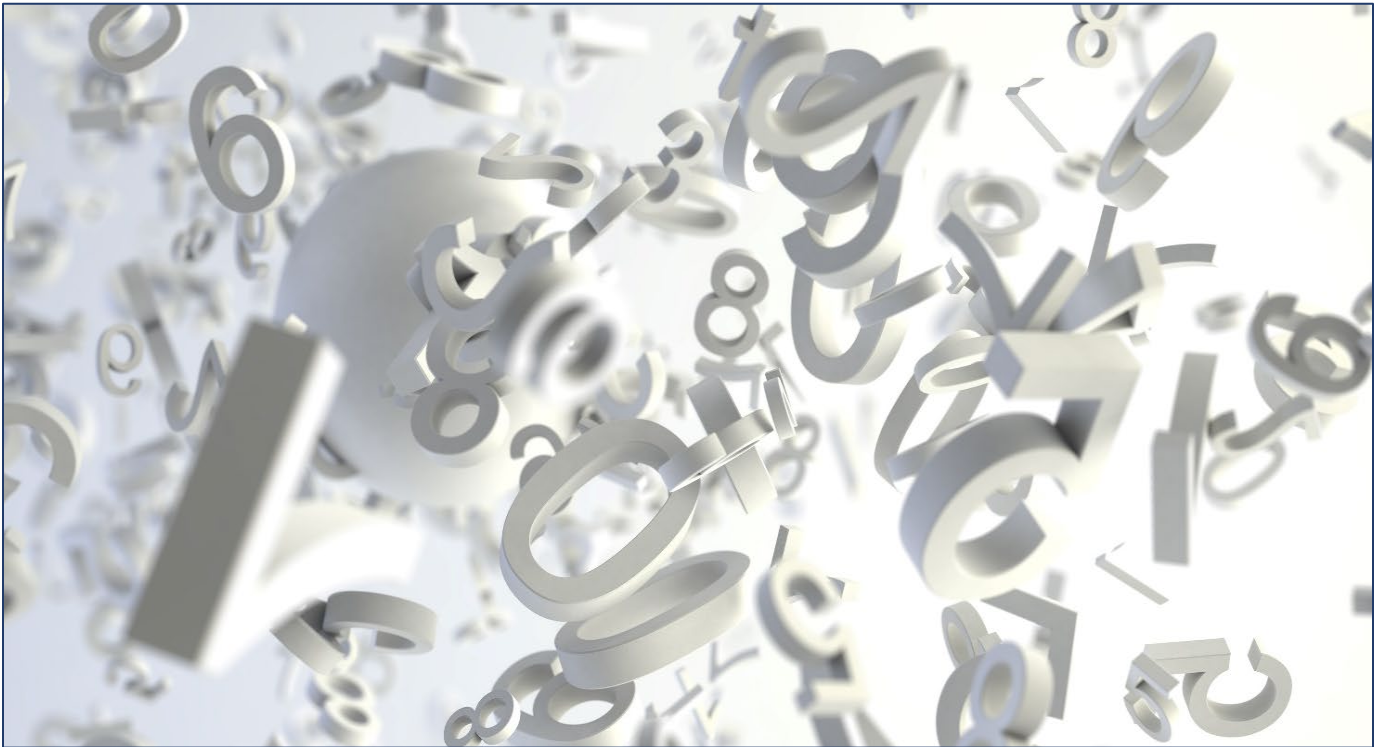


## MARKET COMMENTARY - 2Q 2022

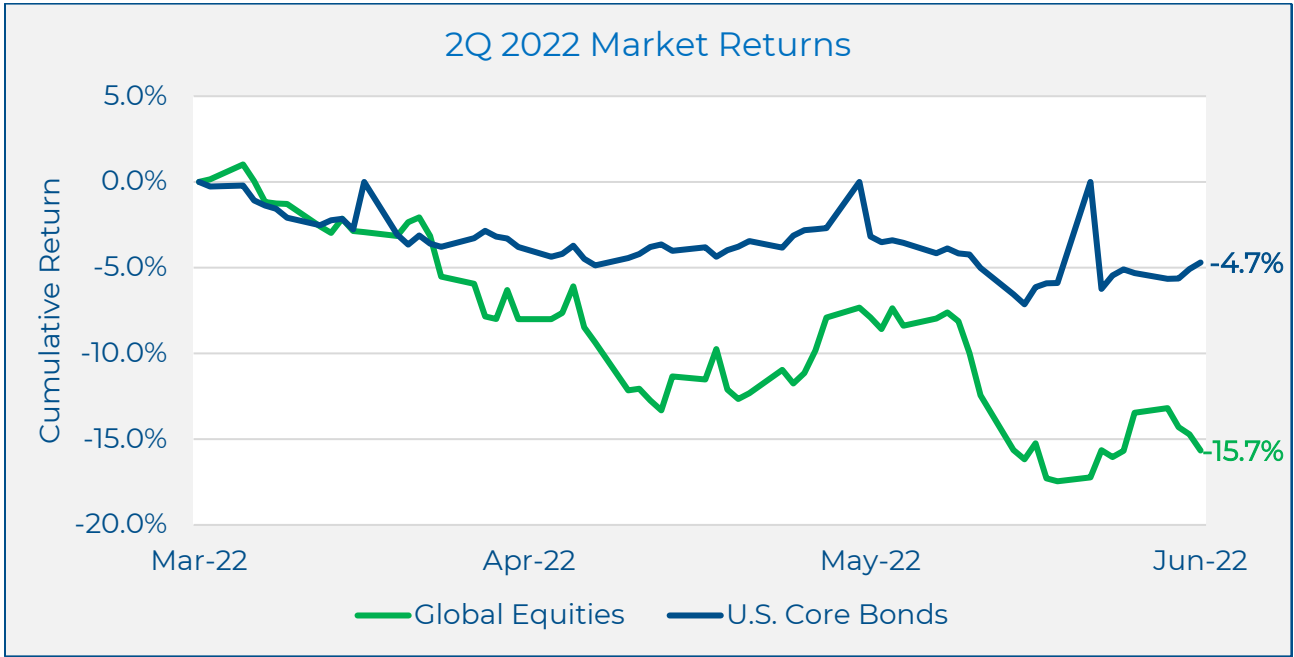


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### 2022 2Q in Review

Global markets have been quite volatile during the 2<sup>nd</sup> quarter as inflation remained at high levels, COVID restrictions in China continued and the conflict between Ukraine and Russia intensified. Collectively, these events have influenced the acceleration of Federal Reserve policy to fight inflation. The Fed has raised the Fed Funds rate by 1.25% so far this year, has hinted at another 0.75% in July, and plans to reduce its balance sheet by allowing existing holdings to mature and not reinvest. Market participants are becoming increasingly concerned about the global economic outlook and the potential for a recession.

Markets sold off during the first 6 weeks of the quarter, briefly rallied, then sold off sharply as news of persistently higher inflation convinced investors that the Fed's hand would be forced to accelerate the magnitude of Fed Funds rate hikes.



