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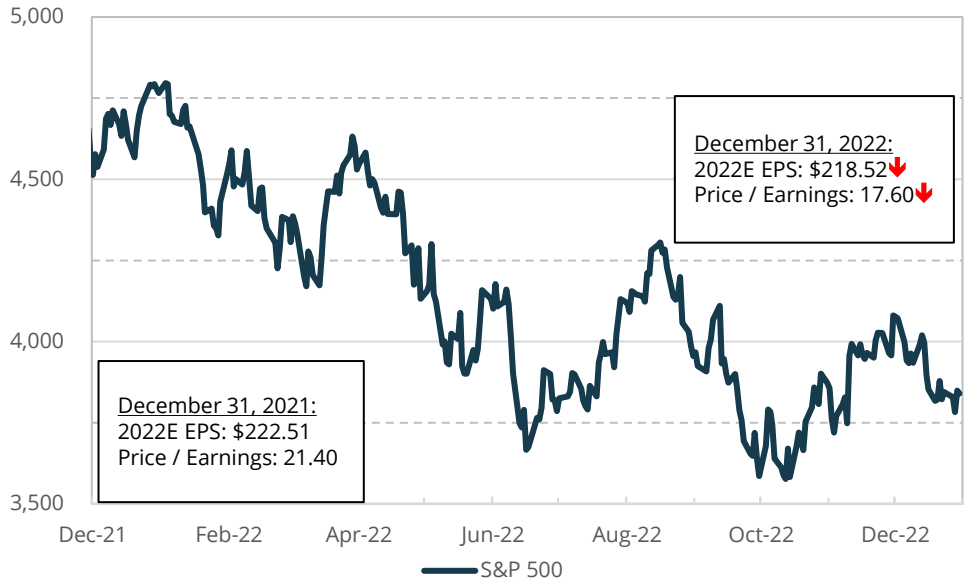
Market Overview
January 2023

Market Overview

2022 Market Recap

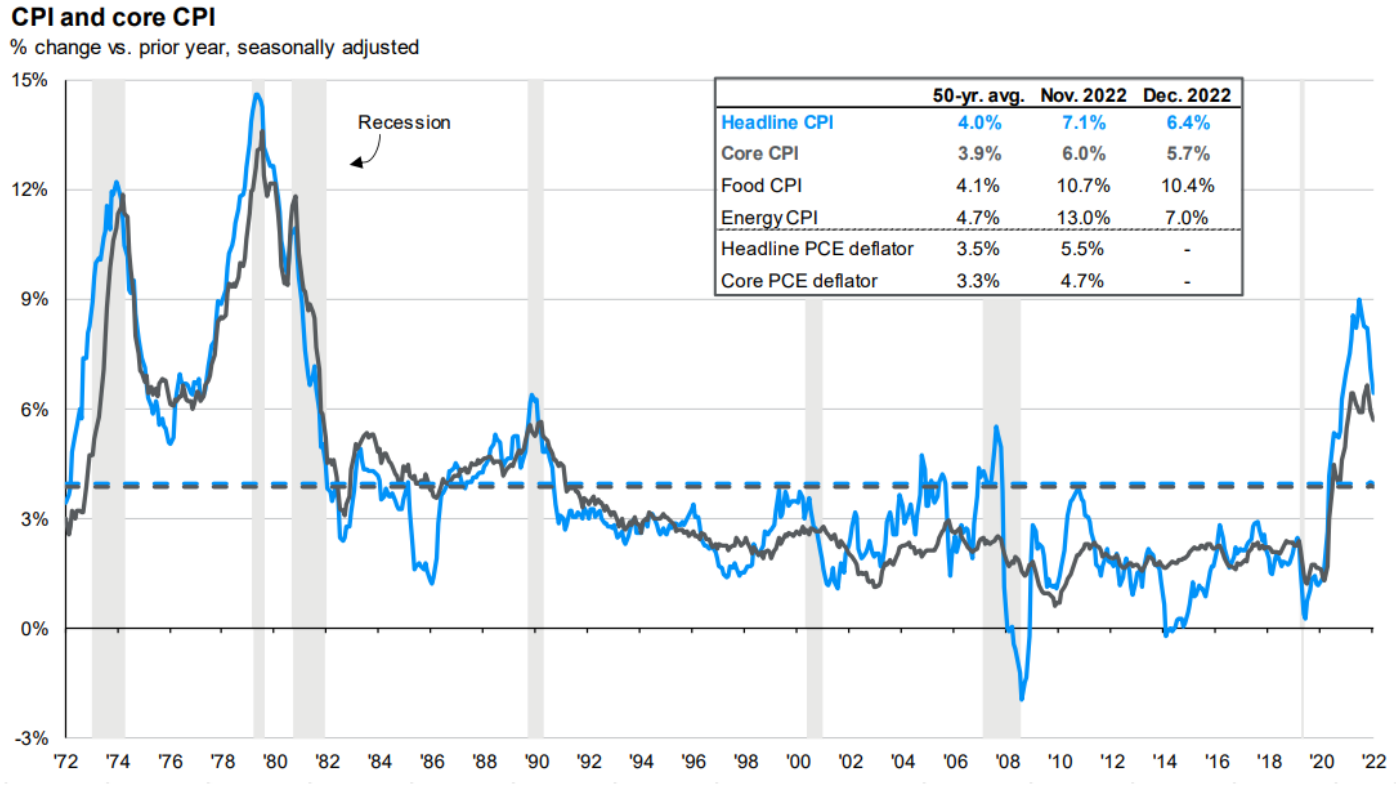
- **Sustainably high inflation had to be addressed after the Federal Reserve's late start**
  - Federal Reserve maintained loose monetary policy from the start of COVID-19 until early 2022, when the Fed acknowledged inflation was not 'transitory'
  - Consumer demand remained strong through 2021, driving prices higher (e.g. housing)
  - Labor, parts, transportation, and commodity shortages raised prices of goods including food, fuel, and vehicles
  - Responses to the Ukraine-Russia war restricted oil imports and squeezed energy prices even higher

- **The Federal Reserve implemented aggressively restrictive monetary policy**
  - FOMC raised the target federal funds rate 7 times in 2022 (4.25-4.5% at year end)
  - Both short- and long-term interest rates surged higher
  - The U.S. dollar appreciated in a flight to safety
  - "Don't Fight the Fed"
    - Higher rates, higher volatility led to lower stock valuations
    - The Fed signal of extreme "hawkishness" is inherently recessionary, and that signal is confirmed by an inverted yield curve



2022 Market Recap: Inflation

- CPI inflation remained well above average throughout 2022

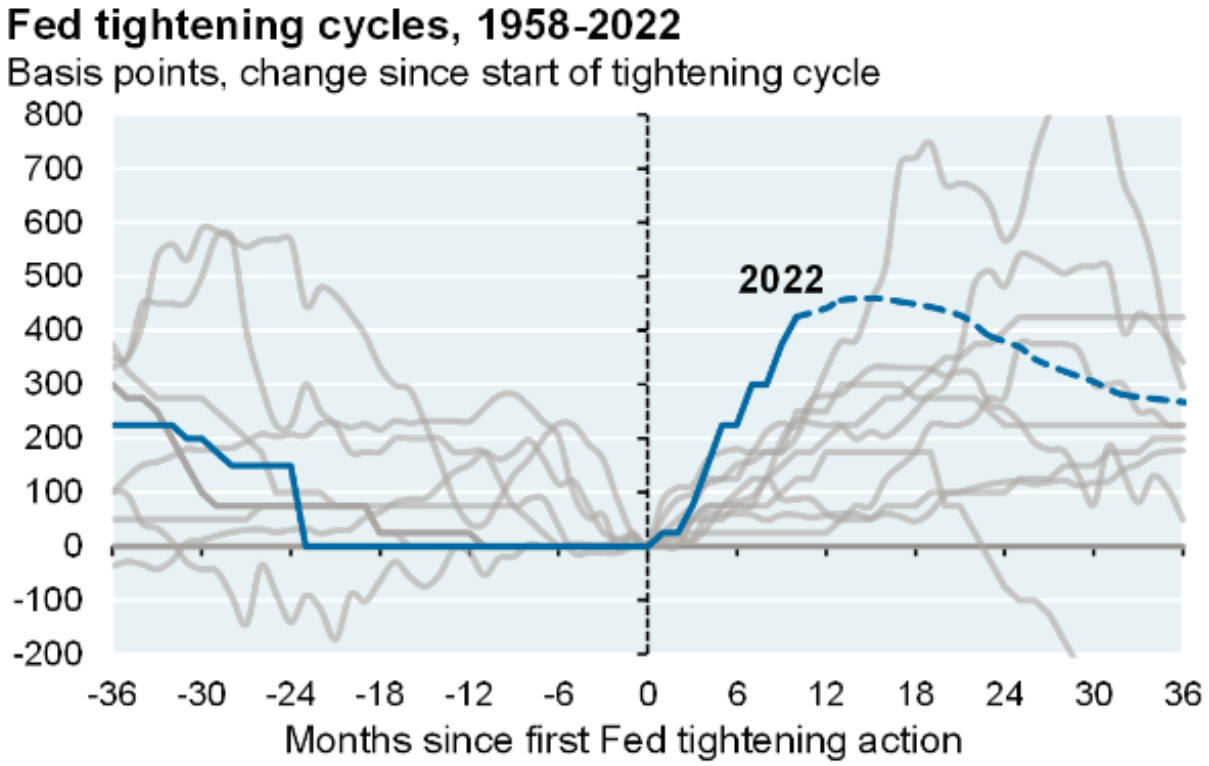


	50-yr. avg.	Nov. 2022	Dec. 2022
Headline CPI	4.0%	7.1%	6.4%
Core CPI	3.9%	6.0%	5.7%
Food CPI	4.1%	10.7%	10.4%
Energy CPI	4.7%	13.0%	7.0%
Headline PCE deflator	3.5%	5.5%	-
Core PCE deflator	3.3%	4.7%	-

