MarketSay"

The first six months of 2022 have been a brutal time to be an investor. The S&P 500 index ended June 21% below the level at the start of the year. The Nasdaq 100 index now trades 30% below its November all-time high levels and returned -29% during the first half of 2022. Both stocks and bonds have posted negative year-to-date returns, a 60% US Equity/40% US Bonds portfolio has had its worst first half return since 1932 (-17%). Gold, viewed as an inflation hedge for the past 2,000 years has delivered a YTD return of -2%. There have been very few places for investors to hide. The trend of equity weakness continued in June. Concerns over rising inflation levels and the chance of an economic recession drove price action.

Policy Watch: Central banks across the globe increase interest rates again in June. The US Fed hiked by 75bps for the first time since the early 1990s, the Reserve Bank of Australia hiked rates by 50bps. Speakers from the US Federal Reserve continued to prepare investors for further hikes in July and beyond. While the European Central Bank now has been preparing the market for a rate hike in July following another record high inflation print in June.

Inflation Watch: Inflationary pressures remain high in the US, UK and Europe. They appear to be building in Australia as well. Expectations of a sharp fall in annual rates with 2021 data rolling-off have not been met and it appears that the path to lower increases will take longer than expected. Supply chains remain disrupted by China's covid-zero policy, although some changes may ease those issues.

Risk Budget: Volatility has been elevated in 2022 and remains the case. The S&P 500 index has registered a daily move greater than 2% on more than 20% of trading days this year, a rate more than 2 ½ times the average during the past 20 years. Four S&P 500 bounces greater than 6% have occurred YTD. Bond volatility is starting to ease from record high levels

Call to Action: We further reduced our equity exposure early in June on our belief that the level of earnings growth baked into the forecasts for US corporates is too high given the interest rate outlook, margin pressure and slowing economic indicators. Our view has not changed. July will bring Q2 corporate updates that are likely, we believe, to reveal lower forward guidance, especially in areas where discretionary spending is a driver of sales. The buy the dip mentality this year has seen small bounces in equity markets – but they have been followed by double digit falls. At a macro index level, we believe that it is too early to 'buy-the-dip' and increase our equity weight. However, the sell off this year has resulted in many high quality companies, particularly in the enterprise software solution space, offer some value for clients with a longer term time frame willing to ride out the next 6-12 months of volatility.

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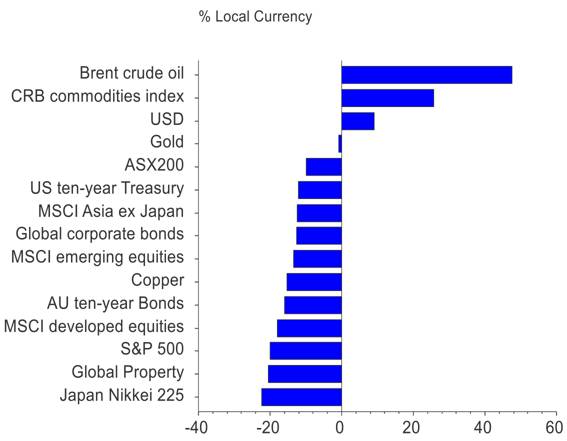
June Review

The first six months of 2022 have been a brutal time to be an investor. The S&P 500 index had fallen by 24% from its peak in early January. It has bounced recently but still trades 21% below the level at the start of the year. The Nasdaq 100 index trades 30% below its November all-time high levels and returned -29% during the first half of 2022. Both stocks and bonds have posted negative YTD returns, a 60% US Equity/40% US Bonds portfolio has had its worst first half return since 1932 (-17%). Gold, viewed as an inflation hedge for the past 2,000 years has delivered a YTD return of -2%. There have been few places for investors to hide.

