



NEPC MARKET OUTLOOK

NAVIGATING MARKET STRESS

OCTOBER 26, 2022

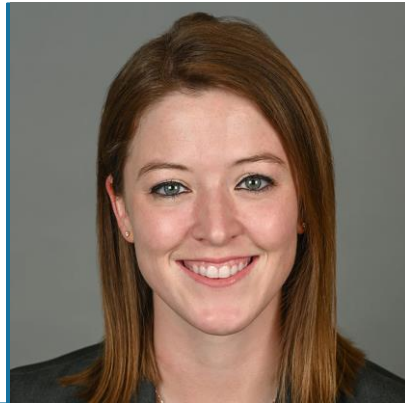


SPEAKERS



Phillip Nelson, CFA

Partner, Head of Asset
Allocation

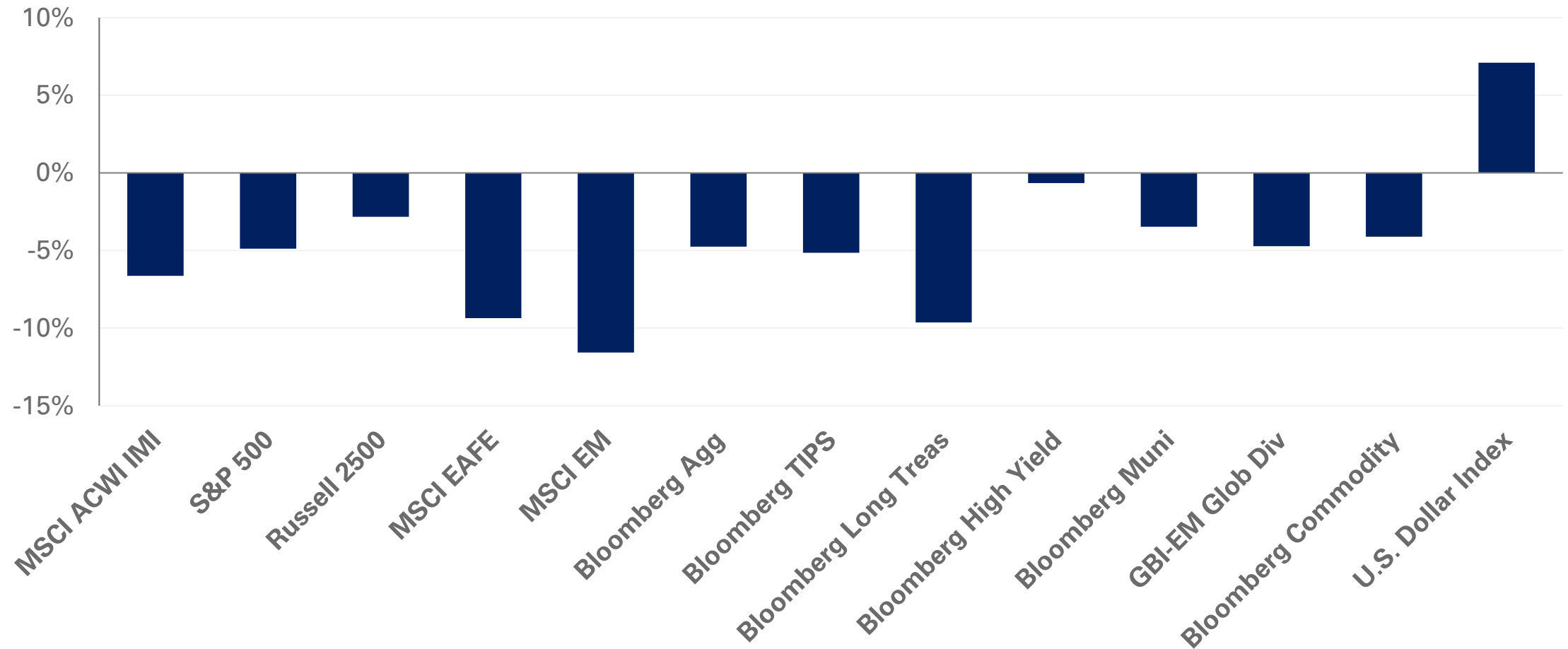


Jennifer Appel, CFA

Investment Director,
Asset Allocation

GLOBAL ASSETS BROADLY DECLINED

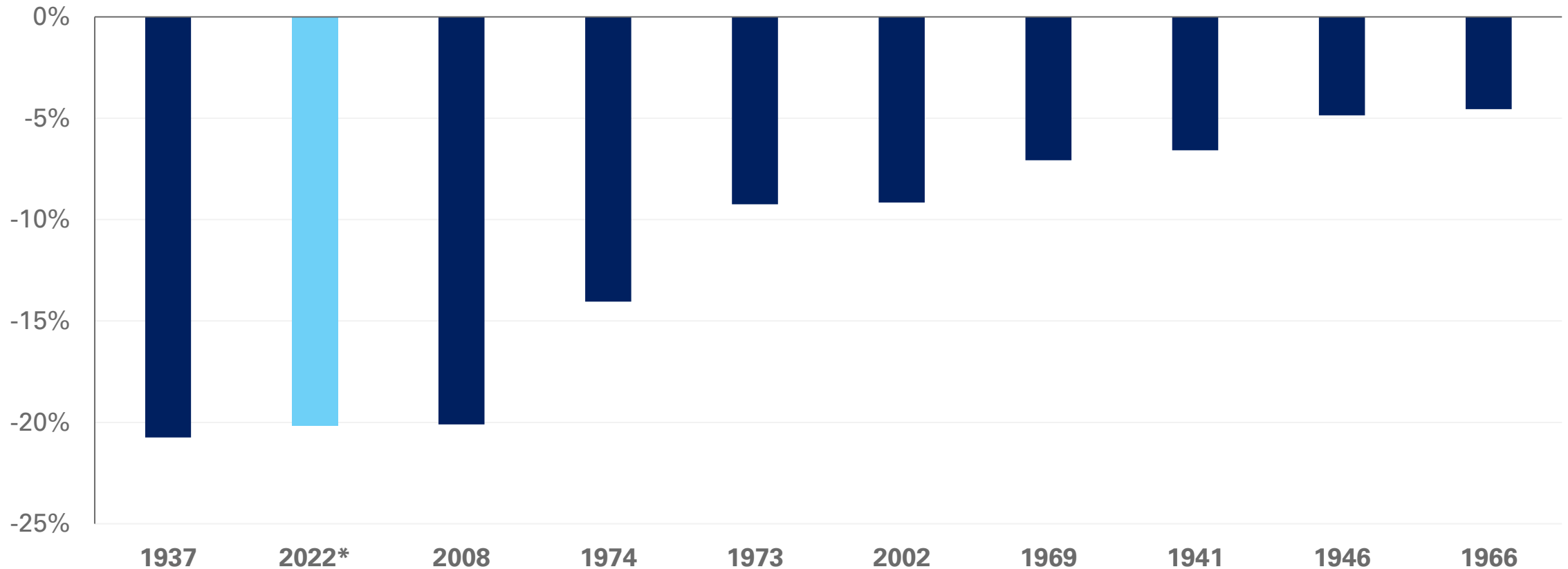
QUARTERLY TOTAL RETURNS



Source: MSCI, S&P, Russell, MSCI, Bloomberg, JPM, FactSet

60/40 PORTFOLIO ON TRACK FOR WORST YEAR

WORST ANNUAL RETURNS: 60/40 PORTFOLIO



60/40 Portfolio represents 60% S&P 500 and 40% U.S. Aggregate Bonds (post 1975) and 40% Treasury (prior to 1974)
Data calculated from 12/31/1936; 2022 represents returns through the first nine months of the year
Source: S&P, Bloomberg, FactSet