Source: J.P. Morgan

2022 Market Recap: Federal Reserve

- The 2022 quantitative tightening effort was the fastest since 1958, with the federal funds rate increasing over 4% in less than one year



Source: Bloomberg, Factset, Fed, JPMAM. December 2022.

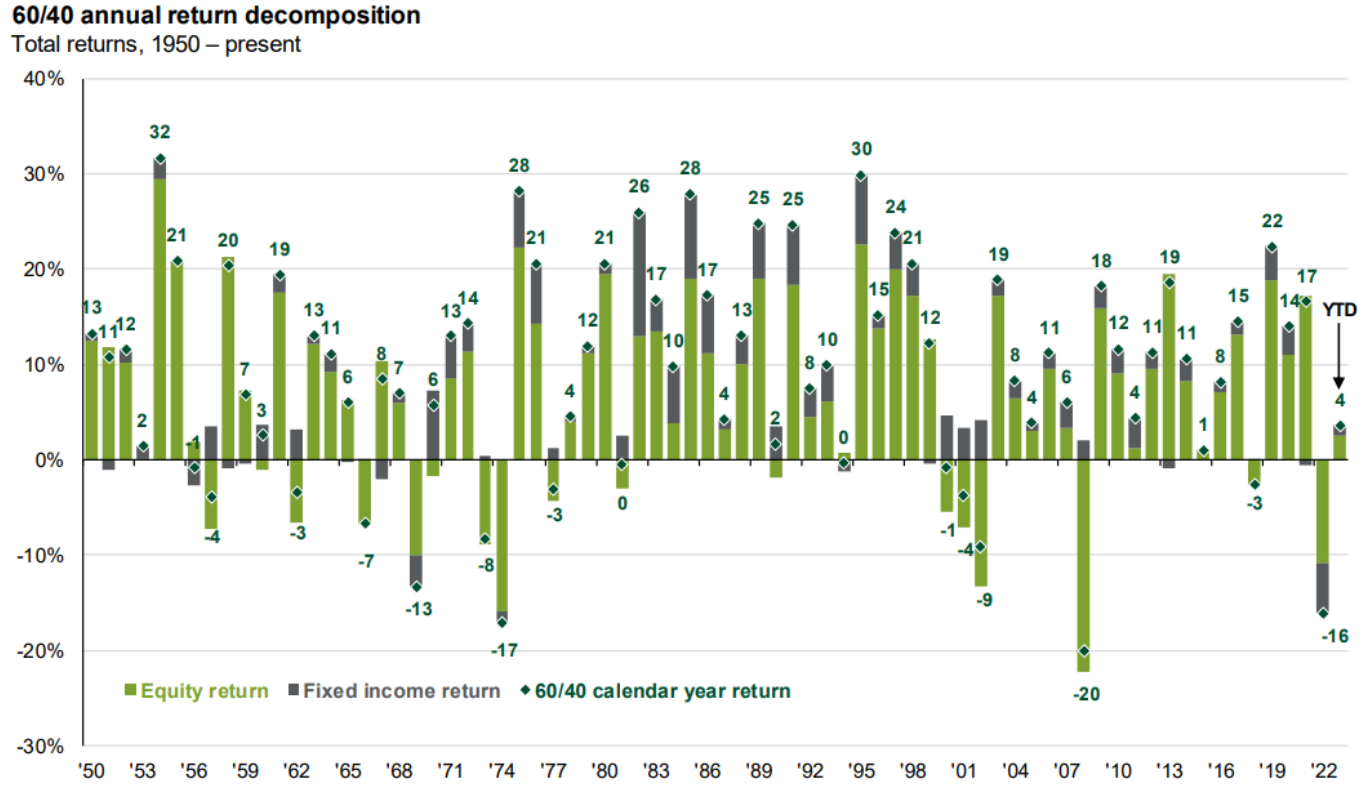
2022 Market Recap: Market Performance

- Equities
  - Speculative and growth stocks drove the declines
  - Nasdaq Composite returned -33.1%
  - Russell 2000 returned -21.6%
  - S&P 500 returned -19.4%
  - Energy & oil services stocks performed extremely well

- Fixed Income
  - Short-term rates surged in advance of the FOMC rate hikes
  - The yield curve was inverted, signaling monetary tightening and slower economic growth in the near term
  - Longer-term bonds did not provide diversification as a flight to safety
  - Fixed Income Aggregate Return Index returned -12%
  - Longer-dated bonds (30-year bonds) suffered major losses, down nearly -29%

2022 Market Recap: 60/40 Portfolio

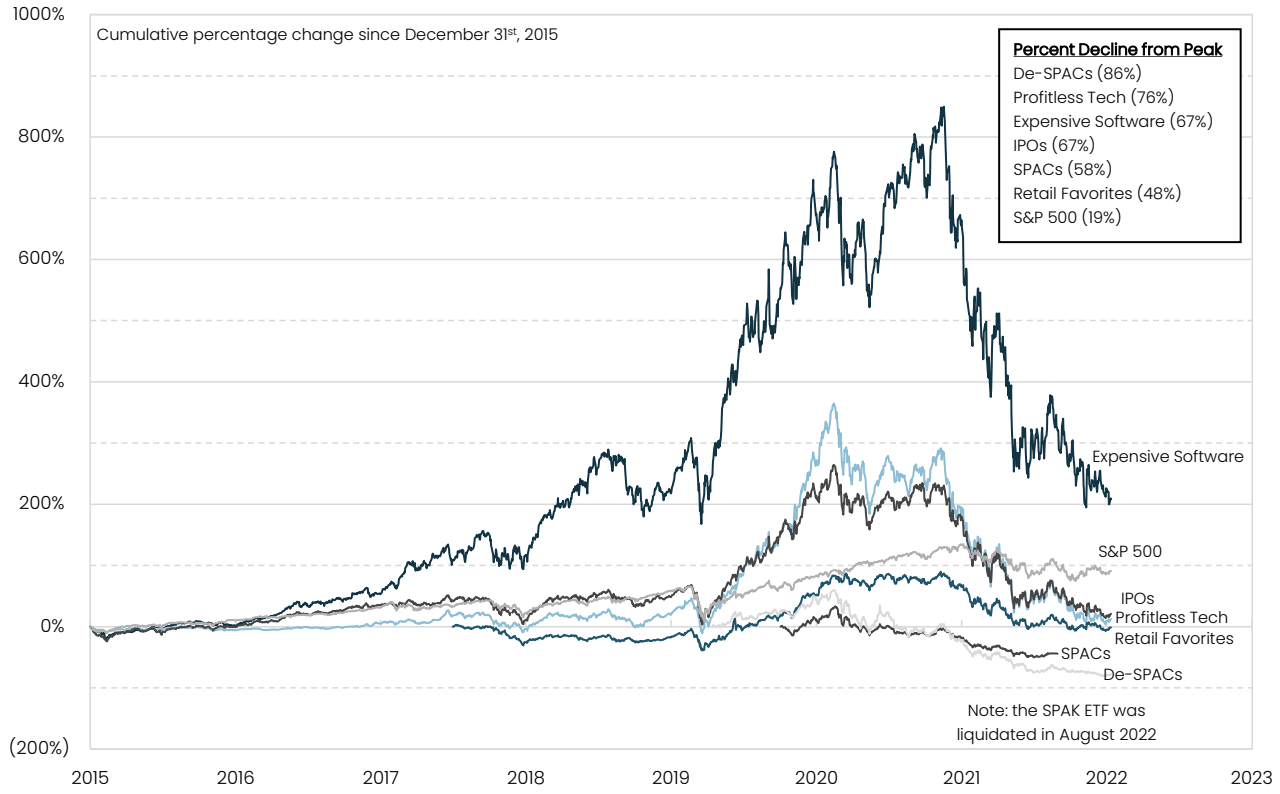
- 2022 was the third worst year over the past 72 years for a 60% equity, 40% fixed income benchmark portfolio
- 2022 fixed income had its worst year since 1950; driven by increased interest rates from historic lows



Source: FactSet, Standard & Poor's, Robert Shiller, Yale University, Bloomberg, Ibbotson/Strategas, J.P. Morgan Asset Management.

