MARKET INSIGHT MONTHLY

May Update

MONTHLY COMMENTARY

UNITED BANK
Wealth Management

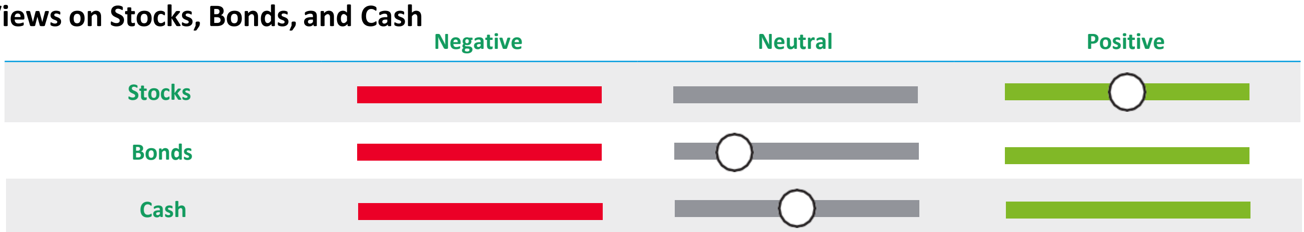
In a 1966 Newsweek article, the eminent economist Paul Samuelson famously quipped that the stock market had predicted nine of the past five recessions. This remark has been often repeated to deride the predictive powers of the stock market. Through 2015, CNBC studied the general accuracy of this statement since WWII. The actual findings reflected the tongue-in-cheek comment. The stock market's accuracy in predicting a true recession is only about 50%. Equity investors are completely justified in being mindful of and attentive to potential economic adversity. But short-term trading activity does not always align with longer-term fundamentals. First quarter 2022 S&P 500 operating earnings are beating estimates by almost 7% and are over 5% higher than one year ago. Earnings for the full 2022 calendar year remain on pace to move 7-10% higher and set additional records. The recent correction has created valuation levels which are attractive despite the modest increase in interest rates. While the Federal Reserve is emphasizing stricter monetary policy in order to tame inflation, history suggests that once investors digest the first several months of higher rates, equity prices tend to regain their upward momentum. As the market decline stretches into its longest stretch since 2011, investors may start to find values quite compelling.

INVESTMENT TAKEAWAYS

- Global and domestic financial markets have been impacted by two critical variables that are in direct conflict. On one hand, the Federal Reserve is attempting to stem inflation, while on the other hand, Russia's invasion has created havoc with not only the civilized world order, but in destabilizing the energy and agricultural sectors. Thus, inflationary pressures continue without an available solution. Market volatility has been present since January as uncertain conditions persist, prompting various actions intended to reduce portfolio risk in the short-term.
- United Wealth Management has always taken risk management into consideration by constructing portfolios that tend to be more risk averse. United's equity exposure is more heavily weighted with large, value-oriented, U.S. based companies. United favors shorter to intermediate term duration fixed income portfolios that should not suffer value declines as precipitously when rates move higher as may be experienced with longer maturity portfolios.
- Despite early year volatility and markedly higher interest rates, we continue to overweight equities within our total asset allocation. We do not believe that either short or long rates will move high enough to lure substantial funds away from the equity markets. Though the chances of a recession have increased, there is currently insufficient evidence to alter our outlook. Corporate earnings for 2022 may be nearly 10% higher than in 2021.
- Our value bias within large, mid and small-cap companies better protects portfolios during volatile periods as is currently being experienced. Companies with strong balance sheets often pay higher dividends and are preferred during less certain environments.
- Though developed nations' equity markets have generally outperformed those of emerging markets (EM), both segments have considerably lagged the U.S. We remain comfortable with our modest international exposure and prefer to wait for more evidence suggesting a higher allocation is warranted.
- We continue to underweight our allocation to fixed income and favor short to intermediate maturities. Rates have recently moved higher, which has negatively affected fixed income returns. We expect rates will move modestly higher from here. We believe much of the anticipated rate increase has already been seen.

BROAD ASSET CLASS VIEWS

Views on Stocks, Bonds, and Cash



EQUITY ASSET CLASSES

We continue to favor stocks relative to bonds despite the recent volatility. There is a general perception that all interest rate increases result in poor equity performance. But this is not the case. Evidence suggests that early-stage interest rate increases (from low real and nominal levels) has only a relatively minor short-term effect on equity prices, and no long-term effect. In fact, an upward bias in the cost of money reveals generally strong demand which propels economic growth. This leads to earnings growth. The record setting domestic earnings of 2021 will carry forward into 2022. We see little evidence suggesting earnings growth will be curtailed, although the rate of earnings growth will be well less than last year. Our U.S. equity preference has proven to be both prudent and profitable. We continue to favor the U.S. We continue to monitor political/economic activities in both Russia and China as authorities in both countries engage in activities contrary to worldwide economic stability.