THE S&P 500 INDEX REMAINS IN A BEAR MARKET

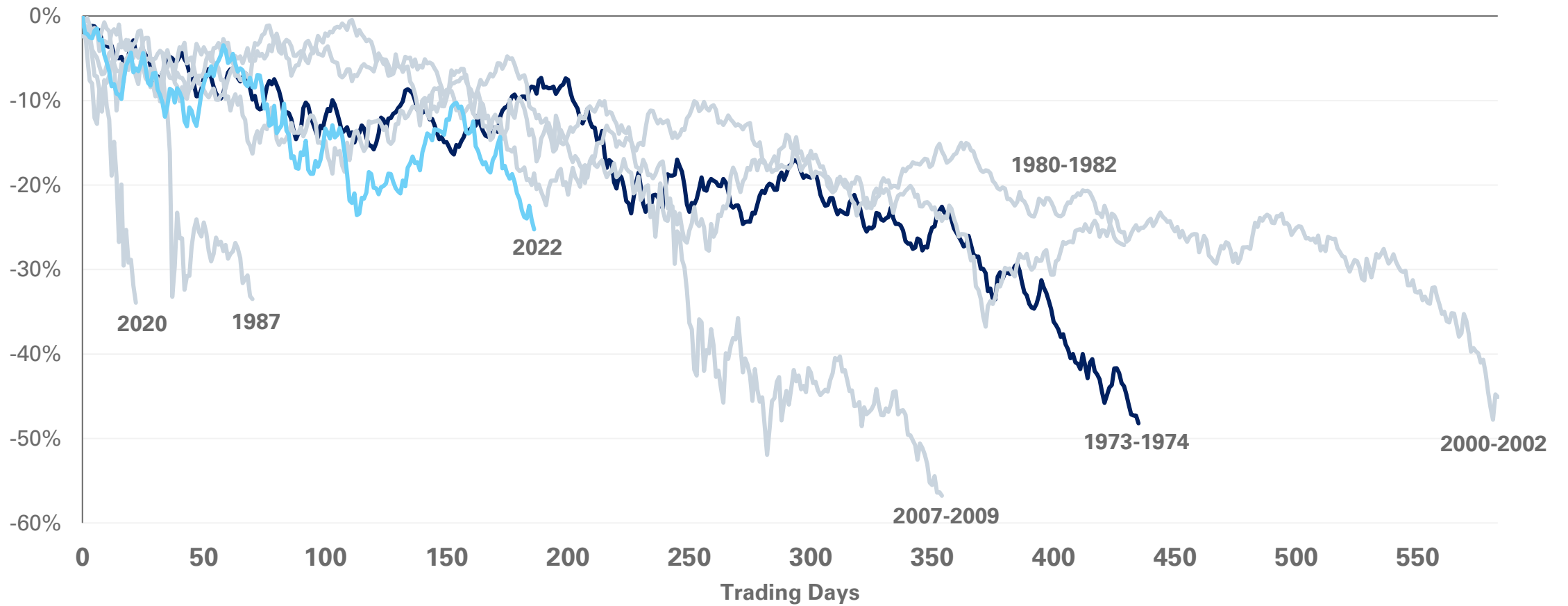
LENGTH AND DEPTH OF S&P 500 BEAR MARKETS

Start	End	Length of Bear Market (Months)	Length of Recovery* (Months)	S&P 500 Decline
01/03/2022	?	9*	?	-24%*
02/19/2020	03/23/2020	1	5	-34%
10/09/2007	03/09/2009	17	59	-55%
03/24/2000	10/09/2002	31	80	-47%
08/25/1987	12/04/1987	3	20	-34%
11/28/1980	08/12/1982	21	3	-27%
01/11/1973	10/03/1974	21	69	-48%

Notes: 2022 bear market is ongoing; represents historical bear markets since 1970. *Length of Recovery represents time to recoup losses from the start of the bear market.
Sources: S&P, FactSet, NEPC

