NEW REPUBLIC PARTNERS

**MARKET COMMENTARY**

**1Q 2022**

NEW REPUBLIC PARTNERS

# Market Commentary

| Market Monitor 2022 | Q1% |
|---|---|
| MSCI ACWI Index | -5.3 |
| S&P 500 Total Return Index | -4.6 |
| Bloomberg Barclays Agg. Bond Index | -5.9 |
| Bloomberg Commodity Index | +25.6 |

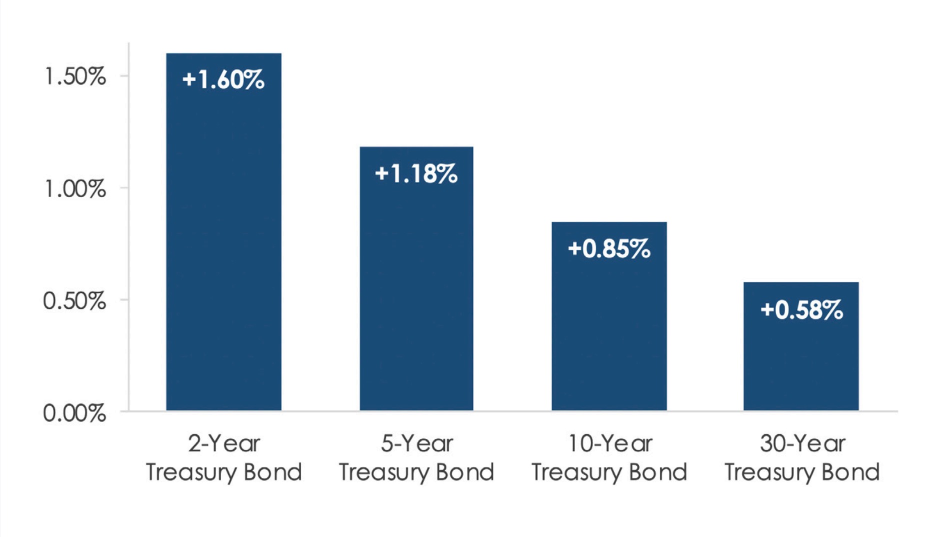
## MULTIPLE THEMES DOMINATE 1Q 2022

There was no shortage of macro themes to dominate the headlines in the first quarter of 2022 with inflation rising to 40-year highs, the Federal Reserve's first interest rate increase since December 2018, and the brutal invasion of Ukraine by Russia.

## Markets React Strongly

Both equity (MSCI ACWI - 5.3%) and fixed income markets (Global Agg -5.9%) fell in sympathy over the quarter, with the latter underperforming the former as U.S. treasuries posted their worst quarter in 50 years! On the flipside, the broad-based commodity index rose 25.6% over the three-month period.

**YTD CHANGE IN U.S. TREASURY BOND YIELDS**




Source: Market Desk, U.S. Treasury. Data as of 3/30/2022.

*"...the back-up in rates and yield curve inversion (should put)...all U.S.-biased 60/40 stock/bond investors on notice that portfolios need to be built differently."*

NEW REPUBLIC PARTNERS

# Market Commentary

## Rising Interest Rates and Inflation Pressures

The massive back-up in interest rates was not unwarranted given the increasingly hawkish guidance from the Fed as it seeks to tame stubborn inflation pressures after achieving the employment goals of its dual mandate. The Consumer Price Index rose +7.9% year-over-year during February 2022, the fastest pace since January 1982. Inflation pressures remained broad with the price of food, vehicles and rent all increasing significantly over the past 12 months. Equities that are more vulnerable to higher interest rates under-performed as highlighted by the continued underperformance of growth stocks relative to value, and the NASDAQ (-9.0%) relative to the broader market (S&P 500 -4.6%).

