



Cerity Partners Market & Economic Update

August 10th, 2022

Q3 2022
**Economic and
Market Outlook:**

Volatility Returns



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Key Themes

2022

Short Term Themes

1. U.S. consumers strength tested by higher commodity prices and tighter monetary policy
 2. Cyclical Stocks Make a Second Comeback
 3. The Economy Hits Growth Recession, Not an Economic Recession
 4. Stocks Find a Floor Around Current Levels
 5. Rates Normalize To a Slower Growth Environment
 6. Labor Market Strength Reaching a Peak
 7. Inflation Declines Due to Inventory Build-Up and Hand Off From Goods To Services
 8. China Is No Longer the Driver of World Economic Growth
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Long Term Themes

1. Continued Financial Repression Necessitates a Never-ending Search for Yield (Watch Real Yields)
 2. Transition Towards Clean Energy/ ESG Driver in the Commodity Markets (demand and supply)
 3. Supply Chain Onshoring to Propel Economic Expansion
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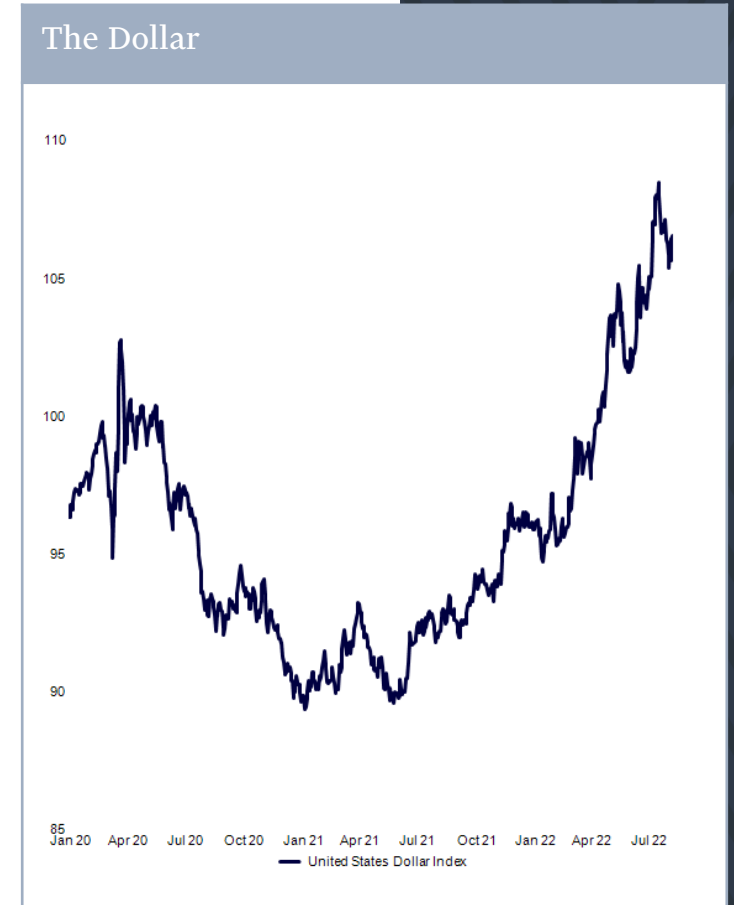
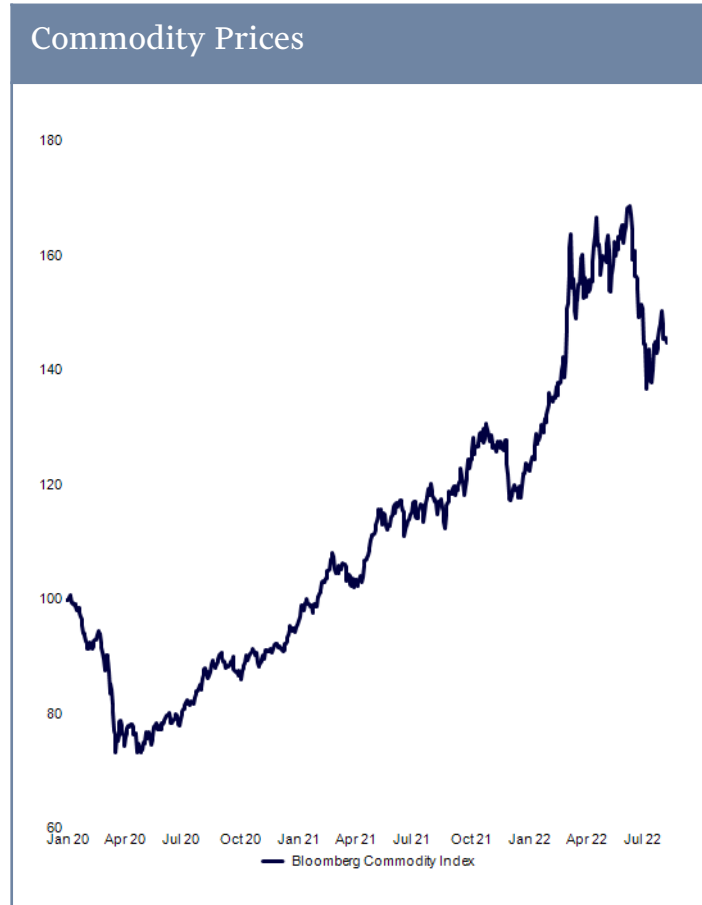
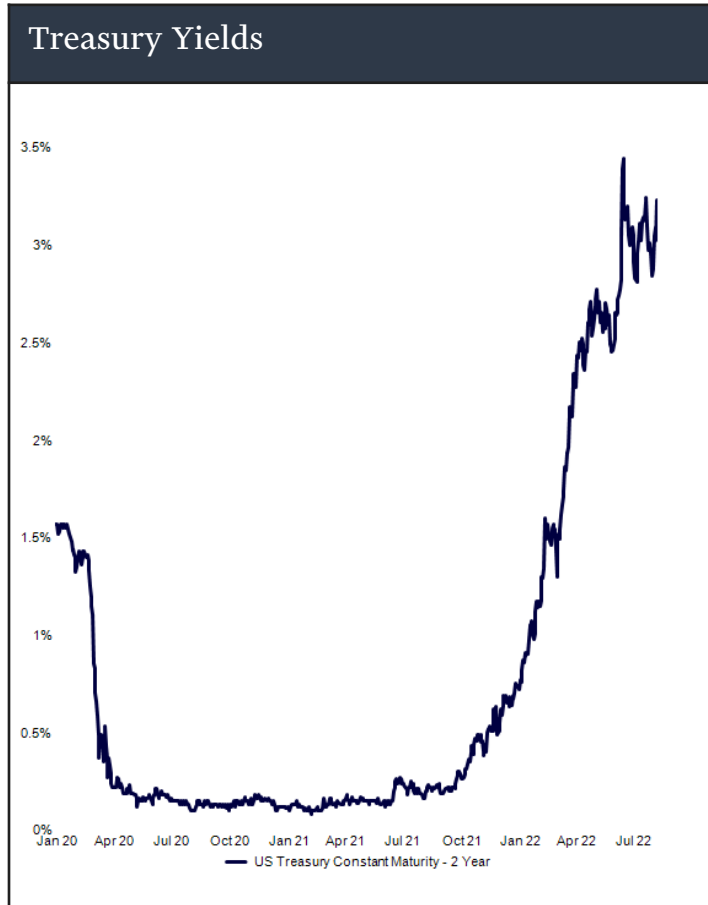
The Big Risks

The market is facing a basket of risks.



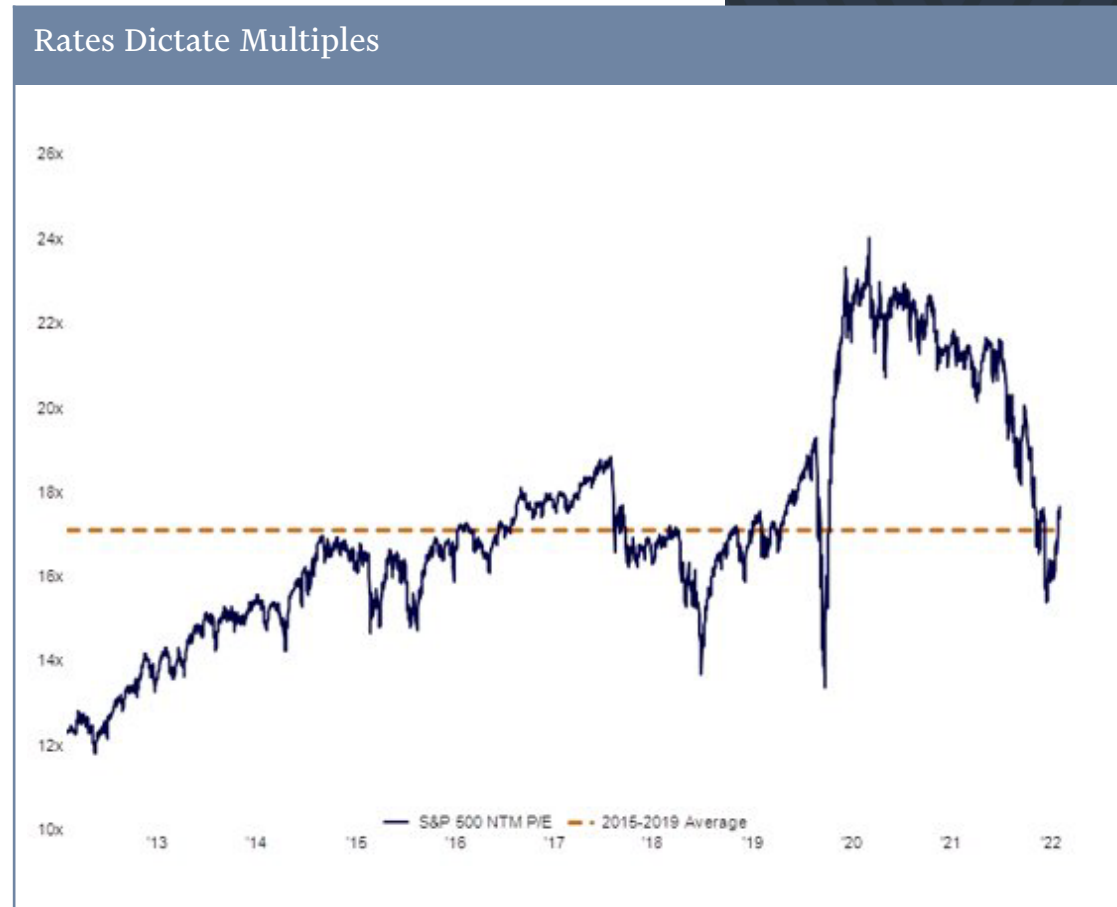
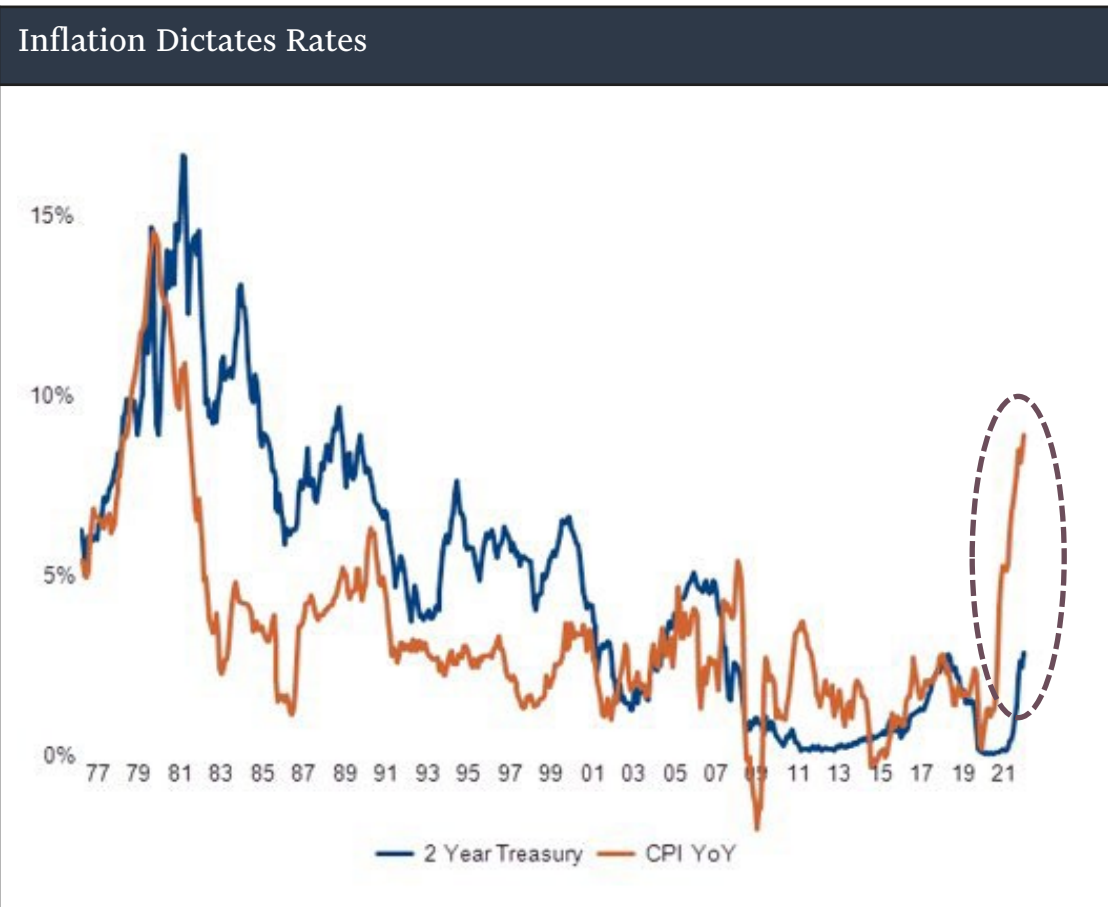
The Triple Witching

The markets have faced tightening financial conditions, though starting to ease.