THE BEAR MARKET IS TRENDING WITH THE PAST

HISTORICAL S&P 500 BEAR MARKET PATHS RELATIVE TO TODAY

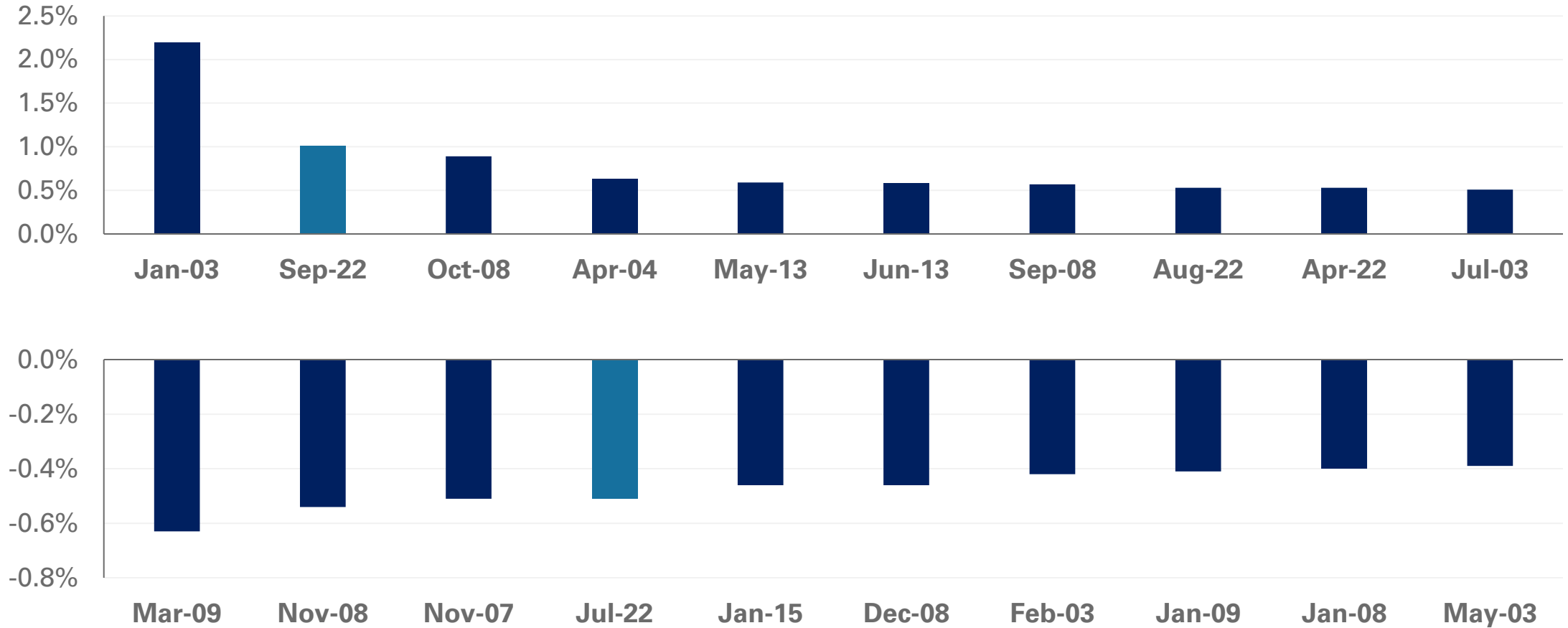


Sources: S&P, FactSet, NEPC



U.S. REAL YIELDS ARE MOVING IN EXTREMES

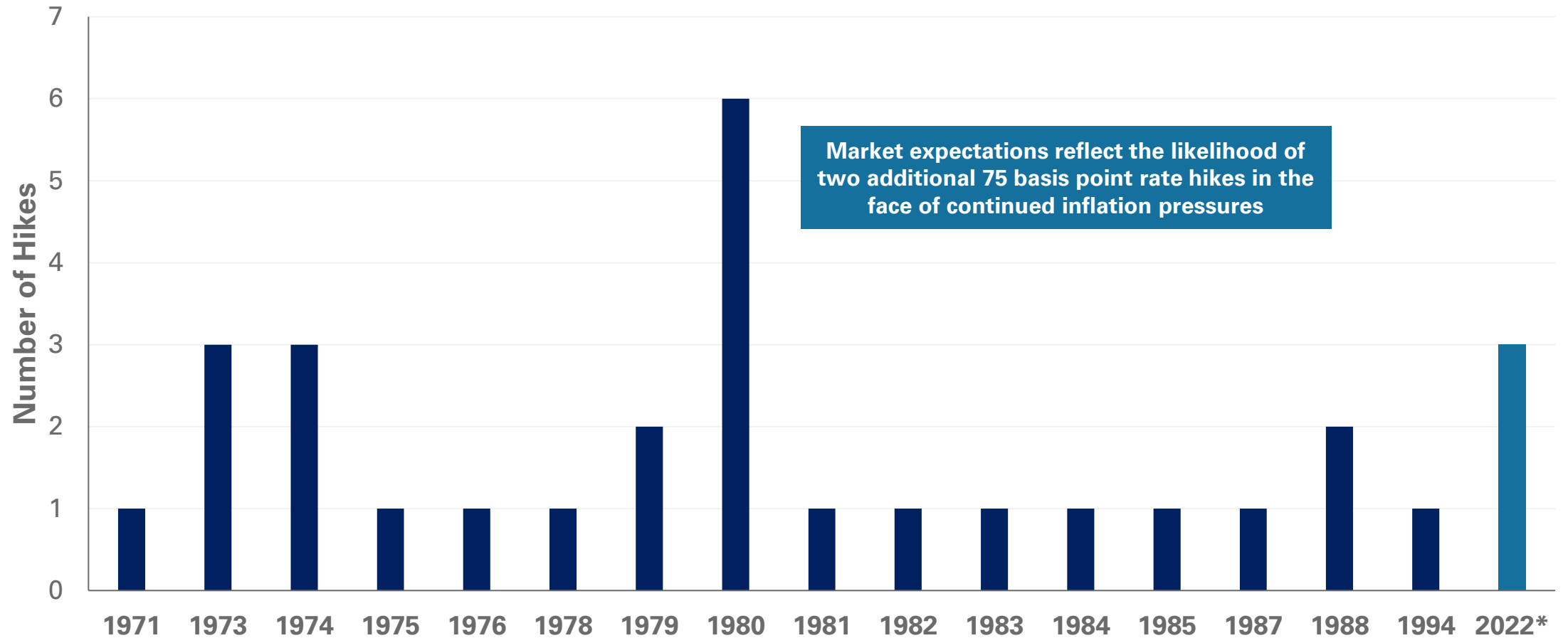
TOP TEN MONTHLY CHANGES: 10-YEAR U.S. TIPS REAL YIELD



Calculated based on data between 12/31/2002 to 9/30/2022
Source: FactSet

THE MOVEMENT IN RATES HAS BEEN SIGNIFICANT

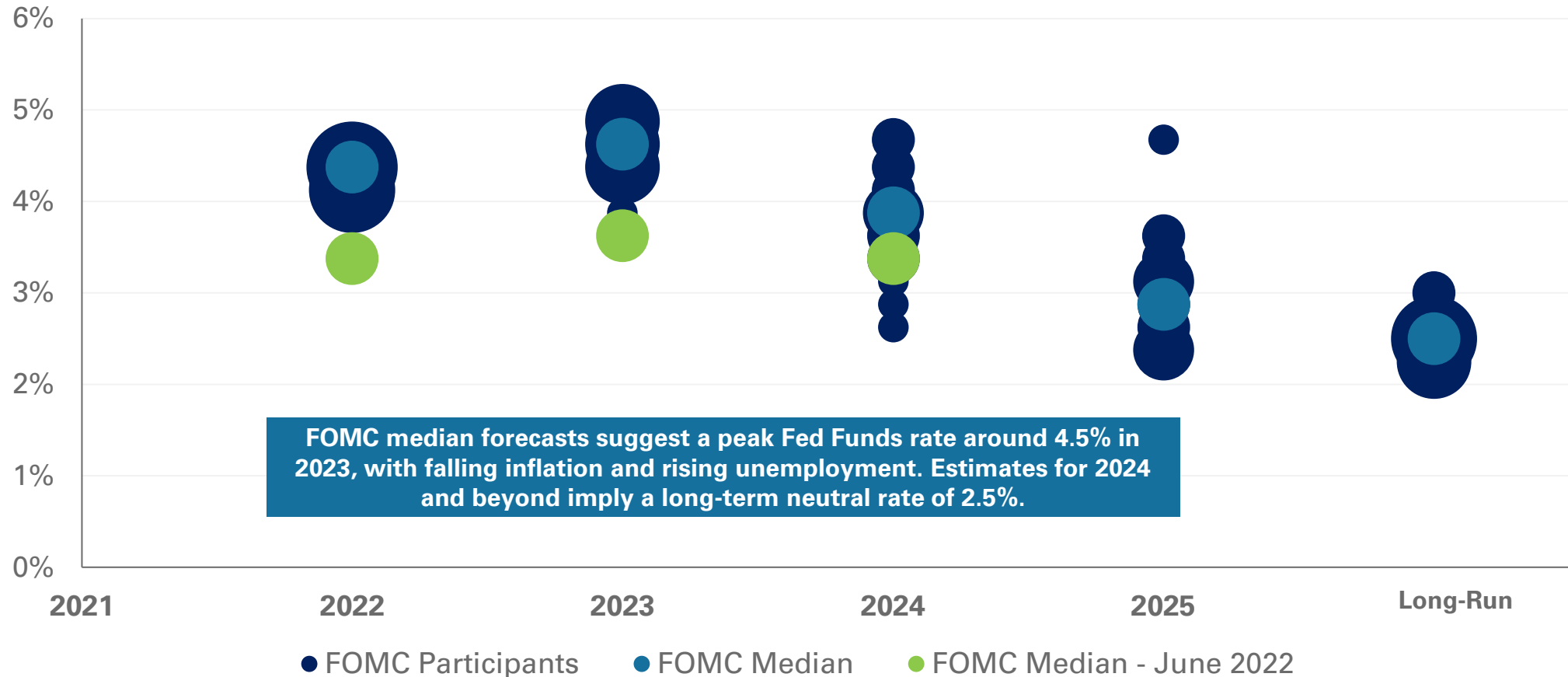
NUMBER OF FED RATE HIKES $\geq 0.75\%$ IN A CALENDAR YEAR



