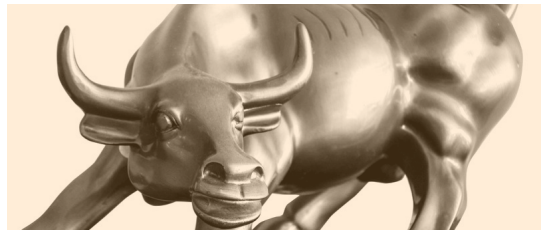
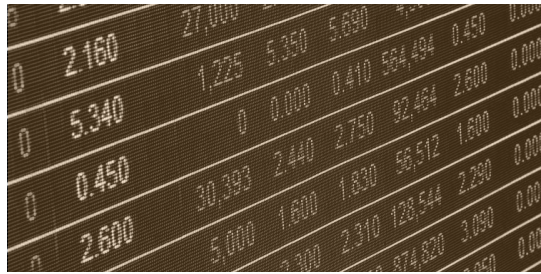


MARKET COMMENTARY

THIRD QUARTER 2022



AT A GLANCE

For the third consecutive quarter, traditional asset classes and categories endured significant volatility, with most corners of the financial markets suffering performance losses amid a tense geopolitical backdrop, weakening economic fundamentals, and further tightening actions by the Federal Reserve (Fed). In response to a historically tight labor market, stubbornly high inflation, and a persistent imbalance between aggregate demand and available supply, the Fed doubled the pace of quantitative tightening in September and issued two 75-basis-point hikes to the federal funds rate, formally placing this key policy rate above the “neutral” level and into restrictive territory.

Global equities posted negative returns for the third consecutive quarter, with domestic equities witnessing relative outperformance versus international developed and emerging markets, and smaller cap companies relatively outperforming their larger cap counterparts. Stylistically, the longer duration and rate-sensitive growth sectors modestly outperformed value, despite a meaningful rise in Treasury interest rates.

Similar to global equity, core bonds suffered a third consecutive quarterly decline, pressured lower by a relentless rise in interest rates, with the floating-rate bank loan sector being one of the few areas within the fixed income markets to eke out a positive return on the quarter. Against a backdrop that included stubbornly high inflation and aggressive Fed rate hikes, the yield on the benchmark 10-Year Treasury Note surged a staggering 82 basis points on the quarter to 3.83%, placing this key interest rate at the highest level since 2010. The upward momentum of the 10-Year Treasury Note has carried over into the fourth quarter, with the yield now measuring over 4%.

Real asset returns were also pressured lower during the quarter, the downward momentum of which was primarily concentrated in September, as the strengthening U.S. dollar (USD), rising interest rates, and ongoing concerns of a loss of global economic growth momentum weighed on the asset class. Among the primary real asset categories, real estate investment trusts (REITs), global listed infrastructure, and commodity futures each declined by double-digit margins, while some pockets of relative strength were witnessed within the energy infrastructure sector.

KEY MARKET THEMES AND DEVELOPMENTS

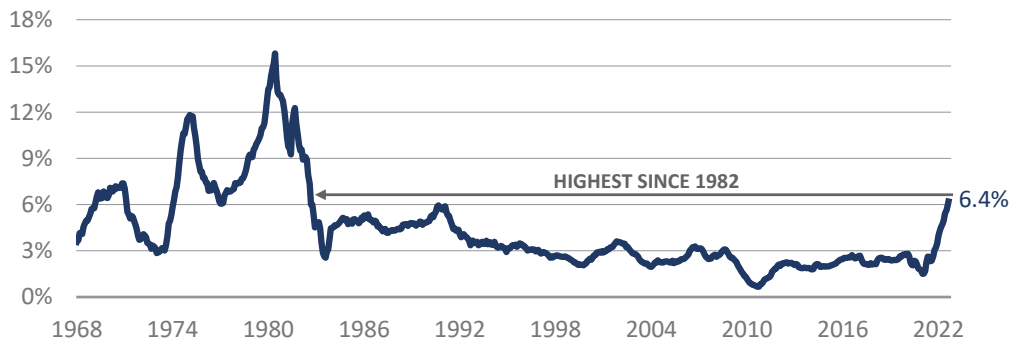
PERSISTENT INFLATIONARY PRESSURES PROMPT FED TO TIGHTEN POLICY FURTHER, DESPITE WEAKENING FUNDAMENTALS

“More of the same” could casually describe the third quarter of 2022, as most key traditional asset classes and categories suffered through a third consecutive bumpy quarter, with performance losses blanketing the landscape. Central to the theme of elevated volatility and negative performance was stubbornly high inflation, both domestically and abroad, with policymakers in the United States and Europe taking further action to help bring aggregate demand and available supply more closely into balance.

In the U.S., both headline and core measures of inflation remained uncomfortably high versus the Fed’s 2% desired level through the quarter, despite meaningful year-to-date progress to tighten monetary and broader financial conditions. The Atlanta Fed’s measure of the “stickiness” of inflation has appeared unrelenting in its rise throughout 2022, despite a less linear ascent across actual core inflation. Through September, this gauge stood at 6.4%—a 40-year high—and does not appear to be moderating its trajectory.

