CHIEF INVESTMENT OFFICE

Investment Insights

Five Stages Of The Reset Period

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All data, projections and opinions are as of the date of this report and subject to change.

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The broader market indexes experienced further weakness this last week with the S&P 500 falling into bear market territory during last Friday's session (traditionally characterized as a fall of 20% or more from the peak) for the first time since the onset of the pandemic in early 2020. With so much uncertainty still clouding the near-term picture investors continue firmly with a risk off position. Market rallies have been sold since the beginning of the year and new concerns seem to extend and/or develop each month. The crisis in Ukraine continues, shutdowns in China have been extended, sticky inflation remains, central banks tightening financial conditions, and energy and food prices are beginning to effect corporate margins and consumer sentiment. In addition, stagflation concerns and rising recession risk have become front and center not to mention U.S. midterm election volatility and new pressures on housing joining the list. Finally, real yields have turned positive and we are now beginning to witness the early stages of the substitution effect in consumer spending. In this regard, consumers negatively affected by rising food and energy prices are substituting higher-end brands for less expensive ones and cutting out some discretionary items or "nice to haves." This is now being picked up in some earnings results this past week.

With all of this converging together, the equity markets are trying to price in a few scenarios that include a soft landing in the economy, a growth recession—a sharp reduction in growth but does not tip into negative territory—and a hard landing resulting in a recession. As this period of uncertainty matures, markets, in our view, will be searching for signs of stability to finally bottom out and create a new base. We believe these "still cloudy" signs (not in any particular order) include a peak in inflation across multiple gauges, order restored in Ukraine, the end of shutdowns in China (for supply chain reasons), and concrete signals that corporate earnings do not enter a long period of decline. In the second half of 2022, more economic, corporate and market data will be released on these fronts and we believe the final workout process stage will be upon us. For now, investor sentiment is likely to remain at some of the lowest levels in decades and an "on guard" posture across markets is warranted, in our opinion. We highlight our five stages and characteristics of the cyclical bear market or reset period below.

Five Stages Of The Reset Period:

One: An initial move off the highs with a big rally in the equity markets that ultimately fades. This stage includes still strong economic data, but market internals are weak. Rolling bear markets present themselves in lower-quality areas. Investors look for bargains but the correction is just beginning, in our view. This is indicative of Q1 2022.

Two: Conditions tighten. Smaller rallies in equities markets are sold as asset managers reposition portfolios and investor redemptions pick up. Defensive postures are built, equity valuations correct significantly and worries emerge about profit declines. This stage is similar to the one unfolding in Q2 2022.

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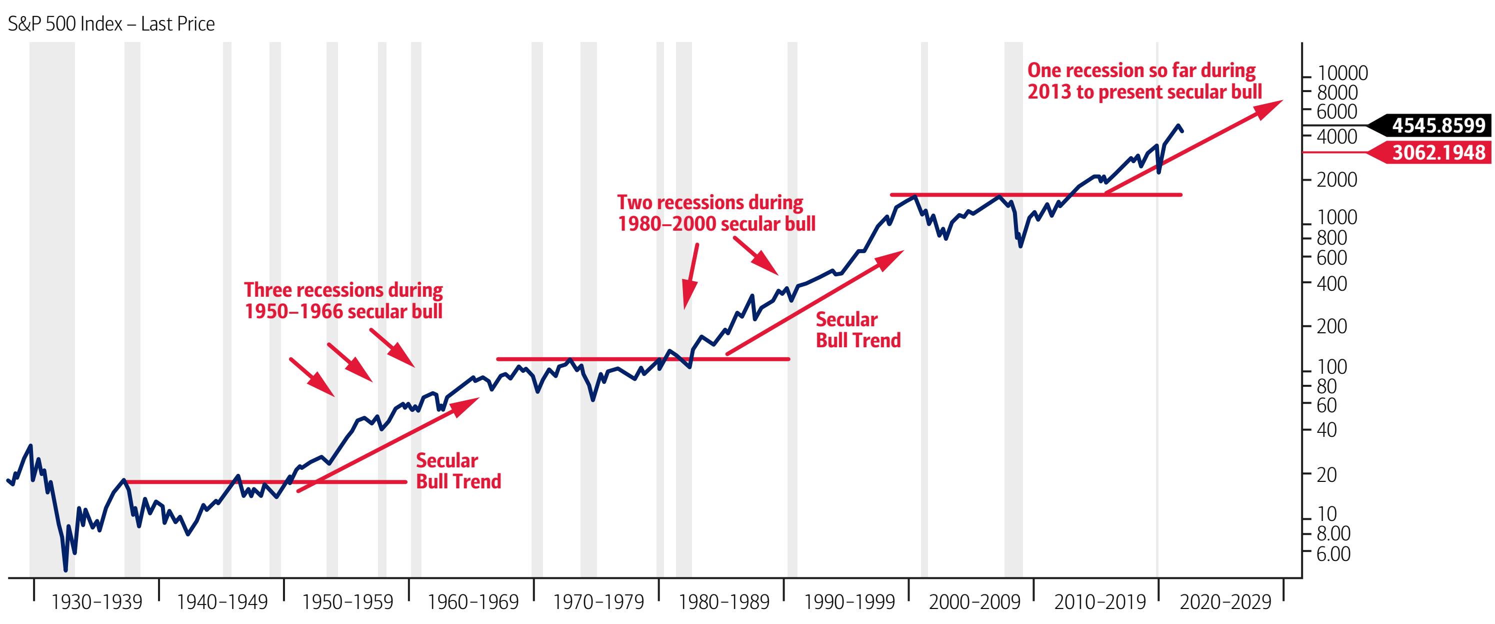
Three: Financial conditions tighten further as central banks raise rates and/or contract the balance sheet. Economic data turns mixed and employment trends begin to show visible weakness. Higher-quality and lower-quality areas of the market correct together. Generally this stage is the final selloff in which investors raise cash, become ultra defensive and potentially some forced selling occurs. This could take three to six months to price in the worst case scenarios. Equity volatility stays elevated with defensive sectors becoming overvalued. According to Evercore ISI Research, when examining a total of 24 market drawdowns since 1929, the average cyclical bear market that does not result in a recession bottoms out around 28% from its peak and takes approximately 7 months. Cyclical bear markets that ultimately include an economic recession decline from their peaks by 42% on average and take about 13 months to finish the process.