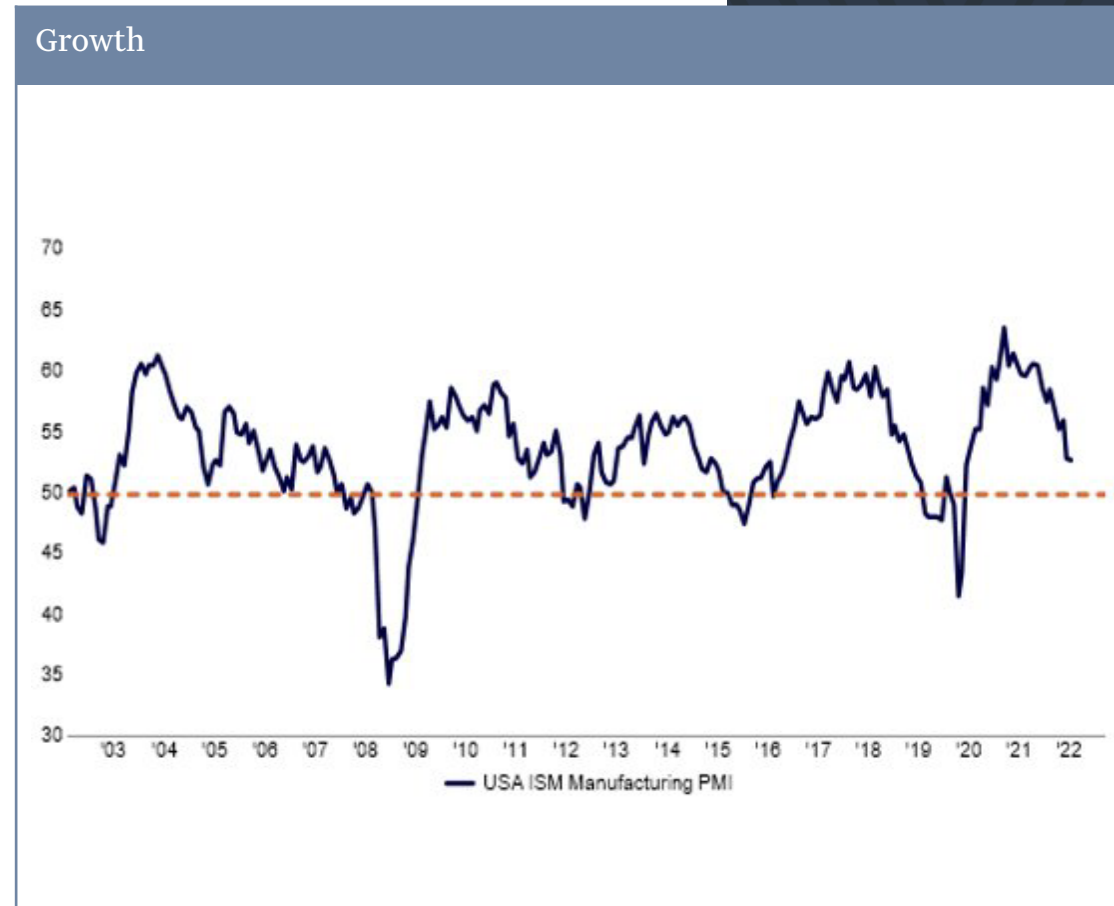
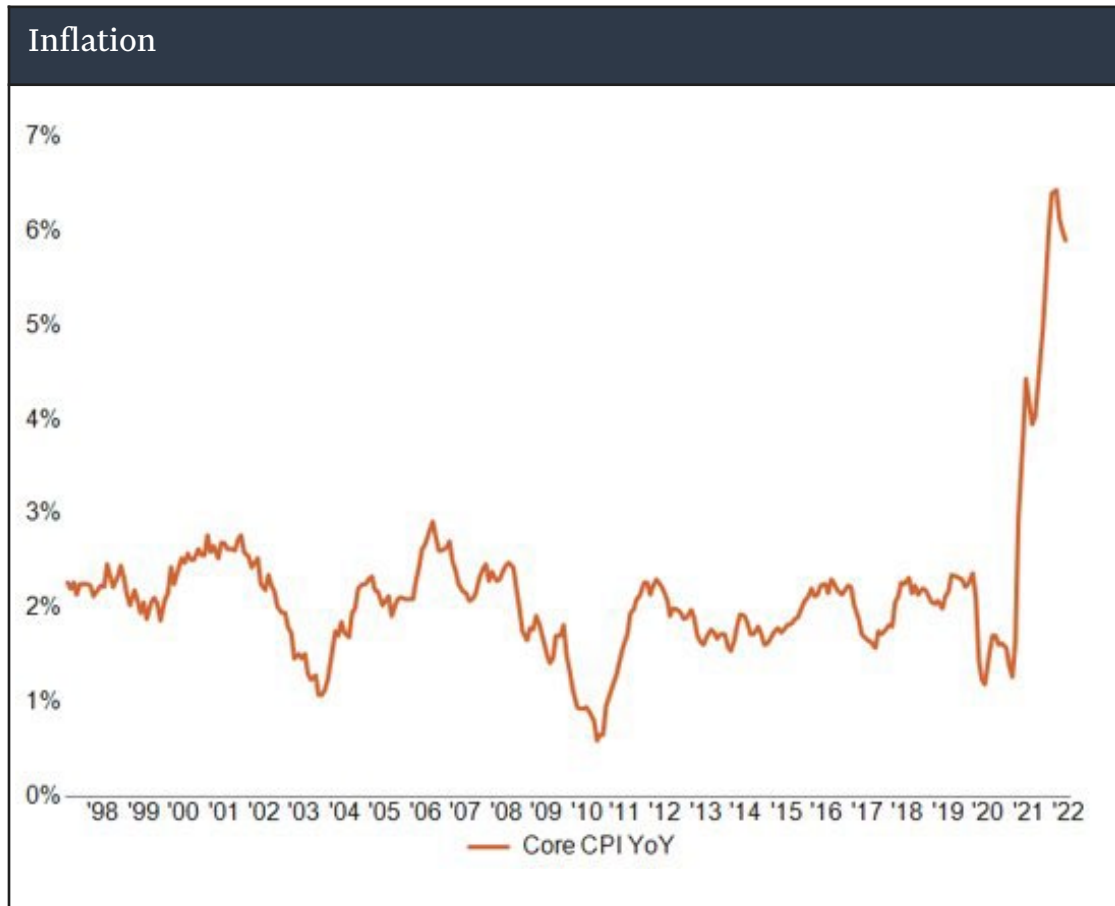
1H Was All About Inflation

If you could forecast inflation, you could probably forecast the market.



2H Is All About Growth

Economic and earnings growth will be the key to forecasting the back half of 2022.



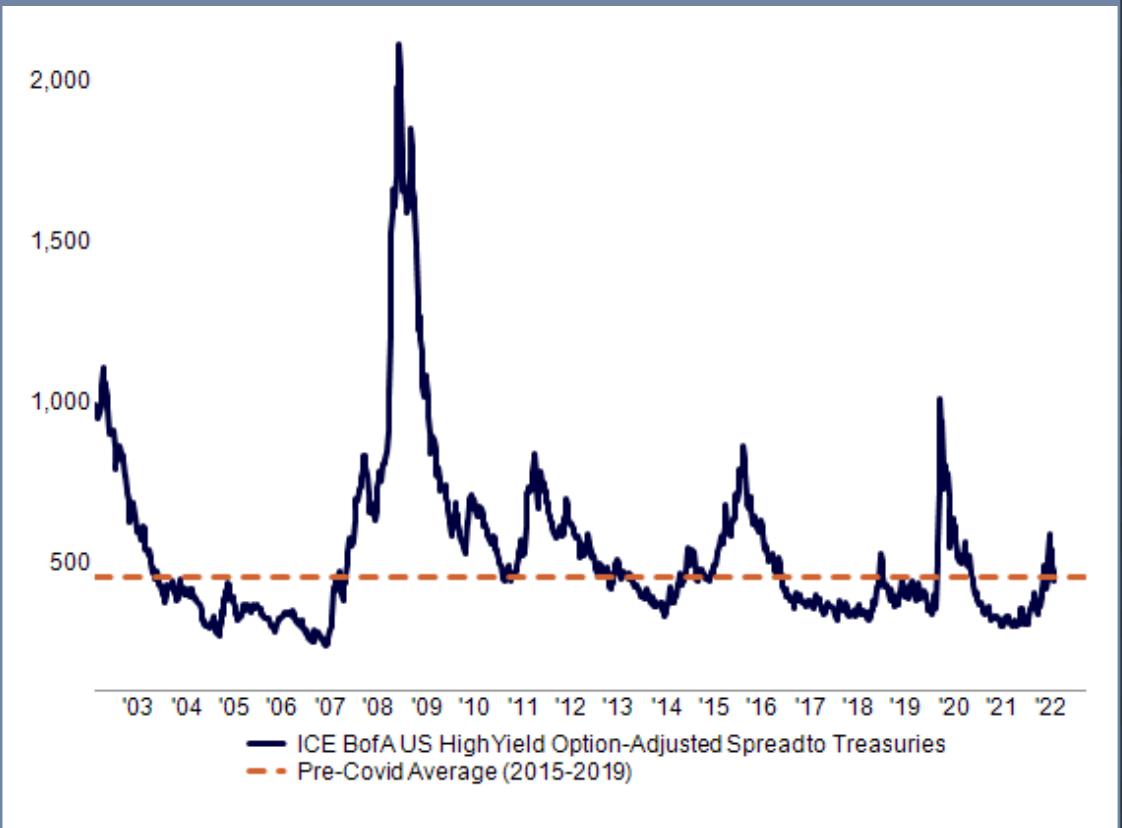
Watching the Leading Indicators

Looking to the bond market and high yield market for signs of a recession.

The Yield Curve is Flashing Red

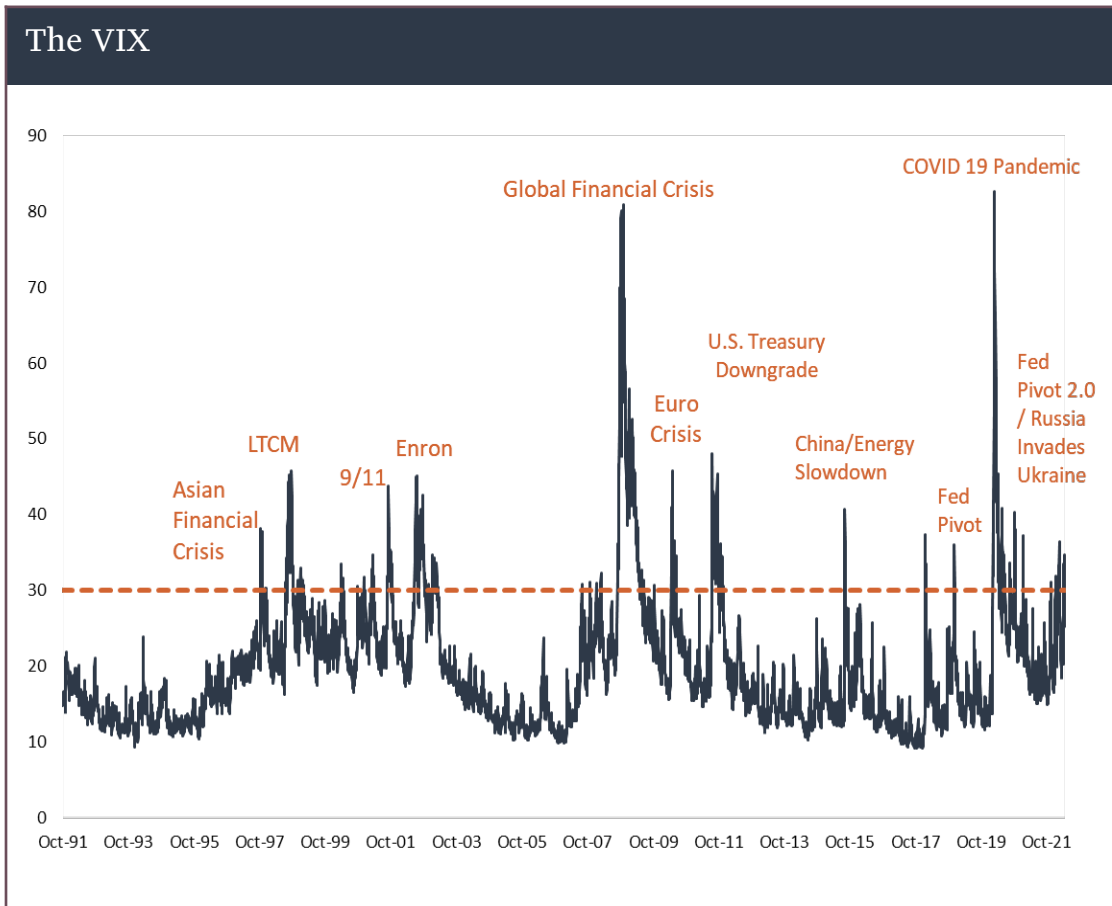


High Yield Spreads are Flashing Yellow



Recession Watch

The key is what has already been priced into the market.



