

Stocks & Bonds Rally as Investors Debate Federal Reserve Policy

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Monthly Market Summary

- The S&P 500 Index produced a +9.2% total return during July, underperforming the Russell 2000 Index's +10.6% total return.
- All eleven S&P 500 sectors produced positive returns during July. Consumer Discretionary (+18.4%) and Tech (+13.5%) were the top performers after underperforming during the first half of 2022. Defensive sectors, such as Health Care (+3.2%), Consumer Staples (+3.2%), and Utilities (+5.4%), underperformed as the S&P 500 rallied.
- Corporate investment grade bonds generated a +4.4% total return, underperforming corporate high yield bonds' +6.7% total return.
- The MSCI EAFE Index of global developed market stocks returned +5.2% during July, while the MSCI Emerging Market Index generated a -0.3% return.

Equity & Credit Markets Rebound After June Selloff

Stocks and bonds both rallied during July after selling off during the second half of June due to recession fears. Riskier asset classes, such as small cap stocks and high-yield corporate bonds, outperformed as investor sentiment turned slightly more positive. Why the change in attitude? Multiple catalysts could be causing the turnaround, one of which includes investor sentiment being too negative entering July. Second quarter 2022 earnings season kicked off during the month, and early results suggest Wall Street's expectations were too low. While the rate of earnings growth is slowing, the overall tone appears to be less bad than feared with commentary from company management teams more optimistic than expected.

One interesting narrative starting to show up in headlines – weak economic growth could cause the Federal Reserve to stop raising interest rates sooner, which could boost investor sentiment and relieve pressure on stocks and bonds. Data indicates the U.S. economy shrank during the second quarter, which would mark the second consecutive quarter of negative GDP growth. Two consecutive quarters of negative GDP growth is the technical definition of a recession, and now there's a debate about whether the U.S. is already in a recession. As discussed below, the prospect of a shorter interest rate hike cycle will be hotly debated over the coming months.

The Big Debate – Price Stability vs Maximum Employment

Congress has given the Federal Reserve a dual mandate to pursue price stability and maximum employment. What does this mean? The Fed defines price stability as ~2% annual inflation, but maximum employment is more difficult to define because many factors affect the structure and dynamics of the labor market. The Fed's own

definition acknowledges this: “The maximum level of employment is a broad-based and inclusive goal that is not directly measurable and changes over time ...”

Where is the Fed’s attention focused currently? Price stability. The Consumer Price Index accelerated +9.1% year-over-year during June, which was the fastest pace since 1981. In contrast, the unemployment rate held steady at 3.6% during June. The Fed’s interest rate increases are intended to promote price stability, but they come with an embedded risk. Higher interest rates relieve inflation pressures by reducing demand for goods and services, which could slow economic growth. The risk is interest rate increases slow the economy and increase unemployment, pressuring the Fed to focus more on its maximum employment mandate and less on inflation and price stability.

The stage is set for a debate. Is price stability or maximum employment more important? The Fed previously stated it’s willing to accept higher unemployment and slower economic growth to bring inflation under control, but the question is how much. A lower tolerance for unemployment could cause the Fed to slow or stop its interest rate hikes sooner, while a higher tolerance for unemployment could give the Fed cover to continue raising interest rates higher and longer. The answer has major implications for both Federal Reserve policy and asset class returns.

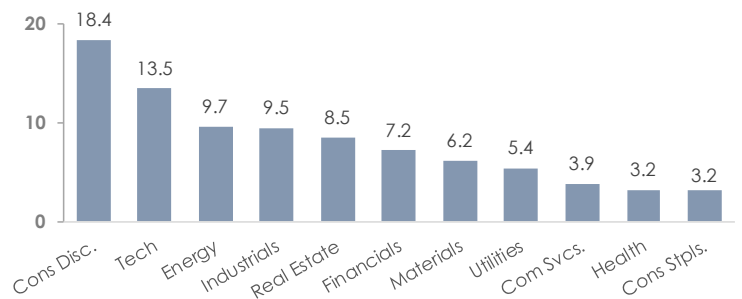
THIS MONTH IN NUMBERS

FIGURE 1
U.S. Style Returns (July in %)

	Value	Blend	Growth
Large	6.6	9.2	12.1
Mid	8.7	9.8	12.2
Small	9.6	10.6	11.3

Data Reflects Most Recently Available As of 7/31/2022

FIGURE 2
U.S. Sector Returns (July in %)



