SECOND QUARTER 2022

Matt's Market Update

IN THIS REPORT

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Market Review

The headline from the Wall Street Journal (WSJ) on June 30th said it all, "Markets Post Worst Half of the Year in Decades". In fact, you have to go back 50 years to find a worst first half of the year for developed market equities. Outside of cash, there were no safe havens for investors. Even the formerly strong Bloomberg Commodity Index rolled over in Q2 (with a -5.66% decline) as recession fears mounted. Per the WSJ, 44% of economists they surveyed expect a recession in the next 12 months, compared to only 18% from the January survey. The broadly followed equity indexes posted double-digit declines with the NASDAQ posting a -22.40% decline as investors continued to sell the growth stocks that have led the market over the past five years. The Russell 2000 (-17.20%), S&P 500 (-16.10%) and the MSCI ACWI ex US (-13.73%) followed suit lower.

Per research from J.P. Morgan, valuations are now well below their average since 1990 in every major region other than the U.S. In the U.S., the cheaper parts of the market now trade at relatively low valuations compared with history, with the Russell 1000 Value Index trading on a price-to-earnings (P/E) multiple of 13, whereas the Russell 1000 Growth Index still trades on a P/E of 21. Consensus analyst forecasts still, perhaps surprisingly, expect positive growth in company profits for both this year and next. This is likely the next shoe to drop in this ongoing equity bear market. We expect analysts to cut their corporate earnings forecasts over the coming quarters. This very likely continues to put downward pressure on equities.

The one-two punch of rising inflation and Federal Reserve rate hikes have driven the sell-off in bond prices this year. The Federal Reserve raised interest rates by 50 basis points (bp) in May and followed this with a 75 bp increase in June as inflation data continued to show strong upward momentum. The Fed is expected to hike another 75 bp at their meeting in late July. Interestingly enough, the key 10-year treasury yield hit a peak of 3.48% on June 14th, only to close the quarter much lower at 2.97%. While more Fed rate hikes are expected in 2022, the question has seemingly shifted to when will the Fed pause? There are two schools of thought on this. The first says a pause will happen when we witness declines in the monthly inflation numbers reported by the Consumer Price Index (CPI). To date, there have been no signs of this happening, but the very recent declines in gasoline and broader commodities is perhaps giving a hopeful sign we're at or near peak inflation. The second school of thought says the Fed will continue on until the economy weakens further or something breaks in the global markets. This would almost assuredly cause demand destruction for goods and services and thus bring down inflation. Yields have fallen further as Q3 got underway. The decline in bond yields combined with the commodity price declines we mentioned has our radar up. Are these markets giving us advanced warning of an incoming recession?

Trouble for the 60/40 Portfolio

For decades, institutional investors have often modeled portfolios after a 60/40 design. Meaning, a 60% allocation to equities and 40% allocation to fixed-income. Within each allocation, the investment policy could vary over factors like market cap of the stocks, the quality ratings for bonds, etc. No matter the construction, the goal was typically the same: a balanced portfolio of stocks and bonds that would be able to weather extreme market environments due to its inherent diversification. In other words, during equity bear markets, the bonds in the portfolio would provide some ballast to limit portfolio downside and vice versa in periods where bonds struggled from rising interest rates. With this concept in mind, please see the next two charts from Charlie Bilello research. During the last eight calendar years when the S&P 500 index was negative, the Bloomberg US Aggregate bond index provided offsetting gains to cushion the downside. So far in 2022, bonds have logged a -10.4% return and have provided no portfolio benefits to balance out the decline in stocks. To put the poor first half of the year in perspective, we've never witnessed a full calendar year where both stocks and bonds (as measured by the indexes in the chart), declined by over 10%.

In fact, as we can see from the second chart, the return for the first two quarters of 2022 ranks as the worst start in history for the 60/40 portfolio by a wide margin. Fortunately, there is time left in the year for recovery, but it's shaping up as record breaking year to the downside for the 60/40 portfolio.

S&P 500 DOWN YEARS (1976-2022)

Year	S&P 500 Total Return (Stocks)	Bloomberg US AggIndex TR (Bonds)	60/40 Portfolio (S&P 500 / Bloomberg Agg)
1977	-7.2%	3.0%	-3.1%
1981	-4.9%	6.2%	-0.5%
1990	-3.2%	9.0%	1.7%
2000	-9.1%	11.6%	-0.8%
2001	-11.9%	8.4%	-3.7%
2002	-22.1%	10.3%	-9.2%
2008	-37.0%	5.2%	-20.1%
2018	-4.4%	0.0.%	-2.6%
2022 YTD	**-20.0%**	**-10.4%**	**-16.1%**