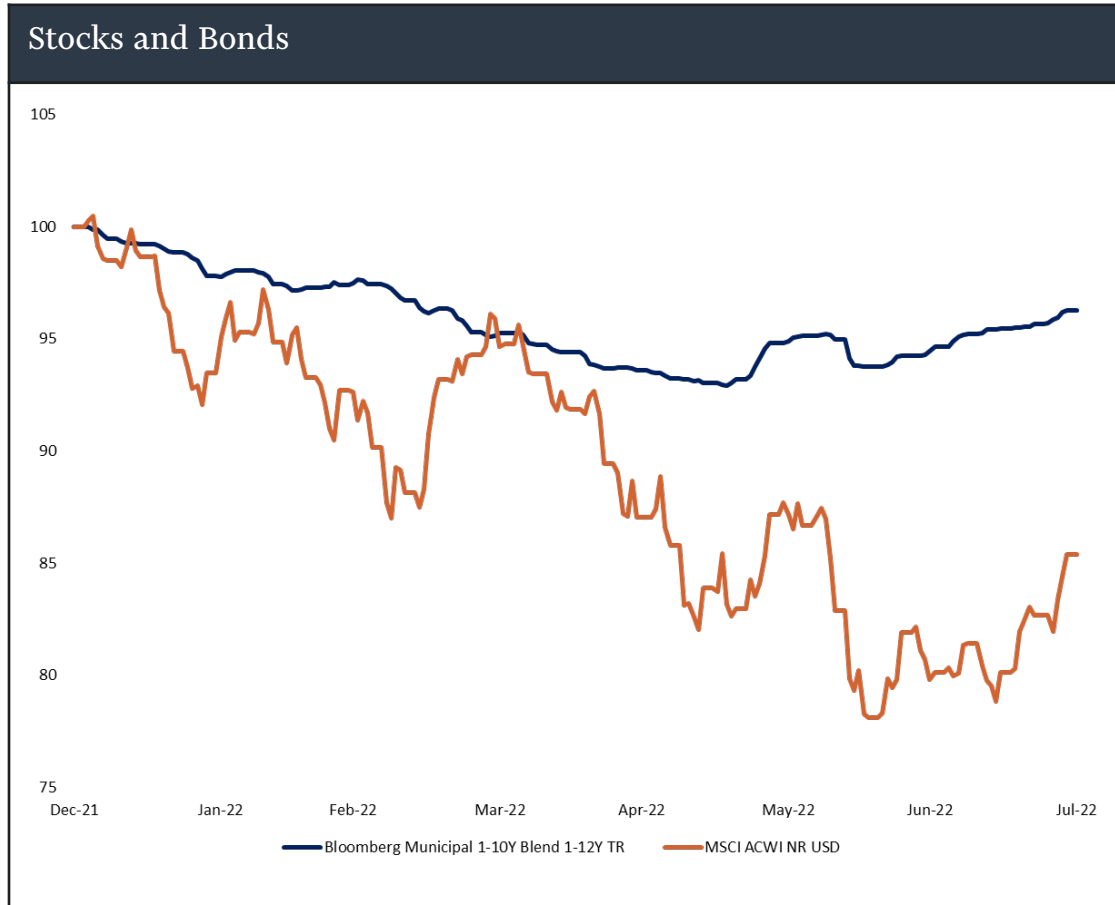
The History of Recent Market Bull & Bear Markets

Bull and bear markets

Bull markets			Bear markets		
Bull begin date	Bull return	Duration (months)	Market peak	Bear return*	Duration (months)*
Jul 1926	152%	37	Sep 1929	-86%	32
Mar 1935	129%	23	Mar 1937	-60%	61
Apr 1942	158%	49	May 1946	-30%	36
Jun 1949	267%	85	Aug 1956	-22%	14
Oct 1960	39%	13	Dec 1961	-28%	6
Oct 1962	76%	39	Feb 1966	-22%	7
Oct 1966	48%	25	Nov 1968	-36%	17
May 1970	74%	31	Jan 1973	-48%	20
Mar 1978	62%	32	Nov 1980	-27%	20
Aug 1982	229%	60	Aug 1987	-34%	3
Oct 1990	417%	113	Mar 2000	-49%	30
Oct 2002	101%	60	Oct 2007	-57%	17
Mar 2009	401%	131	Feb 2020	-34%	1
Mar 2020	114%	21	Jan. 2022**	-24%	5
Averages	162%	51	-	-41%	20

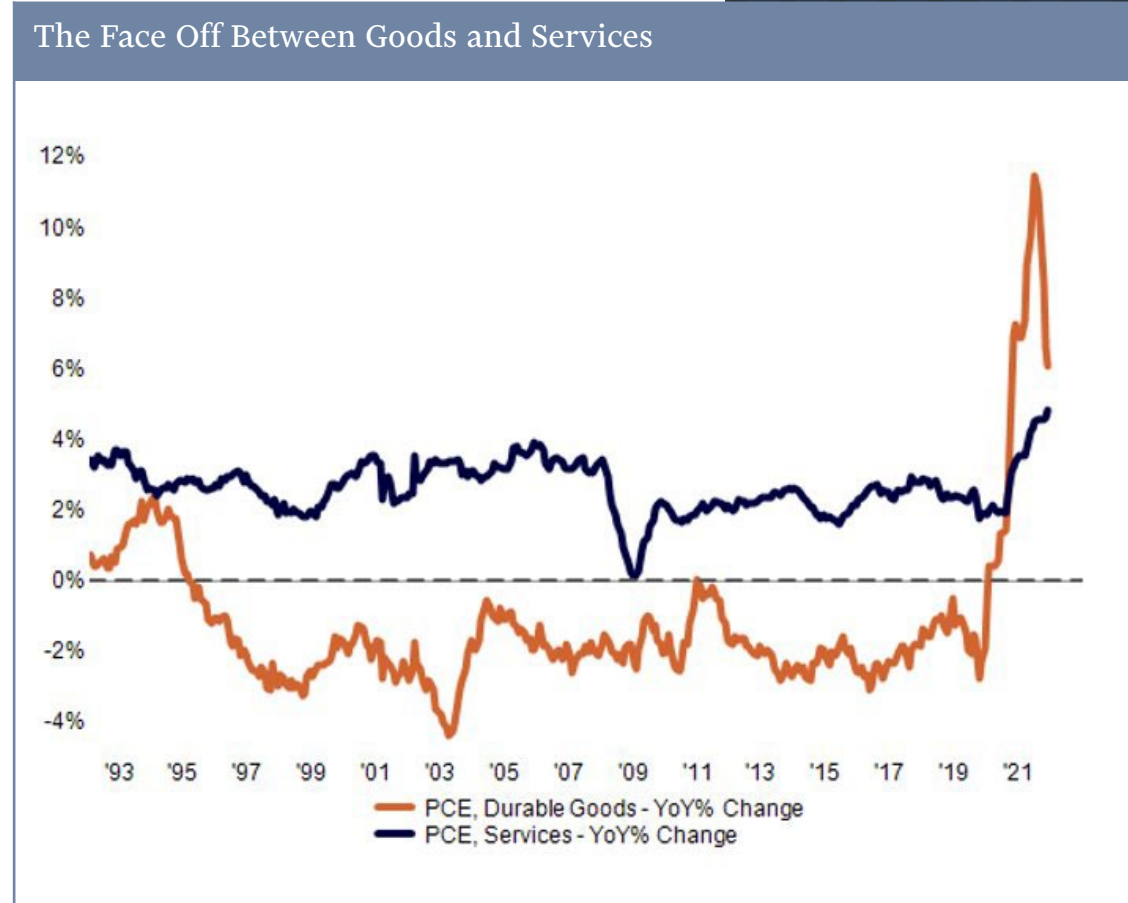
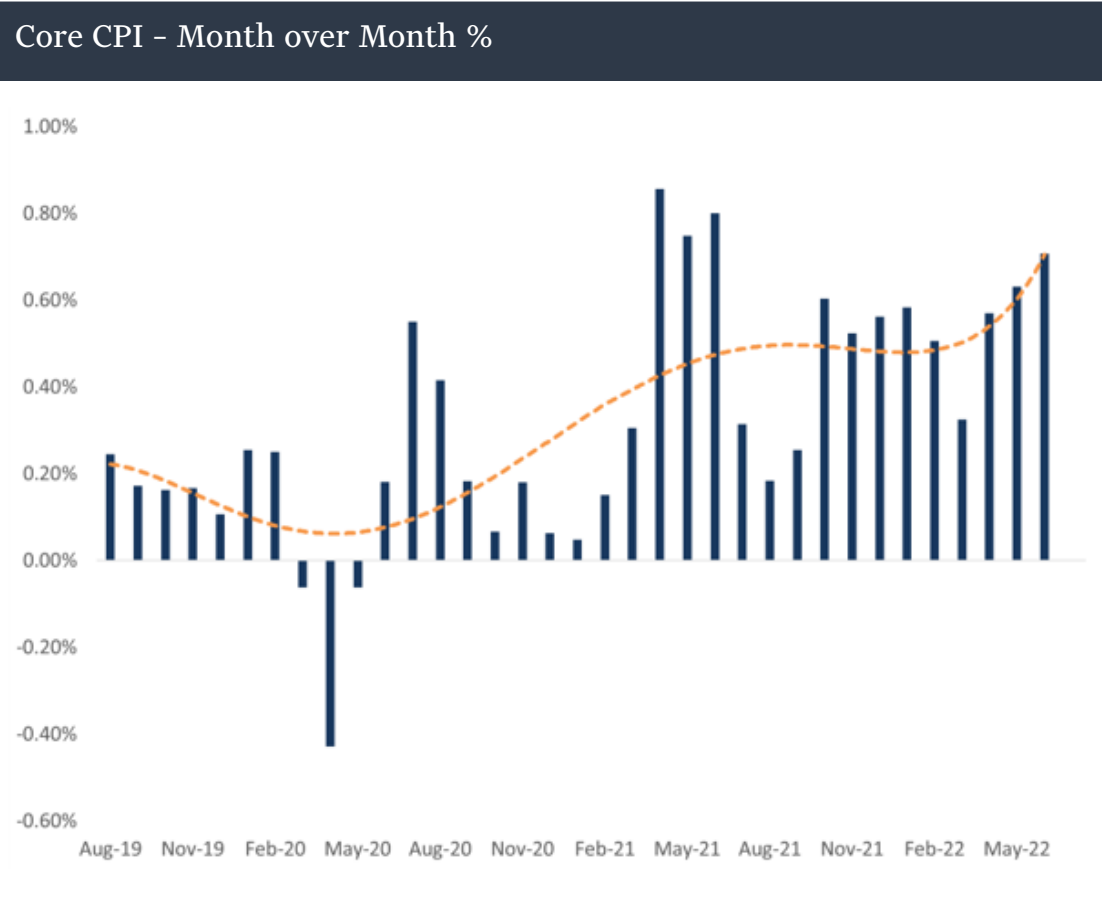
Correlations Work Both Ways

Both stocks and bonds have started to work.



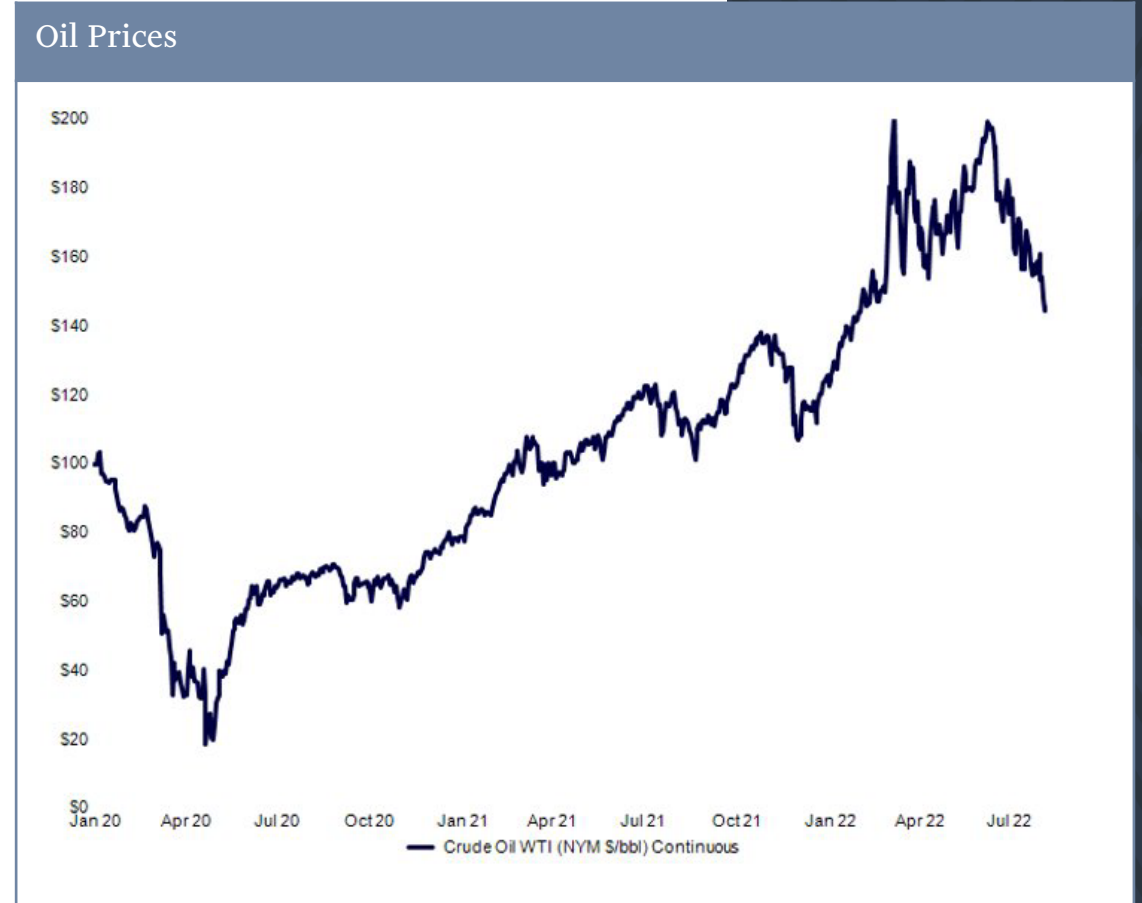
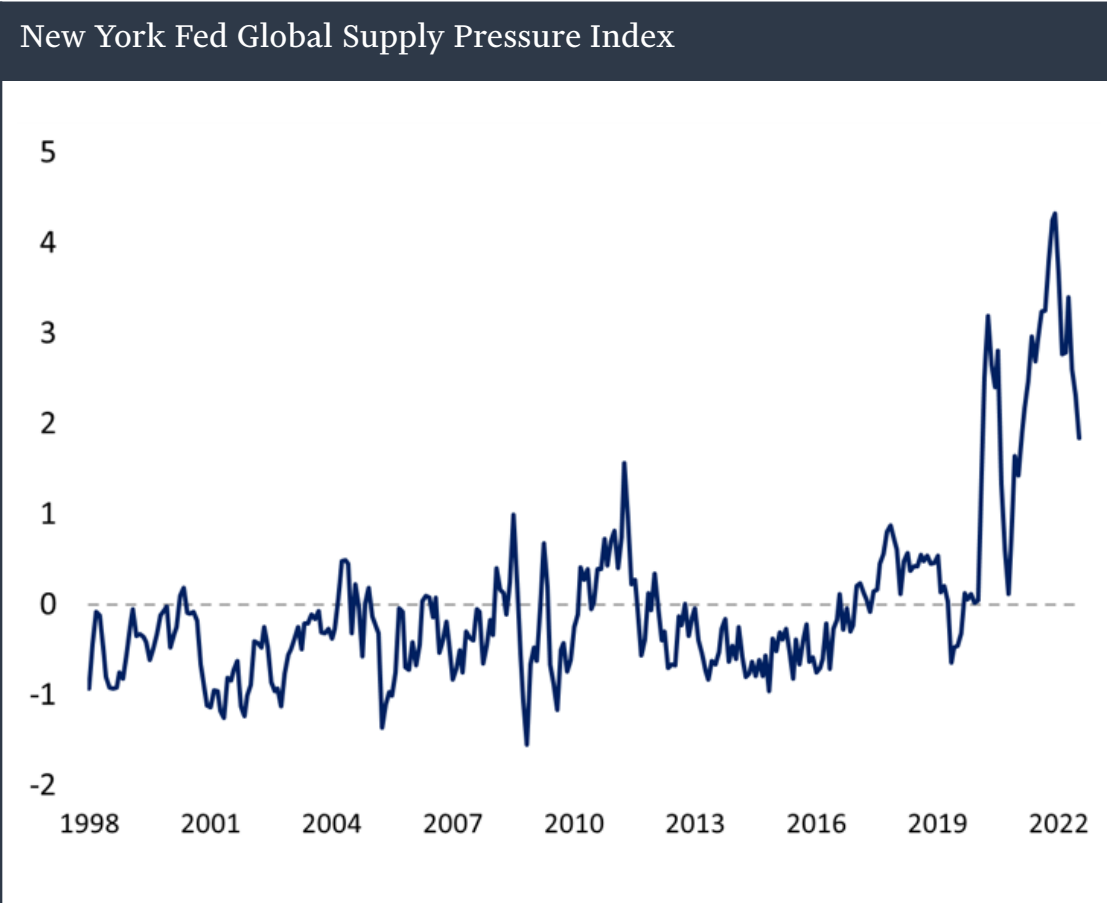
The Inflation Fulcrum

As inflation goes, so does the Fed.