2022 Market Recap: Speculative Investments

- Many speculative investments are down significantly



Source: Bloomberg

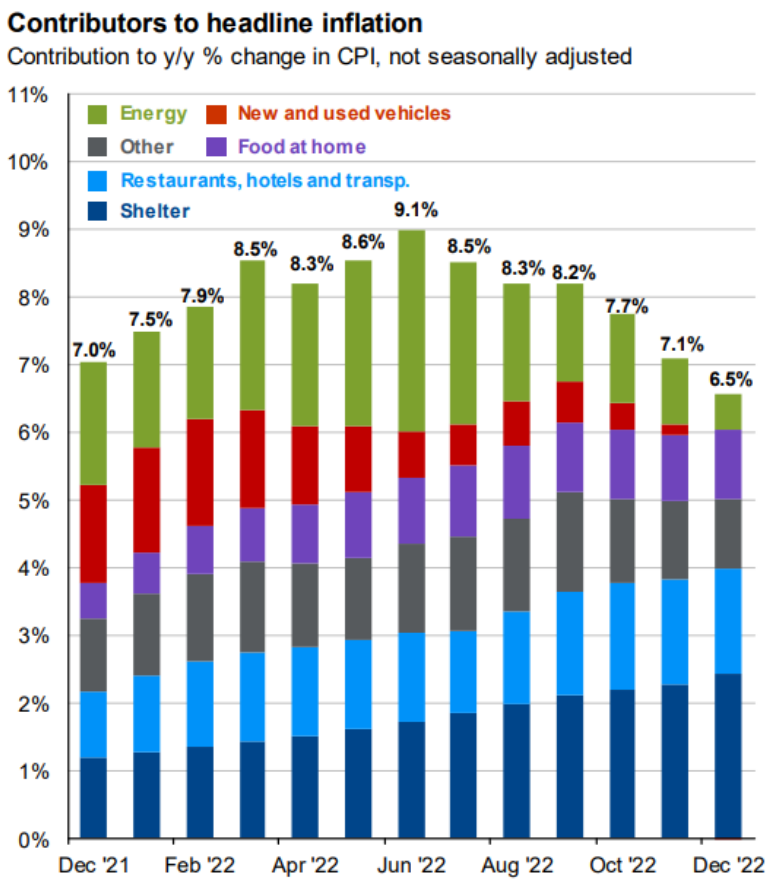
2023 Market Outlook

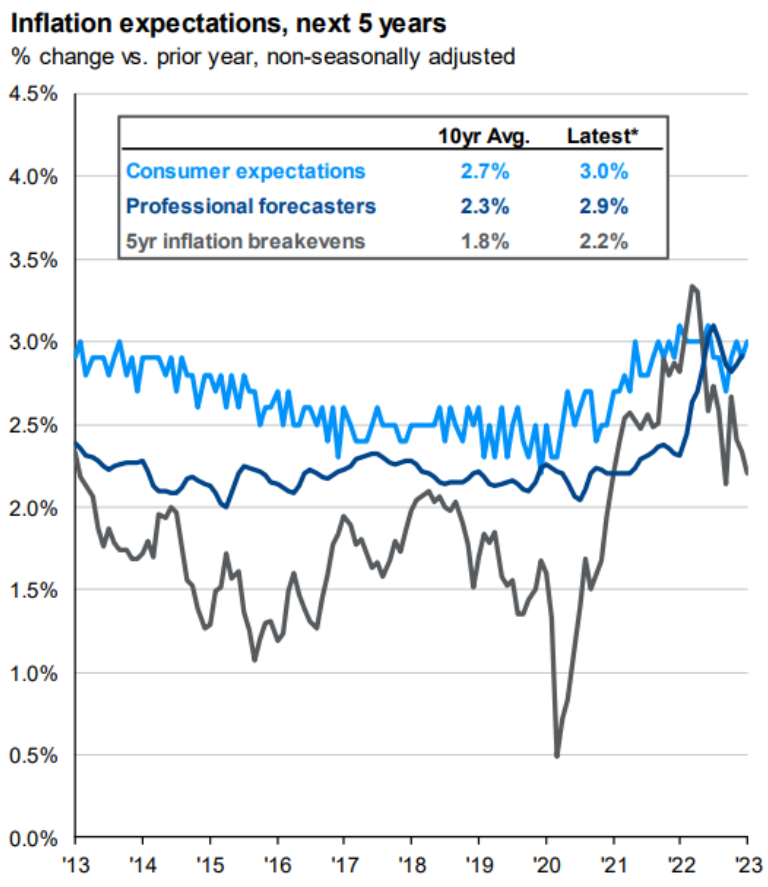
- U.S. Economic Consensus
  - Inflation likely peaked in 2022 near 9%. Inflation is still high, but moderating
  - Rate hikes will continue into 2023 at a moderated pace (e.g. several more 25bp hikes, a pause, then a likely rate lowering into 2024)
  - Economic growth expected to slow moderately in 2023; a recession remains one possible outcome
  - Unemployment will move moderately higher
  - Most signs point to earnings estimates that will likely move moderately lower in spring 2023 (S&P 500 estimates expected to move from $225 EPS towards $210-$215 EPS)

- Investment Consensus
  - Investors will likely favor quality companies with strong cash flows (maintaining a "risk off" posture)
  - Opportunity to be more aggressive as 2023 unfolds (e.g. global supply chains reopening in 2H23)

- ZIG Outlook
  - Stock valuations are reasonable, and consumer sentiment is extremely negative
  - The markets already reflect a great deal of negativity, so we should expect choppy fundamentals and volatile markets
  - There is value to be captured by owning equities for the long term, staying invested with an eye towards an improved 2024
  - Keep fixed income purchases shorter-term to avoid continued interest rate risk on long-duration assets