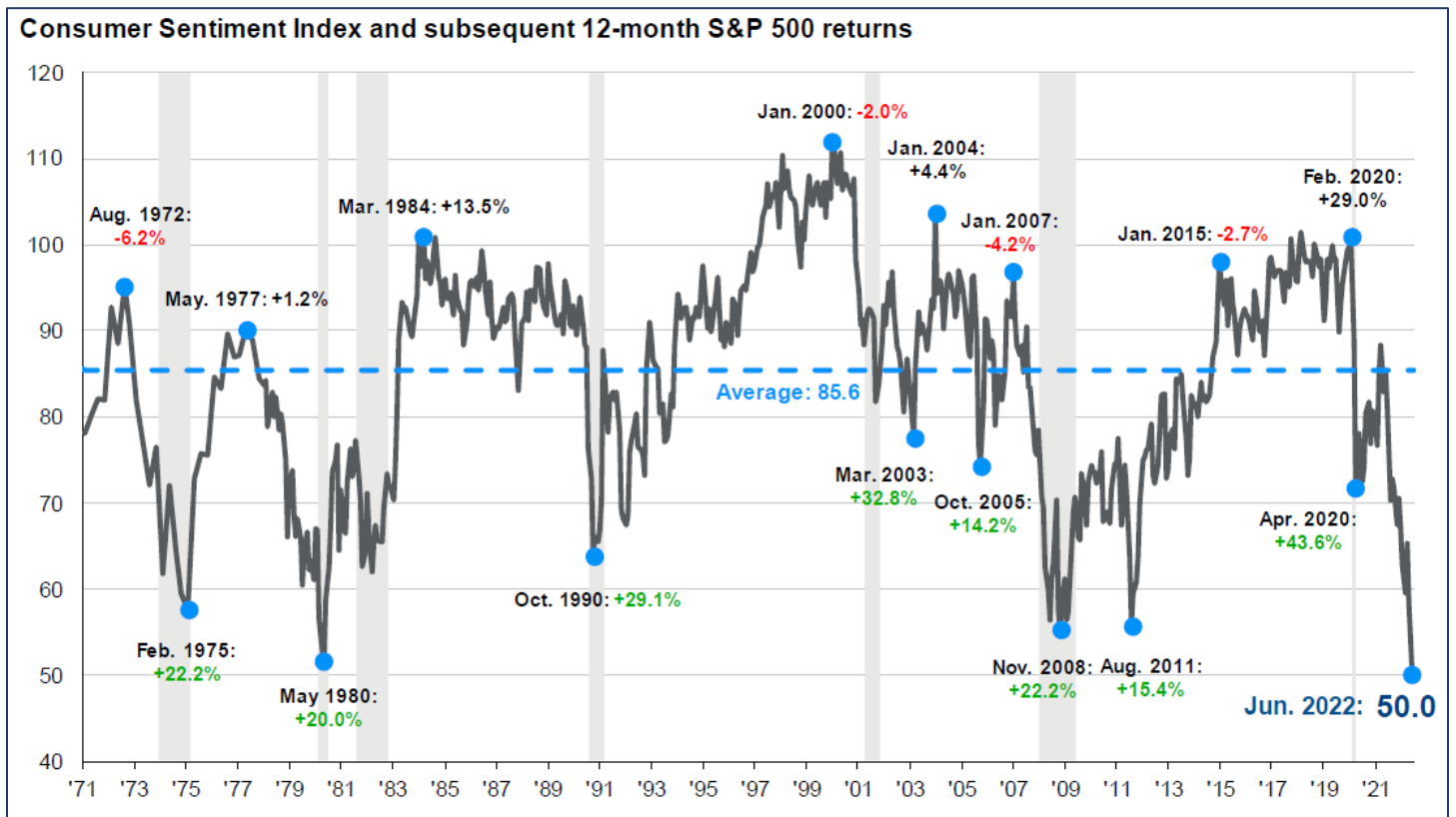
Source: YCharts

Stock valuations have improved as stock prices have fallen, while 3Q and 4Q corporate earnings forecasts have only been marginally affected by the economic backdrop. Consumer demand remains strong and the shutdowns in China has delayed, not eliminated, consumer purchases. There are signs of supply chain bottlenecks easing, which should result in improved company sales during the second half of 2022, thereby supporting earnings estimates. The expected annual returns of equities have risen to mid/high single digits--still significantly higher than cash and bonds.



