MARKET INSIGHTS

from Ziegler Capital Management

Monthly Market Commentary: August 2022

Financial news headlines continue to be led by inflation running at multi-decade highs, recessionary fears, the Ukraine / Russia war, and the related economic sanctions, the pace and size of future increases in the Federal Funds rate and continued albeit improving supply chain disruptions. There was some movement towards end of the month for the narrowly divided Senate to pass a package which raises roughly $739 billion in new revenue and spends $433 billion on climate and healthcare programs. The Democrats have tried and failed for much of the last year to pass a party-line economic package. Republicans oppose the package, saying it will damage the economy. Democrats are using a budget reconciliation process that allows a bill to advance in the Senate with a simple majority, rather than the 60-vote supermajority usually needed.

The S&P 500 returned 9.22% in July, bouncing back from a -8.25% return in June. This is the best monthly return since November 2020. For the year-to-date period through July 31st, the S&P 500 has returned -12.58%. Small cap stocks, as measured by the Russell 2000, returned 10.45% in July and have returned -15.43% on a year-to-date basis as of July 31, 2022. This contrasts with the 14.82% return for calendar year 2021. Large Cap Growth outperformed Value in July, with the Russell 1000 Growth returning 12% and the Russell 1000 Value returning 6.63%. On a year-to-date basis as of July 31, 2022, Large Cap Value has significantly outperformed Large Cap Growth, with a return of -7.08% versus -19.44%. In July, the Russell 2000 Value returned 9.68% and the Russell 2000 Growth returned 11.20%. On a year-to-date basis as of July 31, 2022, Small Cap Value outperformed Small Cap Growth, with a return of -9.30% for Small Cap Value versus Small Cap Growth at –21.55%.

Returns by Sector

	S&P 500		Russell 2000	
Sector	July 2022	YTD	July 2022	YTD
Communication Services	3.71	-27.57	6.59	-24.82
Consumer Discretionary	18.94	-20.10	13.31	-26.13
Consumer Staples	3.30	-2.47	3.69	-6.77
Energy	9.72	44.66	13.52	39.41
Financials	7.21	-12.86	9.19	-11.01
Health Care	3.32	-5.29	10.11	-23.65
Industrials	9.50	-8.88	13.03	-10.23
Information Technology	13.54	-17.01	11.50	-25.47
Materials	6.14	-12.85	8.93	-10.86
Real Estate	8.54	-13.20	9.32	-17.68
Utilities	5.50	4.92	4.98	3.96
TOTAL RETURN	9.22%	-12.58%	10.45%	-15.43%

Source: Bloomberg

WRITTEN: AUGUST 1, 2022

ABOUT ZCM MARKET INSIGHTS

A series that provides a glimpse of our internal thought process through current topics affecting our clients and colleagues.

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Ziegler CAPITAL MANAGEMENT, LLC

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Real gross domestic product (GDP) decreased at an annualized rate of 0.9%% in the first quarter of 2022 according to the "advance" estimate released by the Bureau of Economic Analysis (BEA). This follows a decrease of 1.6% in the first quarter. The decrease in real GDP reflected decreases in private inventory investment, residential fixed investment, federal government spending, state and local government spending, and nonresidential fixed investment that were offset by increases in exports and personal consumption expenditures (PCE). Imports, which are a subtraction in the calculation of GDP, increased. The decrease in private inventory investment was led by a decrease in retail trade (general merchandise stores and motor vehicle dealers). The decrease in residential fixed investment was led by a decrease in "other" structures (specifically brokers' commissions). The decrease in federal government spending reflected a decrease in non-defense spending that was somewhat offset by an increase in defense spending. The decrease in nondefense spending reflected the sale of crude oil from the Strategic Petroleum Reserve, which results in a corresponding decrease in consumption expenditures. The decrease in state and local government spending was led by a decrease in investment in structures. The decrease in nonresidential fixed investment reflected decreases in structures and equipment that were mostly offset by an increase in intellectual property products. The increase in imports reflected an increase in services (led by travel). The increase in exports reflected increases in both goods (led by industrial supplies and materials) and services (led by travel). The increase in PCE reflected an increase in services (led by food services and accommodations as well as health care) that was partly offset by a decrease in goods (led by food and beverages).