2023 Market Outlook: Inflation



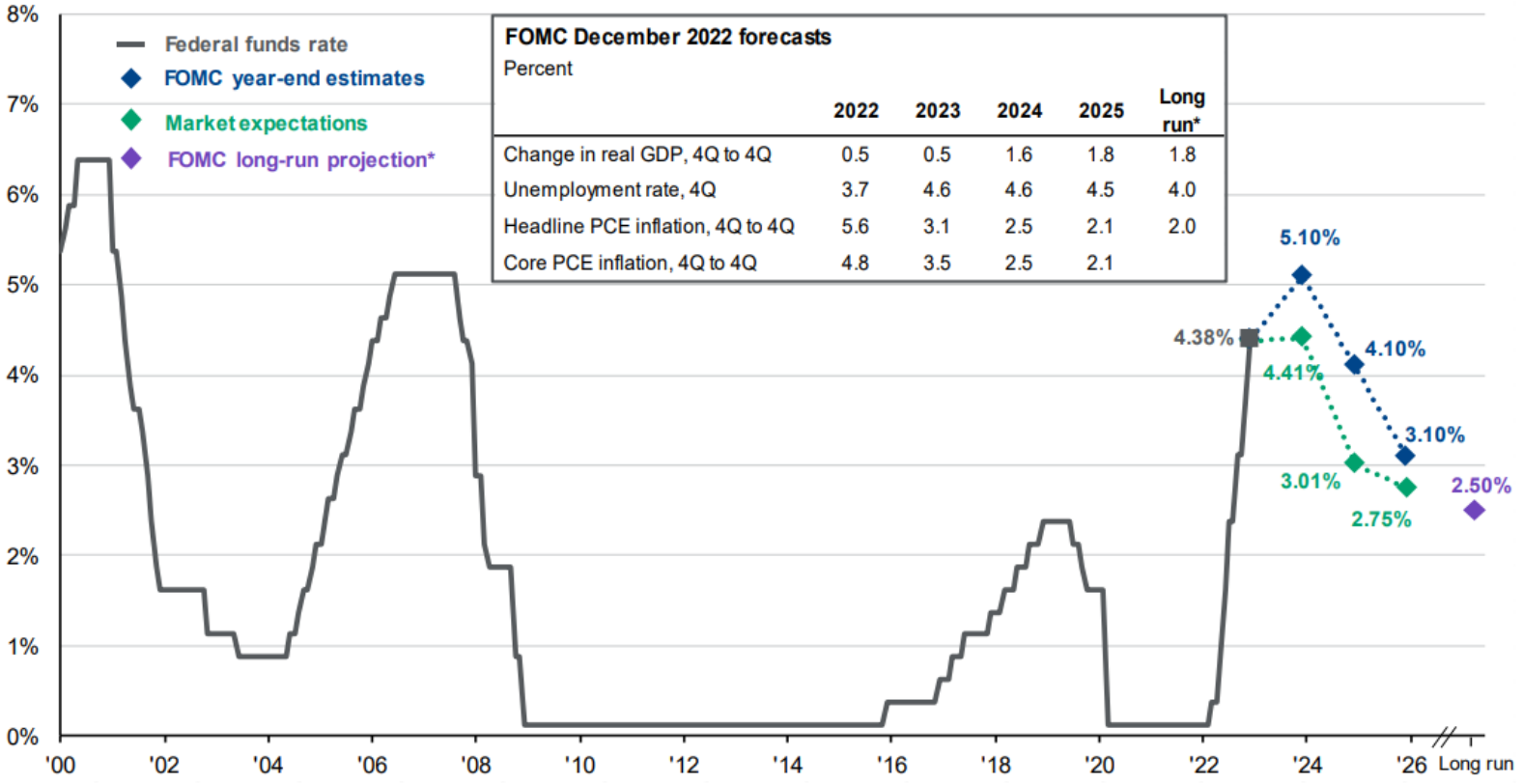


Source: J.P. Morgan

2023 Market Outlook: Federal Reserve

Federal funds rate expectations

FOMC and market expectations for the federal funds rate



FOMC December 2022 forecasts

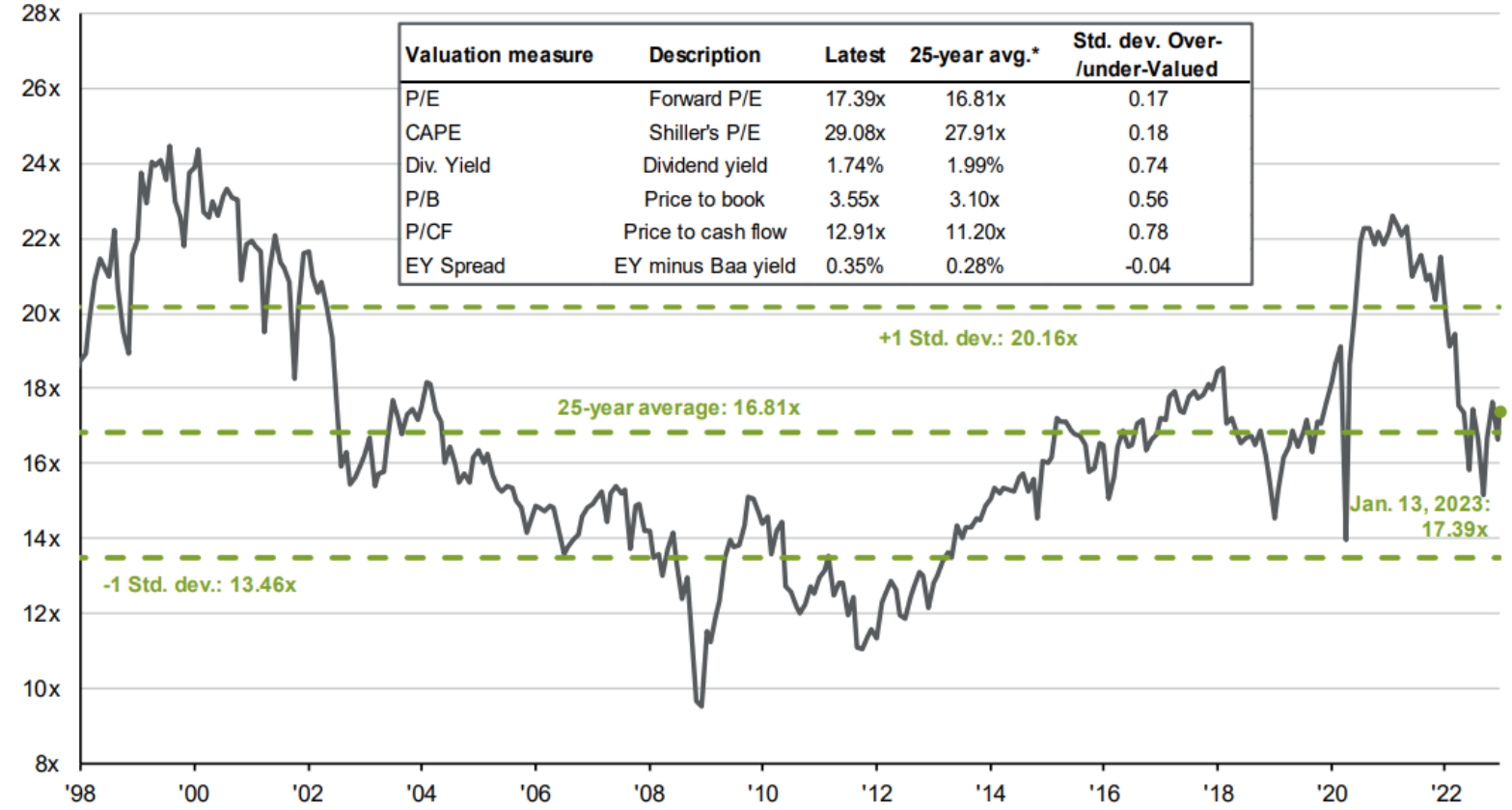
Percent

	2022	2023	2024	2025	Long run*
Change in real GDP, 4Q to 4Q	0.5	0.5	1.6	1.8	1.8
Unemployment rate, 4Q	3.7	4.6	4.6	4.5	4.0
Headline PCE inflation, 4Q to 4Q	5.6	3.1	2.5	2.1	2.0
Core PCE inflation, 4Q to 4Q	4.8	3.5	2.5	2.1	