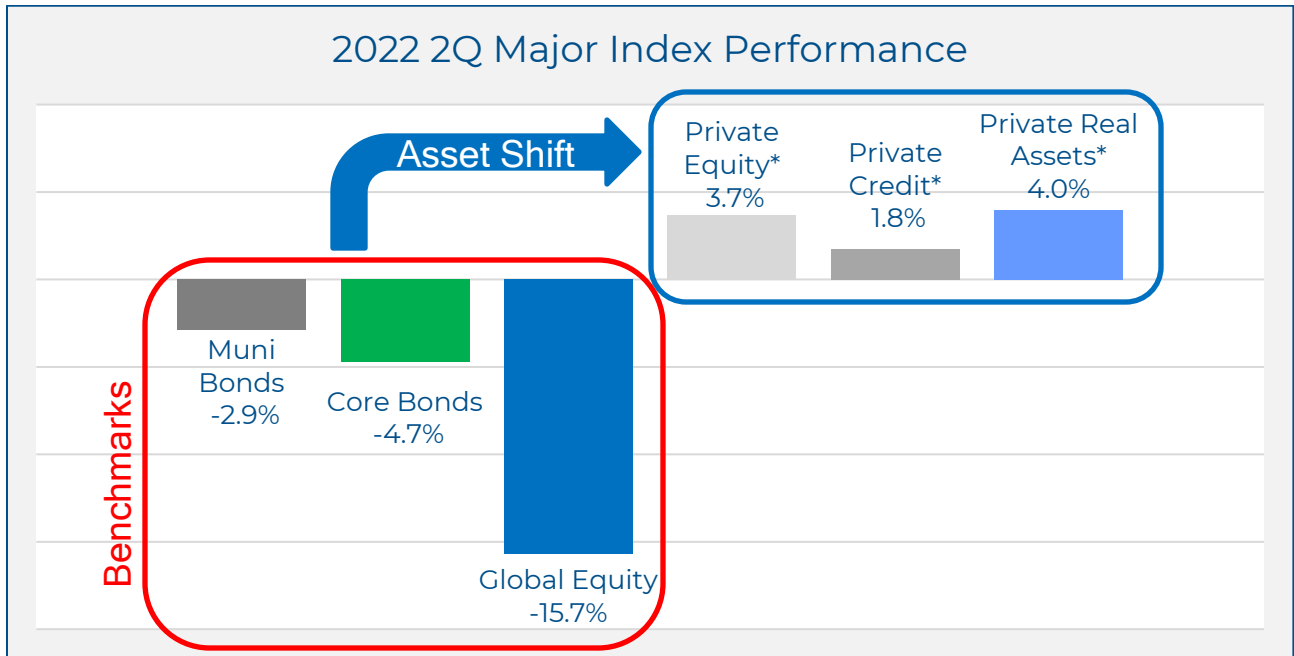
Source: FactSet, JP Morgan

Consumer sentiment has fallen to historic low levels. Behavioral Finance indicates that humans are heavily influenced by recent market events and tend to extrapolate that future asset prices will follow a similar trend. The investment business is the only one in the world where people want to buy more when the price is up and sell when it is down. Thus, Warren Buffett's famous advice for how to make money in the market - "be greedy when others are fearful and be fearful when others are greedy." The below chart plots the Consumer Sentiment Index (CSI) that was created in 1971. The blue dots highlight the peaks and troughs of the CSI. When the CSI is at a trough and consumers are extremely bearish, stock investors have enjoyed fantastic positive returns in eight out of eight periods with an average gain of 24.9% over the next 12 months. Today, investors are fearful and have been selling assets, which has created an opportunity for long-term investors to acquire assets at much more compelling levels.



Source: St. Louis Federal Reserve (FRED), JP Morgan Asset Management

Core Investment Grade bond benchmarks declined **-4.7%** for the Bloomberg U.S. Aggregate index and **-2.9%** for the Bloomberg Municipal Bond index as interest rates rose significantly during the quarter. Global Equities fell **-15.7%** due to persistent inflation, the Fed's actions and the expected impacts. Core Private Market investment returns continued to significantly outperform public markets. In semi-liquid Private Markets, Real Assets were the best performer returning **+4.0%**, Private Equity returned **+3.7%** and Credit gave a strong **+1.8%** return in a tough quarter.



\*Private Market Returns reflect the most recent trailing 3 months of valuations for the semi-liquid core strategies which can be lagged 1 month relative to public markets. GSIS Calculations.

