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April 18, 2022

Dear Partners in Ministry,

Enclosed is the 2022 1st quarter statement for your account(s) at the United Methodist Foundation (statements from 7/1/17 are accessible online). Net of fees, the returns of the fund models are:

| As of 3/31/2022 | 1st Qtr 2022 | Year to Date | Last 1 Year† | Last 3 Years† | Last 5 Years† | Last 10 Years† |
|---|---|---|---|---|---|---|
| **Aggressive Fund** | **-5.92%** | **-5.92%** | **6.24%** | **13.51%** | **11.60%** | **8.92%** |
| Agg. Climate | -6.50% | -6.50% | 5.13% | n/a | n/a | n/a |
| benchmark* | -5.51% | -5.51% | 5.14% | 12.83% | 11.23% | 9.37% |
| | | | | | | |
| **Moderate Fund** | **-5.23%** | **-5.23%** | **3.20%** | **9.93%** | **8.73%** | **6.73%** |
| Mod. Climate | -5.34% | -5.34% | 2.66% | 8.24% | n/a | n/a |
| benchmark* | -5.03% | -5.03% | 2.57% | 9.57% | 8.68% | 7.37% |
| | | | | | | |
| **Conservative Fund** | **-4.62%** | **-4.62%** | **-0.30%** | **5.75%** | **5.41%** | **4.61%** |
| Con. Climate | -4.51% | -4.51% | -0.13% | n/a | n/a | n/a |
| benchmark* | -4.61% | -4.61% | -0.34% | 5.83% | 5.75% | 5.16% |

*"Benchmark" is a blend of benchmarks for the fund's underlying portfolios of stocks and fixed income, relative to the portfolio allocations within the fund's model. †Rates of return (1+ years) are annualized. See the monthly performance reports online: https://umfnic.org/investment-performance-reports/

## Market Commentary from Envestnet | PMC

Brandon Thomas, Co-Founder and Chief Investment Officer, Envestnet, concluded their "Economic and Market Overview: First Quarter 2022" report with the following observations and commentary:

> "The global economy has started to slow after reaching near peak growth in the latter part of 2021 on the backs of historical levels of fiscal stimulus and a strong rebound in China. After a strong fourth quarter of 2021, economic activity has begun to slow more than expected early in 2022 due to rapidly accelerating inflation emanating from goods shortages due to supply chain bottlenecks, as well as a continued jump in inflation driven in part by surging commodity prices brought on by the Russia-Ukraine war. Most of the world is in a better place economically than a year ago, but economists warn that results will be uneven throughout 2022, as new variants of the virus may emerge, and the potential for rising interest rates to suppress growth. With rapidly accelerating inflation and central banks raising interest rates, economists are expressing more concern about the potential for stagflation entering the picture, particularly if central banks hike rates either too quickly, or too slowly. The yield curve is very near inversion, which often presages a recession, and the FOMC will need to walk a fine line to avert such a scenario."[1]

**"surging commodity prices brought on by the Russia-Ukraine war"**

According to the U.S. Energy Information Administration, the U.S. produced 18.61 million barrels of oil per day in 2020, Saudi Arabia produced 10.81 million barrels per day, and Russia 10.5. Respectively, the

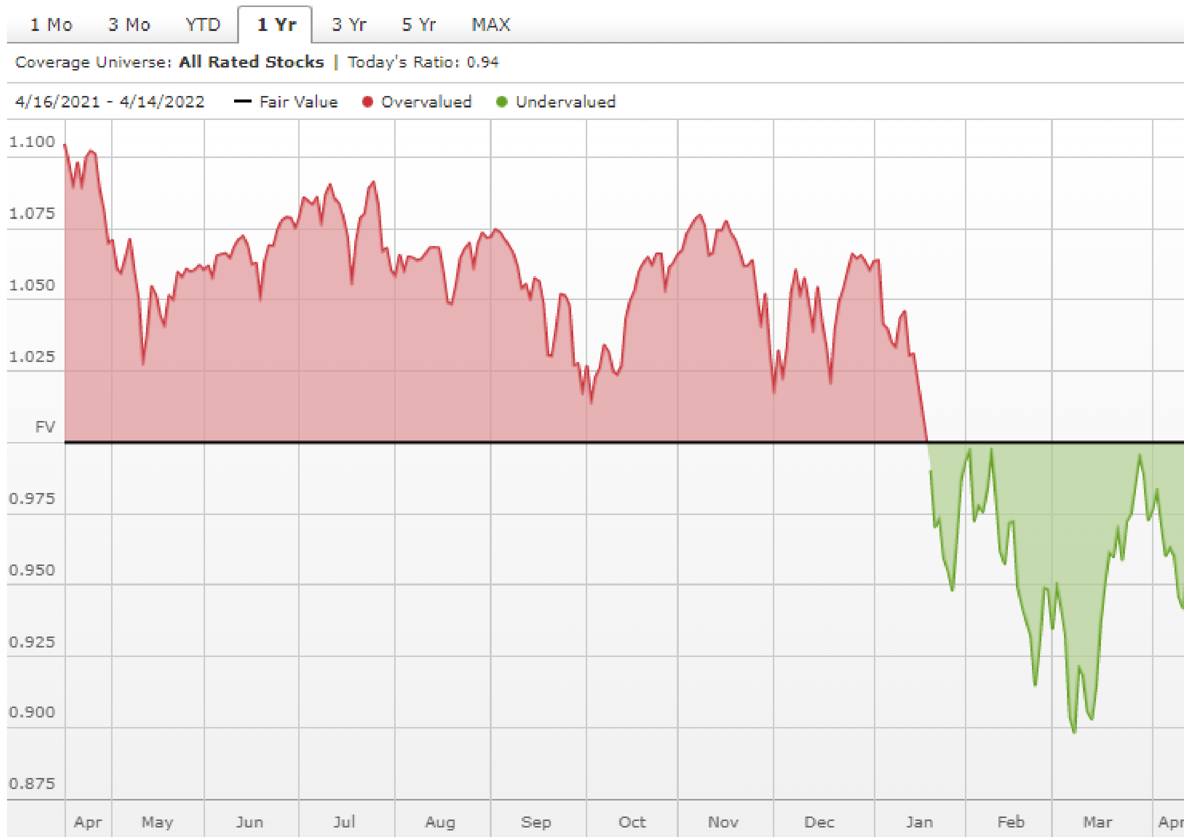
U.S. produced 20% of the world's oil production in 2020, Saudi Arabia 12%, and Russia 11%.[2] The U.S. produces about as much oil as it consumes, but the price of oil is set by worldwide market forces. Therefore, disruption to a major supplier like Russia has effects on commodity prices around the globe. Prices were already going up because production collapsed dramatically with the pandemic shutdown in 2020 and could not bounce back fast enough to keep up with increased demand from the swift economic rebound. And then Russia invaded Ukraine, leading to massive sanctions on Russia by the West.