Source: J.P. Morgan

2023 Market Outlook: Stock Valuation

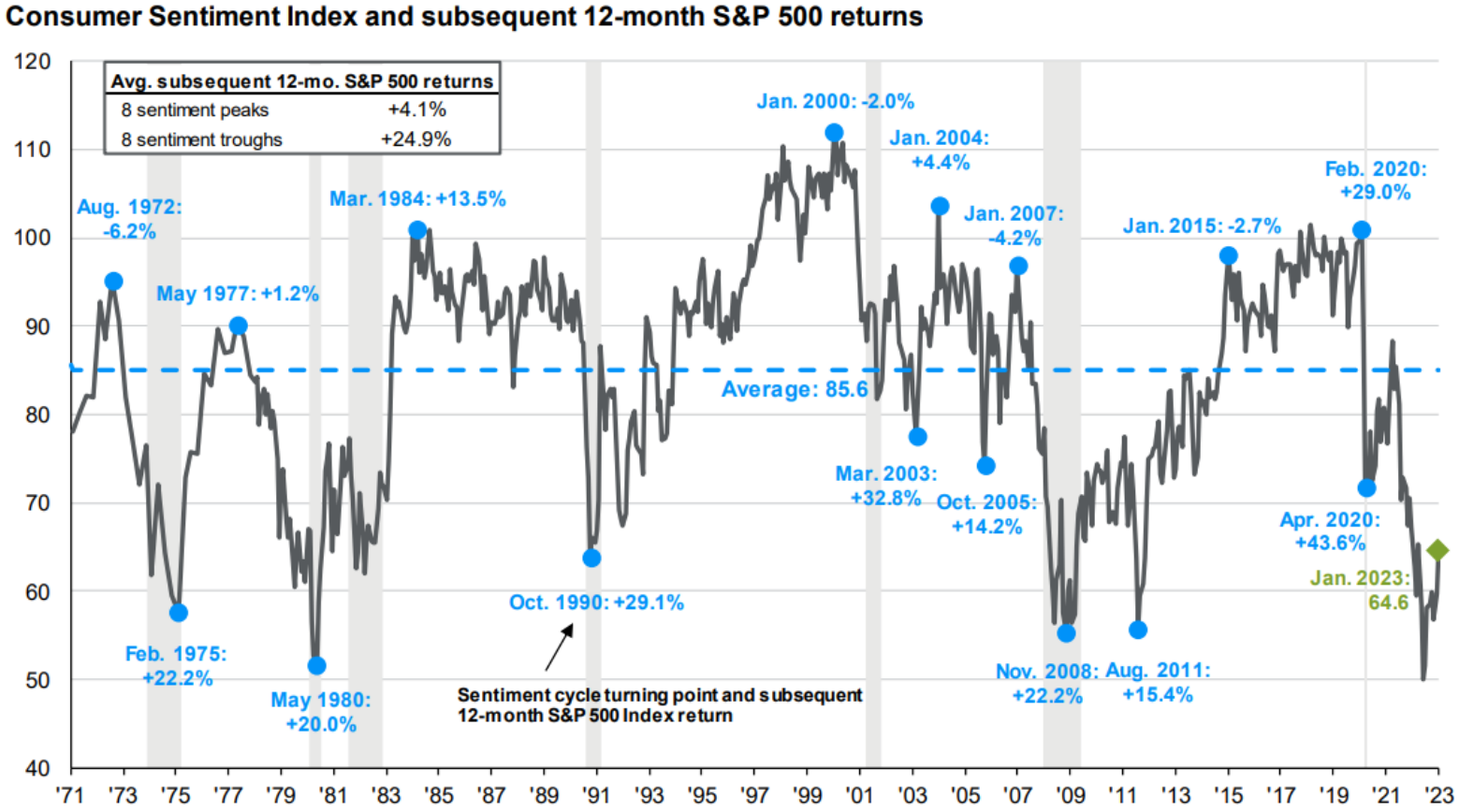
S&P 500 Index: Forward P/E ratio



Valuation measure	Description	Latest	25-year avg.*	Std. dev. Over-/under-Valued
P/E	Forward P/E	17.39x	16.81x	0.17
CAPE	Shiller's P/E	29.08x	27.91x	0.18
Div. Yield	Dividend yield	1.74%	1.99%	0.74
P/B	Price to book	3.55x	3.10x	0.56
P/CF	Price to cash flow	12.91x	11.20x	0.78
EY Spread	EY minus Baa yield	0.35%	0.28%	-0.04

Source: J.P. Morgan

2023 Market Outlook: Consumer Sentiment

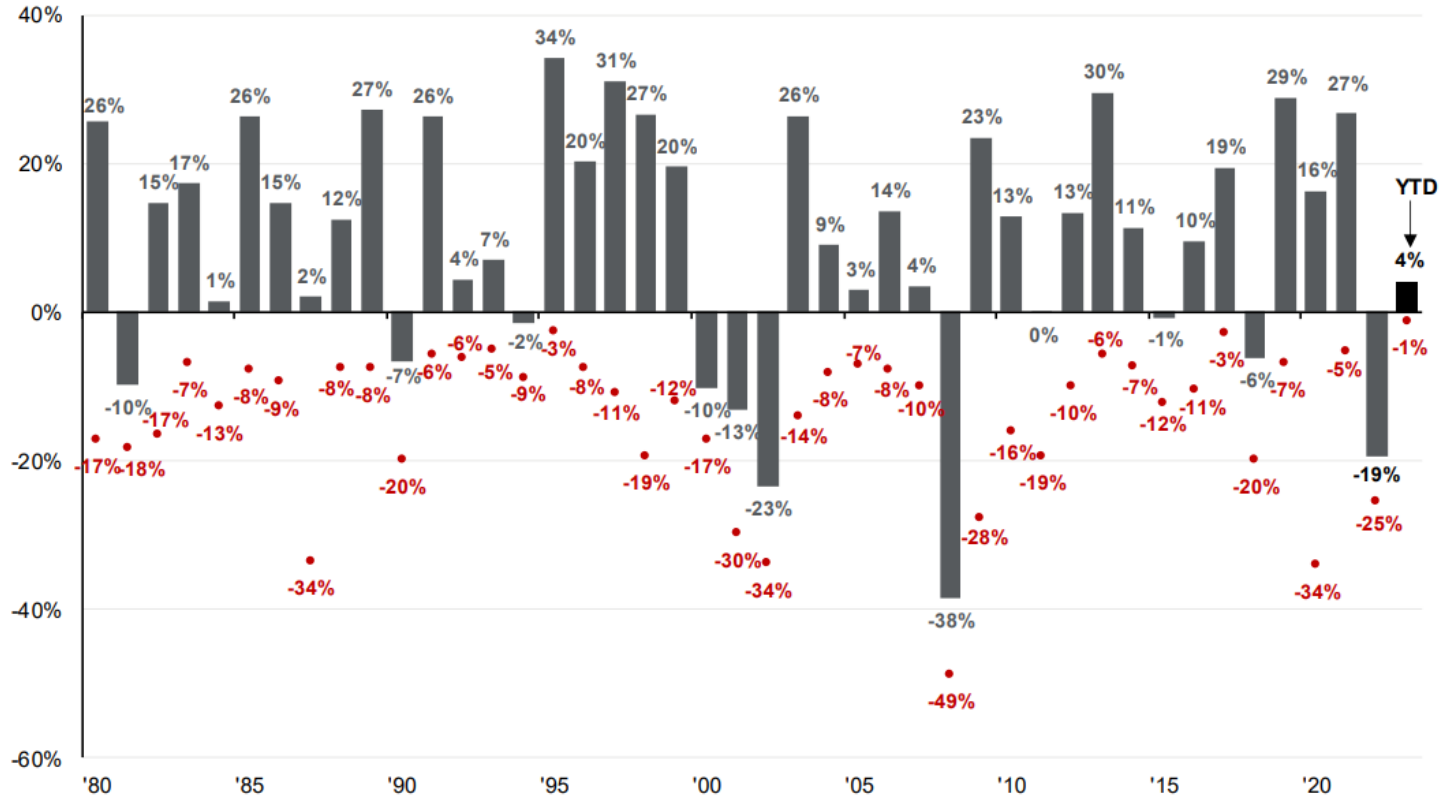


Source: J.P. Morgan

2023 Market Outlook: Staying Invested

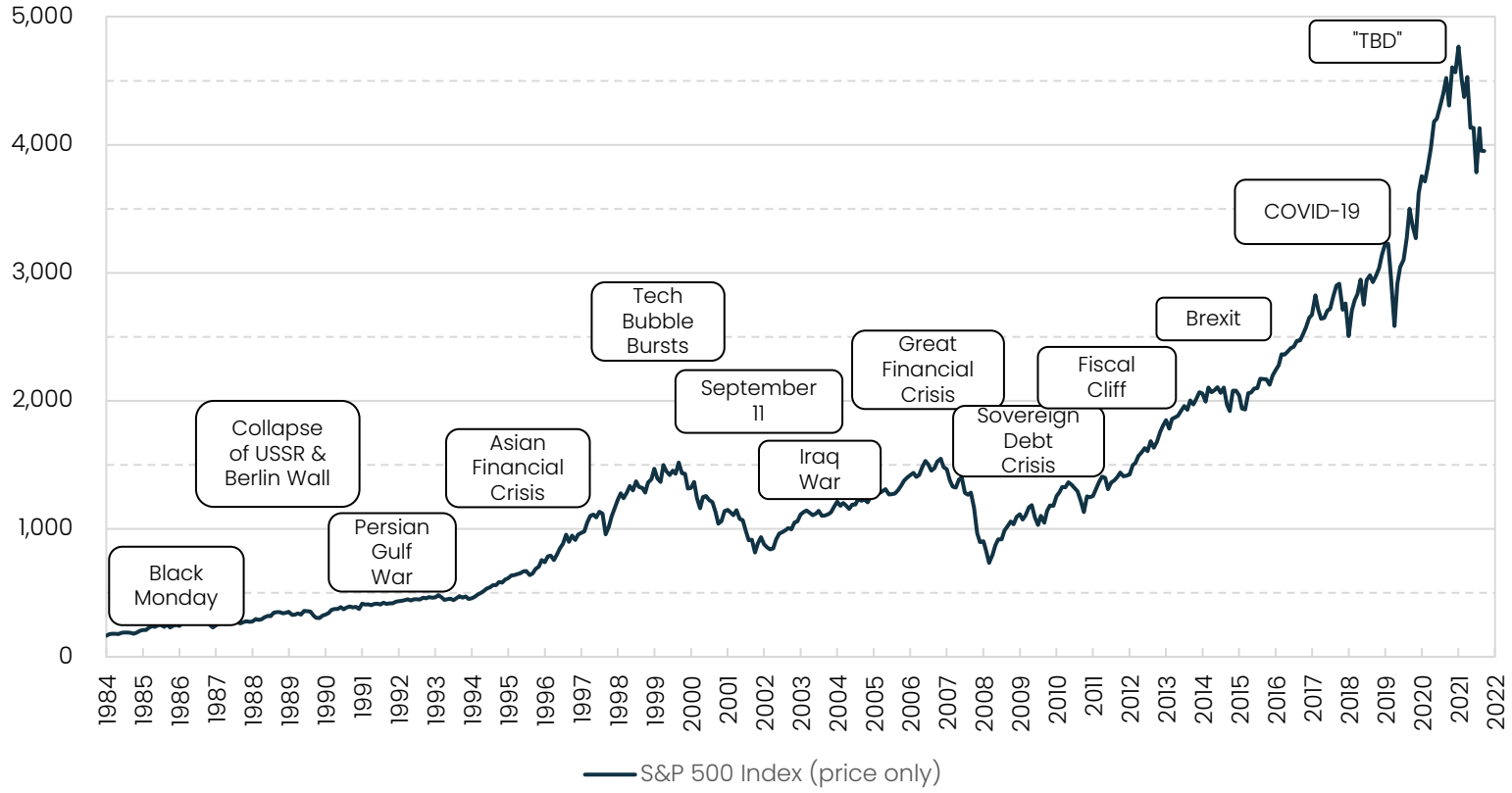
S&P intra-year declines vs. calendar year returns