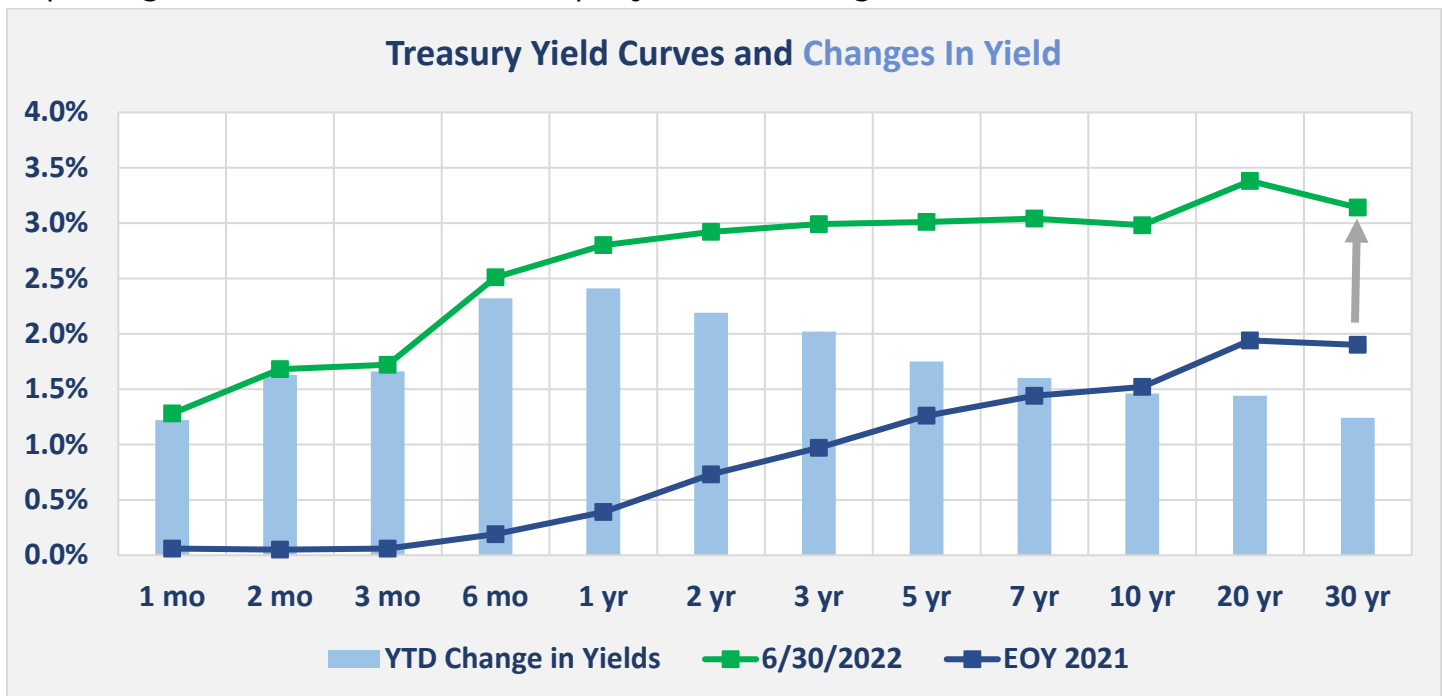
## GSIS 2022 Allocation Positioning

Our rigorous dynamic asset allocation process generated excess performance for the quarter.

- The **Private Credit** portfolios have an underweight to corporate credit risk and lower sensitivity to rising interest rates by employing short term loans and floating rate debt, which held up much better than traditional core fixed income. The 10-year U.S. Treasury interest rate rose significantly from 2.35% to 2.98% resulting in additional negative returns for core bond indexes.
- **Private Real Assets** have demonstrated low-to-negative correlations to equities and fixed income, with less volatility. This asset class was the best performer in client accounts in 2021 and continued to hold the top spot in 2022.
- The **Private Equity** strategies continue to retain value much better than public markets. Private equity managers continued to outperform declining public equities in the second quarter.
- Within **Core Public Fixed Income**, the short duration tilt we implemented outperformed traditional core fixed income benchmarks during the quarter.
- In **Global Public Equities**, our modest overweight in U.S. Large Cap Value over U.S. Large Cap Growth worked well during the quarter with the Russell 1000 Value outperforming the Russell 1000 Growth by +8.7%. The modest overweight to non-U.S. equities over U.S. equities also worked well during the quarter despite a similar central bank response to higher inflation.

## 2022 Headlines – Inflation, Federal Reserve, Russia/Ukraine and COVID

**Inflation** briefly showed signs of slowing in the April data release before jumping higher when the May figures were reported. In response, the **Federal Reserve** approved a previously unlikely 0.75% rate hike in June. Fed chairman Powell recently stated that the Fed is “acutely focused” on bringing down inflation. It was also mentioned that the policy will be flexible, *“If things come in better than we expect, then we’re prepared to do less. If they come in worse than when we expect, then we’re prepared to do more.”* The Fed’s shift in policy has been anything but a soft landing as witnessed by the public market volatility. Interest rates have risen across the yield curve impacting core fixed income and company future earnings.



Source: Treasury.gov

The impact of the **Russia – Ukraine Conflict** still represents a risk to markets and inflation, as Ukraine’s contribution to the global food supply is offline and gas prices continue to sit at high levels.

**COVID-19’s** impact on public markets has mostly vanished except in China, which continually has lockdowns whenever a spike in COVID is observed. These lockdowns diminish the supplies available to meet the high levels of consumer demand and impact supply chains.

It is important to note that these higher interest rates we are experiencing are only high relative to the last couple of years. A healthy longer-term average interest rate and Fed Funds rate resets the Fed’s ability to fight off any future economic problems. In addition, consumers and businesses still remain in a relatively strong financial position. The markets tend to price assets based on forward looking expectations, and have driven current market levels lower.

The active strategic allocation shifts from traditional public assets into core private markets continue to significantly improve absolute and relative performance for our clients. These investments have been significantly accretive to returns while dampening portfolio volatility in this period of increased economic uncertainty and market turbulence.

Thank you for your Trust and Confidence.



**Nick Botticelli**  
Chief Investment Strategist



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