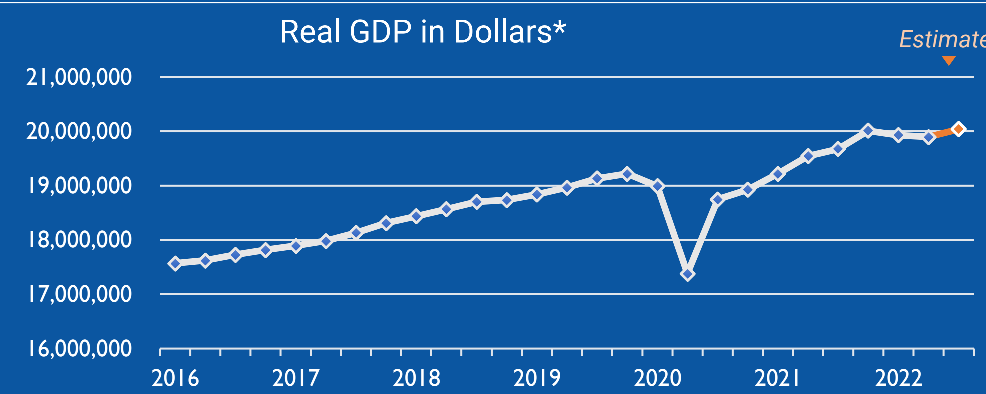
Economic Review

As of September 30, 2022

Other Indicators

	CPI	Unemployment	Sentiment	Crude Oil
Q3: 2021	5.4%	4.8%	70.3	$78
Q2: 2022	9.1%	3.6%	50.0	$120
Q3: 2022	8.2%	3.5%	58.6	$89



*Billions

Inflation, Recession or Stagflation?

- Social Security checks will be 8.7% bigger in 2023, the largest cost-of-living adjustment to benefits in four decades.

- The overall **CPI** increased 8.2% in September from the same month a year ago, pulled down by a drop in gasoline prices that was partially offset by higher food costs. The reading was down from 8.3% in August and 9.1% in June, which was the highest inflation rate in four decades.

- According to the Fed's Beige Book, U.S. businesses are becoming more pessimistic about economic conditions in the face of high inflation and rising interest rates.

- The U.S. is forecast to enter a **recession** in the coming 12 months as the Federal Reserve battles to bring down persistently high inflation. Expectations for a recession have increased because economists increasingly doubt the Fed can keep raising rates without inducing higher unemployment and an economic downturn.

- The U.S. currently has an **inverted yield curve**, as short-term interest rates exceed long-term rates. This type of yield curve has historically preceded periods of economic recession. Shorter rates have risen rapidly over the past year, with 2-year Treasury yields more than doubling. A slowdown could mean somewhat lower rates in the future.

- Pension and other defined benefit plans, as well as DC plan participants, are exposed to yield curve risk. That is the risk that fixed-income instruments (such as bonds) experience as a result from the inverse relationship that bond prices and interest rates have to one another.

- While there is no mathematical formula that defines whether we are experiencing **stagflation**, economists generally agree that it would be a sustained period of both high inflation and slow growth, not just one or two quarters.

Market Review

As of September 30, 2022

U.S. stocks declined broadly in the third quarter, adding to losses in the first two quarters. The S&P 500 Index closed at 3586, down from 3785 on June 30. The index rose 9.2% in July, fell 4.1% in August, and dropped 9.5% in September.

In the U.S., growth outperformed value, and smaller capitalizations outperformed larger.