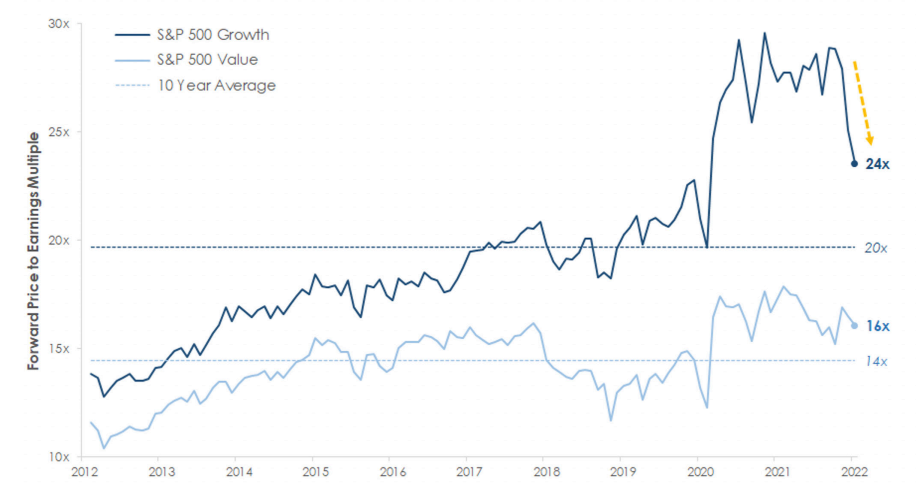
**U.S. STYLE RETURNS (1Q 2022 IN %)**

| | Value | Blend | Growth |
|---|---|---|---|
| Large | -0.7 | -4.6 | -9.0 |
| Mid | -1.9 | -5.7 | -12.7 |
| Small | -2.5 | -7.5 | -12.7 |

*Data Reflects Most Recently Available As of 3/31/2022*

Source: Market Desk.

**S&P 500 GROWTH AND VALUE**




Source: Market Desk.

NEW REPUBLIC PARTNERS

# Market Commentary

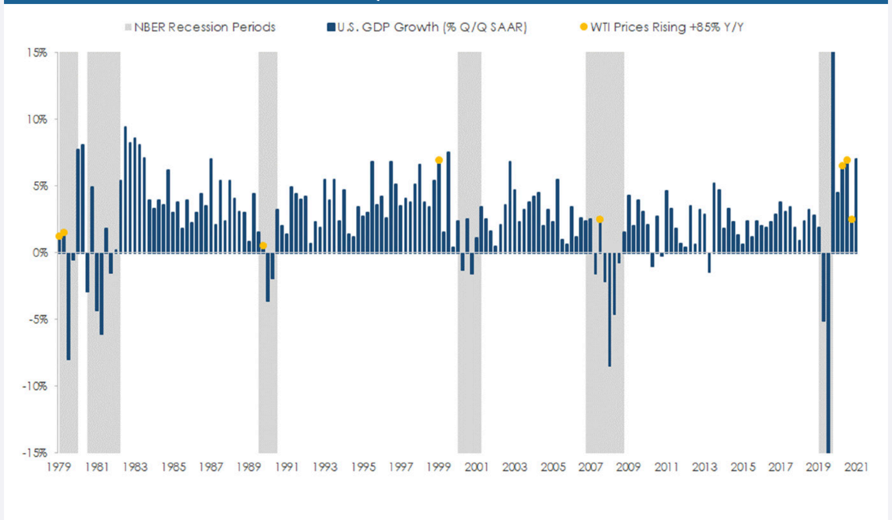
## Russia's Invasion of Ukraine

The striking known/unknown of the quarter was Russia's invasion of Ukraine, which stands to intensify global inflationary pressures. Russia and Ukraine are significant exporters of various commodities, including energy, aluminum and wheat, and Russian sanctions raise the risk of supply shortages and higher prices for key commodities. WTI crude oil traded as high as $130 per barrel in early March, which was the highest level since 2008, while aluminum and wheat prices both reached record highs. The reverberations of the conflict are being felt in Europe's economy as the rise in fuel and input prices are denting consumer demand and re-opening trends.

## U.S. Consumers Faring Well

Amidst the uncertainty around inflation, the Fed's tightening path, and the inflamed geopolitical tensions in Eastern Europe, the U.S. consumer still stands in a good position with household net wealth at an all-time high, moderate indebtedness and a strong savings cushion. Whether measured by TSA passenger throughput or OpenTable reservations, re-opening metrics have nearly reached pre-coronavirus pandemic levels. Elevated energy prices are a concern, but reside at the lower end of U.S. consumer spending at 4% relative to healthcare at 16%, rent at 15% and food at 8%. However, food and energy comprise 30% of consumer spending for the bottom quintile of wealth in the U.S. which deserves a watchful eye.

**SURGING OIL PRICES, SLOWING ECONOMIC GROWTH**




Source: Market Desk.