The Choking of Supply Chains

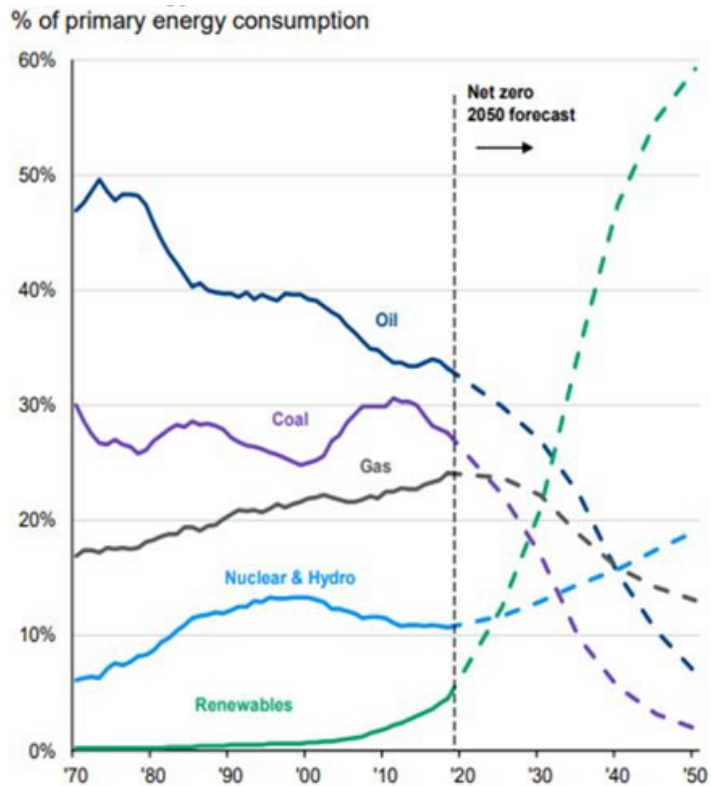
Supply chain pressures are still here but may be fading.



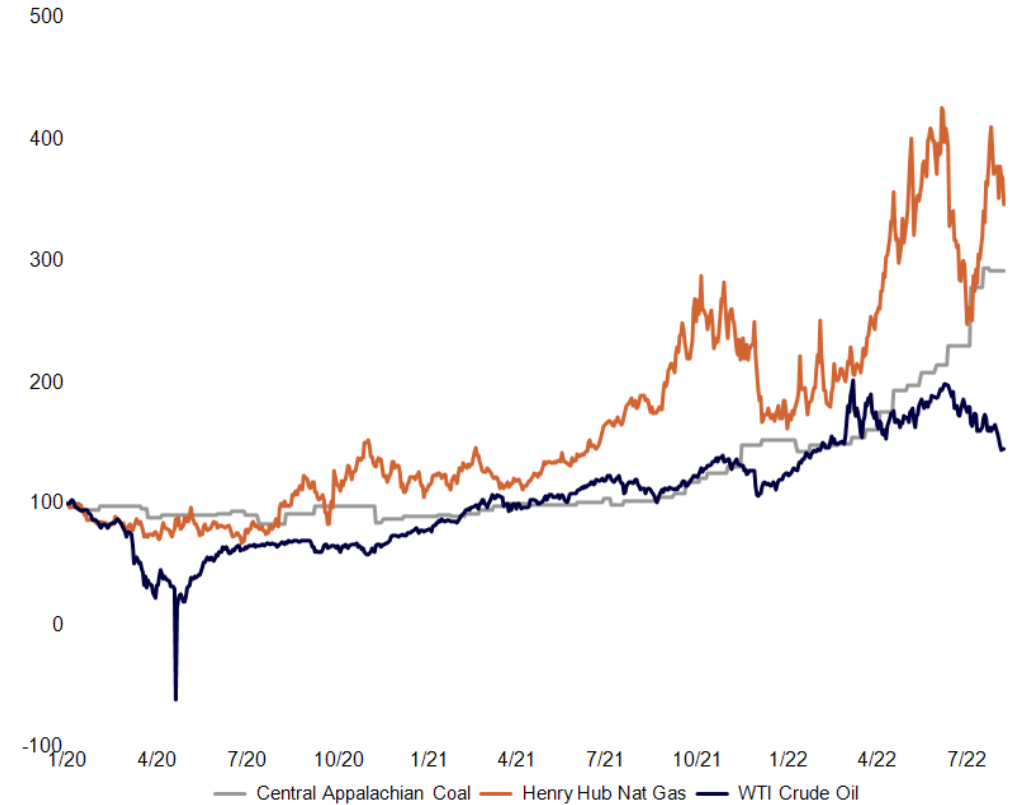
Energy Transition

The energy transition may create unintended consequences along the way.

Global Energy Mix

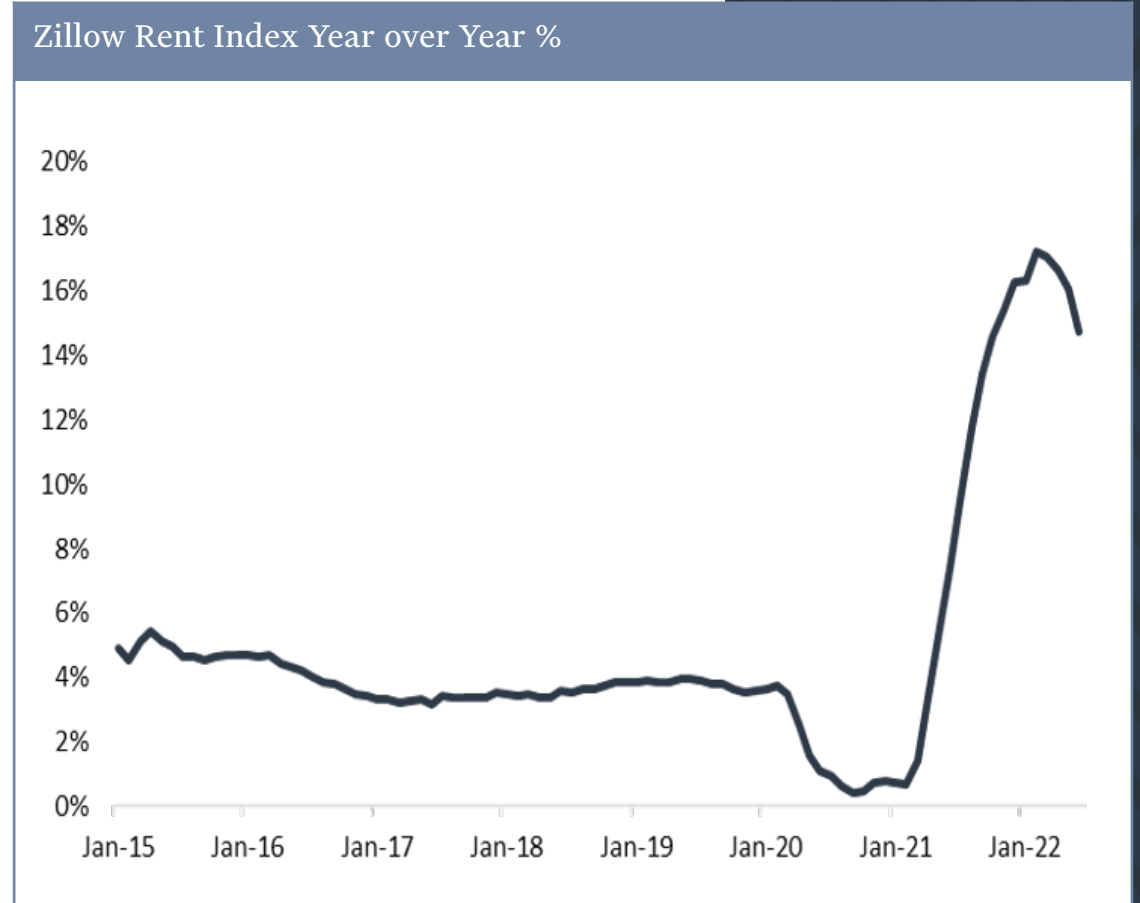
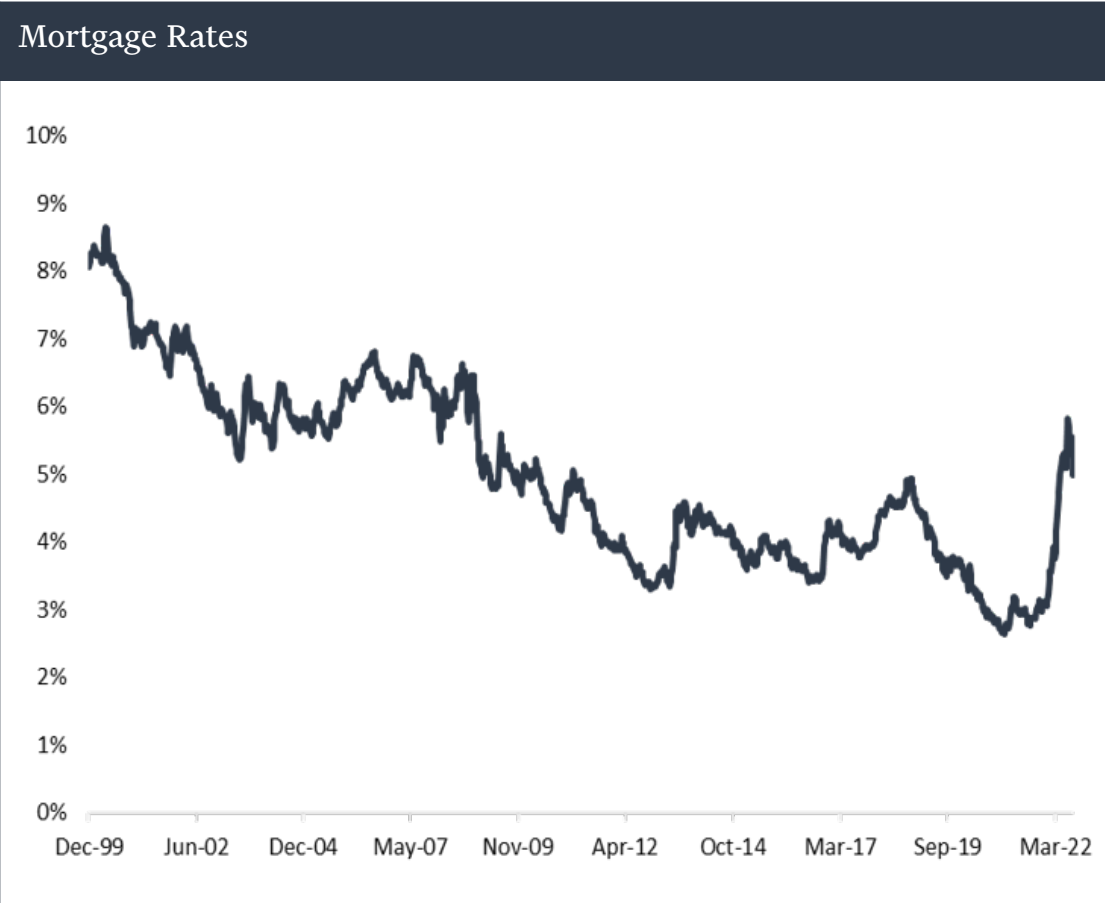