THE FED CONTINUES TO TIGHTEN AMID PERISISTENT INFLATIONARY PRESSURES

Atlanta Fed "Sticky" CPI Index (Core)



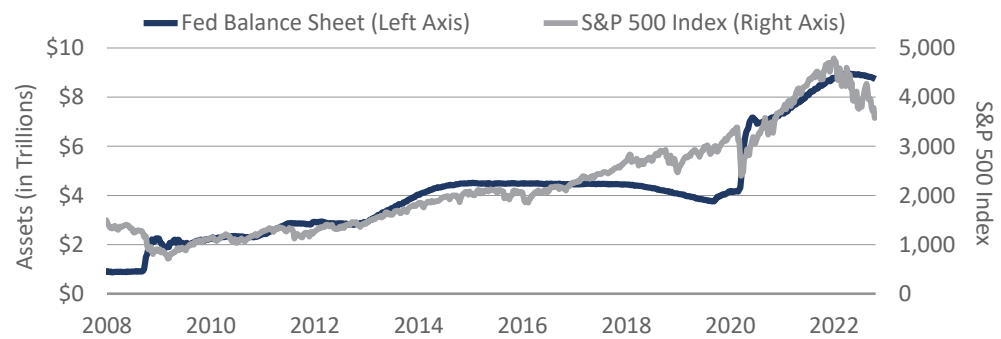
Data sources: Atlanta Fed, Bloomberg, L.P.; Data as of September 2022

In the third quarter, the Fed not only hiked the policy rate by 75 basis points on two separate occasions—once in July and another in September—but also ramped up the pace of quantitative tightening through an acceleration of their balance sheet winddown. After peaking at just shy of \$9 trillion in April, the Fed’s balance sheet has since declined approximately \$200 billion. Interestingly, despite inflation running well above target at the time, the Fed was still purchasing both Treasury and agency mortgage-backed securities this past spring, albeit at a moderated pace.

The dual forces of a higher policy rate and incremental declines in the size of the balance sheet have weighed on investor risk appetites throughout 2022, placing meaningful downward pressure on risky asset prices.

DECLINING FED LIQUIDITY CONTINUES TO WEIGH ON RISK ASSETS

Federal Reserve Balance Sheet Assets and S&P 500 Index



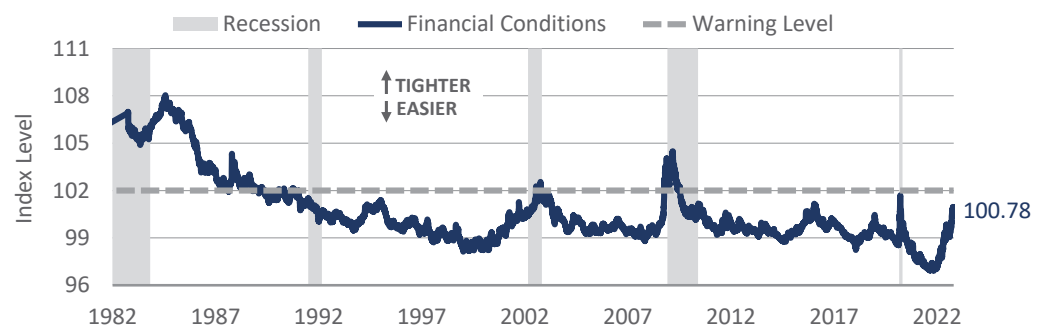
Data sources: Fed, ECP, BOJ, Bloomberg, L.P.; Data as of October 19, 2022

Tighter domestic monetary conditions have not only served as a headwind to risk assets, they have also transmitted into the broader financial markets through higher market interest rates, increasing credit risk premiums, and a sharp rise in the exchange rate value of the USD.

The commonly-referenced Goldman Sachs U.S. Financial Conditions Index helps highlight this linkage, as the abrupt pivot from an ultra-accommodative policy stance to one of incremental tightening over the trailing year has coincided with a meaningful tightening in financial conditions. Importantly, Goldman Sachs’ gauge remains modestly below levels that have historically signaled cyclical slowdown pressures, implying further Fed tightening is likely in order to slow the economy and tamp inflation.