The story of the market so far in 2022 has largely been centred around higher-than-expected inflation readings translating into a faster-than-expected pace of Fed tightening, which has prompted a rise in bond yields (10-year Treasury yields 1.4% to 3.0%) which has compressed the S&P 500 P/E multiple by 24% (from 21x to 16x) and led to a 20%+ decline in US equities. Earnings growth forecasts are now only starting to be revised.

Focusing on June, it was another weak month for global equities with investors concerned about rising inflation levels and the chance of an economic recession. S&P 500 declined -8.3%. Australian markets underperformed, S&P/ASX 200 falling (-8.8%).

Chart 1: 2022 YTD Asset Class Performance

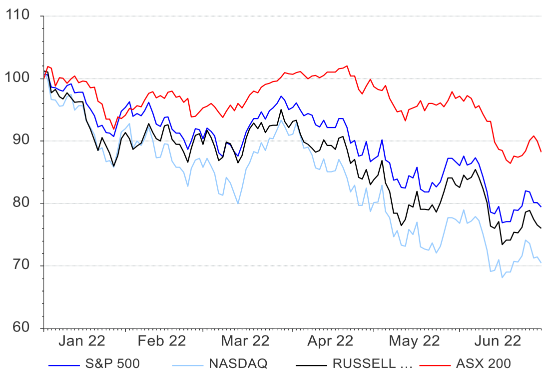


Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

Australian 10-year yields moved in reaction to the tightening monetary policy, selling off 32bps to 3.66%. US yields also sold off 13bps to 2.98%, yields spent most of the month above 3% as key inflation metrics continue to surprise to the upside. Growing US inventories saw Brent Oil prices pull back US$8 to US$114/bbl. While recession concerns and a strong US Dollar drove a repricing of commodities. Iron Ore prices dropped US$16 to US$123/Mt as China's demand and profit margins in domestic steel mills continue to decline. Gold dropped by US$22 to US$1,817 as rising global rates push investors into other safe haven assets.

In June in Australia, Consumer Staples (+0.2%) was the strongest performing sector, while Energy (-0.3%), and Health Care (-3.1%) also outperformed. The Materials (-12.4%), Financials (-11.9%) and IT (-11.0%) sectors were the worst performers. All S&P500 sectors ended the month lower, with the Energy (-16.8%) and Materials (-13.8%) the worst performers. Consumer Staples outperformed losing 2.5%.

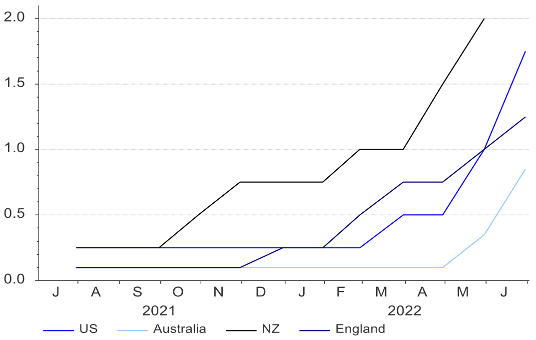
Chart 2: US and Australian Equity Markets YTD Relative Performance (100 = 1 Jan 2022)



Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

Monetary policy continues to dominate market price action. Both central bank rhetoric and actions are being closely watched. In June the Reserve Bank of Australia hiked by 50bps, the US Fed hiked by 75bps (its largest since 1994), the bank of England by 25bps and the Swiss National Bank surprised markets with a 50bp move. The European Central Bank is yet to lift interest rates but has strongly indicated that this will occur in July.

