MATRIX PRIVATE CAPITAL GROUP

CIO Market Outlook Q2 2022: Inflation, Rates, and Russia

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Financial markets in the first quarter of the year saw a significant rise in volatility, primarily driven by inflation, interest rates, and a marked change in the geopolitical landscape. Inflation continues to be at multi-decade highs, with the headline CPI rising to 7.9% YoY (as of the end of February 2022), due to the impact of the Federal Reserve's monetary policy, fiscal policies implemented during COVID, and continued supply chain issues coming out of the global pandemic.

The quarter also saw the Fed's first increase in interest rates since the beginning of the pandemic, which many market observers argue may be too late given where inflation is today. As such, the Fed finds itself in a precarious position of balancing the need for steady prices and maximum employment, in the face of a deteriorating geopolitical backdrop.

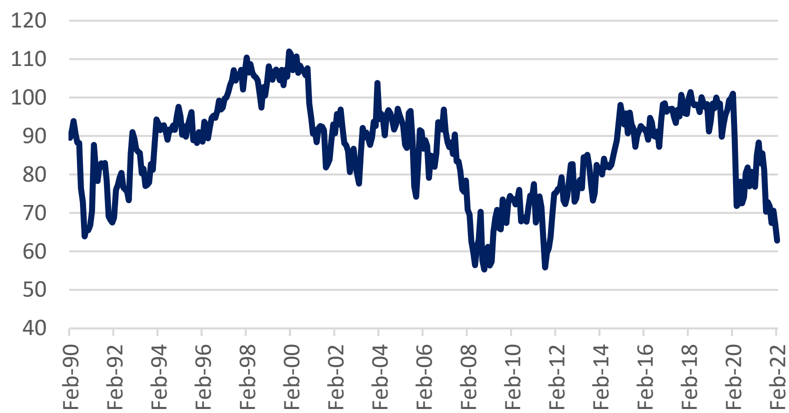
Display 1: Unusually High Inflation Suggests the Fed is Behind the Curve

Source: Bureau of Labor Statistics; Data from Feb 1980– Feb 2022.

Despite these issues, GDP remains quite robust here in the U.S. with strong employment and solid balance sheets in the private sector. It should be noted however that the consumer, which accounts for approximately 70% of GDP, has shown some weakness recently – which may partly be due to inflation and the political climate. Consequently, we continue to closely monitor growth dynamics as the Fed attempts to bring down inflation and simultaneously avoid recession.

As investors anticipate the Fed raising rates, there has been significant discussion and concern around the steepness of the Treasury yield curve and its potential to forecast recession. Research has shown that yield curve inversion does not necessarily signal immediate recession – in fact, many times equity markets continue to deliver positive returns a year or two after inversion.

Display 2: Consumer Sentiment Has Been Unusually Weak



Source: University of Michigan; Data from Feb 1990 – Feb 2022,

As such, our base case scenario does not call for a recession here in the U.S. in 2022. However, as we had anticipated, the Fed's change in posture has had an effect on the drivers of the market's performance. We have seen significant pressure on P/E multiples of highly speculative growth companies with limited or no earnings in favor of higher quality companies with sustainable and growing earnings. It is our belief that we will continue to see these types of companies outperform in a tighter rate environment.

Diversification Matters Again

The recent volatility has made investors far more cognizant of the importance of asset allocation, and we continue to manage portfolios using portfolio diversification as a key tool for risk mitigation.

In terms of market outlook, we are overweight U.S. equities relative to equities abroad. Within our equity allocation, we believe that quality of earnings and balance sheets will continue to be a significant driver of market returns. As such, we favor high quality/defensive factors such as those found in healthcare and staples, along with pockets of value such as those found in energy.

It is now also more important than ever to actively manage our fixed income allocations to take advantage of rising interest rates. We see opportunity to allocate to some higher yielding segments of the fixed income market where quality still prevails. Finally, we are also maintaining a modest overweight to commodities, broadly as an inflationary hedge.

As we often say, "with volatility comes opportunity". We continue to tactically manage portfolios to capitalize on market dislocations which will inevitably present themselves in an ever-evolving global backdrop.

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Tactical Outlook

+, ==, – denotes positive, neutral, and negative views, respectively

Q2 2022 Broad Assets	– –	–	==	+	++
Equities					
US Equity				●	
Developed Non-US			●		
Emerging Markets			●		
Fixed Income					
US Rates			●		
High Yield Credit		●			
Emerging Credit		●			
Commodities					
Crude Oil				●	
Gold			●		
Broad Comm.			●		

US Equity Sectors	– –	–	==	+	++
Technology			●		
Healthcare					●
Cons. Staples					●
Utilities				●	
Cons. Discretionary	●				
Materials			●		
Industrials		●			
Financials			●		
Energy				●	
Communications		●			
Real Estate				●	

Global Regional	– –	–	==	+	++
United States				●	
United Kingdom					●
Eurozone		●			
Developed Asia	●				
Emerging Asia		●			
Latin America				●	
Frontier Markets				●	

Commodities & FX	– –	–	==	+	++
Gold			●		
Silver			●		
Oil				●	
NaturalGas				●	
Agriculture				●	
Metals				●	
DevelopedFX		●			
EmergingFX		●			

Asset Class Views

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