STOKES CAPITAL ADVISORS, LLC

Market Commentary
March 31, 2022

Quarterly Market Review ^

Global equity markets witnessed heightened downside volatility as global monetary policies began to tighten. The virus continued to disrupt activity, supply chain challenges persisted, and inflation sizzled. The Russian invasion into Ukraine exacerbated the backdrop as markets grappled with the global implications of a war. Surging inflation, tightening financial conditions, and festering pandemic disruptions were chief among the drains on conviction, partially offset by continued above-trend economic growth. Weak currencies also held back many emerging markets. Chinese stocks struggled as weaker economic growth weighed on consumer discretionary stocks, and technology fell in the wake of a government clampdown on some high-profile companies.

The U.S. economy decelerated but continued to expand. Inflation persisted, with the Consumer Price Index (CPI) hitting a 40-year high as the demand-driven, supply chain-constrained environment continued. Together with tightening labor conditions, the Fed launched its rate hike campaign. Consumer spending remained steady, although inflation, stock price volatility, and ebbing consumer confidence posed threats. Internationally, optimism about above-trend economic and earnings growth was tarnished somewhat by tightening monetary policies and uncertainty regarding the ultimate impact on Europe after Russia's invasion of Ukraine. China's stagnant growth continued, and the U.S. dollar remained firm, applying pressure on global growth, while the persistent surge in commodity prices, notably crude oil, grains, and metals aided resource-reliant economies.

The Fed has embarked on its rate hike campaign, which is expected to deliver multiple interest rate increases in 2022 and 2023. The March Federal Open Market Committee (FOMC) statement cited strength in economic activity but "highly uncertain" economic implications of the war in Eastern Europe. With high inflation and tightening monetary policies, in addition to the uncertainty regarding the impact on economic growth, Treasury yields have seen a wild ride that led to higher rates. Corporate option-adjusted spreads continue to bounce off cyclical lows but remain below the long-term average. Muni yield spreads have also increased but there are few credit concerns due in part to strong fiscal support. The U.S. dollar found support from the Fed's move to begin raising rates, which has fostered comparably higher U.S. rates, as well as the skittishness toward the war in Ukraine.

The advance in commodity prices was resuscitated by the crisis in Europe, which saw energy, grain, natural gas, and metals prices surge, defying ongoing weakness in Chinese growth, and strength in the U.S. dollar. The S&P GSCI rose during Q1 but relinquished some of the gains with volatility toward the end of the quarter. While demand for oil continues to recover, supply has been curtailed by OPEC and a slow return of U.S. production capacity—although the market is becoming more balanced with the U.S. rig count rising and inventories stabilizing. The Energy Information Agency (EIA) forecasts global supply and demand to converge in 2022. Gold regained its inflation "go-to" status and has threatened the record highs reached a year ago.

Global Economic Outlook *

- **United States**

Vanguard continues to foresee GDP growth around 3.5% in the United States in 2022, though oil prices and geopolitical risks from the Ukraine crisis bear watching.

We currently see less risk from events in Ukraine to the U.S. economy than to that of the euro area, though the risk of recession would increase if financial conditions significantly tighten and oil prices settled into a $130 to $150 range. GDP increased at an annual rate of 7.0% in the fourth quarter, up from 2.3% third-quarter growth, according to the second estimate from the Bureau of Economic Analysis. For all of 2021, real GDP grew by 5.7%, compared with a contraction of 3.4% in 2020, when the pandemic set in.

- **Euro area**

Vanguard expects factors led primarily by higher energy prices to shave up to a percentage point from our previously anticipated 3.5% growth outlook. (Other factors include diminished consumer and business confidence and tighter financial conditions.) Energy price impacts are likely to be greater in the euro area, which derives 40% of its natural gas and 25% of its crude oil from Russia, than in the United Kingdom and the United States. The further downgrade to our growth view comes even as the COVID-19 situation improves, with daily cases, hospitalizations, and deaths declining. For the fourth quarter, GDP grew by 0.3% on a seasonally adjusted basis compared with the third quarter.

- **China**

The National Bureau of Statistics in China released stronger-than-expected economic data on March 15, but the numbers don't capture significant headwinds that have since developed in what was always going to be a challenging year.

The increase in COVID-19 cases has led to shutdowns beginning the week of March 14. China set an official 2022 growth target "around 5.5%" at the early-March National People's Congress, its lowest growth target ever. Vanguard maintains its forecast for growth around 5%, which in our view is the minimum that policymakers will accept. We believe economic spillovers from the war in Ukraine will shave 50 basis points off China's growth in our base case scenario, and that stimulus will be introduced as necessary.

- **Emerging Markets**

Direct economic spillovers from the war in Ukraine are largely limited to Central Europe and Eastern Europe and are not a major threat to emerging markets broadly. Persistently higher prices for both energy and non-energy commodities add to inflation, leading to more restrictive monetary policy and slowing growth. We continue to foresee growth around 5.5% for all of 2022 for emerging markets, though we emphasize now that risks are clearly skewed to the downside.

- **Unemployment**

The United States added jobs at a strong pace in February, and the unemployment rate fell to its lowest since before the COVID-19 pandemic. The Bureau of Labor Statistics reported that 678,000 jobs were created in February, more than 50% above the consensus expectation. Vanguard expects the unemployment rate to fall to its 3.5% pre-pandemic level in the second quarter and even further by year-end.

- **Inflation**

The Consumer Price Index in the United States climbed by 7.9% in February compared with a year earlier—the highest increase in the gauge since January 1982. Vanguard expects core Personal Consumption Expenditures Price Index (PCE), which excludes volatile food and energy prices, to fall back toward 3% by the end of 2022. Our upside scenario of core PCE remaining above 4% at year's end would become more likely with continued geopolitical tensions and elevated oil prices.

- **The Fed**

The Federal Reserve raised the target range for its federal funds rate by 25 basis points, to a range of 0.25% to 0.50%, on March 16. Higher oil prices stemming from Russia's invasion of Ukraine have increased upside risks to inflation and downside risks to growth.

The Fed sent a clear signal that controlling inflation means a 2022 of regular rate hikes. The Fed is poised to announce the start of a reduction in its bond holdings as soon as its May 4 policy-setting meeting.

Capital Markets Scorecard

Benchmark Description	Q1	1 Year
U.S. Treasury 3 Month T-Bill	0.04%	0.06%
Barclays Aggregate Bond Index	-5.93%	-4.15%
S&P 500 Index Total Return	-4.60%	15.65%
NASDAQ Composite TR	-8.95%	8.06%
NASDAQ Dividend Achievers TR	-5.21%	12.27%
Russell 2000 Index TR	-7.53%	-5.79%
Alerian MLP Index TR	18.81%	36.56%
China SCI 300 Index LC	-14.53%	-14.87%
Japan Nikkei 225 Index LC	-2.48%	-2.81%