Source: COMPOUND, Data as of 6/30/2022. @CharlieBilello

WORST US 60/40* RETURNS THROUGH JUNE (1976-2022)

Rank	Year	Total Return
1	**2022**	**-16.1%**
2	2008	-6.7%
3	2002	-6.4%
4	1984	-3.6%
5	1994	-3.6%
6	2001	-2.6%
7	1982	-2.0%
8	2010	-1.9%
9	1977	-1.7%
10	1981	-0.5%

**60/40 = 60% S&P 500/40% Bloomberg US Agg*
Source: COMPOUND, @CharlieBilello

Wealth Management Corner

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Planning for retirement is becoming more and more challenging as the needs of retirees are growing as well as the expenses in retirement. As folks, transition from working life to their golden years it becomes vital to understand the common factors, which affect retirement income. These factors include investment risk, inflation, long-term care costs, and taxes. If these areas are not planned for carefully, it can put you in the position where you may not be able to enjoy the retirement you envisioned.

The first factor to focus on is Investment risk. The concern being that fluctuations in the overall market may result in the reduction of the value of your retirement savings. It is important to align your time horizon with your investments especially if you need to withdraw from your accounts to supplement your retirement income. The two main factors, which determine how long your investments will, last are the amount of the withdrawals you take and the growth and/or earnings your investments experience. Unfortunately, the market does not always generate positive returns. There are periods when the market provides negative returns. If not planned for carefully, constant withdrawals from your retirement savings combined with prolonged negative market returns can result in the depletion of your retirement savings far sooner.

Another area which can affect your retirement income and one that is timely is inflation. This is the risk that the purchasing power of a dollar will decline over time, due to the rising cost of goods and services. While inflation is much higher today, assuming inflation runs at its historical long-term average of about 3% , the purchasing power of a given sum of money will be cut in half in 23 years. A simple hypothetical example illustrates the impact of inflation on retirement income. Assuming a consistent annual inflation rate of 3%, and excluding taxes and investment returns in general, if $50,000 satisfies your retirement income needs this year, you'll need $51,500 of income next year to meet the same income needs. In 10 years, you will need about $67,195 to equal the purchasing power of $50,000 this year. Therefore, to outpace inflation, you should try to have some strategy in place that allows your income stream to grow throughout retirement.

Long-term care is an area where most often folks overlook. Long-term care may be needed when physical or mental disabilities impair your capacity to perform everyday basic tasks. As life expectancies increase, so does the potential need for long-term care. Paying for long-term care can have a significant impact on retirement income and savings, especially for the healthy spouse. While not everyone needs long-term care during their lives, ignoring the possibility of such care and failing to plan for it can leave you or your spouse with little or no income or savings if such care is needed.

The last area to cover is the effect of taxes on your retirement savings and after-tax income. It is an often overlooked but significant aspect of retirement income planning. Taxes can eat into your income, reducing the amount you have available to spend in retirement. It is important to be aware of your investment accounts and how they are taxed. Income, like interest and dividends are taxed at ordinary income tax rates. Other income, like long-term capital gains and qualifying dividends, currently benefit from a generally lower maximum tax rates. Some specific investments, like certain municipal bonds, generate income that is exempt from federal income tax altogether. You should also understand how the income generated by your investments are taxed, so that you can factor the tax into your overall planning. The impact of Taxes can be even more significant in cases where a portion of your savings and/or income comes from tax-qualified accounts such as pensions, 401(k)s, and traditional IRAs. Most, if not all, of the withdrawals from these accounts is subject to income taxes.

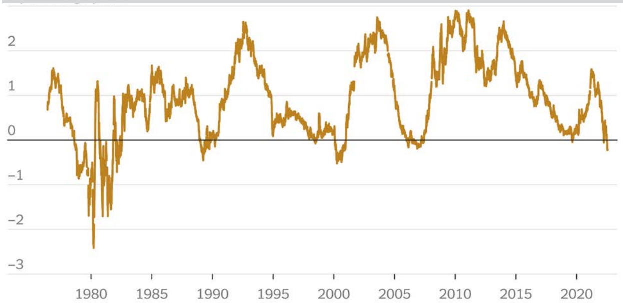
Retirement planning can be complex and have many moving parts. It is important to have a comprehensive financial plan in place, where you are reviewing your financial situation regularly and making changes as needed. If you currently do not have a financial plan in place, you may want to consider working with a CERTIFIED FINANCIAL PLANNER ™. Sentinel's team of planners are well versed in all aspects of retirement planning and are readily available to help guide you through the planning process. You can find out more information on Sentinel's financial planning services by visiting our website.