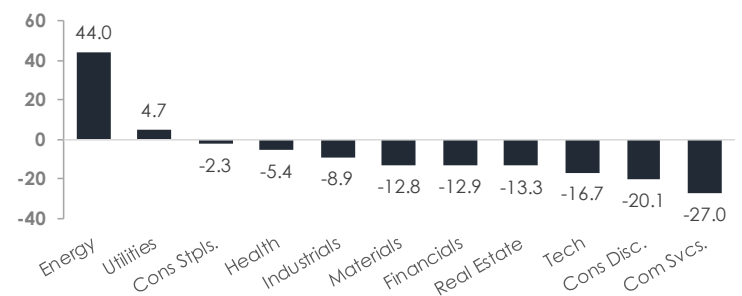
Data Reflects Most Recently Available As of 7/31/2022

FIGURE 3
U.S. Style Returns (YTD in %)

	Value	Blend	Growth
Large	-7.2	-12.6	-19.5
Mid	-9.1	-13.9	-22.6
Small	-9.5	-15.4	-21.5

Data Reflects Most Recently Available As of 7/31/2022

FIGURE 4
U.S. Sector Returns (YTD in %)



Data Reflects Most Recently Available As of 7/31/2022

FIGURE 5
Market Data Center

Stocks	Level	1 month	3 months	YTD	1 year	3 years
S&P 500	4,130	9.2%	0.4%	-12.6%	-4.7%	44.3%
Dow Jones	32,845	6.8%	0.2%	-8.6%	-4.2%	28.9%
Russell 2000	4,685	10.6%	1.5%	-15.4%	-14.3%	23.5%
Russell 1000 Growth	1,630	12.1%	0.7%	-19.5%	-12.1%	54.9%
Russell 1000 Value	939	6.6%	-0.8%	-7.2%	-1.6%	27.2%
MSCI EAFE	1,249	5.2%	-2.1%	-14.6%	-13.5%	12.0%
MSCI EM	59,422	-0.3%	-4.9%	-17.5%	-20.4%	2.9%
NASDAQ 100	12,948	12.6%	0.9%	-20.5%	-13.0%	67.8%

	Dividend Yield	NTM P/E	P/B
S&P 500	1.46%	17.1x	4.1x
Dow Jones	1.85%	16.4x	4.4x
Russell 2000	1.20%	18.3x	2.1x
Russell 1000 Growth	0.67%	23.3x	10.5x
Russell 1000 Value	1.86%	13.6x	2.4x
MSCI EAFE	4.58%	12.2x	1.6x
MSCI EM	2.74%	11.0x	1.7x
NASDAQ 100	0.59%	21.0x	6.7x

Fixed Income	Yield	1 month	3 months	YTD	1 year	3 years
U.S. Aggregate	3.42%	2.5%	1.7%	-7.9%	-8.9%	-0.2%
U.S. Corporates	4.38%	4.4%	2.5%	-12.3%	-13.5%	0.5%
Municipal Bonds	3.37%	2.3%	2.2%	-5.8%	-5.9%	1.6%
High Yield Bonds	7.72%	6.7%	0.8%	-8.0%	-6.9%	3.5%

Commodities	Level	1 month	YTD
Oil (WTI)	98.30	-7.1%	30.7%
Gasoline	3.16	-16.4%	42.0%
Natural Gas	8.29	53.7%	132.9%
Propane	1.15	-5.2%	10.4%
Ethanol	2.49	-7.8%	1.4%
Gold	1,783	-1.4%	-2.5%
Silver	20.33	-0.1%	-12.9%
Copper	3.58	-3.5%	-19.6%
Steel	855	-2.8%	-40.4%
Corn	6.22	0.4%	4.9%
Soybeans	16.17	-6.5%	23.2%

Key Rates	7/31/2022	6/30/2022	4/30/2022	1/31/2022	7/31/2021	7/31/2019
2 yr Treasury	2.90%	2.93%	2.69%	1.16%	0.18%	1.87%
10 yr Treasury	2.64%	2.98%	2.89%	1.78%	1.23%	2.02%
30 yr Treasury	2.98%	3.12%	2.94%	2.10%	1.89%	2.53%
30 yr Mortgage	5.40%	5.90%	5.41%	3.78%	2.98%	3.87%
Prime Rate	5.50%	4.75%	3.50%	3.25%	3.25%	5.50%

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