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June 2022 Recap

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At any point in time, we expect to receive a mix of good and bad economic data. As the month of June unfolded, however, evidence of economic weakness continued to mount. Headline consumer price index rose 8.6% YoY for May, while average hourly earnings fell -3.0%, adjusted for inflation[1]. With real wages falling, it makes sense that real personal spending would fall as well, -0.4% for the same time period[2]. In addition, cracks began to show in the U.S. labor market with initial jobless claims now clearly heading north. In this environment, it is not hard to see why the University of Michigan consumer sentiment would fall to the lowest on record going back to the late 1970's. With evidence piling up on the "economic contraction" side of the ledger, it has become clear that the S&P 500's footing in the bear market territory is not a technical repricing but a signal of a potential consumer-led recession.

GLOBAL EQUITY

The rout in the equity markets continued through the month of June, with major indices posting upper-single-digit losses. Recession fears mounted as the consumer price index stayed elevated, weighing on more cyclical sectors and consequently on the Russell 1000 Value Index. Financials, Energy, and Materials sectors pulled the S&P 500 Index downward, with Consumer Discretionary sector coming in as a close fourth. Investors found respite in defensive sectors especially Consumer Staples and Health Care, reflecting where consumer spending is expected to be stable in a highly inflationary environment. The fears about a consumer-led recession became more realistic as the Q1 GDP growth's personal consumption component was revised downward from 3.1% to 1.8%, and personal spending for May fell to a tepid 0.2% nominal increase, and when adjusted for inflation -0.4% for the month[3].

TABLE 1: **Global Equity**	JUN	QTD	YTD	1 YR
Dow Jones Industrial Average	−6.56	−10.78	−14.44	−9.05
S&P 500 Index	−8.25	−16.10	−19.96	−10.62
Russell 2000	−8.23	−17.21	−23.45	−25.24
Russell 1000 Growth	−7.92	−20.92	−28.07	−18.77
Russell 1000 Value	−8.74	−12.21	−12.86	−6.82
MSCI ACWI USD	−8.43	−15.66	−20.18	−15.75
MSCI EAFE USD	−9.28	−14.51	−19.57	−17.77
MSCI EM USD	−6.65	−11.45	−17.63	−25.29
MSCI ACWI ex US USD	−8.60	−13.73	−18.42	−19.42

Source: Bloomberg, as of 6/30/2022. Past performance does not guarantee future returns.

Looking ahead to Q2 2022 reporting season, the estimated earnings growth rate for the S&P 500 is 4.3%. This is a downward revision from the 5.9% year-over-year growth expected on March 31st. The recent selloff brings the forward price-to-earnings ratio down to 15.8x for the S&P 500 Index, and while that is below both the five-year average of 18.6x and the 10-year average of 16.9x, we must remember that we may see more downward revisions in earnings in the coming months[4]. The U.S. equity market valuation may not be as attractive as the current forward P/E ratio suggests.

Losses mounted in international markets as well, and currencies continue to project heavy influence on returns. Stronger U.S. dollar (USD) signals a shortage of the reserve currency around the world and investors' preference for safety amidst market turbulence, neither of which are favorable. In particular, the Japanese Yen has been losing value against the USD down to a twenty-year low as the monetary policies diverge between the two countries: the Fed's ambitious hiking cycle clashes with the Bank of Japan's determination to keep the 10-year yield at 0%. In Europe, the energy shortage situation continues to be a concern, with Germany's producer price index increasing 33.6% YoY in May, driven by

1 Bureau of Labor Statistics
2 Bureau of Economic Analysis
3 Ibid.
4 All S&P 500 earnings and P/E calculations are from Factset Earnings Insight, 6/24/2022

crude- and natural-gas-related price jumps[5]. Energy issues plague emerging market nations as well, with food insecurity adding to the challenge in the coming quarters. Both the MSCI EAFE and the MSCI EM indices reflected these growing concerns, although emerging markets outperformed developed markets for June. This was driven by Chinese equities rebounding aggressively upon easing of COVID-19 restrictions in Shanghai and may not reflect the forward-looking concerns around a global slowdown. The investor sentiment regarding the challenges that lie ahead may be felt more accurately in the −15.6%, −11.6%, and −6.5% returns of MSCI Korea, Taiwan, and India indices, respectively.