The Inverted Yield Curve

The terms "yield curve" and "inverted yield curve" are coming back into the mainstream news media as market participants try to estimate the odds of an economic recession in the U.S. First, some quick definitions. The yield curve is a graphical representation of the yields offered by bonds of similar issuers (ex. treasuries) over different future maturities. Typically, the yield curve would slope up and to the right on a chart. This demonstrates that as you go further out in the future, investors expect to be paid a higher yield on their bonds to compensate them for the risk of lending money over a longer time period. By contrast, an inverted yield curve is the opposite. While rare, this condition exists when short-term bonds have higher yields than long-term bonds. It is a sign of deep pessimism on behalf of investors related to the near-term outlook for the economy.

The chart on this page shows the difference between two- and ten-year yields. When the gold line goes below zero, this means the yield on two-year securities are greater than ten-year securities, thus an inverted yield curve. As of early July, the U.S. treasury 2/10 curve is now inverted. Historically speaking, nearly all recessions have been preceded by inverted yield curves, but not all yield curve inversions have been followed by recessions. Bottom line: inverted yield curves are rare, but very important signs for investors to be aware of. Think of it as a flashing red light on the state of the economy.

THE DIFFERENCE BETWEEN 2- AND 10-YEAR TREASURY YIELDS (3 PERCENTAGE POINTS)



Source: Federal Reserve Bank of St. Louis. By the New York Times

Our Portfolio Strategy & Allocation Outlook

Clearly, this was not a quarter filled with great news for investors. After many years of strong equity market gains, a bear market pullback was inevitable. Our positioning has changed very little since our last update. What small changes we've made have been with defense in mind. Now is not the time for large portfolio changes or increased risk taking. There are two questions we received from multiple clients over the past quarter. First, how close are we to a bottom for stock prices? Second, what is going to happen with the Fed and future rate hikes?

We'll briefly offer our best guess on both questions. We don't think we've seen the bottom in stock prices. While there are cheap stocks and sectors for sure, the market indexes have not declined to a point where valuations are in line with historical medians across any number of measures. Analysts have not aggressively lowered their earnings forecasts for this year and next. We think this is coming as the full impact of both inflation and the stronger dollar are yet to be factored into corporate earnings. Regarding the Fed, after the July rate hike, there is no meeting in August and another rate hike at the September meeting is likely. From there it gets interesting. We'll have two more CPI readings on inflation to consider and we'll be on the doorstep of the November elections. We would not be surprised to see the Fed pause in their rate hike campaign prior to the elections. Needless to say, we'll be watching closely.

Please let us know if you'd like to discuss your personal investing and financial planning needs.

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Market Scoreboard

Index Returns (%)	Q2 2022	YTD	1 Year	3 Year	5 Year	10 Year
S&P 500	-16.10	-19.96	-10.62	10.60	11.31	12.96
DJIA	-10.78	-14.44	-9.05	7.24	9.99	11.71
NASDAQ	-22.44	-29.51	-23.96	11.26	12.43	14.16
Russell 2000	-17.20	-23.43	-25.20	4.21	5.17	9.35
MSCI ACWI Ex USA	-13.73	-18.42	-19.42	1.35	2.50	4.83
Barclays Aggregate Bond	-4.69	-10.35	-10.29	-0.93	0.88	1.54

Source: Morningstar
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Diversification and asset allocation do not ensure a profit or protect against loss.

S&P 500 TR: A market capitalization-weighted index of 500 widely held stocks often used as a proxy for the large-cap segment of stock market.

Russell 2000 TR: Consists of the smallest 2000 companies in the Russell 3000 Index, representing approximately 7% of the Russell 3000 total market capitalization often used as a proxy for the small-cap segment of the stock market.

Barcap Aggregate Bond TR: The Barclays Capital Aggregate Bond Index is a market capitalization-weighted index, meaning the securities in the index are weighted according to the market size of each bond type. Most U.S. traded investment grade bonds are represented. The index includes Treasury securities, Government agency bonds, Mortgage-backed bonds, Corporate bonds, and a small amount of foreign bonds traded in U.S.

MSCI EAFE NR USD: Widely accepted as a benchmark for international stock performance, the EAFE Index is an aggregate of 21 individual country indexes that collectively represent many of the major markets of the world.

DJ US Industrials TR USD: Computed by summing the prices of the stocks of 30 U.S. companies and then dividing that total by an adjusted value--one which has been adjusted over the years to account for the effects of stock splits on the prices of the 30 companies.

NASDAQ: Measures the performance of all issues listed in the Nasdaq Stock Market and is often used as a proxy for the large-cap technology segment of the U.S. stock market.

DJ/UBS Commodity: The DJ-UBSCI is composed of futures contracts on physical commodities and is often used as a proxy for broad-based exposure to the commodity markets.

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