NEW REPUBLIC PARTNERS

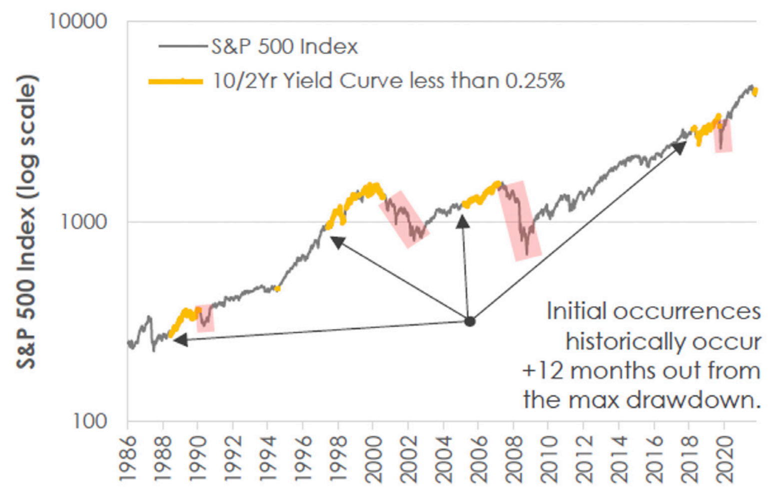
# Market Commentary

## A Key Economic Inflection Point

Looking forward, with a strong job market, increasing inflation and a tightening Fed, we believe we have reached an inflection point in the current economic expansion in the U.S.

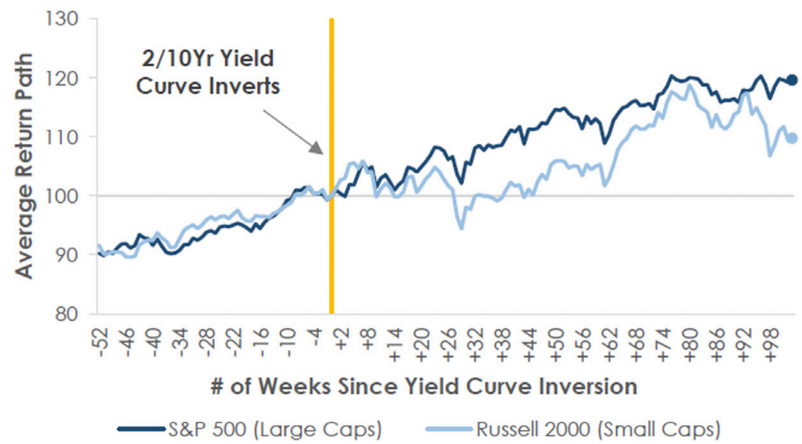
The recent inversion of the yield curve, specifically between the 2- and 10-year treasury bonds, is a notable sign of this turn as the inversion has historically preceded a recession in the U.S. by an average of 20 months. There has been a lot of ink spilled on this indicator of late, questioning its forecasting ability given the high level of Fed intervention in bond markets post the coronavirus pandemic. Given the highlighted strength of the U.S. consumer, we believe the market is "giving notice" that we've moved to a late cycle tightening phase and a recession is on the horizon for later in 2023. More notably, an inversion is not a bearish event for markets, as in the ensuing 12 months U.S. large caps have produced double digit gains in four out of the five past inversions.

**S&P 500 FOLLOWING YIELD CURVE INVERSIONS**




Source: Market Desk, U.S. Treasury.

**LARGE VS SMALL CAP RETURN PATHS AFTER YIELD CURVE INVERSIONS**




Source: Market Desk, U.S. Treasury. Analysis is based on price returns indexed to 100 the week of the yield curve inversion.