BROADER FINANCIAL CONDITIONS CONTINUE TO TIGHTEN

Goldman Sachs U.S. Financial Conditions Index



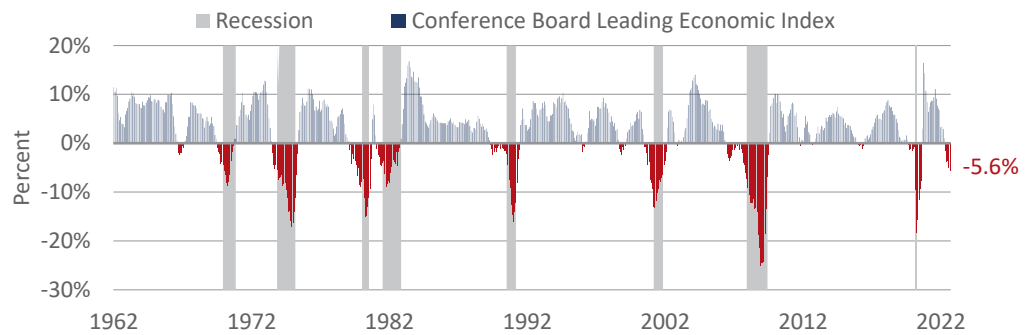
Data sources: Goldman Sachs, Bloomberg, L.P.; Data as of October 14, 2022

Headline and core inflation is still running strongly above both the Fed’s desired long-run level of 2.0% and the upper bound on the federal funds rate (3.25%). With more space to tighten broader financial conditions further, the Fed is anticipated to remain active on their tightening campaign through the duration of 2022 and into the early months of 2023, despite growing concerns the economy is headed for a hard landing.

One of the key cyclical indicators that maintains a solid historical track record of identifying inflection points in the business cycle has started to flash warning signs. The Conference Board’s Leading Economic Index (LEI), a composite of economic factors that—according to the Conference Board—in aggregate, lead turning points in the business cycle by an estimated seven months, has witnessed a marked deceleration over the trailing six months. Through September, the LEI had declined 2.8% over the preceding six-month period, representing a 5.6% annualized decline and a pace that has historically coincided with imminent recessionary conditions.

LEADING INDICATORS POINT TO GROWING RECESSIONARY RISKS

Conference Board Leading Economic Index Six-Month Change (Annualized) and Cycles

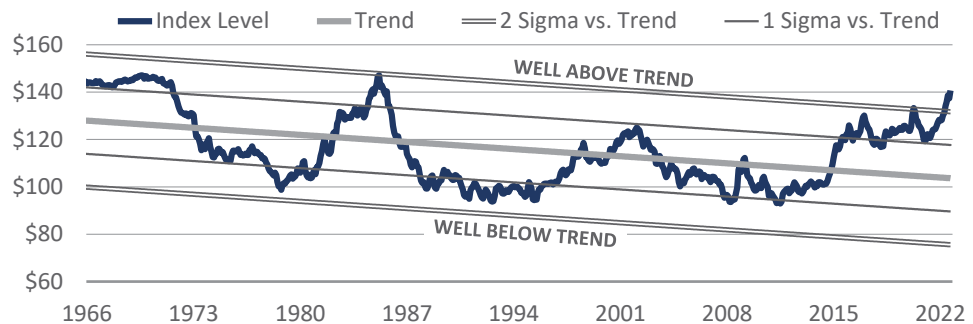


Data sources: Conference Board, NBER, Bloomberg, L.P.; Data as of September 2022

In addition to applying downward pressure on economic fundamentals, the significant tightening initiatives detailed above helped underpin a meaningful appreciation of the USD during the quarter, with associated weakness felt across developed and emerging market currencies alike. The euro, British pound, Japanese yen, and liquid emerging market currencies each slumped to multi-decade low levels versus the USD in the third quarter, prompting interventionist market responses by both the UK government and the Bank of Japan in a bid to help stem further declines.

Through September, on an inflation-adjusted and trade-weighted basis, the Bank for International Settlements’ Real Effective Exchange Rate (REER) for the USD stood at an index level of 140.66, 35% above the historical average, 2.5 standard deviations above the long-run trend, and the highest level since 1985.

U.S. DOLLAR HAS STRENGTHENED TO A NEARLY 40-YEAR HIGH
Real Effective Exchange Rate (REER)



Data sources: BIS, Bloomberg, L.P. FEG; Data as of September 2022

Ultimately, it appears the more persistent inflationary pressures remain, the harder the Fed will have to hit the brakes. This would, in turn, support a further rise in the exchange rate value of the USD and, unfortunately, a likely additional increase in global risk premia that would weigh on asset prices.

CONCLUDING THOUGHTS AND OUTLOOK

Both risk-seeking and high quality-oriented global investors suffered through a third consecutive quarter of elevated financial market volatility and broad-based performance losses across key global asset classes and categories. Persistent positive inflationary momentum in conjunction with a historically tight labor market supported the need for additional tightening measures by the Fed, despite mounting evidence of developing broad-based economic weakness.

In the coming months, the anticipated Fed path implied by the bond market points to further monetary restraint in a quest to restore both price stability and a balance in supply and demand. While steep losses have plagued the financial markets year-to-date, further downside volatility may be in order, should inflation fail to smoothly subside and evidence of a hard landing become more abundant.

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Published October 2022.

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The S&P 500 Index is a capitalization-weighted index of 500 stocks. The S&P 500 Index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

Information on any indices mentioned can be obtained either through your advisor or by written request to information@feg.com.

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