	Sector	Overall View	Relative Trend	Rationale
Market Capitalization	Large Caps			No asset class is completely immune to economic changes. But within the global equity arena, U.S. large cap stocks have been the most reliable segment for the last several years. Record earnings generated in 2021 influenced investors to continue holding and buying large-cap cyclical value and earnings-driven growth stocks. The recent modest correction has created a value opportunity as earnings should grow nearly 10% in 2022. We believe investors will be rewarded by holding quality names.
	Mid Caps			In 2020 and 2021, mid-cap companies' earnings and stock prices grew dramatically with economic expansion. The recent correction is partly due to the uncertainty associated with interest rate increases. With a higher degree of certainty associated with Fed actions, we expect mid-caps will resume their upward bias. Valuations remain very attractive.
	Small Caps			Much like mid-caps, the small cap sector has been impacted by interest rate risk. Though this segment was among the strongest performers of 2021, it is generally a bit more susceptible to higher volatility as uncertainty increases. We feel that valuations are more attractive based on strong earnings growth prospects through 2022. We remain overweight small caps.
Style	Growth			Large-cap growth stocks are more rate sensitive and have suffered more than value stocks during this correction due to current and expected rate increases. To some degree, this growth correction has elements of a reversion to the mean. Growth stocks have outperformed value stocks for decades. Though rates will generally move higher, we feel that most of the move is now priced in and quality growth stocks should be well positioned for the remainder of 2022.
	Value			United has maintained a value stock overweight during the economic expansion. The companies held in our value-based Large Cap Dividend Strategy maintain sterling balance sheets and are clearly preferred by many investors. We continue to believe select value companies will exceed expectations and lower portfolio risk.
Region	United States			We see the potential for better performance in the U.S. stock market during 2022. The events of the first 4 months have been unsettling and important responses to these events remain elusive and unfulfilled. We do know that the free world stands opposed to Russian aggression and solutions to the energy and food shortages are being negotiated. While the Fed will fight inflation, they are unlikely to raise rates to the point where economic prosperity will suffer. The U.S. remains both a place of opportunity and refuge. Strong earnings are likely to set additional records. We believe the U.S. will play the lead role in moving forward. We will remain overweight.
	Developed International			Developed countries around the world have faced economic concerns since the start of the COVID pandemic. Though most of the world is now in a sustainable recovery, investors have been recently challenged by geographic proximity to conflict. Therefore, an encouraging economic path has become more compromised. We maintain our baseline weight to developed country equities.
	Emerging Markets			Chinese government intervention and continued EM pandemic health concerns cast a shadow over EM in 2021. Early in 2022, Russian aggression has resulted in de-listing Russia from EM benchmarks. Though we believe in EM over the long term, self-inflicted obstacles have weighed on investor sentiment to this segment. We have only a modest baseline weight to EM.

FIXED INCOME

Limit Rate Sensitivity with Intermediate Focus

The rapid escalation of interest rates over the past several months is clearly due to policy changes within the Fed. While they have now increased the Fed Funds rate twice, by a total of 75 basis points, they intend to aggressively fight inflation and have indicated that further rate increases will occur. Had the Russian invasion not occurred, the yield path would have been modestly higher rather than the sharply higher path we are experiencing. The pressure on global energy prices, and to some degree agricultural prices, are prolonging elevated inflation and forcing the Fed to take remedial action. They likely otherwise would have allowed inflation to eventually fall under its own cycle as supply catches up with demand. Should the situation in Ukraine continue with little resolution in sight, the same segments will continue to feel stress which may prolong relatively high inflation and delay rate stability. Should the opposite occur, we would expect some relief. In our view, compensation for longer-maturity bonds remains unattractive, as rates will likely move modestly, but not substantially higher from current levels. We continue to suggest a blend of high-quality short-to-intermediate bonds in all fixed income portfolios.

The continued economic expansion allows for high yield bonds issued by stable but growing companies to be a productive use of fixed income capital. We remain committed to a modest high yield position in both corporate and municipal bonds. As previously stated, inflation primarily rose in 2021 due to an expanding global economy, but one in which access to goods were compromised due to many COVID related supply chain shortages. Though this dilemma has not been completely solved, several factors suggest the worst may be behind us. Unfortunately, as long as the Russian conflict exists, inflationary fears will remain. Thus, we continue to promote inflation protection in fixed income portfolios via a position in Treasury Inflation Protected Securities (TIPS).

We favor municipal bonds for tax-sensitive accounts. Infrastructure spending, strong state revenues and the potential for higher personal tax rates provide support to municipal markets.

		Low / Medium / High	Rationale
Positioning	Credit Quality		Credit spreads have recently widened and are more aligned with historical averages.
		Short / Int. / Long	
	Duration		Concerns over rising interest rates/inflation remain viable with the prospect of a return to normalized economic growth with reduced government stimulus.

COMMODITIES

Our precious metals view remains neutral. Gold prices saw a pronounced increase in the early stages of the Russian conflict but have given back all gains. Gold is now trading at pre-invasion levels. Broad baskets of commodities, including those associated with the agricultural trade have also increased in price, but are stabilizing for the moment.

The global demand for goods and services has clearly improved over the last 18 months. Energy prices started to rise in late 2020 and continued moving higher for much of 2021 due to relatively low supply. West Texas Intermediate Oil spiked to nearly $130 a barrel as a direct consequence of the Russian conflict. Currently trading at just over $110 a barrel, oil will likely rise and fall as a direct consequence of the military conflict. Should the threat abate, prices are unlikely to remain this elevated.

CONCLUSION

The Russian military conflict has clearly heightened anxiety and is exacerbating already high inflationary conditions. But much of the recent volatility is due to rising interest rates and uncertainty over Federal Reserve policy. Though the U.S. consumer and corporate world has been steadfast in their resolve to move forward, investors have turned wary as both the magnitude and velocity of interest rate changes were not fully expected.

As we examine market and economic risks, we understand that even well-constructed portfolios are not immune from short-term fluctuation. But over time, diverse portfolios created to withstand occasional uncertainty ultimately benefit from economic expansion.

Disclosures

The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual security. To determine which investment(s) may be appropriate for you, consult your financial advisor prior to investing.

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Economic forecasts set forth may not develop as predicted.

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