Despite average intra-year drops of 14.3%, annual returns were positive in 32 of 43 years



Source: J.P. Morgan

2023 Market Outlook: Staying Invested



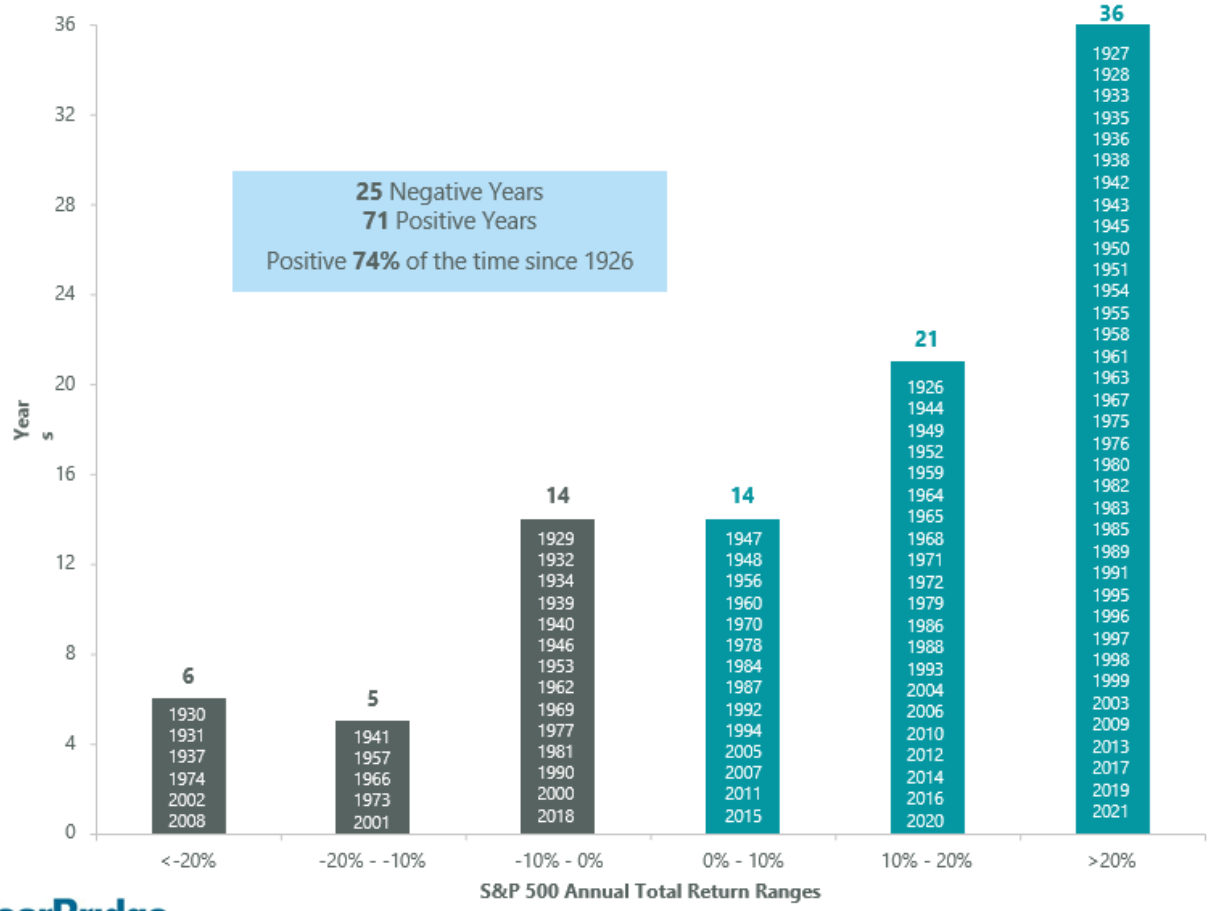
Staying invested in equities, through all the ups and downs, remains the best way to build long-term wealth.

Source: Fidelity, Bloomberg

2023 Market Outlook: Staying Invested

Market Annual Returns

Distribution of S&P 500 Total Returns Since 1926



ClearBridge Investments

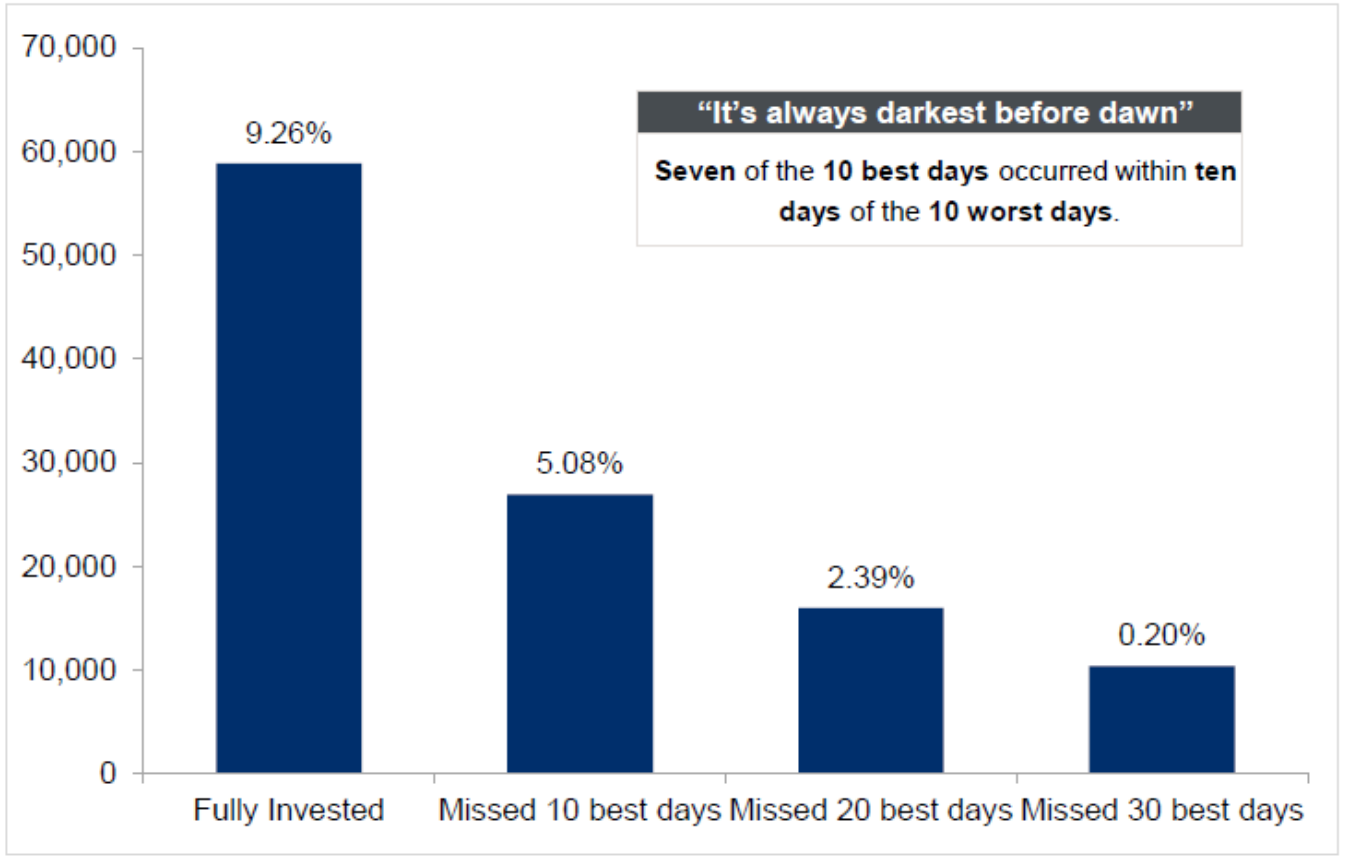
As of Dec. 31, 2021. Source: FactSet. Past performance is not a guarantee of future results. Investors cannot invest directly in an index, and unmanaged index returns do not reflect any fees, expenses or sales charges.