FIXED INCOME

TABLE 2: **Fixed Income**	JUN	QTD	YTD	1 YR
Bloomberg US Aggregate	−1.57	−4.69	−10.35	−10.29
Bloomberg 1-3 Yr Gov/Credit	−0.70	−0.63	−3.11	−3.56
Bloomberg Treasury 5-7 Yr	−0.88	−2.81	−8.28	−8.90
Bloomberg Investment Grade Corp	−2.80	−7.26	−14.39	−14.19
Bloomberg High Yield Corp	−6.73	−9.83	−14.19	−12.81
JPMorgan EMBI Global Diversified	−6.21	−11.43	−20.31	−21.22

Source: Bloomberg, as of 6/30/2022. Past performance does not guarantee future returns.

The Federal Reserve raised the fed funds rate by 75 basis points during their June meeting. The upward pressure on the front end was felt along the curve, raising yields in the process. Most fixed income indices experienced the rate increases with negative returns for the month. Corporate credit spreads also widened, with high yield spreads increasing as much as 163 bps for June as the risk-off sentiment in the equity markets climbed the capital structure to influence the credit markets. The new issuance market has also seen a pause during the month. High yield issuance in particular is down near 80% compared to a year ago, making 2022 the lowest first-half since 2009. Rising borrowing costs as well as careful investors are keeping borrowing at bay.

Throughout the first half of 2022, the tone of the Federal Reserve became increasingly hawkish. We began the year with discussions of 25-bp rate increases, but as inflationary pressures mounted the Fed ended June with a 75-bp hike. The Fed has also changed its view on the health of the U.S. economy, from exuding confidence of managing a soft landing with monetary policy to admitting that we may need to accept the realities of a recession to tackle inflation. This recent example brings our attention to the tendency of the Fed to overcorrect a situation that may be self-correcting if left alone. The global supply chain has been thawing, partly due to the decreasing demand we experience from high prices. But with the implementation of contractionary monetary policy in a bear market, we may be exacerbating the economic slowdown that would have occurred anyway. The Fed has not hiked into a recession and a bear market before. We are entering an unfamiliar territory in the land of monetary policy.

5 German Federal Statistical Office

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The weak economic data by themselves do not always mean that a recession is looming. When we look at the cause of disruptions in the energy and food markets, however, there are reasons to believe that high prices will persist for the foreseeable future, continuing to put pressure on our wallets. Unless the Federal Reserve reverses course on the rate hike plans or prices are reduced due to better energy supply dynamics, the current challenges are not amenable to a healthy, growing economy. While no one knows the timing of when two consecutive quarters of negative GDP growth will take place, we are sure about what we see and feel: poor consumer sentiment, shrinking purchasing power in our take-home pay, and eye-popping prices at the gas pump. We may be in for difficult times ahead as recession risks rise.

Anna Rathbun serves as the Chief Investment Officer for CBIZ Investment Advisory Services. Her tenure with the firm has spanned economic and market research, portfolio construction, and creating insights in investment themes to share with the investment community. Anna began her career in investments at Wellington Management, and subsequently, Harvard. She has served as a Managing Director for a registered investment advisory firm where she specialized in alternative investments. She is a graduate of Harvard University with a B.A. in Economics. Her early passion for the arts led her to classical music, for which she obtained a Master of Music and Doctor of Musical Arts from the Cleveland Institute of Music. Anna's career in music spanned a wide spectrum of performances to a faculty position at her alma mater. With a unique background that embraces both finance and the arts, Anna is dedicated to the issue of financial sustainability for organizations serving a mission.