Supply Shortages Overwhelm in the Near Term



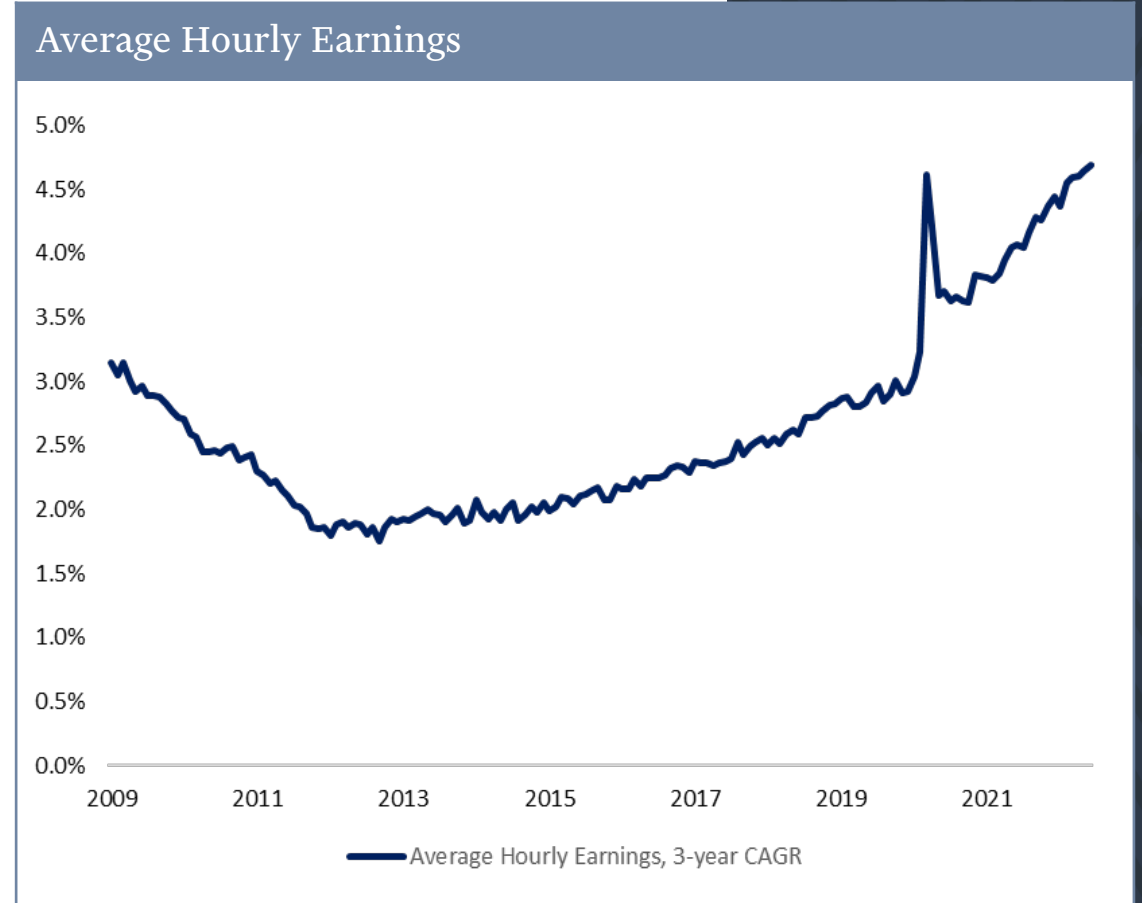
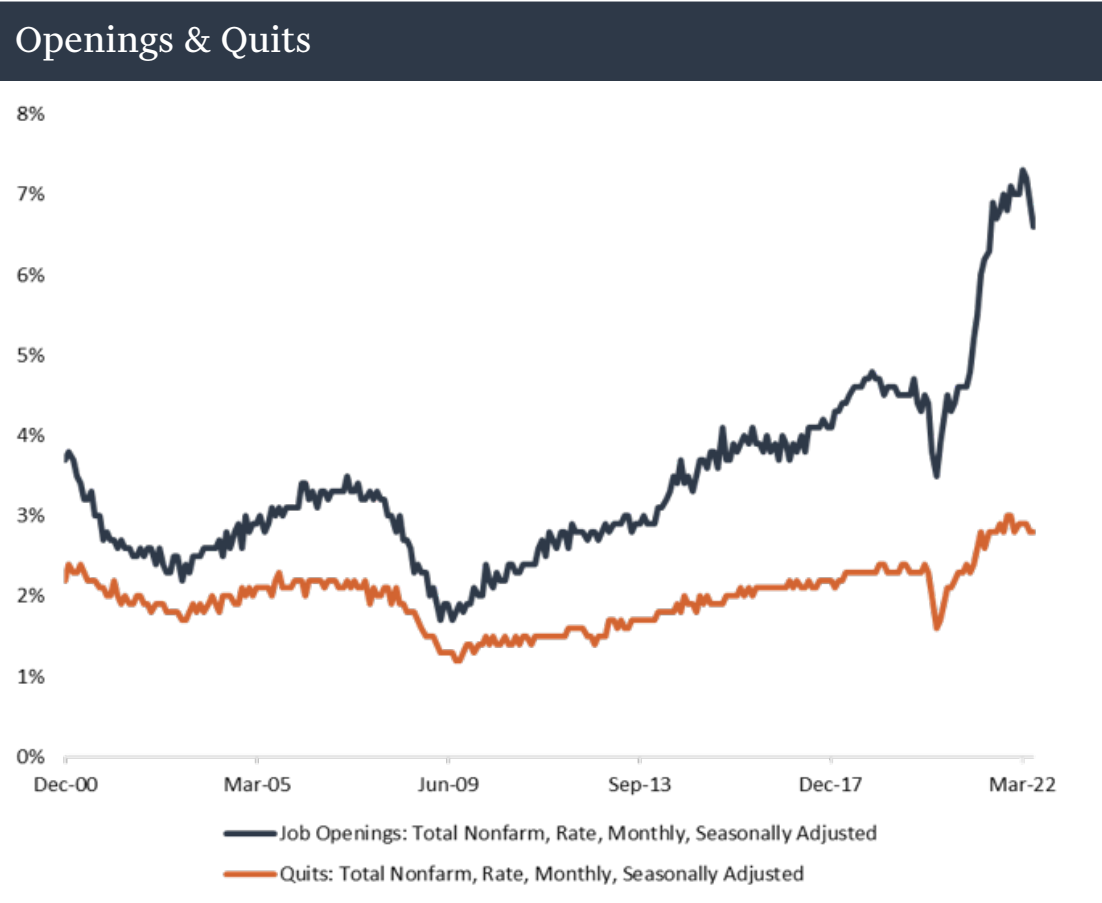
Housing Market, Transitioning?

Rising rates should sap demand in the red-hot housing market.



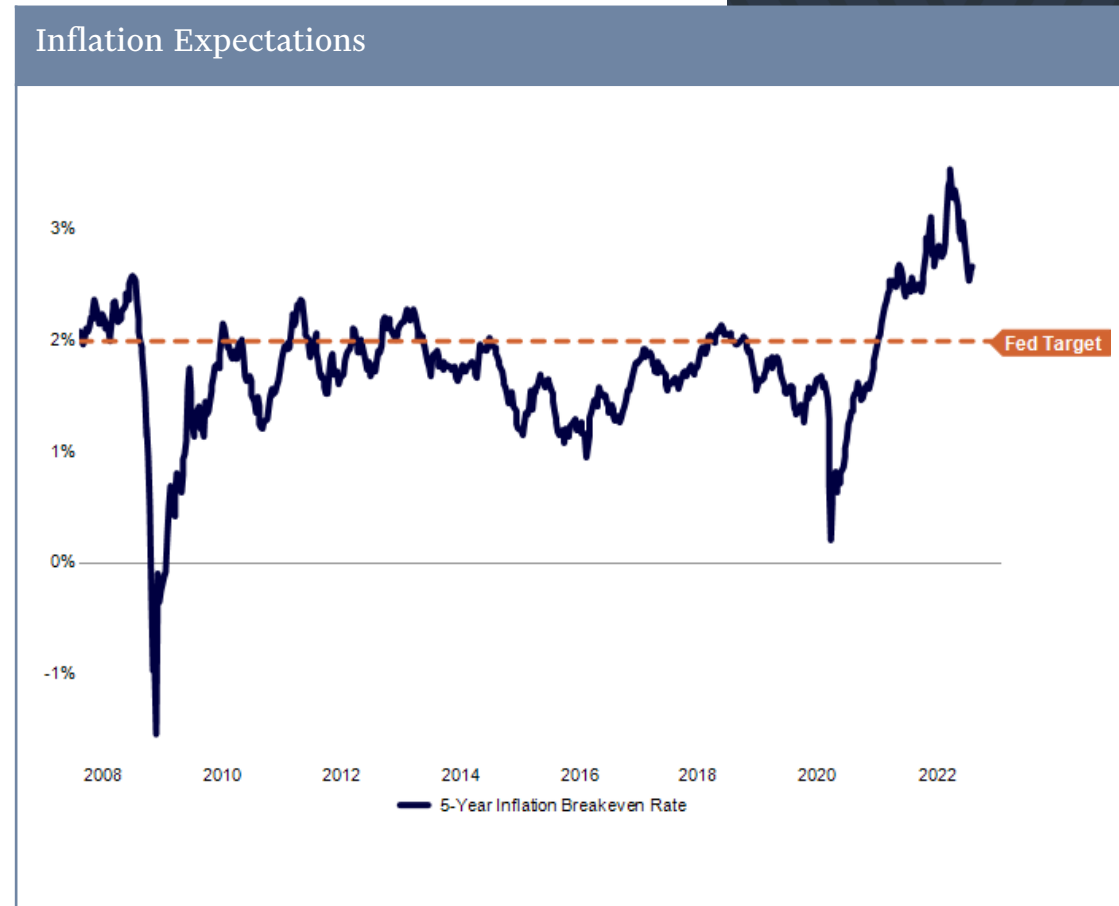
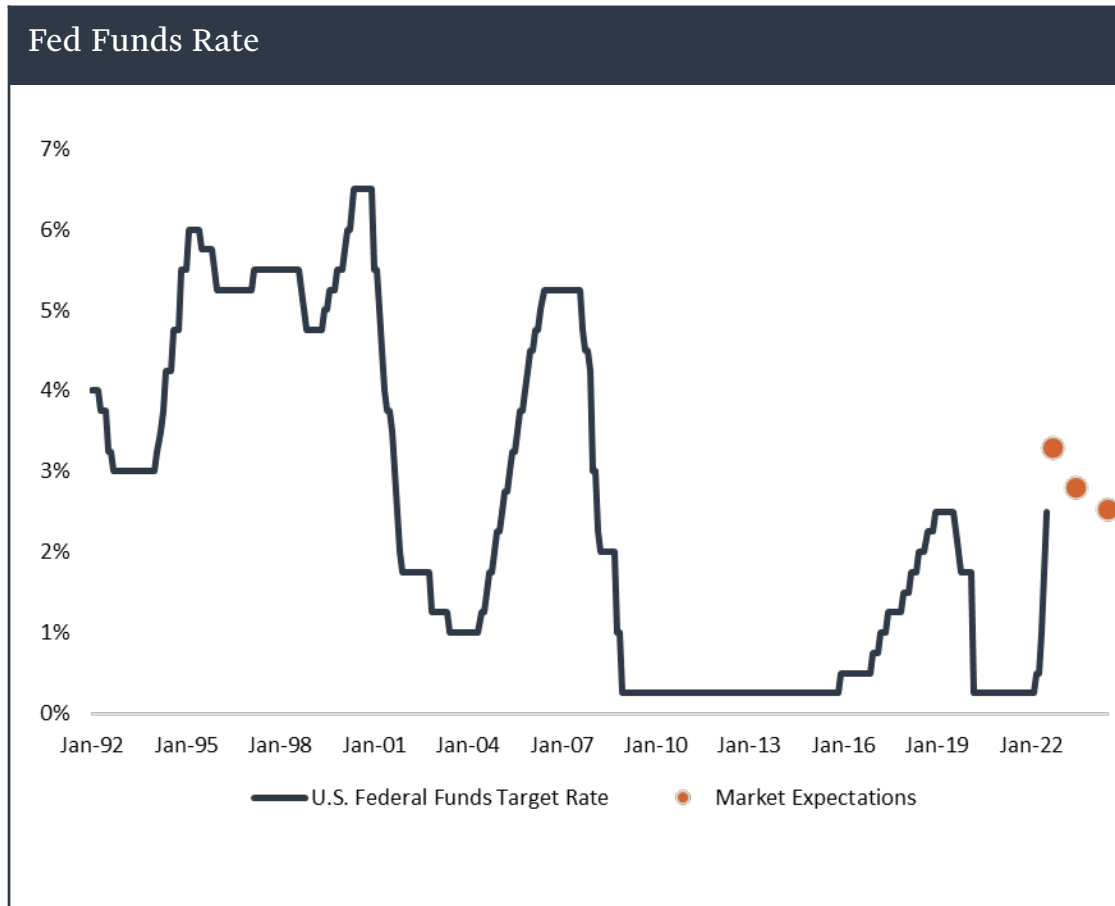
Tightness in the Labor Markets

Labor supply needs a services increase to help guide down inflation.



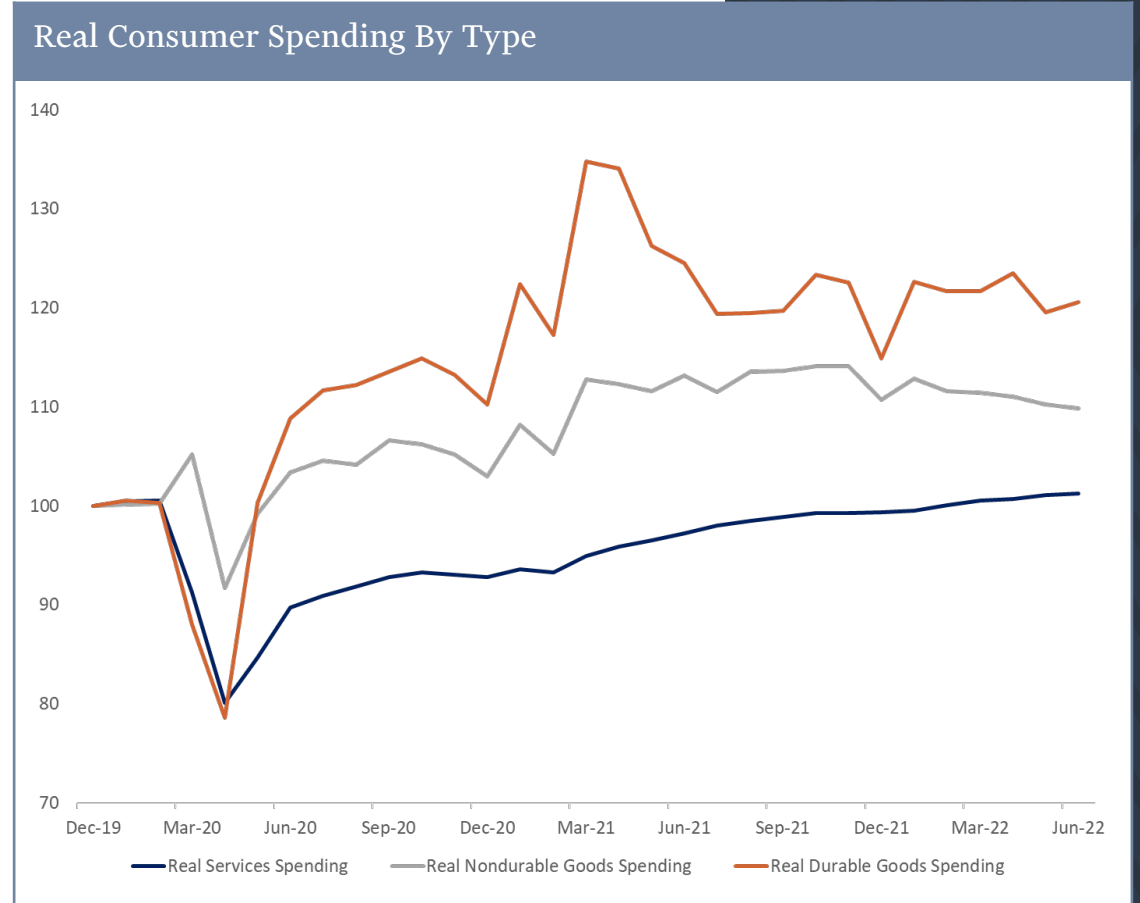
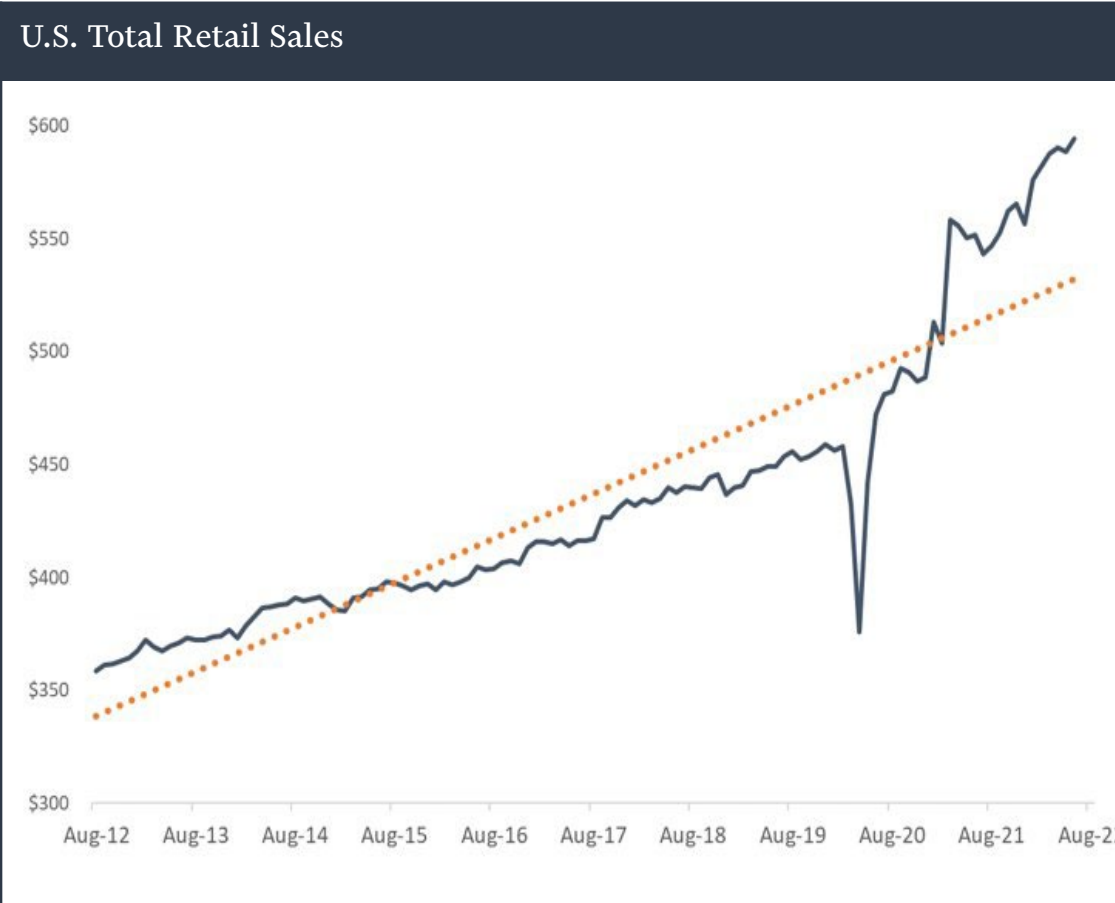
How High Will the Fed Have to Go?