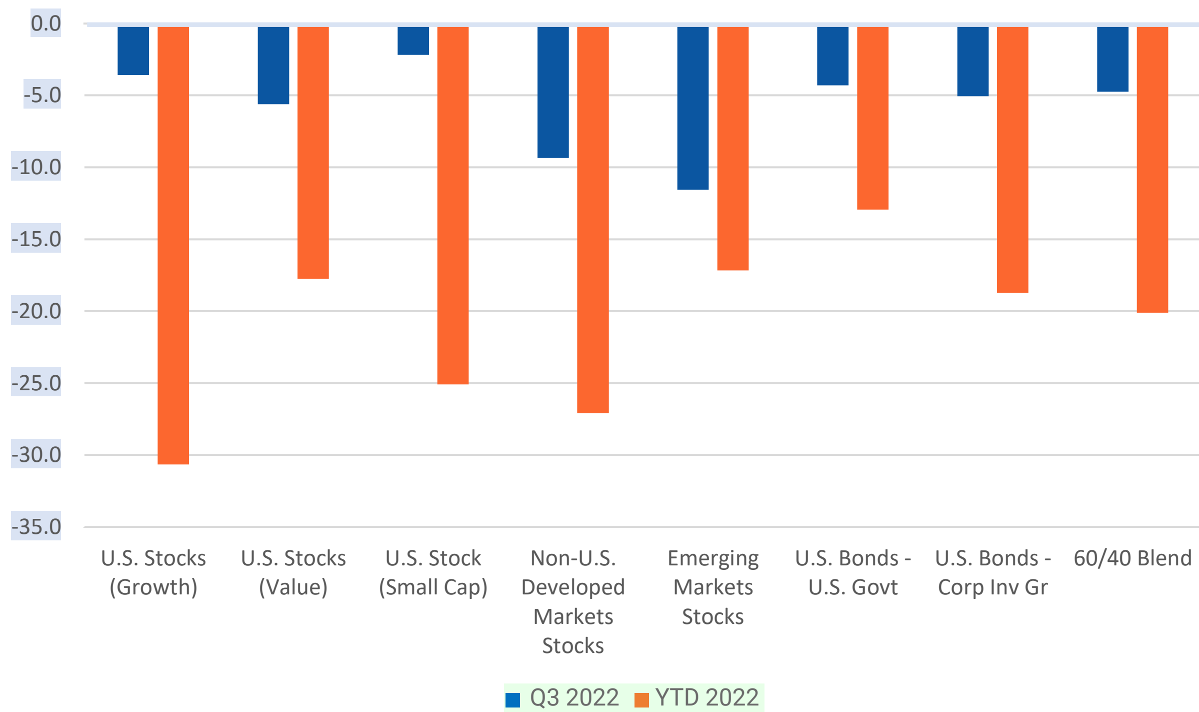
Only two sectors of the S&P 500 had positive returns – Consumer Discretionary (helped by Amazon) and Energy. The worst performers were Communications Services and REIT's.

Information Technology was the largest detractor because of its weight in the index (27%), but the sector only modestly underperformed the index. Individual securities had mixed performance: Tesla, Netflix, and Apple were among the largest contributors, while Microsoft, Alphabet (Google), NVIDIA, and Meta Platforms (Facebook) were among the largest detractors..

In the U.S., stocks had broadly negative returns; smaller capitalizations and growth outperformed.

Outside the U.S., both developed and emerging markets declined. Within the emerging markets, the Hong Kong-based China 50 Index fell 22.9%.

Within U.S. fixed income markets, interest rates on U.S. Treasury bonds rose across the yield curve again. The US Aggregate Index fell 4.8%.



Asset class returns are represented by the following indexes: Russell 1000 Growth and Value, and Russell 2000 Index (U.S. Stocks), MSCI EAFE Index (Non-U.S. Developed Stocks), MSCI Emerging Markets Index (Emerging Market Stocks), Bloomberg Barclays U.S. Government Index (U.S. Bonds - Govt), and Bloomberg Barclays US Corporate Bond Index (U.S. Bonds – Corp IG). The Blend is 60% S&P 500/40% US Aggregate.

Drivers of Capital Markets Returns

- Fixed income investments are debt instruments typically issued by governments and corporations. They generally pay a periodic fixed amount of interest until maturity, at which time the principal is repaid. Investors in fixed-income instruments are **lenders.**
- Corporations can also raise capital by selling shares, also known as equity. Equity investors share in a company's success or failures over time. Investors in equity are **owners**.

The price of the S&P 500 Index as of September 30, 2022, was 3,585.62.

Returns to Lenders

Inflation ⬇ 8.2%

September's CPI was 8.2% above the month a year ago. Energy prices contributed 1.6% of the increase (vs. 3.6% in 2Q); the core rate was higher at 6.7%.

Interest Rates ⬆ 0.82%

The yield of a 10-year U.S. Treasury bond rose from 2.98% on June 30 to 3.80% on September 30. The rate for a 2-year note rose 127 bps.

Credit Spreads ⬆ 0.24%

The yield spread of a generic A/BBB-rated corporate bond rose 24 basis points to 238 basis points. The yield spread measures the yield of 10 – 15-year corporate debt compared to U.S. Treasury Bonds of equivalent maturity.

Returns to Owners

Growth (GDP)

2Q 2022	3Q 2022E
-0.6%	2.8%*

The Atlanta Fed forecasts a return to positive real growth of GDP in the third quarter. Persistent high employment supports real growth of personal expenditures, offset by declining residential investment.

Profitability

2022E	2023E	%Change23E
$224.00	$241.15	7.7%

The consensus estimate of 2023 earnings for the S&P 500 *declined* by 3.8% during the third quarter. The estimate for 2023 was 7.7% above 2022.

Valuation

2022E P/E	2023E P/E
16.0	14.9

On September 30, the price of the S&P 500 was 14.9x its estimated 2023 earnings. The multiple declined as the price fell by more than the earnings estimate.

**October 14, 2022 – Federal Reserve Bank of Atlanta GDPNow estimate*