Appendix

2023 Market Outlook: Staying Invested

PERFORMANCE OF THE S&P 500

Annualized performance of a $10,000 investment between March 2002 and March 2022



Source: JP Morgan Asset Management

Market Overview: Staying Invested

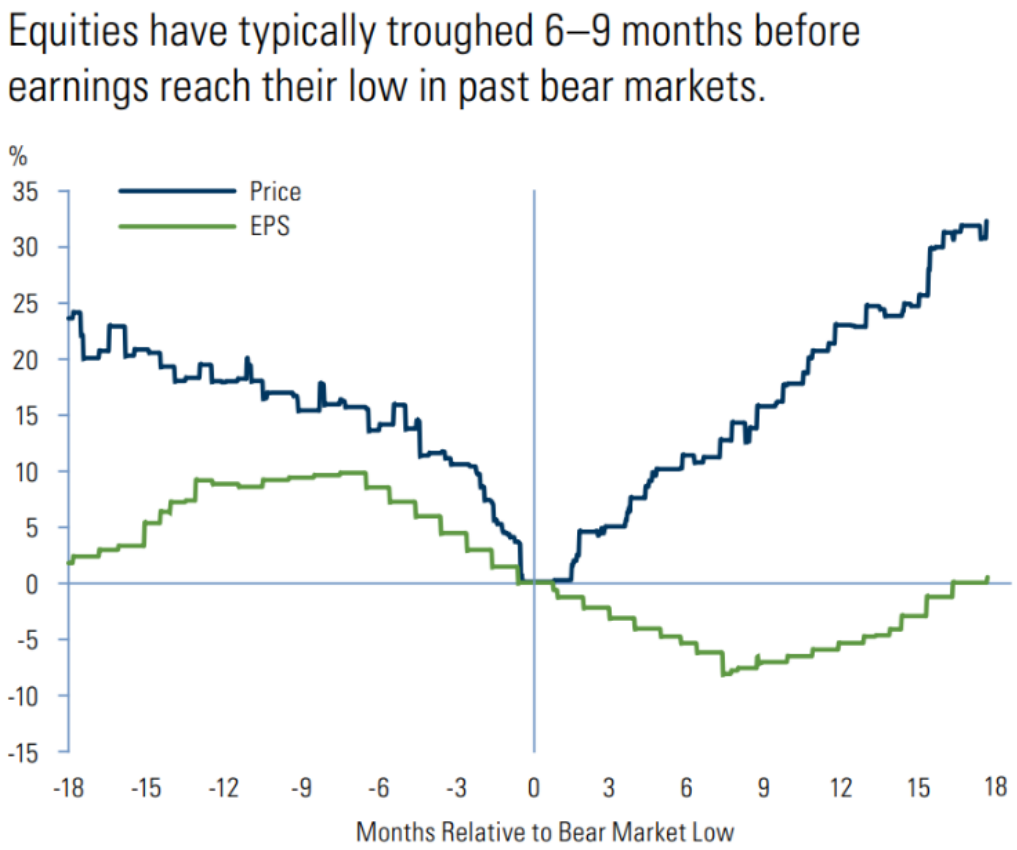
Rare Occurrence

Frequency of Observation of Positive / Negative Returns in US Stock and Bonds over Rolling 12-Month Periods Since 1926

BOND RETURNS \ STOCK RETURNS	NEGATIVE	POSITIVE
POSITIVE	23%	67%
NEGATIVE	2%	8%

Source: Goldman Sachs

Market Overview: Equity Trough



Source: J.P. Morgan

Market Overview: Speculative Investments

- Overvalued and unprofitable companies that made up large portions of Equity and Total US Market Cap have been heavily compressed.

What is priced in so far
Profitless innovation stocks have been decimated

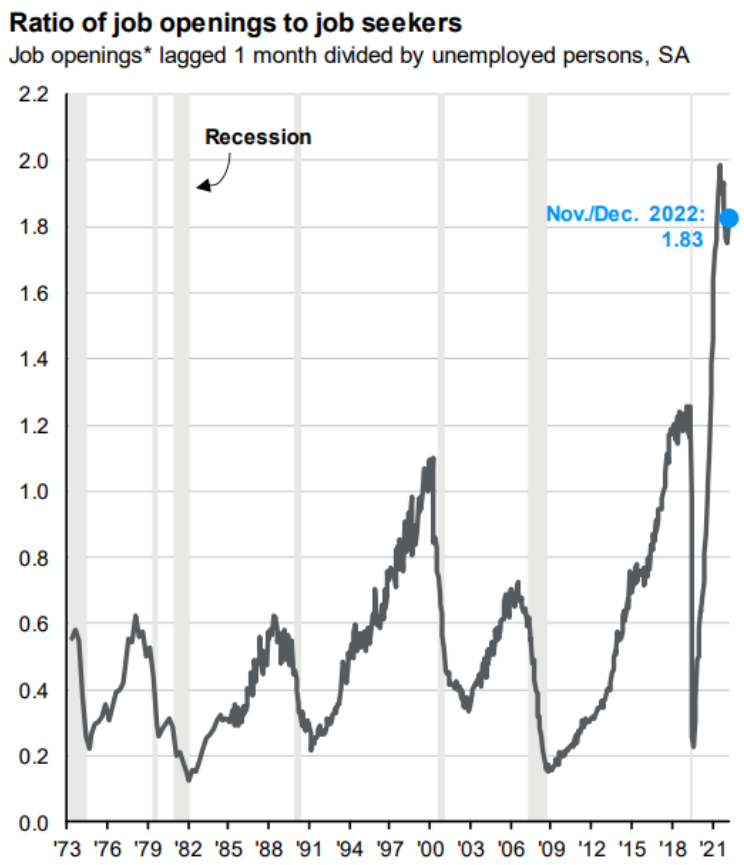
The YUCs: Young Unprofitable Companies
% of equity market capitalization

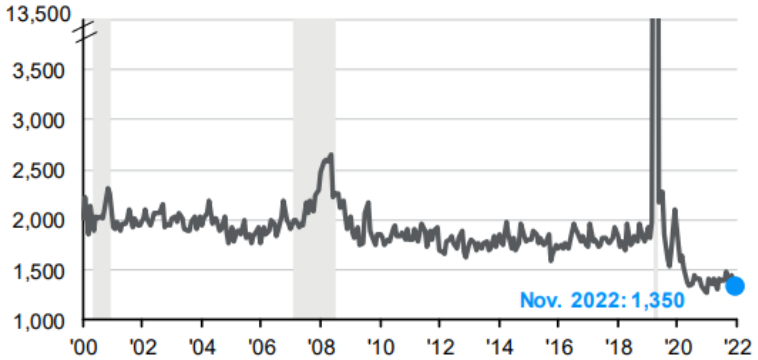
Source: Factset, JPMAM. December 27, 2022.

The MUCs: Megavalued (P/E >50x) or Unprofitable Companies, % of total US market capitalization

Source: Factset, JPMAM. December 27, 2022.