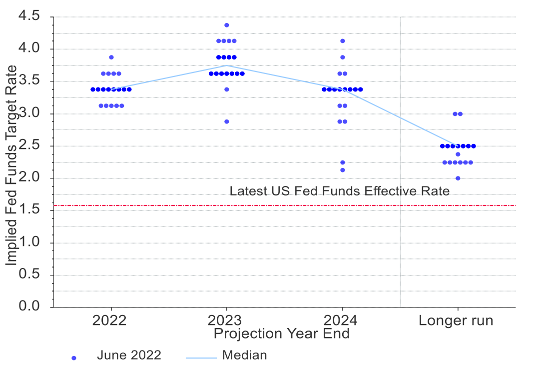
Chart 3: Central Bank Hiking



Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

Comments from Fed Chair Powell soothed some concerns, saying that he doesn't expect moves of this 75bps size to be common and that either 50 bps or 75 bps was most likely at the next meeting in July. The new Funds Rate projections were released and show that the median interest expectation from FOMC members for end 2022 lifted from 1.75-2.0 to 3.25-3.5 equating to another 175 bps of tightening over the remaining four FOMC meetings this year, with three 50 bp hikes. In 2023 the median dot is raised from 2.75 to 3.75 while for 2024 the Fed is now predicting the start of an easing cycle with a 3.25- 3.50 median dot. The Market had already priced in Fed easing in H2 2023 ahead of this meeting.

Chart 4: FOMC Dot Plot



Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

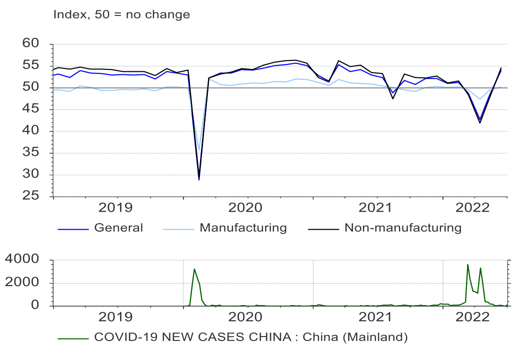
Emerging Markets have outperformed developing markets so far in 2022, in local currency and USD terms. This trend continued in June with a continued turnaround in Chinese equities occurring since April. Markets have been rallying on the back of a decline in new covid cases in Shanghai, some changes to covid-policy, including mass testing rather than lockdowns, government support for the economy and monetary policy support through key lending rate cuts. Sayers portfolios have exposure to Chinese technology names across our Emerging Market Equity Exposures, in particular the Asia 50 ETF added in late March.

Chart 5: China, Australia & US Equities

Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

Towards the end of the month Chinese manufacturing PMIs recovered by more than expected. Traffic numbers are returning to more normal levels as lockdown measures ease, however there continues to be nervousness. We believe that economic stimulus remains likely, to achieve government growth goals, any recovery is likely to be more modest than the post-covid recovery in 2020.

Chart 6: Chinese PMI & New Covid Cases



Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

Inflationary pressures in the US remain stubbornly high. Expectations had been that base effects (large monthly increases in March, April and May 2021) would be replaced by much lower numbers this year, however monthly numbers have surprised to the upside. High headline inflation data includes food

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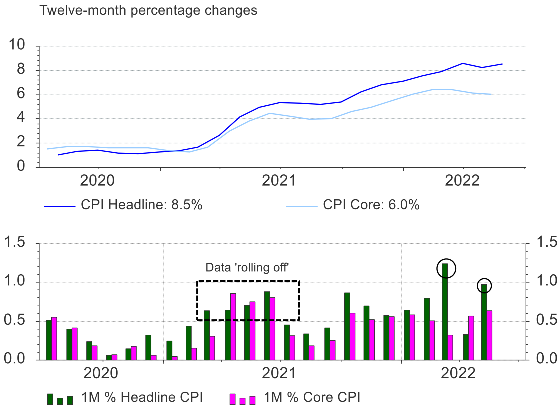
and energy costs which have been rising in 2022. Despite core measures slowing, they are not doing so as fast as expected suggesting the US Fed will have to continues there very aggressive hiking path.