Source: Federal Reserve, FactSet, NEPC

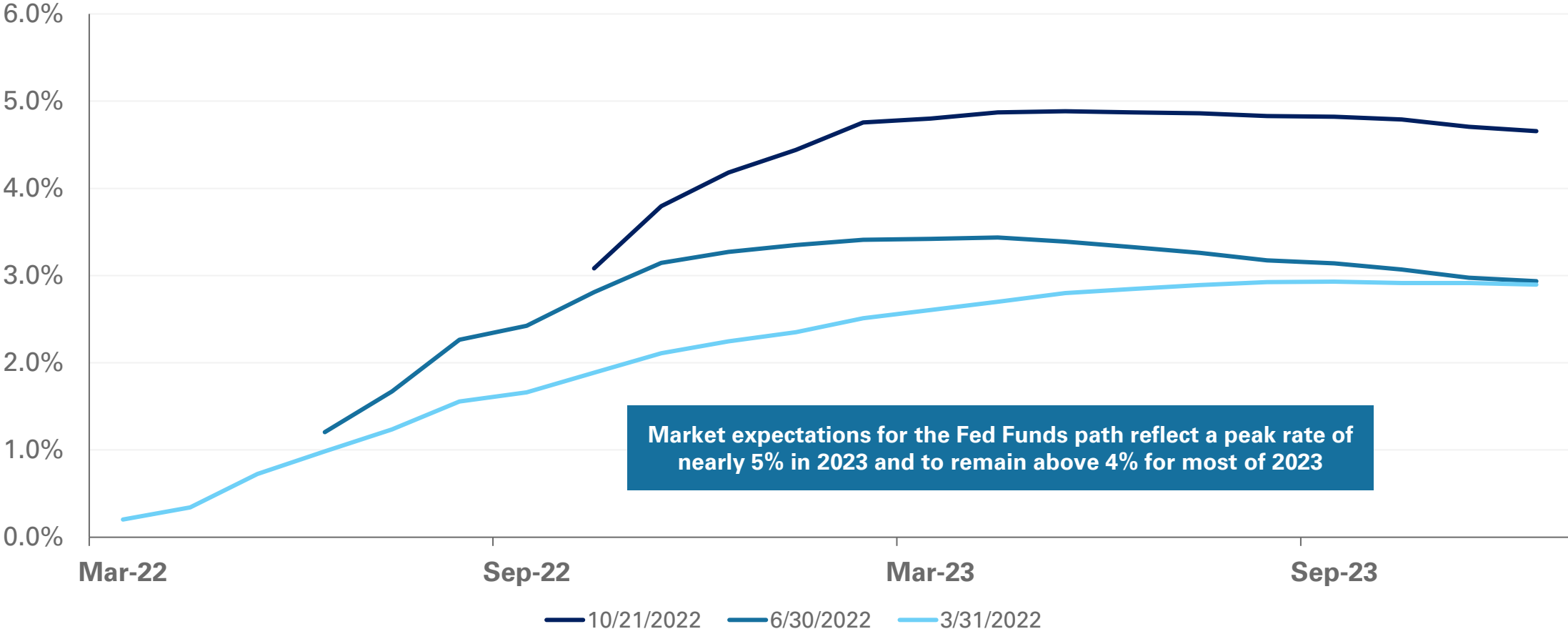
FOMC PROJECTS LOWER RATES IN 2024

FOMC DOT PLOT PROJECTIONS



FED FUNDS EXPECTATIONS CONTINUE TO RISE

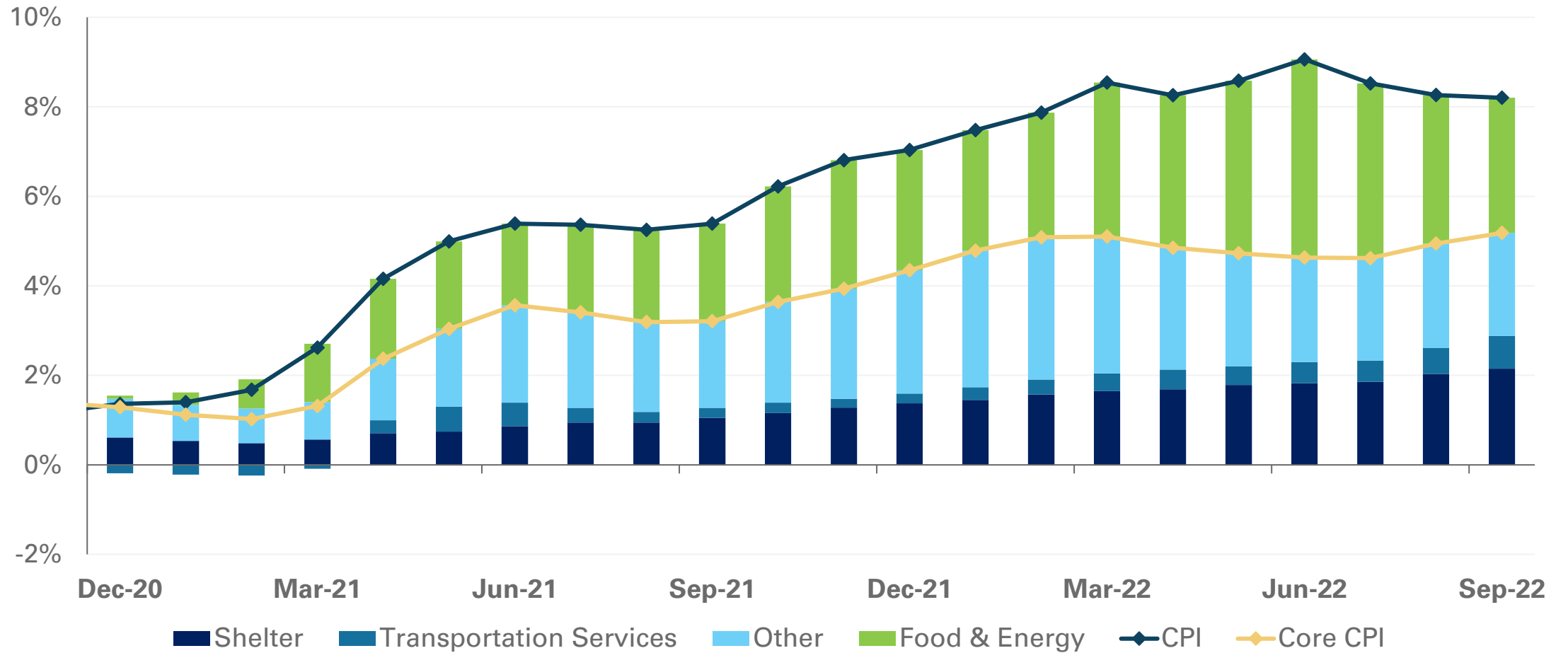
FEDERAL FUNDS FUTURES



Source: FactSet

CORE INFLATION CONTINUES TO REMAIN HIGH

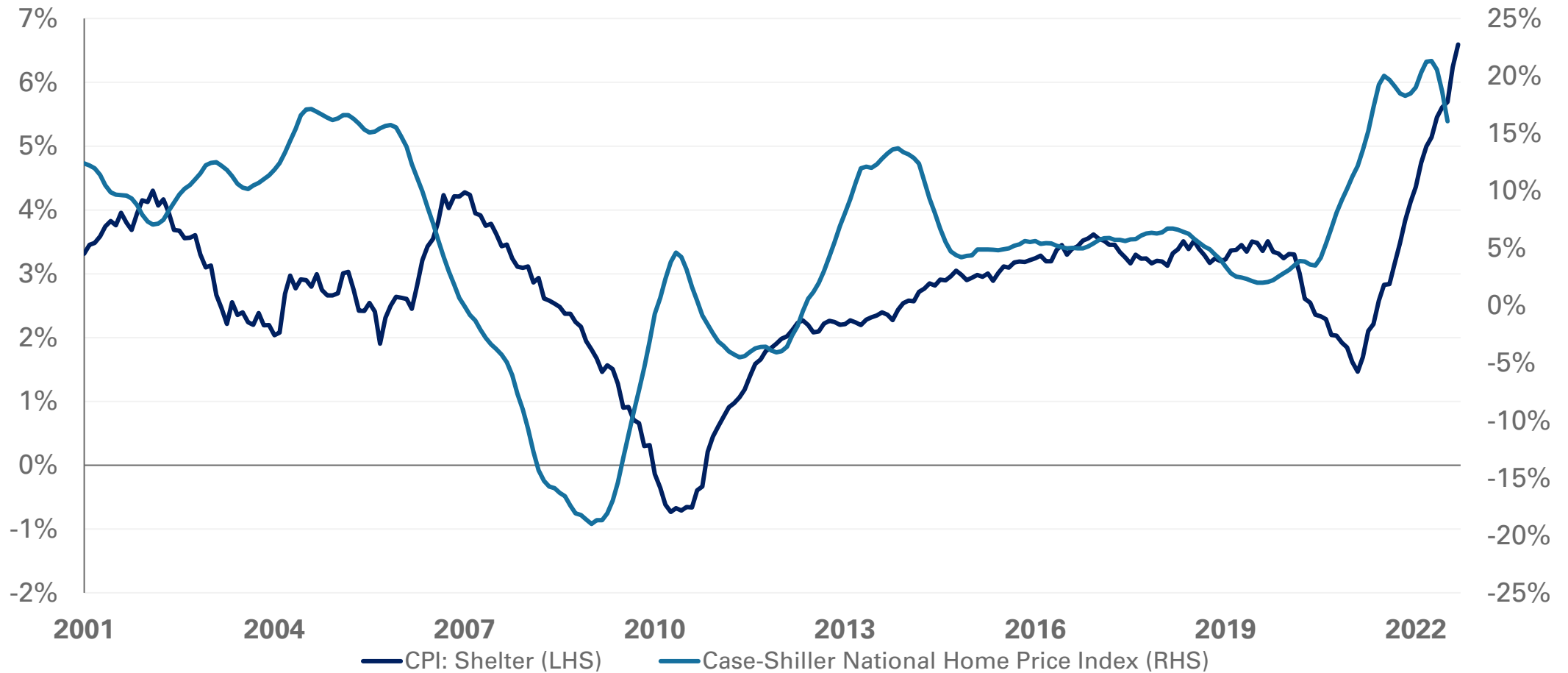
ANNUAL U.S. CPI-U CHANGES



Source: Department of Labor, FactSet

SHELTER IS STILL APPLYING UPWARD PRESSURE

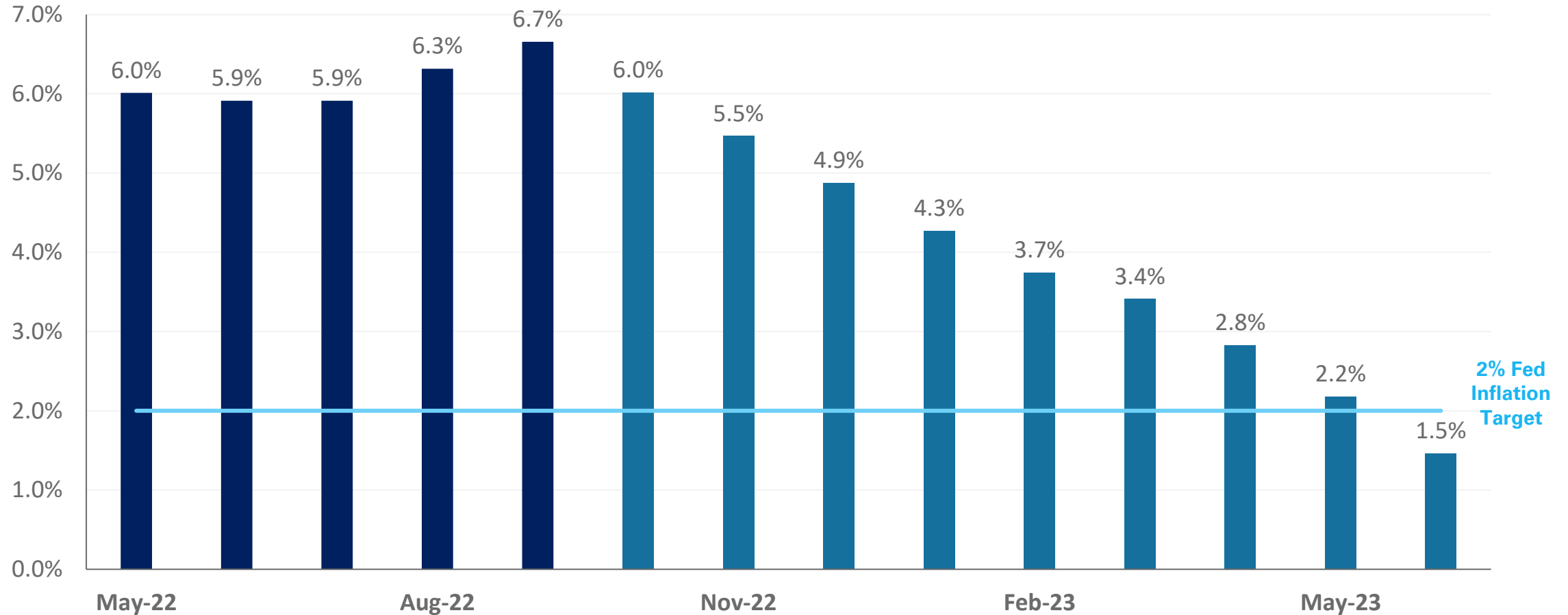
SHELTER CPI LAGS HOME PRICE AND RENTAL RATE GROWTH



Sources: Dow Jones, Bureau of Labor Statistics, FactSet

HEADLINE INFLATION WILL REMAIN ELEVATED

PROJECTED CHANGE IN U.S. CORE CPI WITH 0% MONTHLY CHANGE



Notes: Figures calculated pulling forward the September index value
Sources: U.S. Department of Labor, FactSet, NEPC



KEY THEMES FOR INVESTORS



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Stagflation dynamics pose a challenge to portfolio diversification and represent a headwind for equity valuations and profit margins

The path of U.S. corporate earnings do not reflect material weakness for 2023 despite the tightening monetary policy environment

Europe's economy is exposed to an energy shock as its infrastructure undergoes an emergency transplant to pivot from Russian energy

China's zero-COVID policy has global supply chain implications and continues to dampen consumer spending and industrial activity

U.S. Dollar strength reveals risks in the global financial system and will continue to pressure weaker markets, companies and nations