The good news is that long-term inflation expectations are remaining anchored.



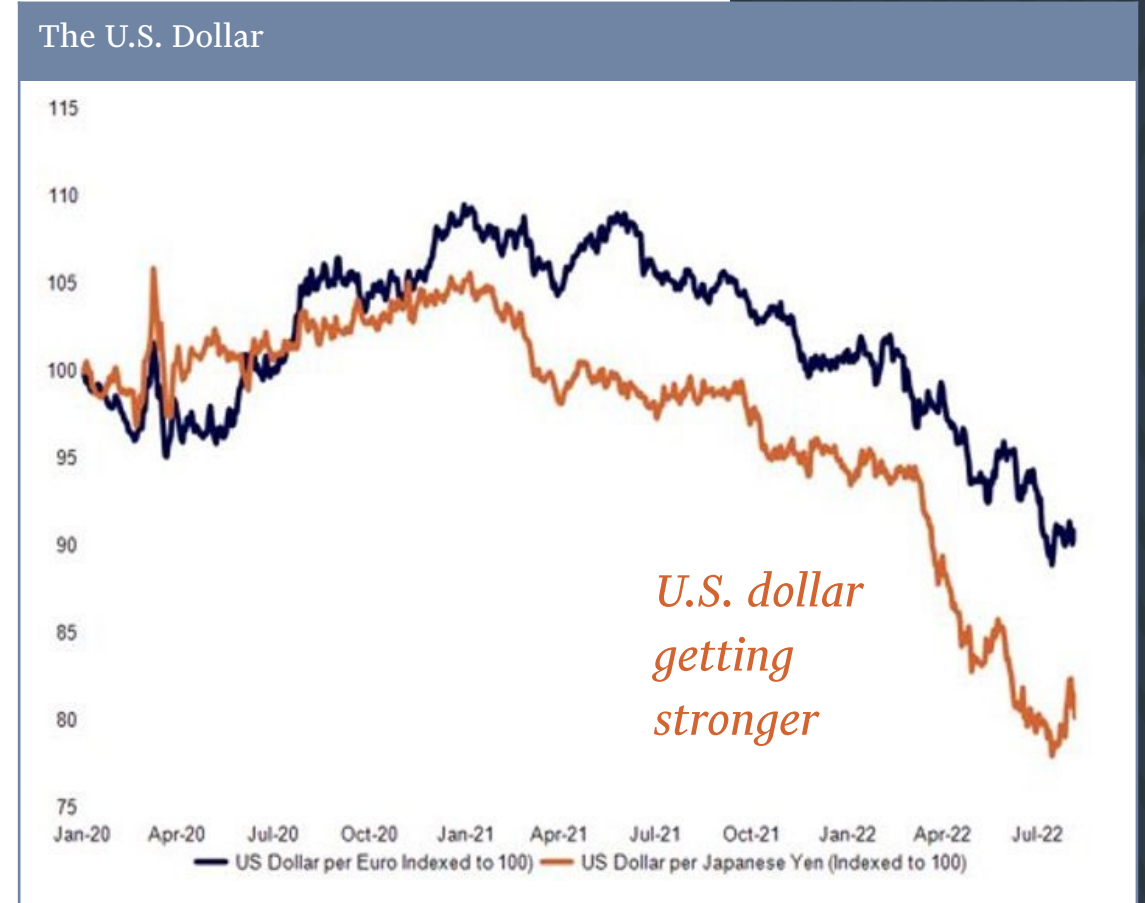
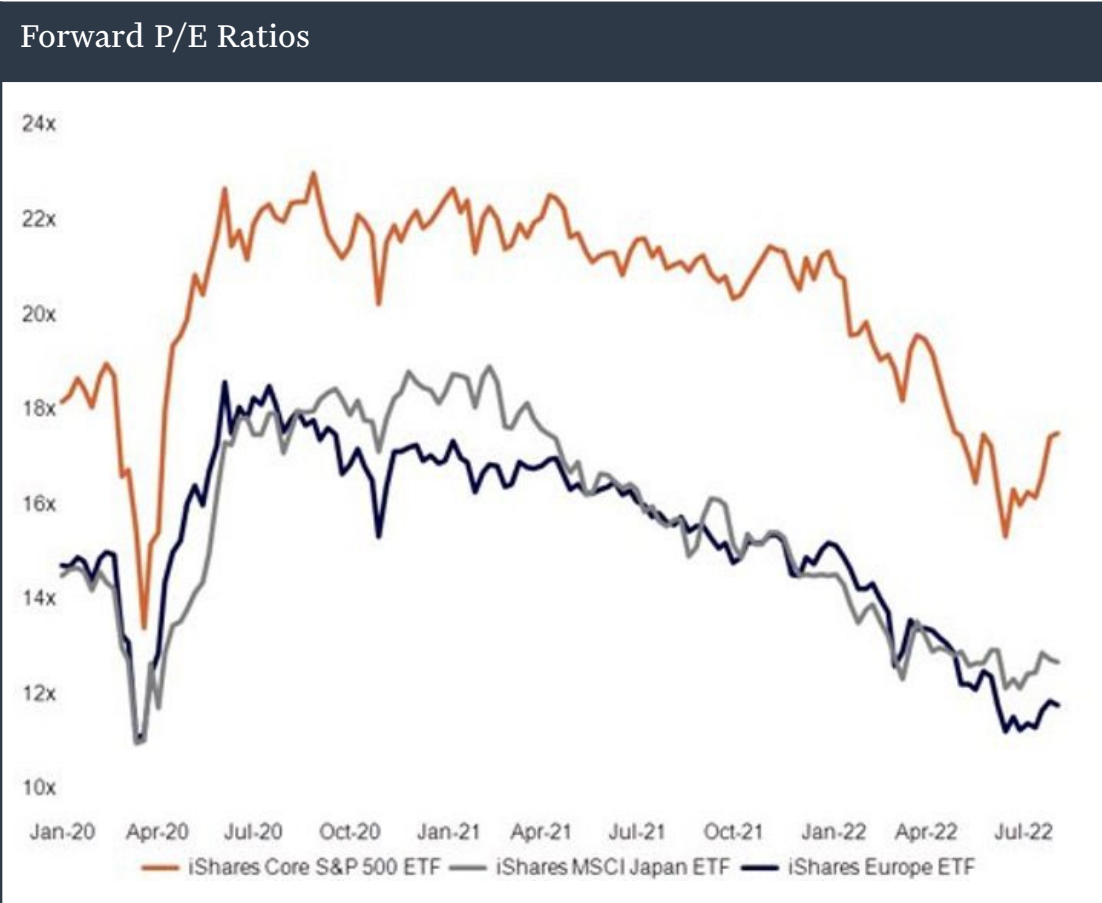
The U.S. Consumer Has Not Stopped Spending

The excess savings binge fueling consumer spending is coming to an end.



The International Markets Discount

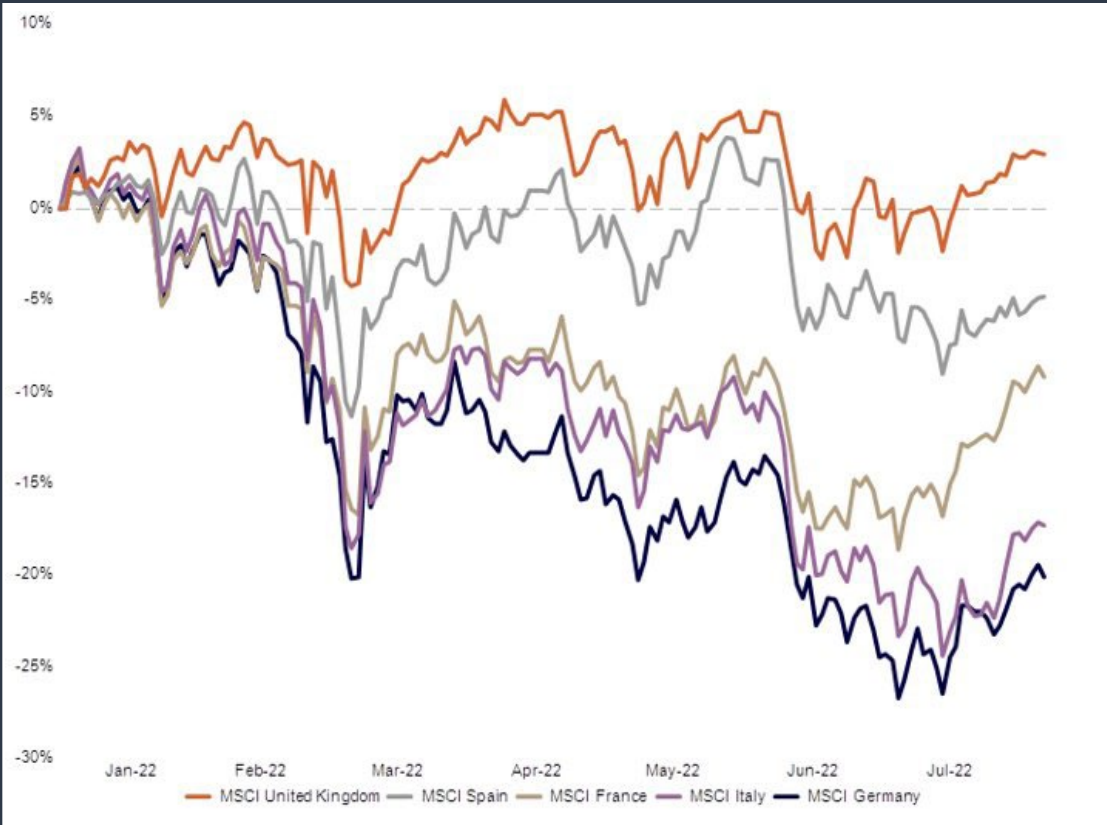
The strength of the dollar acts as another headwind to the overseas markets.



European Recession Coming?

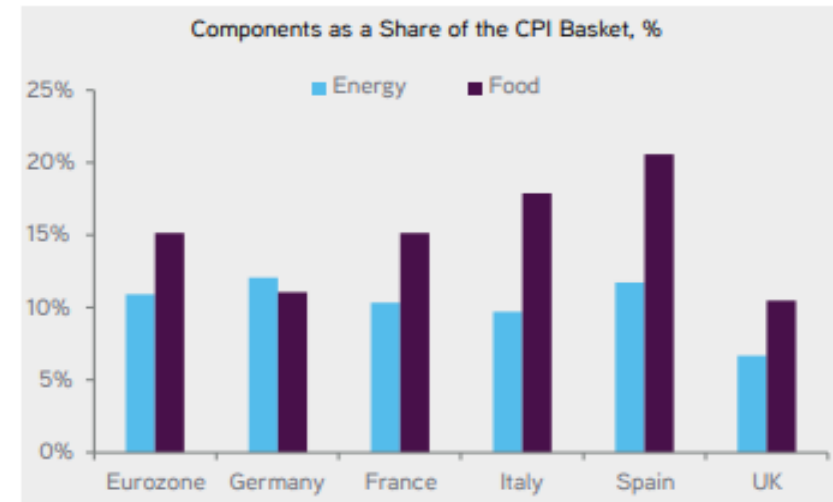
Europe may be unable to avoid an economic downturn.