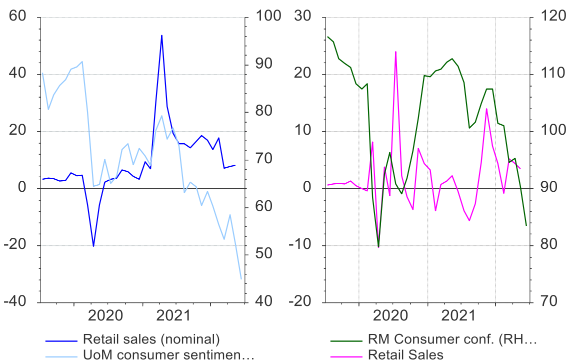
Chart 7: US CPI



Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

The increasing talk of recession and rising interest rates has dented consumer confidence in developed markets. Regardless of market, the story is much the same, retail sales for now are holding up given high savings rates from government stimulus and previously low interest rates. While labour markets remain tight in markets like the US and Australia (depicted below) increasing mortgage rates paired with rising cost of living are pushing consumer confidence readings to recessionary levels. This suggests that it is only a matter of time before this flows through to actual spending.

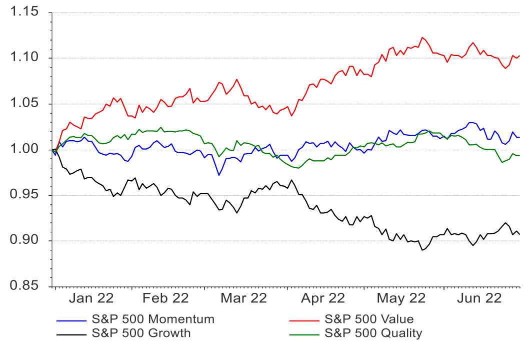
Chart 8: US & Australia Retail Sales & Consumer Confidence



Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

Value has been the more dominant factor in US markets year-to-date, with a clear rotation out of growth stocks as real yields rise. Quality and moment have had little impact.

Chart 9: S&P500 Equity Factor Relative Performance (YTD)

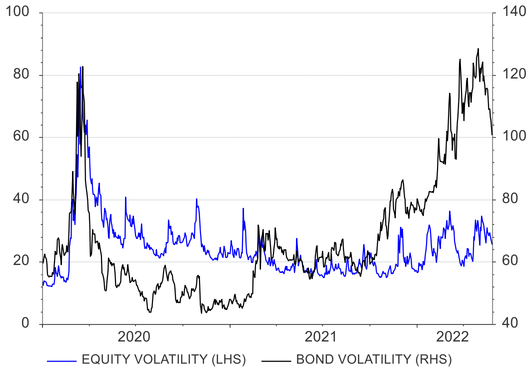


Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

Risk

Volatility has been elevated. The S&P 500 index has registered a daily move greater than 2% on more than 20% of trading days YTD, a rate more than 2 ½ times the average during the past 20 years. Four S&P 500 bounces greater than 6% have occurred YTD.

Chart 10:US equity & bond Volatility (MOVE)



Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

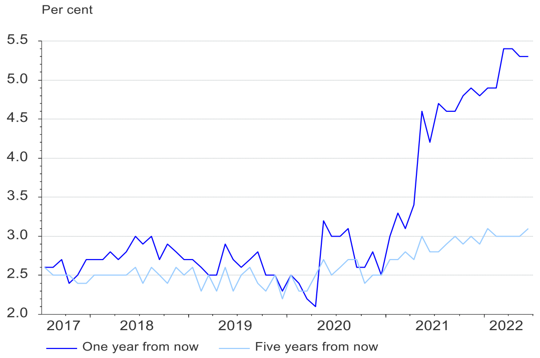
Outlook

Regaining control of inflation, and more particularly inflation expectations, will be the key policy objective of central banks for the next year. Ronald Reagan once said that "inflation is as violent as a mugger, as frightening as an armed robber and as deadly as a hit man". There is no doubt that inflation destroys savings, impedes planning, and discourages investment – which leads to less productivity and a lower standard of living.