INVERTED CURVE ECHOES STAGFLATION CONCERN

10Y-2Y TREASURY YIELD SPREAD

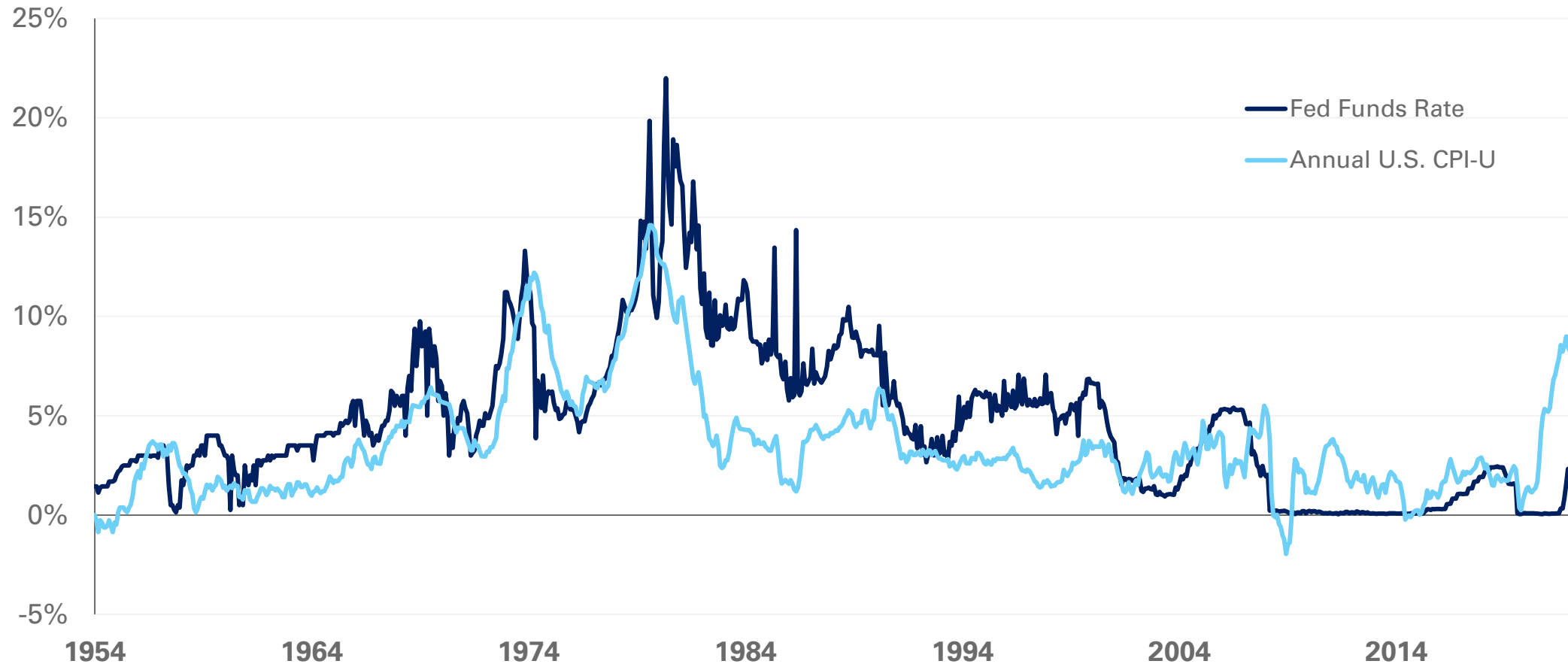


Source: FactSet



INFLATION AND FED FUNDS NEED TO CONVERGE

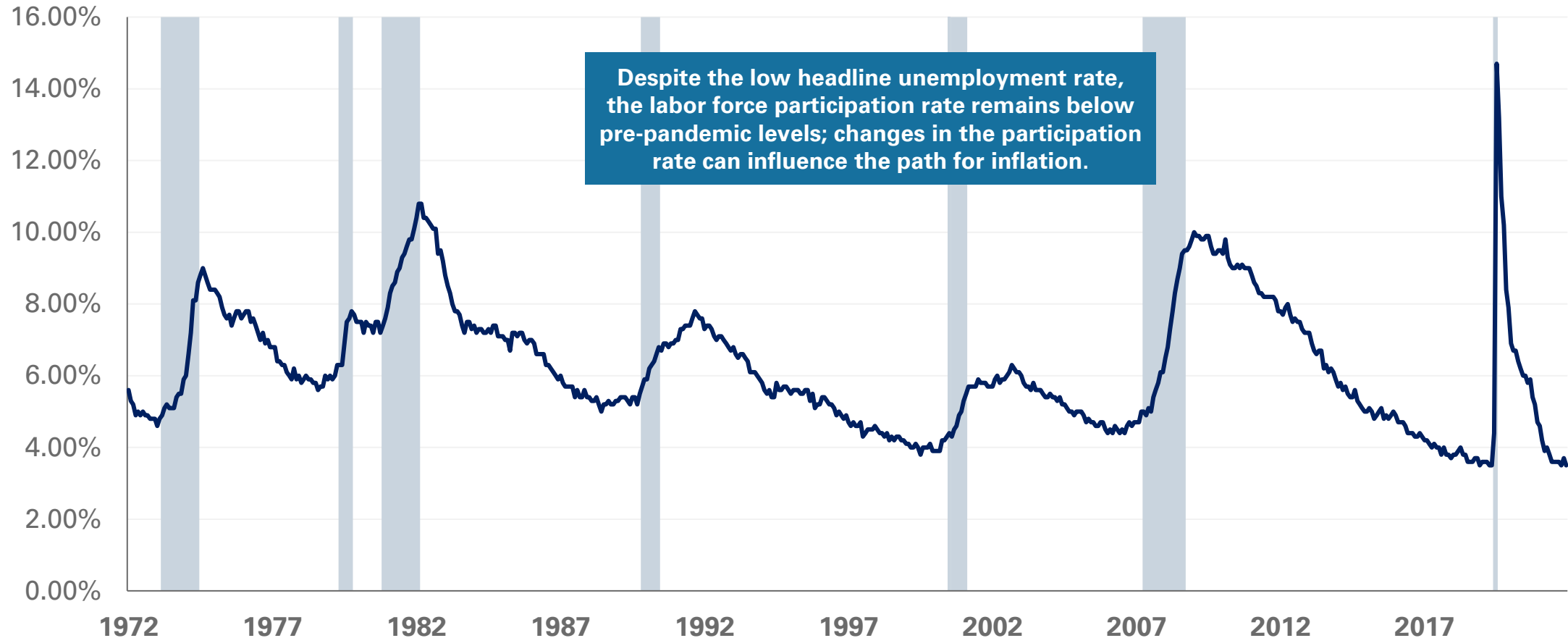
HISTORICAL RELATIONSHIP BETWEEN FED FUNDS AND INFLATION



Sources: U.S. Department of Labor, Federal Reserve, FactSet

THE LABOR MARKET REMAINS TIGHT

U.S. UNEMPLOYMENT RATE

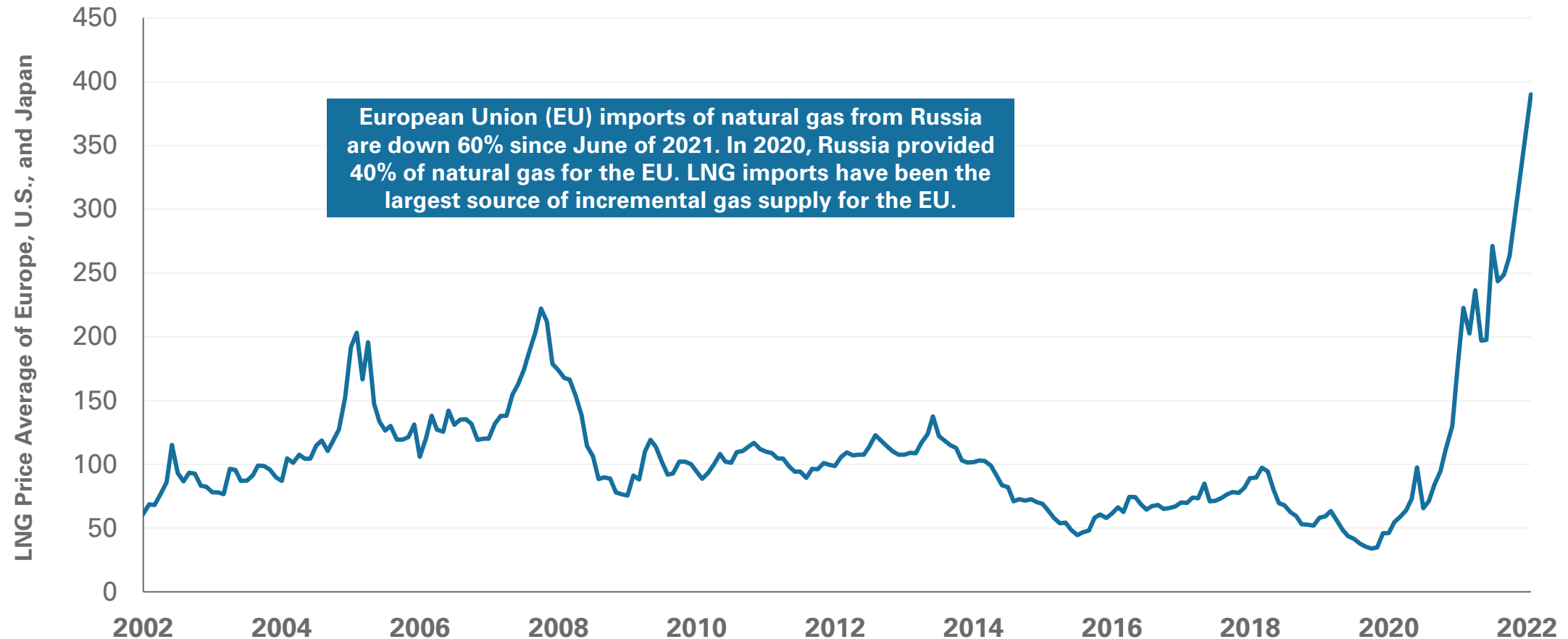


Notes: Shaded areas represent
Sources: U.S. Department of Labor, FactSet, NEPC



ENERGY SUPPLY IS A KEY RISK FOR EUROPE

INDEXED AVERAGE PRICE OF LIQUID NATURAL GAS (LNG)