Four: Economic data is weak but begins to stabilize. Central bank communication starts to turn less hawkish. Defensive positioning gets over extended. Bargain hunting ensues as selling pressure is exhausted. An entirely new equity market base is built and a small seesaw channel uptrend begins. New leaders emerge with a combination of value and solid growth opportunities which provides a larger opportunity set for long term investors.

Five: A new market cycle is firmly established which converges back into the long-term secular bull market trend. Central bank tightening generally ends with the profit cycle rising again. Investors begin to climb a smaller "wall of worry" as economic growth begins to rise again. Investor sentiment turns upward with tactical Equity allocations increasing.

Moreover, according to technical strategy analysis at BofA Global Research "recessions did not derail prior secular bull markets (secular means multi-business cycles). Recessions do occur during secular bull markets but the magnitude of market weakness is significantly different than secular bear market periods. The 1950–1966 bull market had three recessions, the 1980–2000 bull market had two, and the 2013–present bull market has had one. The silver lining is that the S&P 500 pullbacks associated with recessions during secular bull trends are much less severe and have averaged 21.9% (median of 20.8% and range of 13.9% to 33.9%) rather than the average 39.6% drawdown (median of 36.8% and range of 0.0% to 86.2%) for recession pullbacks during secular bear phases."

Exhibit 1: S&P 500 with National Bureau of Economic Research recessions: Monthly chart



Gray bars represent recession periods. Sources: BofA Global Research, Bloomberg. Data as of May 20, 2022. **Past performance is no guarantee of future results.**

With our view that this latest cyclical bear market period should eventually converge back into the secular bull market trend it's important to begin to re-examine your asset allocation and long-term goals in the coming months. A dollar cost averaging approach during market weak periods can help add to diversification through the market cycle and also keep your strategic asset allocation anchored for the long-term in place. Throughout the balance of this year, we continue to emphasize a small overweight and diversified balance in Equities relative to Fixed Income. However we will be 'on guard' for any rebalancing opportunities the market may provide either through higher bond yields and/or aligning our asset allocation to an appropriate equity risk posture with respect to the unfolding macro-economic environment. We prefer high-quality investments across both asset classes and believe that some Fixed Income yields are likely to become attractive again later in the year.

Index Definitions

Securities indexes assume reinvestment of all distributions and interest payments. Indexes are unmanaged and do not take into account fees or expenses. It is not possible to invest directly in an index. Indexes are all based in U.S. dollars.

S&P 500 Index: includes a representative sample of 500 leading companies in leading industries of the U.S. economy. Although the index focuses on the large-cap segment of the market, with approximately 75% coverage of U.S. equities, it is also an ideal proxy for the total market.

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