SAWGRASS ASSET MANAGEMENT LLC

Financial Review & Outlook
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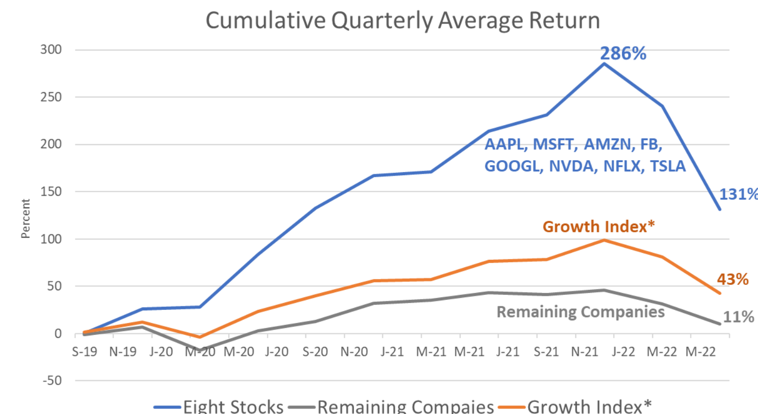
Equity Market

- The equity markets finished off their worst first half of the year since the early 1970s after a double-digit percentage quarterly loss. After a historic run over the past few years, the impetus for the decline was the Federal Reserve's pivot to inflation fighting and the subsequent rise in interest rates which was more than an extended equity market could handle.
- The sharp rise in rates has taken a toll on valuations especially in the higher growth portions of the market while value-oriented indices have been able to withstand some of the damage and post strong relative returns to their growth counterparts. The inflation theme has also become more prominent in earnings outlooks as companies attempt to adjust to the rise in prices to mitigate the overall damage from higher input costs.
- Stocks have reached bear market 20+% declines from recent highs in a relatively short period of time despite no real outward signs of investor panic. This unusual occurrence potentially portends a further decline in prices for sufficiently negative investor sentiment to put in a more meaningful bottom.
- Factor performance continued to favor attractive valuation and lower risk characteristics with the signals generated by these factors over the past 7-8 months the strongest and most consistent seen in multi-year periods. This strength is possibly the opening salvo to a longer-term powerful trend in favor of these factors and investment strategies that favor this approach to investing.
- The quarterly losses were broad across the cap range as value significantly outperformed growth with strong relative sector performance in consumer staples, utilities, and energy and weak sector performance in consumer discretionary, information technology, and communication services.
- Stocks enter the 2nd half of the year clearly on the defensive as the current fundamental headwinds combination of inflation, interest rates, Federal Reserve tightening, downward earnings adjustments, and valuation contraction have become more entrenched and will likely continue to affect investor sentiment for much of the rest of year. Sharp rallies should be expected as the markets price in these adjustments but will not likely develop into more meaningful gains until the markets find a better risk/reward level.
- Despite the bear market decline in stocks over the past six months, the coming years are likely to see more normal returns than we have seen during the Fed amplified bull market of the last 15 years. Active management has potentially entered a better environment given the prospect of higher volatility, lower return conditions.

2nd Quarter Scorecard		*Table 1*
Index	**Quarter**	**1 Year**
S&P 500	-16.1%	-10.6%
Russell 1000	-16.7%	-13.0%
Russell 2000	-17.2%	-25.2%
Russell 3000 Growth	-20.8%	-19.8%
Russell 3000 Value	-12.4%	-7.5%
Barclays Capital US Aggregate	-4.7%	-10.3%
3 Month T-Bills	0.1%	0.2%