Notes: Liquid Natural Gas Index Average of Europe, US, and Japan (2010=100)
Sources: Eurostat, FactSet, IMF

DOLLAR STRENGTH IS NEAR 20 YEAR HIGH

THE U.S. DOLLAR INDEX

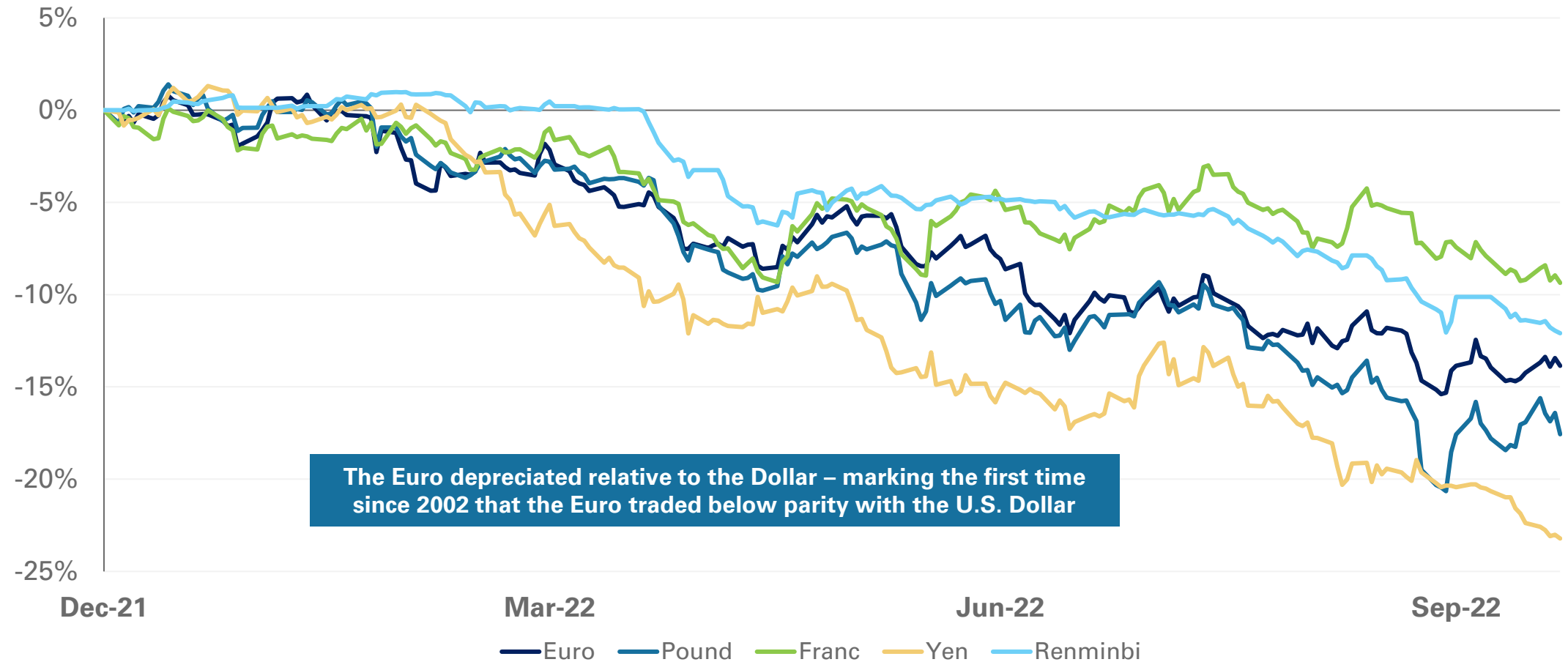


U.S. Dollar Index represents the value of the U.S. Dollar relative to the currencies of major trade partners. The Euro, Japanese Yen, Pound Sterling, and Canadian Dollar represent the largest weights within the Index.
Source: FactSet



CURRENCY WEAKNESS ACCELERATED IN 2022

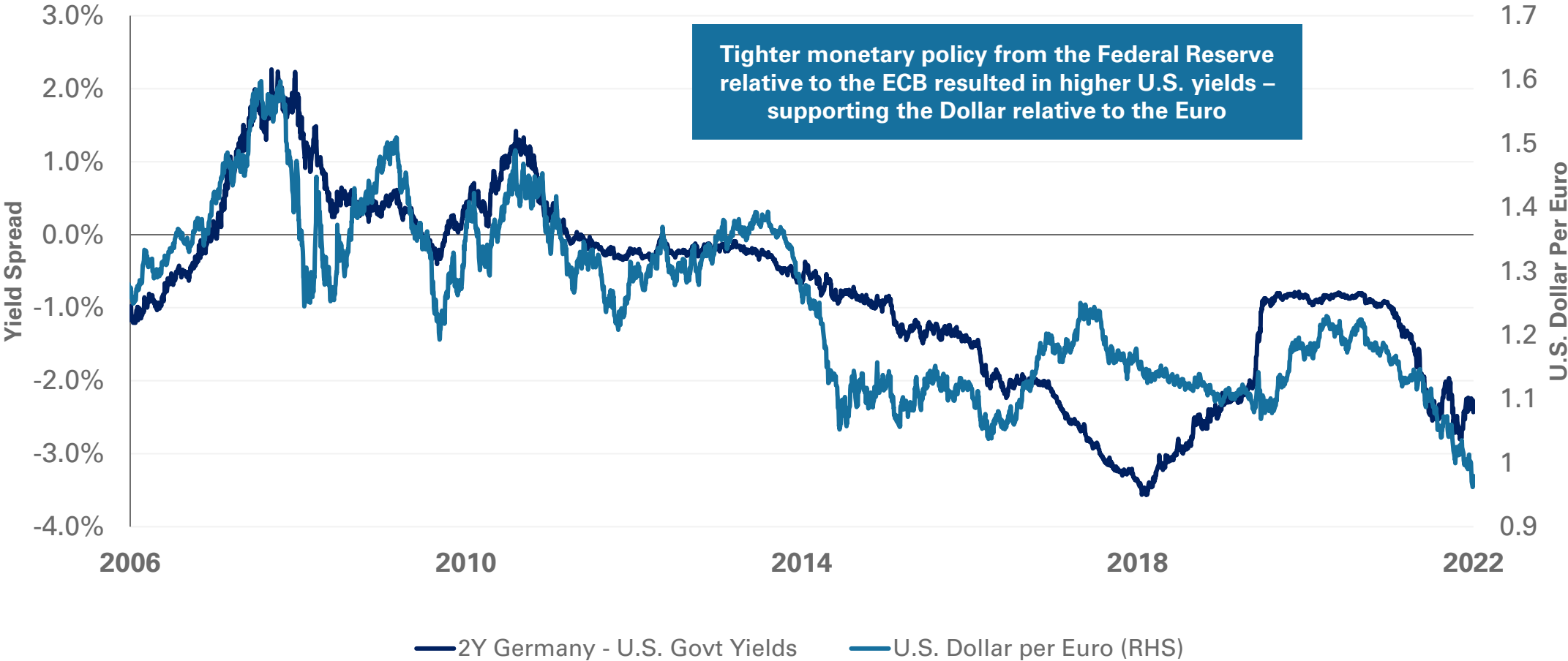
CUMULATIVE CURRENCY RETURNS



Source: FactSet

HIGH RELATIVE CARRY BENEFITS THE DOLLAR

GERMANY VERSUS U.S. GOVERNMENT YIELD DIFFERENTIAL



Source: FactSet

STRATEGIC ASSET ALLOCATION OUTLOOK

We have transitioned to an investment regime characterized by **entrenched inflation** and significant **economic growth headwinds**

Higher interest rates lift public credit return assumptions and support larger strategic targets to investment grade fixed income

