level of government stimulus, both fiscal and monetary, continues to raise concerns about deficit spending and the corresponding growth in national debt. While such stimulus may be critical in times of stress, the long-term implications for economic growth are likely to be negative. In the near term, uncertainties around these policies (among other developments) will likely result in continued high levels of market volatility.

In periods of higher market volatility, maintaining investment discipline will be more difficult emotionally. However, we need to remember that market timing as an investment strategy has never worked consistently (and results in lower longer-term yields). Trying to time markets has a high probability of creating permanent losses.

As always – stay with a consistent and disciplined investment strategy – it is the only course of action with any track record of success (in any investment environment). There is no reason to believe, even with the changing economic dynamics, that the disciplined approach to investments will be less effective than in the past at delivering the best possible relative returns.

At the most fundamental level, match your investment time horizon to your spending timeline – if you have short term cash needs then those funds should be in short term investments. These are simple asset/liability matching principles practiced by the most sophisticated investment managers every day (but far too complex to explain in sound bites and not conducive to selling products). Additionally, don't try to solve short-term financial problems with long-term equity exposure. If you try to chase returns, you may get lucky sometimes but, if pursued long enough, it always ends in extreme frustration and often with serious financial losses. The reality is that no one has ever consistently predicted investment markets and they never will - and there is always a consequence to continued unsound financial behavior.

As always, if your personal or family situation has changed (or is likely to), a discussion with us as to how this may impact your financial plan and your overall asset allocation is warranted. Or, if you simply



feel a need to discuss any aspect of your portfolio and/or financial plan, or you haven't had a planning update within the last 12 months, please contact us to review your financial plan and investments.

### **Risks**

Investors should be aware of the risks associated with all portfolio strategies and variable market conditions. Monetary policy changes, military activity abroad, the level and change in market interest rates, corporate earnings, domestic and foreign governmental policies, global economic data, vaccine missteps, other geopolitical events can have a substantial effect on portfolio performance and the effectiveness of strategic and tactical portfolio approaches.

**Your financial plan is the most important financial document that you possess! Keep it updated and use it.**

Please note that you are entitled to receive Fullen Financials' Form ADV whenever you would like to. This document outlines many details of who Fullen Financial is, their investment methodologies and their advisor's education and experience. You may do so by contacting Paula Miller (paula@fullenfinancial.com) and requesting such. Alternatively, you can go to the Fullen Financial website at [www.fullenfinancial.com](http://www.fullenfinancial.com) and click on "Resources" in the top menu bar, and then on "Client Forms."

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## Appendix: Economic Indicators and Outlook

Economic Indicators: G7 & Europe				
	2020	2021	2022F	2023F
Real GDP (annual per cent change)				
<b>G7 (30.1%)*</b>	-5.0	5.1	2.4	1.4
U.S.	-3.4	5.7	2.2	1.4
Japan	-4.5	1.7	2.0	1.5
Euro Area	-6.5	5.4	2.6	1.3
Germany	-4.9	2.9	1.8	1.5
France	-8.0	7.0	2.8	1.3
Italy	-9.1	6.6	2.6	1.1
United Kingdom	-9.3	7.4	3.6	0.8
Canada	-5.2	4.5	3.7	1.7
Consumer Price Index (annual per cent change)				
<b>G7</b>	0.9	3.3	6.8	3.3
U.S.	1.2	4.7	7.9	3.3
Japan	0.0	-0.2	2.0	1.4
Euro Area	0.3	2.6	7.2	3.6
Germany	0.4	3.2	7.3	3.5
France	0.5	2.1	5.3	2.9
Italy	-0.1	1.9	6.6	3.2
United Kingdom	0.9	2.6	8.4	5.7
Canada	0.7	3.4	6.7	3.5
Unemployment Rate (per cent annual averages)				
U.S.	8.1	5.4	3.6	4.0
Japan	2.8	2.8	2.6	2.5
Euro Area	8.0	7.7	7.0	7.2
Germany	5.9	5.7	5.0	5.0
France	8.0	7.9	7.2	7.5
Italy	9.3	9.5	8.4	8.7
United Kingdom	4.5	4.5	3.8	4.1
Canada	9.6	7.4	5.3	5.8
*Share of 2019 world gross domestic product (GDP) at PPP. Forecast as at June 2022. Source: National statistics agencies, TD Economics.				

Global Economic Outlook				
Annual Per Cent Change Unless Otherwise Indicated				
	2019 Share*	Forecast		
Real GDP	(%)	2021	2022	2023
<b>World</b>	100.0	6.1	2.9	2.7
<b>North America</b>	19.2	5.5	2.3	1.5
United States	15.8	5.7	2.2	1.4
Canada	1.4	4.5	3.7	1.7
Mexico	1.9	5.0	2.0	2.0
<b>European Union (EU-28)</b>	15.4	5.3	2.7	1.4
Euro Area (EU-19)	12.5	5.4	2.6	1.3
Germany	3.5	2.9	1.8	1.5
France	2.4	7.0	2.8	1.3
Italy	2.0	6.6	2.6	1.1
United Kingdom	2.4	7.4	3.6	0.8
EU accession members	2.9	5.4	3.5	1.7
<b>Asia</b>	43.2	6.6	3.6	4.2
Japan	4.1	1.7	2.0	1.5
Asian NIC's	3.5	5.3	2.8	2.8
Hong Kong	0.3	6.4	1.0	3.4
Korea	1.7	4.0	2.6	2.7
Singapore	0.4	7.6	3.8	2.6
Taiwan	0.9	6.4	3.4	2.9
Russia	3.1	4.8	-9.8	-3.3
Australia & New Zealand	1.2	4.7	4.0	3.0
Emerging Asia	31.4	7.6	5.2	5.5
ASEAN-5	5.7	3.3	5.4	5.0
China	17.3	8.4	4.0	5.2
India**	7.1	9.0	8.2	6.6
<b>Central/South America</b>	5.6	7.6	2.3	1.8
Brazil	2.4	5.0	0.8	1.3
<b>Other Emerging Markets</b>	13.0	5.7	2.0	1.9
<b>Other Advanced</b>	1.1	5.0	3.6	2.3
*Share of world GDP on a purchasing-power-parity (PPP) basis. Forecast as at June 2022. **Forecast for India refers to fiscal year. Source: IMF, TD Economics.				

**Important Disclosures:** This material is for informational purposes only. It is not intended as and should not be used to provide investment advice and is not an offer to sell a security or a recommendation to buy a security. This summary is based exclusively on an analysis of general market conditions and does not speak to the suitability of any specific proposed securities transaction or investment strategy.

Judgement or recommendations found in this report may differ materially from what may be presented in a long-term investment plan and are subject to change at any time. This report's authors will not advise you as to any changes in figures or views found in this report.



Investors should consult with their investment advisor to determine the appropriate investment strategy and investment vehicle. Investment decisions should be made based on the investor's specific financial needs and objectives, goals, time horizon and risk tolerance.

Except for the historical information contained in this report, certain matters are forward-looking statements or projections that are dependent upon risks and uncertainties, including but not limited to such factors and considerations such as general market volatility, global economic risk, geopolitical risk, currency risk and other country-specific factors, fiscal and monetary policy, the level of interest rates, security-specific risks, and historical market segment or sector performance relationships as they relate to the business and economic cycle.