Source: Bloomberg & Russell Investments

Graph 1

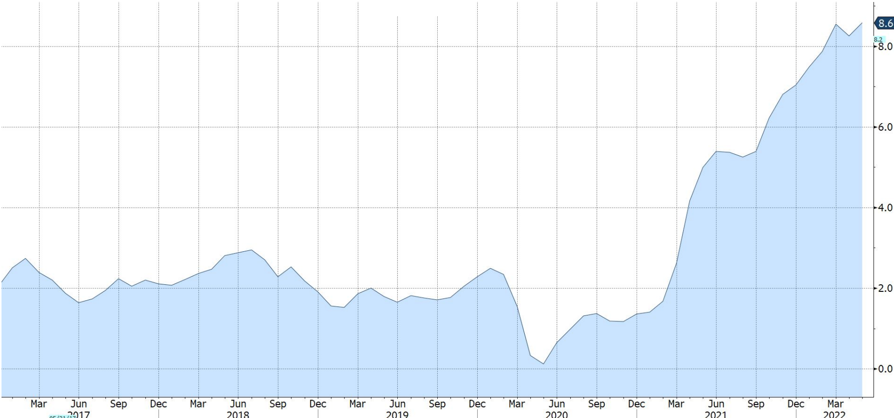


Source: FactSet

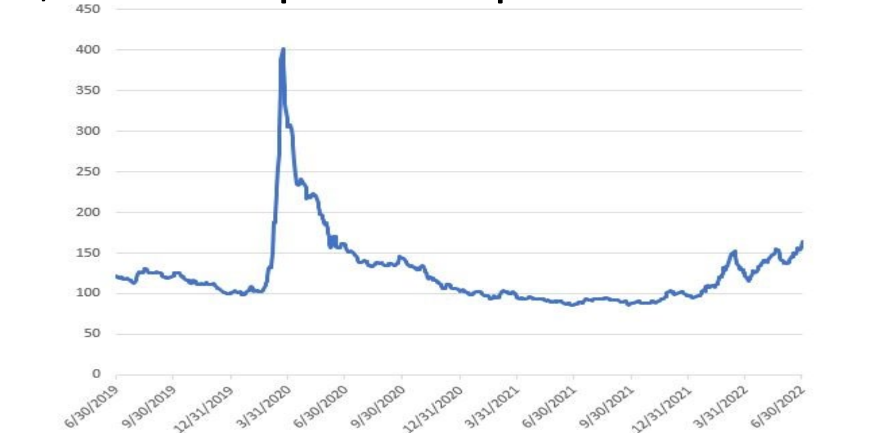
Fixed Income Market

- For much of the 2nd quarter, both the Federal Reserve and the bond market attempted to catch up to the trend of persistent inflation. Following up on a 25bps increase of the Fed Funds Rate in March, the Federal Reserve raised by another 50bps in May. After a CPI print of 8.6% (See Graph 2) in early June, the Federal Reserve felt the need to become more aggressive and raised the Fed Funds Rate by an additional 75bps in June.
- Similar to the 1st quarter of 2022, the bond market exhibited a large negative return. The Bloomberg Aggregate index was down -4.7%, bringing the YTD return to -10.35%. This marks the worst start of the year in the history of the bond index.
- Due primarily to the rate hikes and high level of inflation, the reaction from the Treasury market was an increase in yields across the entire curve. The 5-Year Treasury was up 58bps while the 30-Year was up 74bps.
- With economic concerns continuing to weigh on markets and a risk-off mentality taking hold, corporate bond spreads widened out by 44bps for the quarter. At the current level of 164bps over equivalent U.S. Treasuries (See Graph 3), the spread is now the highest since June 2020.
- After an historic move in the bond market over the first half of the year, the outlook for the second half will depend on the path of inflation and the economy. The Federal Reserve has amplified their actions in combatting inflation but doing so provides a narrower path to succeeding while not upending the economy.
- The era of quantitative easing appears to be over and with that has come a period of sustained volatility in the bond market. We believe that the importance of risk management and owning high quality assets is more paramount than ever as we navigate the future uncertainty.

Graph 2 **CPI**



Graph 3 **Corporate Bond Spreads**



Interest Rate Summary					*Table 2*
	6/30/2022	**3/31/2021**	**6/30/2021**	**Quarter Change**	**12-month Change**
3 Month T-Bills	0.9	0.5	0.0	0.4	0.9
5 Yr Treasury	3.0	2.3	0.9	0.8	2.1
10 Yr Treasury	3.0	2.3	1.5	0.7	1.5
30 Yr Treasury	3.2	2.5	2.1	0.7	1.1
5 Yr Corporate (A)	4.0	3.0	1.2	1.0	2.8
10 Yr Corporate (A)	4.4	3.4	2.1	1.0	2.3
30 Yr Fixed Rate Mortgage	5.8	4.9	3.1	0.9	2.7

Source: Bloomberg (Graph 2, 3 & Table 2)

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