The Institute for Supply Management's (ISM) Purchasing Managers' Index (PMI) registered 52.2 in July, a decrease from the June reading of 53.0. This figure indicates expansion in the overall economy for the 26th month in a row after a contraction in April and May 2020, but is the lowest reading since June 2020 when it registered 52.4. A reading of over 50 is considered to be expansionary. According to the ISM, "The U.S. manufacturing sector continues expanding — though slightly less so in July — as new order rates continue to contract, supplier deliveries improve and prices soften to acceptable levels. According to Business Survey Committee respondents' comments, companies continue to hire at strong rates, with few indications of layoffs, hiring freezes or headcount reduction through attrition. Panelists reported higher rates of quits, reversing June's positive trend. Prices expansion eased dramatically in July, but instability in global energy markets continues. Sentiment remained optimistic regarding demand, with six positive growth comments for every cautious comment. Panelists are now expressing concern about a softening in the economy, as new order rates contracted for the second month amid developing anxiety about excess inventory in the supply chain".

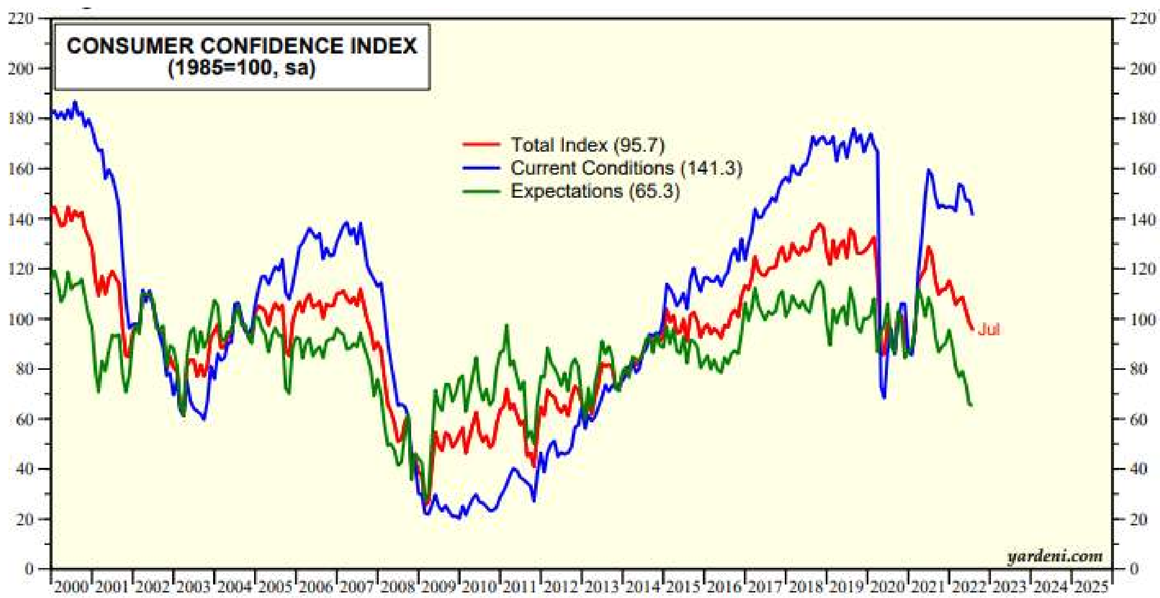
According to the U.S. Bureau of Labor Statistics (BLS), the unemployment rate was unchanged in June, at 3.6%, the same as the previous three readings. Total non-farm payroll employment rose by 372,000 in June. Notable job gains occurred in professional and business services, leisure and hospitality, and health care. The number of unemployed was essentially unchanged at 5.9 million. Both measures continue to fall and are significantly lower than their April 2020 highs and are now roughly in line with their February 2020 pre-pandemic levels of 3.5% and 5.7 million people. The labor force participation rate was 62.2% in June, little changed since February. It has remained in a narrow range since June 2020.

The U.S. savings rate was 5.1% in June, a decrease from 5.4% in May. The long-term average savings rate is approximately 9% after its stunning peak of 32.2% in April 2020. Personal income increased $133.5 billion in May (0.6%), according to the Bureau of Economic Analysis (BEA). The increase in personal income in June primarily reflected increases in compensation (led by private wages and salaries) and proprietors' income (mainly nonfarm). Other current transfer receipts increased $12.9 billion in June, reflecting a legal settlement from a corporate business to individuals. The national income and product accounts record these settlements on an accrual basis in the month when the settlement is reached, regardless of when they are recorded on companies' financial statements. The $181.1 billion increase in current-dollar PCE in June reflected an increase of $94.9 billion in spending for goods and an increase of $86.2 billion in spending for services. Within goods, gasoline and other energy goods was the leading contributor to the increase. Within services, the largest contributors to the increase were spending for health care and for housing and utilities (mainly housing).