European Equity Prices



Highly Sensitive to Food Prices

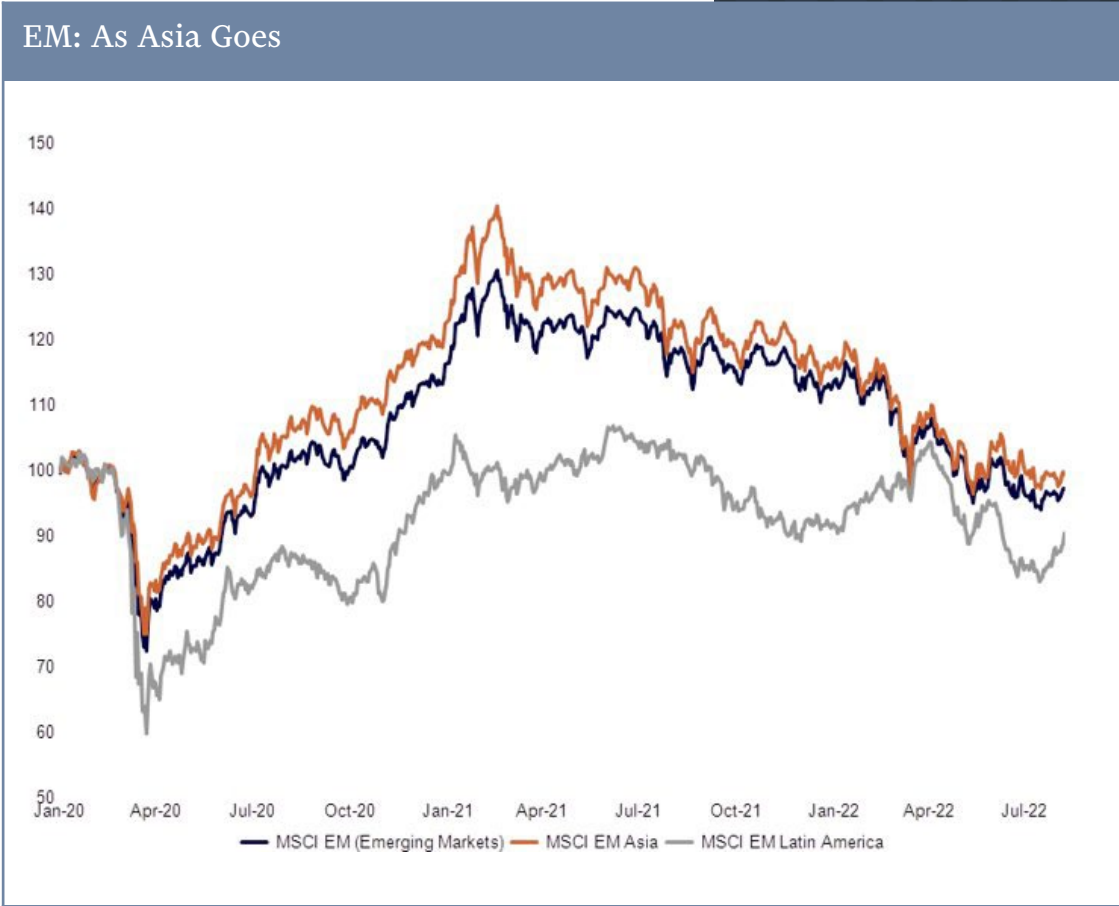
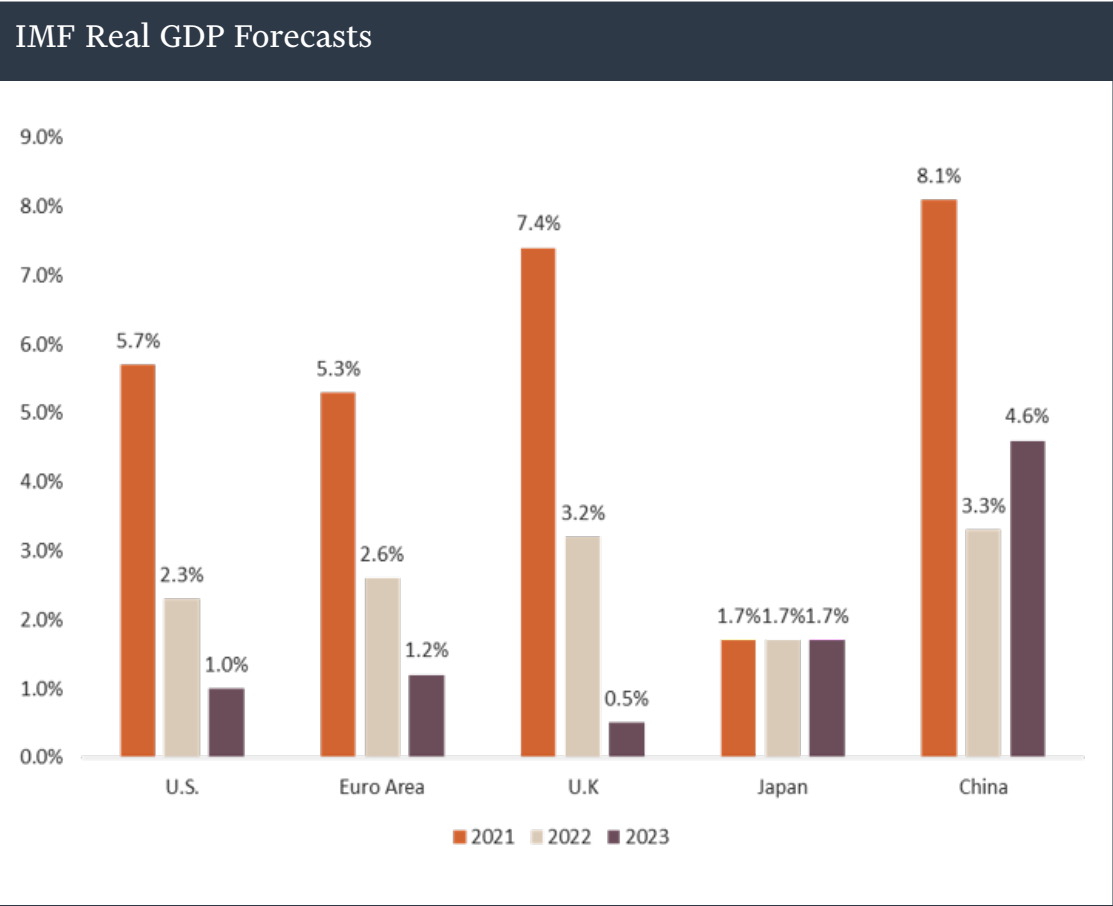
Food Makes Up 15% of the Consumer Inflation Basket (HICP) in the Eurozone, With Italy and Spain Standing Out for Above-Average Sensitivity



Note: HICP = Harmonized Index of Consumer Prices. Data as at April 30, 2022.
Source: ONS, Eurostat.

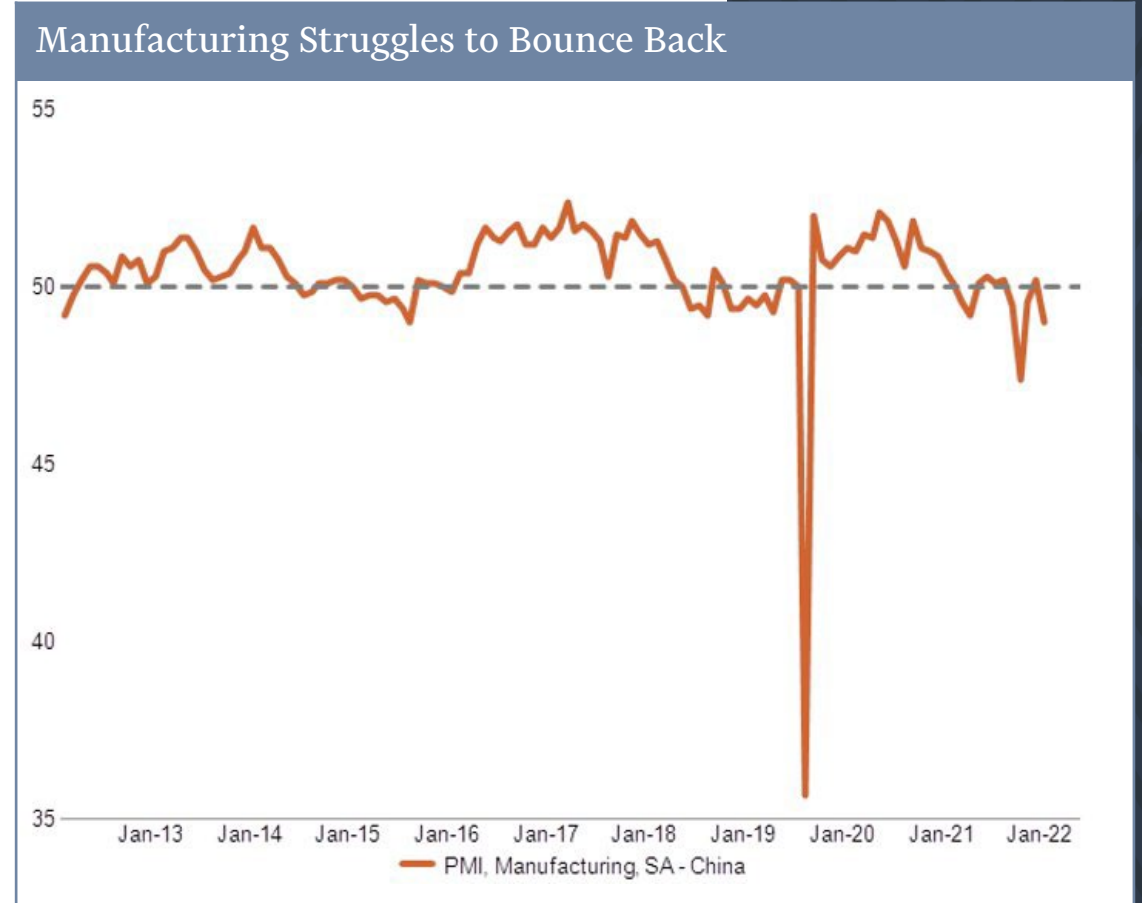
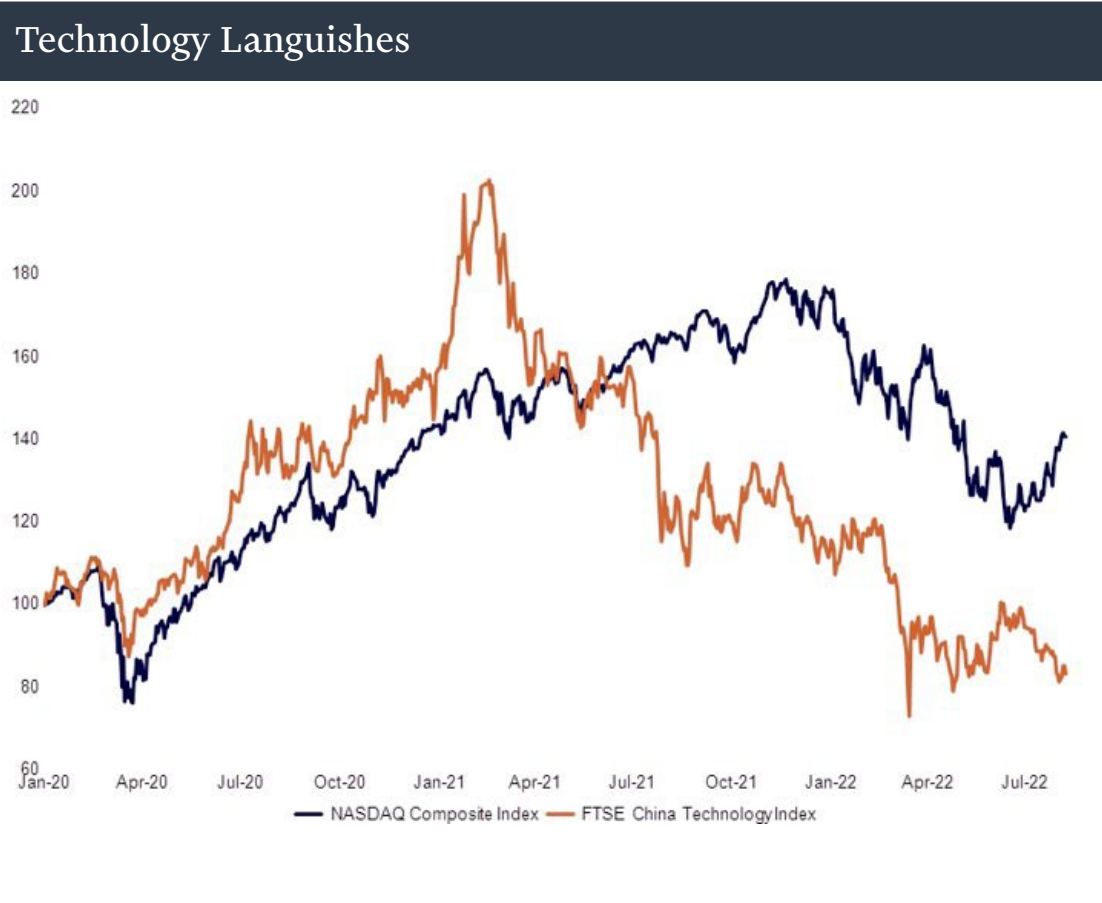
China, No Longer the Growth Engine

The regulatory actions in the education, housing, and health sectors are continued headwinds to Chinese growth.



China, The Pain Continues

Zero-Covid policy, deflating real estate bubble, continued tech crackdown all put pressure on a 5.5% GDP target.



Source: Factset



State of Equity Markets

Summer 2022



Pessimism Abounds

It has become fashionable to be negative on the economy and markets

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Markets
Economics

Shallow Recession Calls Are ‘Totally Delusional,’ Roubini Warns

- A reason Roubini cites is historically high debt ratios
- This time it ‘could be worse than ‘70s,’ economist says

PIPER | SANDLER

US Economics | **Macro Research**

July 27, 2022

The Profit/EPS Downturn Is Here.