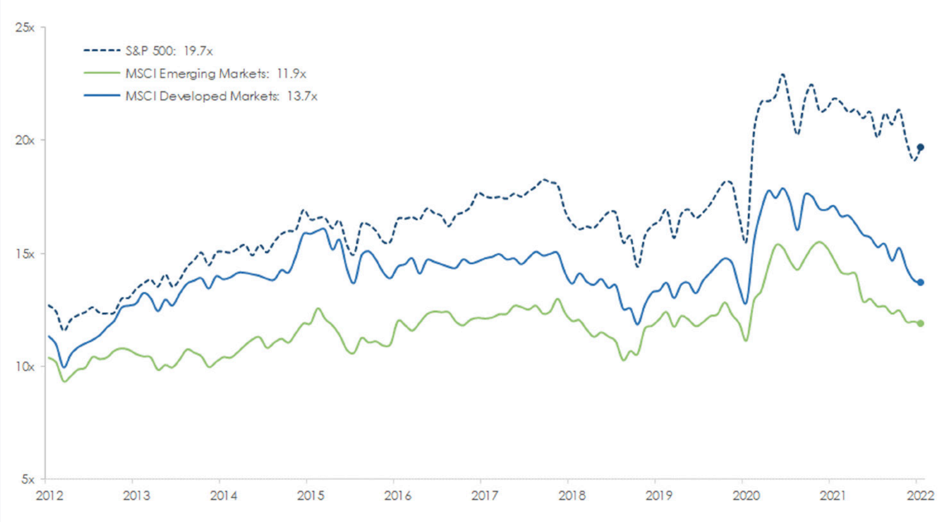
NEW REPUBLIC PARTNERS

# Market Commentary

## A Key Economic Inflection Point continued

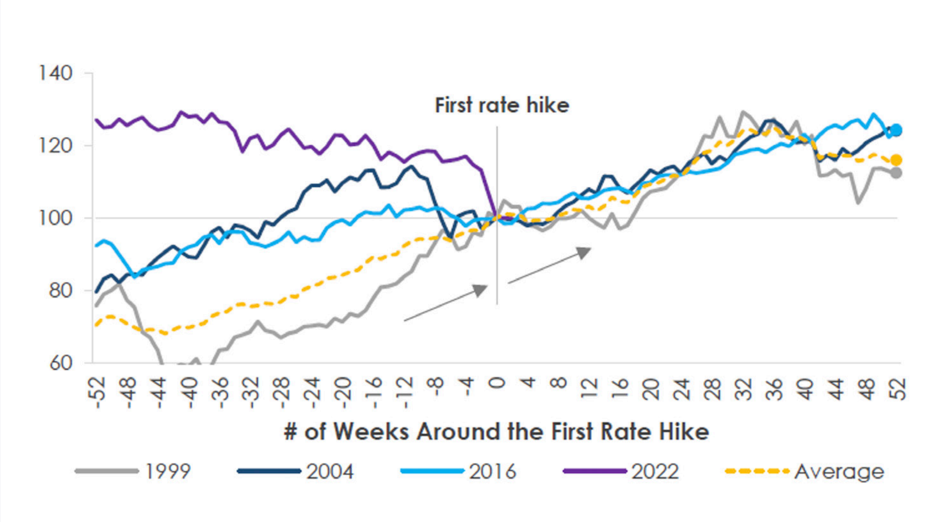
Perhaps less intuitively, the advent of a new Fed tightening also bodes well abroad for emerging markets as EM equities tend to outperform after the first Fed rate hike. Typically, the start of a Fed tightening cycle kicks off a period of U.S. dollar weakness and EM equities historically perform better in a weak USD environment. Furthermore, while China is still dealing with COVID-19 outbreaks due to its zero-COVID-19 policies, it was encouraging to see the government pledge support for its capital markets and take measures to boost economic growth in March. Market participants also took this as a sign that the government would dial back the pressure on its tech and real estate industries that have produced a strong headwind for the past nine months. EM and developed international equities also look very cheap relative to U.S. equities as highlighted in the chart below.

**GLOBAL MARKET VALUATIONS (P/E NTM)**




Source: Market Desk.

**MSCI EM PERFORMANCE BEFORE & AFTER FIRST RATE HIKE**




Source: Market Desk. Analysis is based on the price return of the MSCI Emerging Market Index. Return path is indexed to 100 week of first rate hike.

NEW REPUBLIC PARTNERS

# Market Commentary

## A Key Economic Inflection Point continued

While the back-up in rates and yield curve inversion may put investors on notice that the U.S. economy is shifting to late cycle, it should also put all U.S.-biased 60/40 stock/bond investors on notice that portfolios need to be built differently. We recommend international diversification, the addition of private equity and private credit, exposure to real assets, and incorporating public alternatives through hedged equity and absolute return strategies. These investment strategies are all arrows that allocators need in their collective quiver as they brave through market, economic and geopolitical uncertainty ahead.

As always, we encourage all of our clients to contact their client advisor to learn more about how the New Republic Partners team continues to build portfolios designed not just to weather the current environment but to preserve and grow wealth for decades in a changed investment landscape.

## Disclosure



Investment Committee

**Thomas K. Hoops, CFA**

**Samuel B. Bowles**

**Michael P. Phipps, CAIA**

**J. Keith Benedict**

NEW REPUBLIC PARTNERS

704.626.1526

NEWREPUBLICPARTNERS.COM