The Federal Reserve's July statement noted, "Recent indicators of spending and production have softened. Nonetheless, job gains have been robust in recent months, and the unemployment rate has remained low. Inflation remains elevated, reflecting supply and demand imbalances related to the pandemic, higher food and energy prices, and broader price pressures. Russia's war against Ukraine is causing tremendous human and economic hardship. The war and related events are creating additional upward pressure on inflation and are weighing on global economic activity. The Committee is highly attentive to inflation risks". The Fed reiterated its objectives of maximum employment and a 2% inflation rate over the longer run. The Fed raised the target range for the federal funds rate by 75 basis points to a range of 2.25% to 2.50% and anticipates that further rate increases will be warranted. This was the fourth rate-hike so far in 2022 and the largest (along with June) since 1994. As previously announced, the Committee will continue reducing its balance sheet holdings. It further stated, "In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals. The Committee's assessments will take into account a wide range of information, including readings on public health, labor market conditions, inflation pressures and inflation expectations, and financial and international developments."

Consumer Confidence decreased in July to 95.7 from a downward revised 98.4 in June and is at its lowest level since February 2021. Consumer Confidence recently reached a peak of 128.9 in June 2021. According to a statement from the Conference Board, "Consumer confidence fell for a third consecutive month in July. The decrease was driven primarily by a decline in the Present Situation Index—a sign growth has slowed at the start of Q3. The Expectations Index held relatively steady, but remained well below a reading of 80, suggesting recession risks persist. Concerns about inflation—rising gas and food prices, in particular—continued to weigh on consumers. As the Fed raises interest rates to rein in inflation, purchasing intentions for cars, homes, and major appliances all pulled back further in July. Looking ahead, inflation and additional rate hikes are likely to continue posing strong headwinds for consumer spending and economic growth over the next six months." The Current Conditions Index (which is based on consumers' assessment of current business and labor market conditions) fell to 141.3 from an upward revised 147.2 in June. The Expectations Index (which is based on consumers' short-term outlook for income, business, and labor market conditions) fell slightly to 65.3 in June from a revised 65.8 in June. According to information from the BEA, the consumer is responsible for approximately 70% of the U.S. economy.

Consumer Confidence



Source: The Conference Board.

The Bloomberg U.S. Aggregate Bond Index returned 2.44% in July and has returned -8.16% on a year-to-date basis as of July 31st. July was only the 2nd positive month for the index in 2022. This return is on the heels of a -1.54% return for calendar year 2021. The 10-Year U.S. Treasury ended July at 2.65% after ending June at 3.02% and beginning the year at 1.51%. It has increased dramatically since hitting an all-time low of 0.54% in July 2020. The 2-Year U.S. Treasury and 10-Year Treasury spread ended July with a spread of -24 basis points (2-year: 2.89% and 10-year: 2.65%). This contrasts with figures from the beginning of the year with a spread of 78 basis points (2-Year: 0.73 % and 10-Year: 1.51%). Option Adjusted Spreads (as represented by the Bloomberg Corporate Index) ended July at 144 basis points, 11 basis points tighter than the June month end of 155 basis points. Spreads began 2022 with a reading of 92 basis points.

West Texas Intermediate (WTI) finished July at $98.62 per barrel, decreasing 6.8% from June at $105.76 per barrel. WTI has increased 31.1% since beginning 2022 at $75.21 per barrel. This is on the heels of a 58.9% increase in 2021. Turmoil from the invasion of Ukraine by Russia, the related sanctions and increasing demand have been a significant factor in the increases so far in 2022. WTI is significantly higher than April 2020's close at $18.84 per barrel during the Saudi/Russia price war.

The Volatility Index (VIX) ended July at 21.33, decreasing 24.3% from the June month-end reading of 28.17. The VIX has increased 23.9% after beginning 2022 with a reading of 17.22. Movement in the VIX has largely been driven by market turbulence over inflation, increasing interest rates, recessionary fears and the war between Russia and Ukraine. It remains lower than the March 16, 2020, COVID-19 pandemic peak of 82.69. The long-term average of the VIX is approximately 20.

We actively monitor the capital markets and are prepared to respond accordingly. As we have stated in the past, we continue to advise our clients to adhere to their long-term plans and objectives.

ZIEGLER CAPITAL MANAGEMENT, LLC
30 South Wacker Drive | Suite 2800 | Chicago, Illinois | 60606 | www.zieglercap.com

22-02001
Printed Internally