The pivot of central banks from transitory to inflation hawks, and the more aggressive market pricing of cash rate increases, is all aimed at lowering inflation expectations and avoiding the problem of people's expectations of future inflation anchoring at higher levels. The anchoring of inflation expectations is a necessary condition for central banks to maintain price stability, as it prevents temporary shocks to inflation from feeding into the mechanisms of wage and price formation.

While the equity markets will continue to find pockets of confidence when data shows actual inflation coming down or aggregate demand slowing more quickly, it is more likely that central banks will retain an aggressive tightening bias until inflationary expectations start to come down. When it comes to anchoring inflation expectations at lower levels, it's better to have short term pain for long term gain in the central bank playbook.

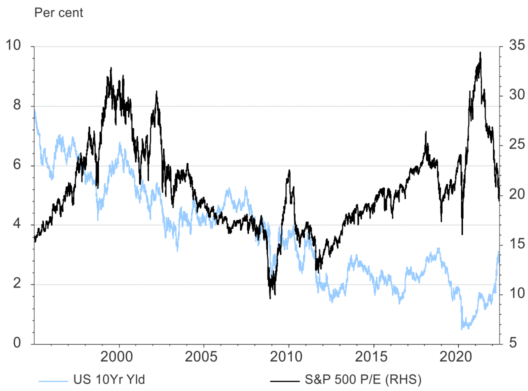
Chart 11: US Inflation Expectations



Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

The real issue is that global supply chains remain disrupted and there is little sign of a significant improvement coming. Lockdowns and enforced isolation have severely impacted the ability to provide much of the goods and services we need. Resources, which are suddenly in demand again, have had years of under investment and supply is constrained. Labour supply and mobility is not what it was before the pandemic. These supply shocks, combined with the invasion in Ukraine impacting energy and soft commodity supply, means that aggregate demand is likely to have to fall significantly to get prices back towards a more normal level.

Chart 12: US Bond Yields vs P/E Ratio



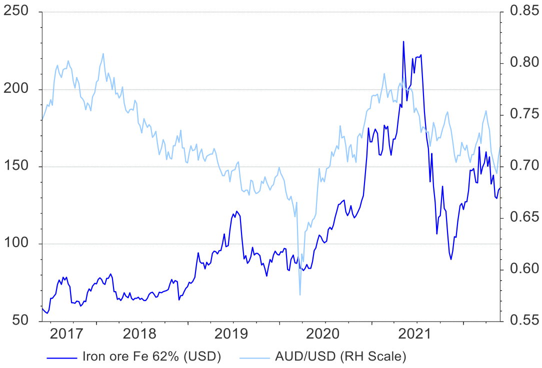
Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

Long bond yields have been volatile and currently sit around 3 per cent. While this level can provide some comfort to equity valuations, the likelihood is that bond yields will need to rise further as central banks get into their work. As yet, corporate earnings have not been downgraded, and the market sell off in 2022 has largely been a derate of the price earnings multiple from 21 to 17. The next issue for equity markets will be the likely downgrades for corporate earnings as growth slows. Q2 reporting season in the US kicks off shortly, and investors will be very focused on margins and the outlook statements. Until it is clear that inflation is getting back under control, equities will remain volatile and struggle to rally up through resistance levels. In all likelihood, we have seen the highs in equity markets already this year.

That said, there always opportunities in markets to by dynamic and add value to portfolios. Companies with good balance sheets and the ability to pass on higher prices to protect margins are still likely to be well supported. Regional markets appear to be out of synch, and there will be opportunities to change regional allocations to add value. We continue to favour an overweight to Asia. It remains cheap on a relative value basis and is likely to benefit from stronger growth in China as they slowly emerge from their pandemic lockdowns.

The relative strength of the $US has seen the $A weaken to below $US0.70 cents despite commodity prices remaining strong. The $A is expected to bounce around between 68-75.

Chart 13: AUD & Iron Ore Price



Source: Refinitiv Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

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Sayers Capital Solutions Group

8 July 2022

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