Evaluate the scope of strategic currency hedging programs, as the strength of the dollar has provided outsized gains for currency hedges

The **emergence of stagflationary trends** challenges the behavioral biases investors have been conditioned to expect over the last decade

PORTFOLIO POSITIONING



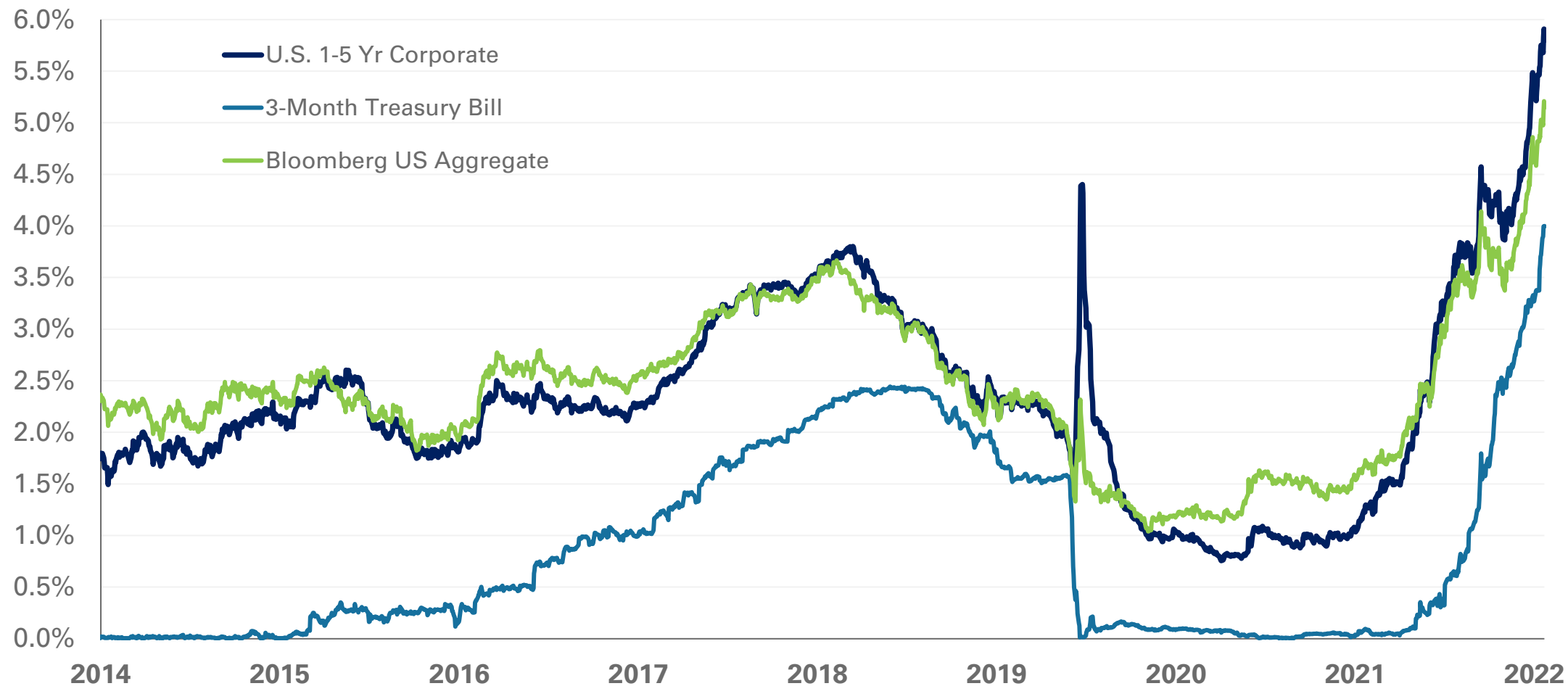
EQUITY REMAINS LESS ATTRACTIVE VS CREDIT

S&P 500 EARNINGS YIELD LESS BBB BOND YIELD



Sources: S&P, FactSet, NEPC

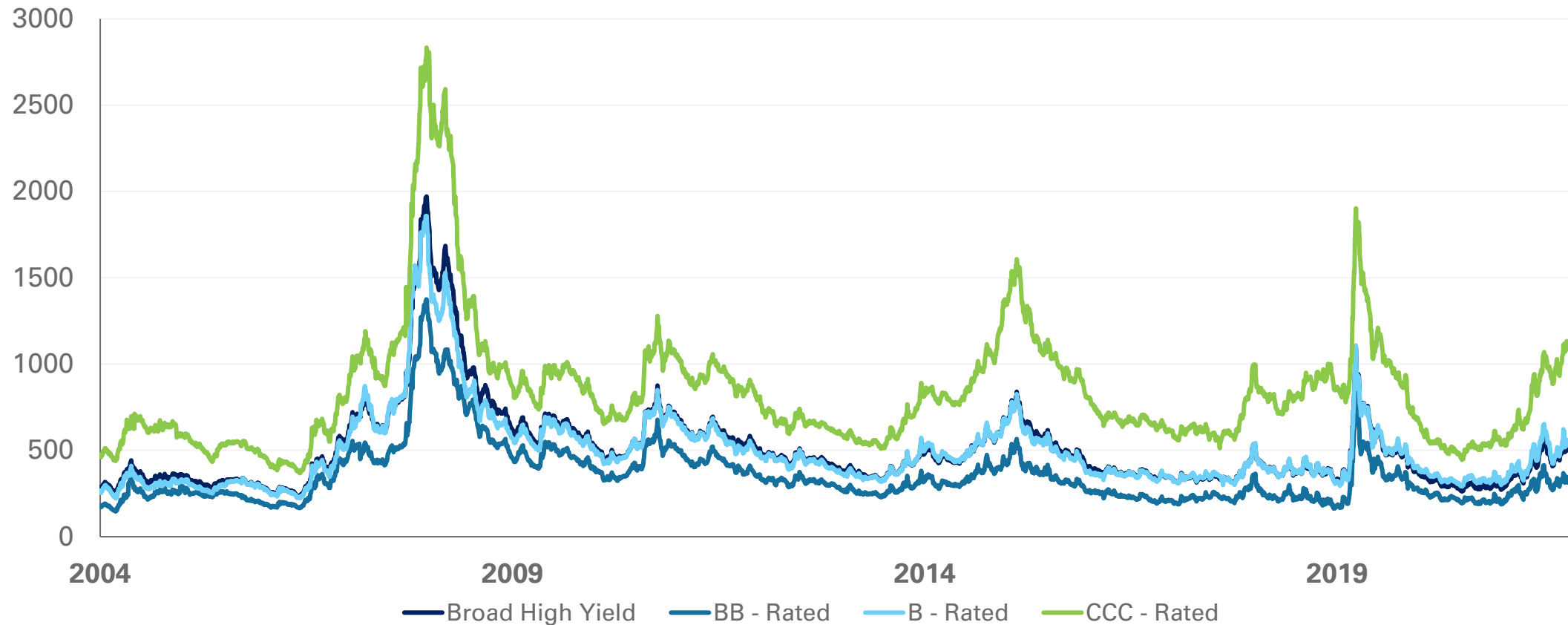
SHORT-TERM BOND YIELDS ARE COMPELLING



Sources: Bloomberg, FactSet

KEEP AN EYE ON SPREADS AS AN OPPORTUNITY

U.S. CORPORATE HIGH YIELD SPREADS



Sources: Bloomberg, FactSet

PORTFOLIO POSITIONING VIEWS

Maintain an **underweight equity posture** due to concerns related to the path of corporate earnings and stagflation growth dynamics

Our **conviction remains high** regarding the addition of value exposure to U.S. large-cap equity and the use of active global equity strategies

Despite the challenging environment, **we encourage maintaining adequate portfolio duration** with safe-haven fixed income exposure

Look to **build exposure to short-term investment grade credit** as higher yields boost our outlook relative to risk assets

THANK YOU

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