There are lots of moving parts that have to come together to ramp up oil production. Even in normal, non-pandemic, and peaceful times, it takes about 6-8 months to drill a well and bring it online.[3] Elevated oil and natural gas prices are likely to stick around for a while.

There's an expression in the oil industry: "The cure for high oil prices is high oil prices." Higher prices make it more lucrative for upstream companies (exploration and production) to extract resources, and higher prices cause end users to use less product. The result, eventually, will be lower prices.

**"economists warn that results will be uneven throughout 2022"**

As I mentioned two quarters ago, the average price-to-earnings ratio of the S&P 500 for the previous 30 years was 25. Today the S&P 500's PE is 22, and that's based, arguably, on weaker earnings due to the pandemic. According to Morngingstar, the current prices of individual stocks they evaluate are trading collectively at a 6% discount to their collective fair value:



Source: Morningstar's "Market Fair Value"[4]

Brandon Thomas's commentary in the previous quarter that "2022 is likely to be more volatile than 2021" has proven true so far. There is a lot of uncertainty in the markets now, and that is the number one thing that markets do not like, uncertainty. We will do well to remind ourselves again that in times like these, uncertainty is temporarily impacting the market as a discounting mechanism.[5] So far in Q1 2022,

the vast majority of companies have reported earnings and/or revenues higher than expectations. As I write this, we're still early in earnings season, but so far, so good.

**"concern about the potential for stagflation"**

Mr. Thomas used the word "stagflation," a word we have not heard in a long time. Stagflation is "a period of inflation combined with a decline in the gross domestic product (GDP)."[6] High unemployment also characterizes stagflation. We currently have low unemployment. The Federal Reserve will have to expertly manage their rate increases to maintain, yet moderate, economic growth to get inflation under control. The Fed's mandate is to promote "maximum employment, stable prices, and moderate long-term interest rates."[7] I have heard some Fed observers opine the Fed is late to the game with their rate increases. At least one member of the Fed's Open Market Committee wanted a half-percentage point increase instead of the quarter-percentage point increase announced. The minutes of the March 15-16 meeting contained extensive comments on the war in Ukraine, which appears to have affected the thinking and the decision-making about rate increases.[8] Time will tell how their actions play out.

**"yield curve is very near inversion"**

The "yield curve" gets a lot of attention as an indicator of possible future recession because it has been so accurate in the past. The yield curve has flattened, yes, but as an indicator of possible recession the short-term rate (3-month Treasury yield) has to invert with the long-term rate (10-year Treasury yield) for a quarter or more, according to the person who created the indicator, Campbell Harvey, Professor of Finance at Duke University. The media often compares the 2-year with the 10-year. The yield curve has flattened but not inverted, according to Professor Harvey's research. Curious about the "yield curve?" Check out NPR's April 13, 2022, The Indicator from Planet Money, "Yield curve jitters."[9]

Be safe, be blessed, and enjoy Spring. It will finally arrive!

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[1] https://www.investpmc.com/sites/default/files/documents/PMC_QuarterlyMarketEnvironment.pdf
[2] https://www.eia.gov/tools/faqs/faq.php?id=709&t=6
[3] https://www.npr.org/2022/03/19/1086925726/gas-prices-oil-crude-drilling
[4] https://www.morningstar.com/market-fair-value
[5] https://www.investopedia.com/terms/d/discounting-mechanism.asp
[6] https://www.investopedia.com/terms/s/stagflation.asp
[7] https://www.federalreserve.gov/monetarypolicy/monetary-policy-what-are-its-goals-how-does-it-work.htm
[8] https://www.federalreserve.gov/monetarypolicy/fomcminutes20220316.htm
[9] https://www.npr.org/2022/04/13/1092678307/yield-curve-jitters

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