[Report Link](#)

Conclusion: Profits always fall in recessions, and we’re moving into one now. On average, in recessions profits & EPS decline -12%, and -24%, respectively. We’re now forecasting S&P EPS to decline -8% cumulatively in 2022 & 2023 -- to \$200 in 2022, and \$190 in 2023. (pgs 2-4)

Morgan Stanley | RESEARCH

July 11, 2022

US Equity Strategy | North America

Weekly Warm-up: Strong Dollar Just Another Headwind for Earnings, Leaving Unfinished Business for the Bear

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Markets

JPMorgan Sees ‘Stratospheric’ \$380 Oil on Worst-Case Russian Cut

The Market Has Reflected the Pessimism

More than a correction



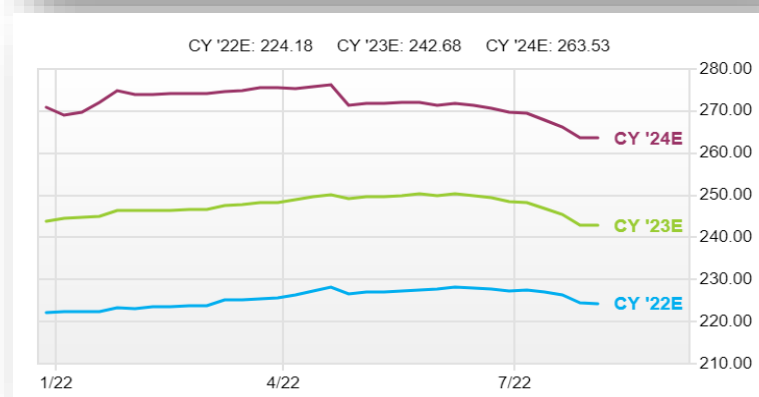
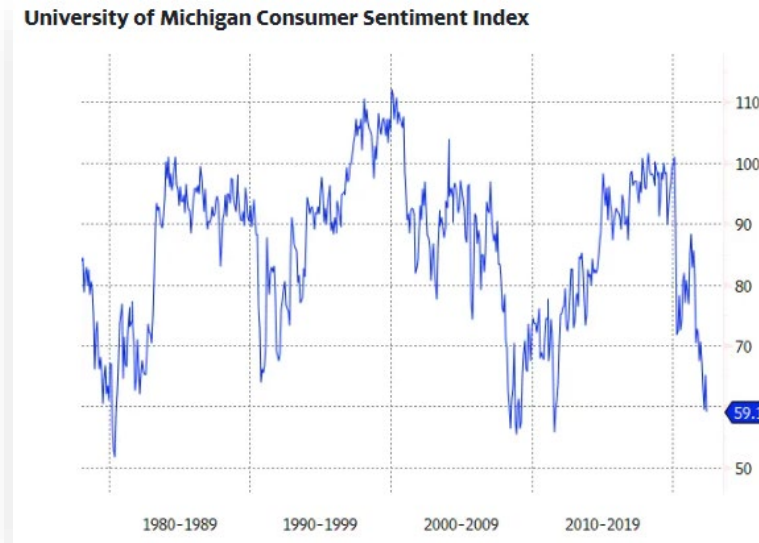
Source: Factset

There Are Legitimate Reasons To Be Pessimistic

(there's another slide after this)

1. Inflation
2. Federal Reserve
3. 1H'22 Negative GDP
4. War in Ukraine
5. Political Turmoil - here and abroad
6. Turn in the Labor Markets
7. Plunging Sentiment Surveys

All of this is leading to discussions of stagflation or worse.

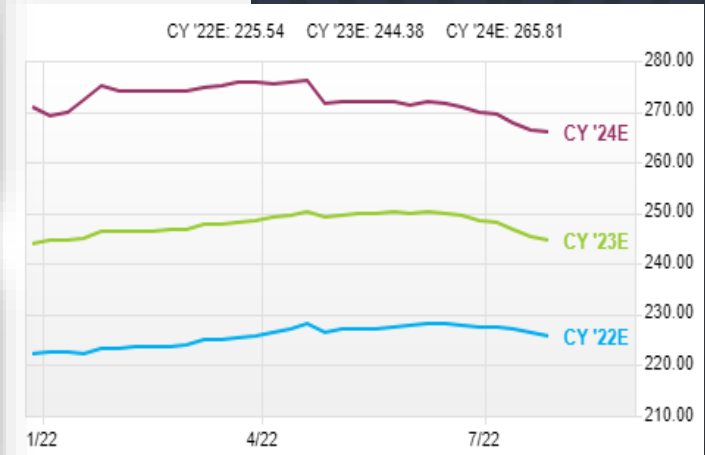
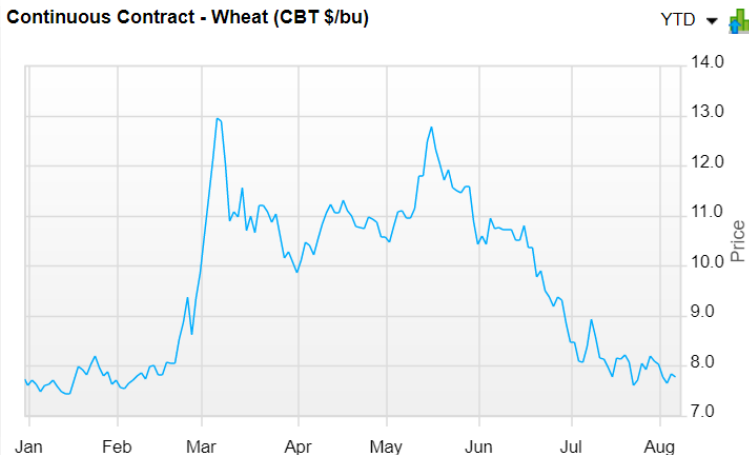


Source: Factset

But There Are Reasons to Be Positive As Well

(See, I told you there was another slide coming)

1. Labor Market Strength
2. Sound Banking System
3. Profits Still Growing
4. Commodity Prices Declining
5. Earnings Commentary
6. Recent Market Action



Half-Full-Half-Empty Commentary on Earnings Calls

2Q'22 earnings season presented a wide array of opinions from corporate leaders

Forbes

Delta Air Lines Demand Is So Strong 'There Is A Fight To Get On The Airplane,' CEO Says

 **CNBC**

Walmart's slashed profit outlook sends warning about state of the American consumer

 **CNBC**

Bank of America CEO Brian Moynihan says nothing will slow U.S consumer from spending money

FINANCIAL TIMES

Twitter and Snap results send shudders through digital advertising market

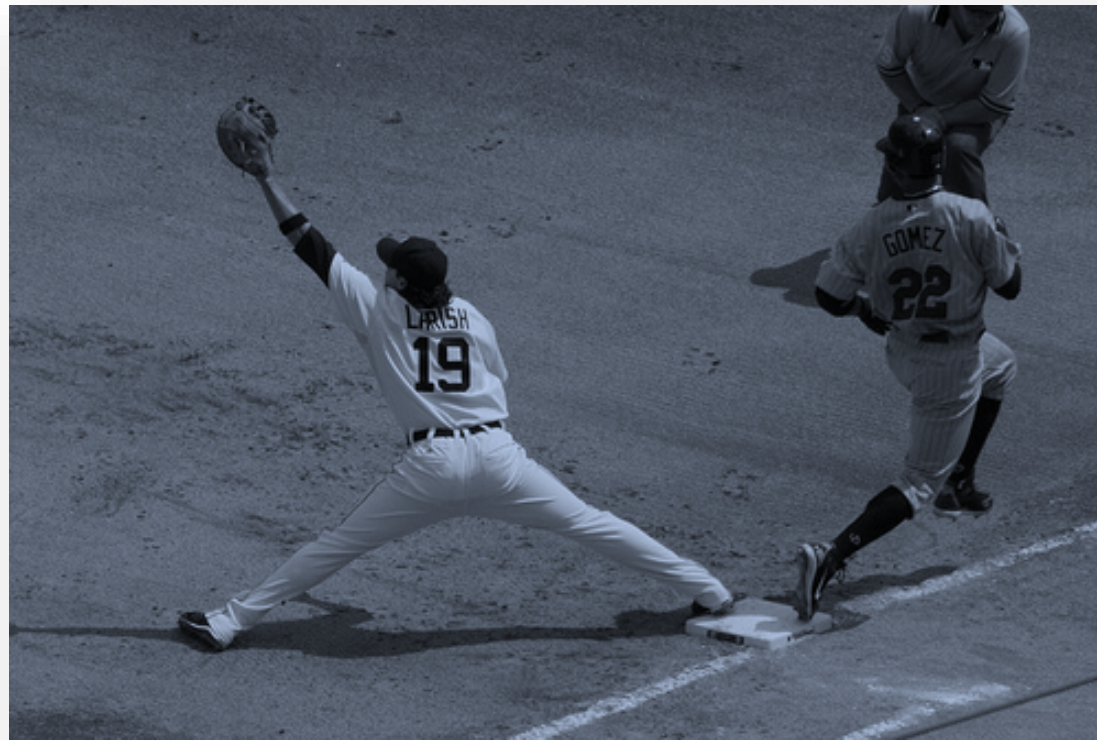
So, What Do You Do?

How do you make investment decisions when every topic shows two sides?



So, What Do You Do?

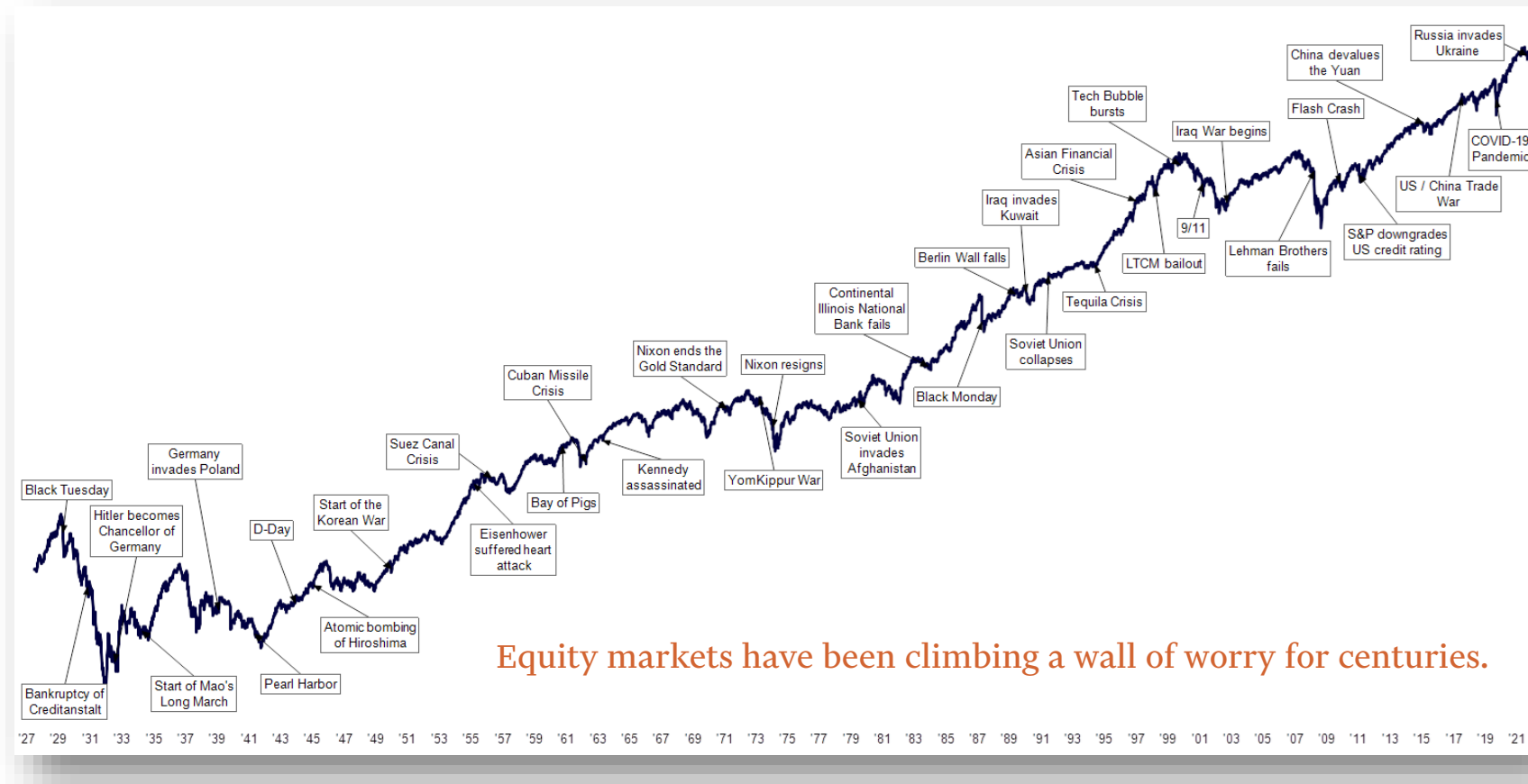
How do you make investment decisions when every topic shows two sides?



In baseball, a tie goes to the runner. And in investing?

So, What Do You Do?

In investing, a tie goes to the bulls

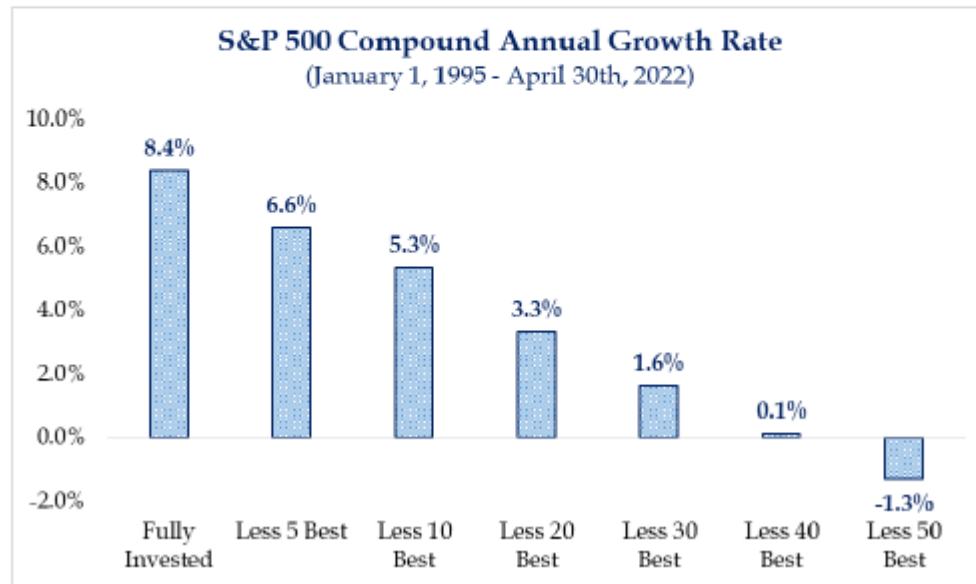


So, What Do You Do?

Balance the positives and the negatives

Time In The Market More Important Than Timing The Market

The daily swings in the equity markets can be uncomfortable to stomach, but staying the course is often the best approach. With the best and worst performing days often clustered near one another, trading in and out of the market can create missed opportunities. After all, compounding over time is the most powerful tool many investors have when it comes to markets.



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