Market Overview: Labor Force

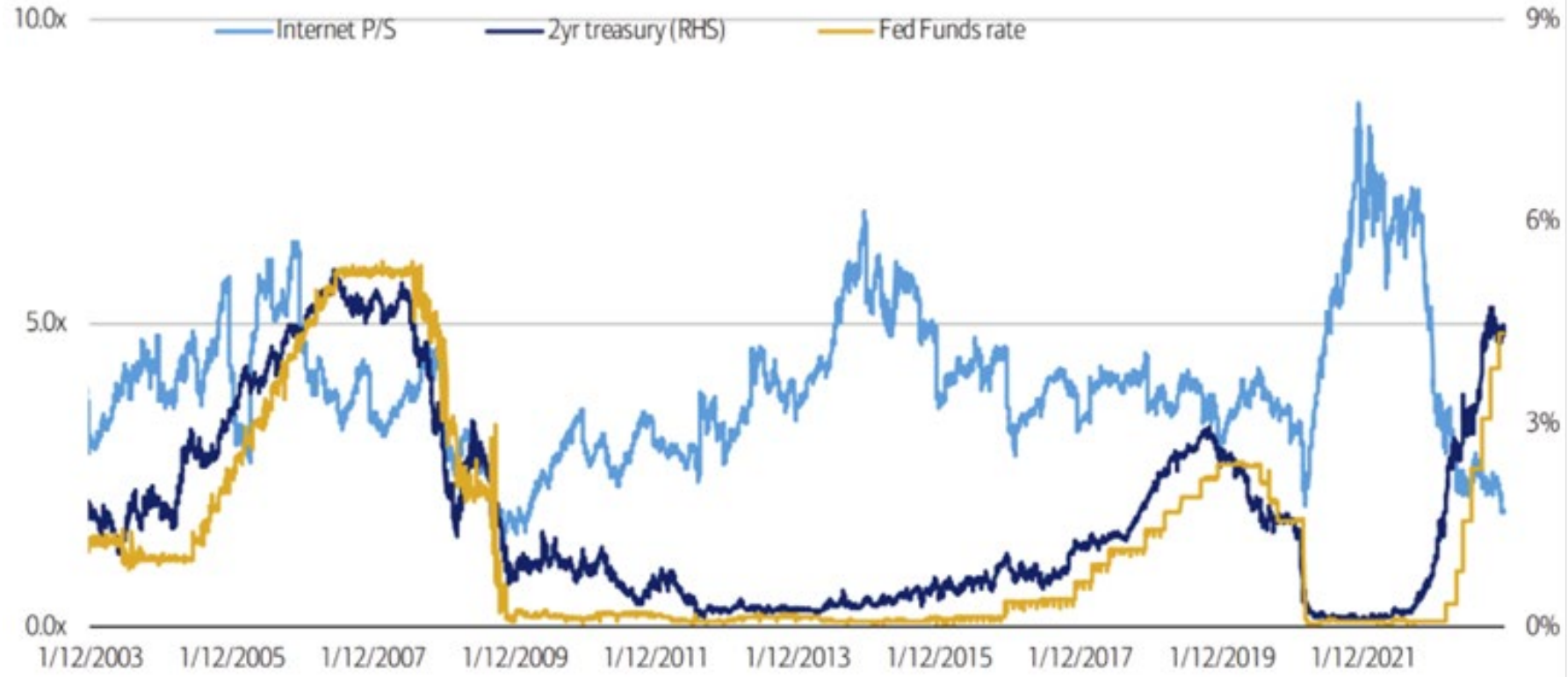




Source: J.P. Morgan

Market Overview: Internet P/S

Exhibit 10: Internet valuation vs. Fed Fund Rate and 2yr US treasury
A steep increase in short term rates has contributed to a significant decline in Internet valuations



Source: BofA Global Research, Bloomberg

Bear Market History

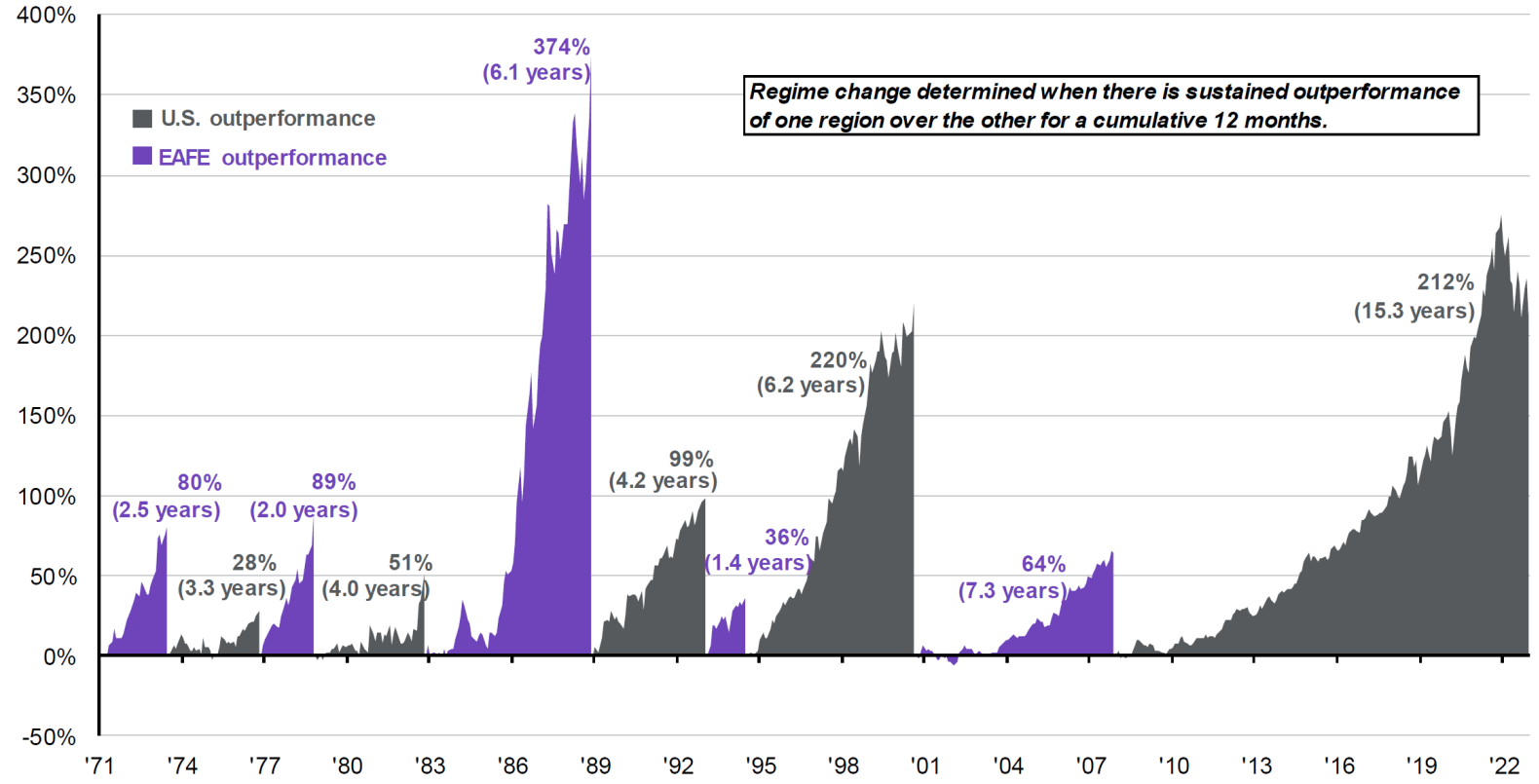
Starting Peak	Bear Market Low	Amount of Decline	Duration (Months)	Recession?	Return 1 Year after Low	Time to Regain Prior Peak (Months)
May-46	May-47	-28%	12	No	19%	37
Jun-48	Jun-49	-21%	12	Yes	42%	12
Aug-56	Oct-57	-22%	15	Yes	31%	11
Dec-61	Jun-62	-28%	6	No	33%	14
Feb-66	Oct-66	-22%	8	No	33%	7
Nov-68	May-70	-36%	18	Yes	44%	21
Jan-73	Oct-74	-48%	21	Yes	38%	69
Nov-80	Aug-82	-27%	20	Yes	58%	3
Aug-87	Dec-87	-34%	3	No	23%	20
Mar-00	Oct-02	-49%	31	Yes	34%	56
Oct-07	Mar-09	-57%	17	Yes	68%	49
Feb-20	Mar-20	-34%	1	Yes	75%	5
Average		**-34%**	**14**		**42%**	**25**
Median		**-31%**	**13**		**36%**	**17**

Source: ISI, Bloomberg, National Bureau of Economic Research, Haver Analytics, FMRCo (Asset Allocation Research Team).

Market Overview: International vs. U.S. Markets

MSCI EAFE and MSCI USA relative performance

U.S. dollar, total return, cumulative outperformance*

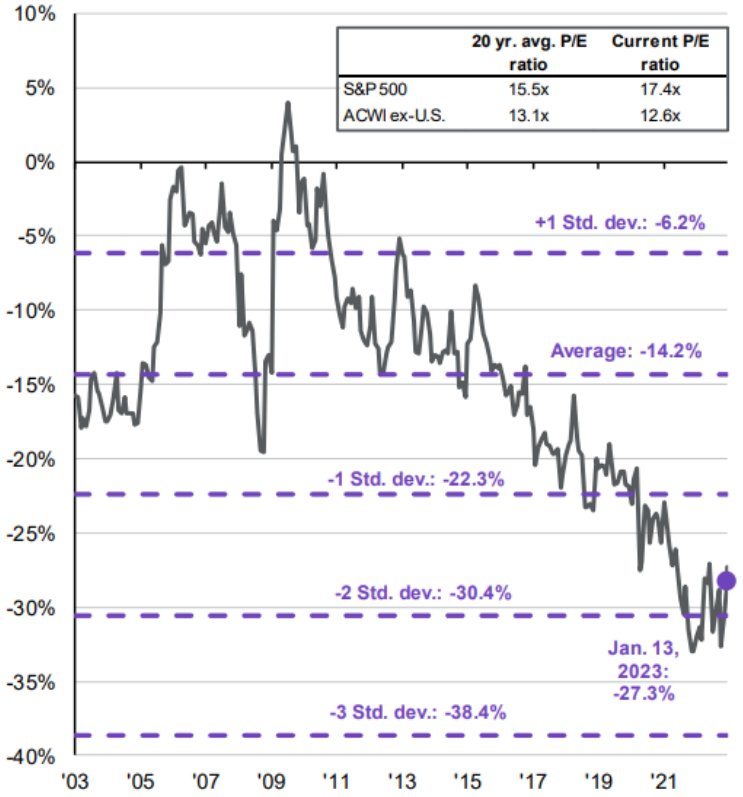


Source: FactSet, MSCI, J.P. Morgan

Market Overview: International vs. U.S. Markets

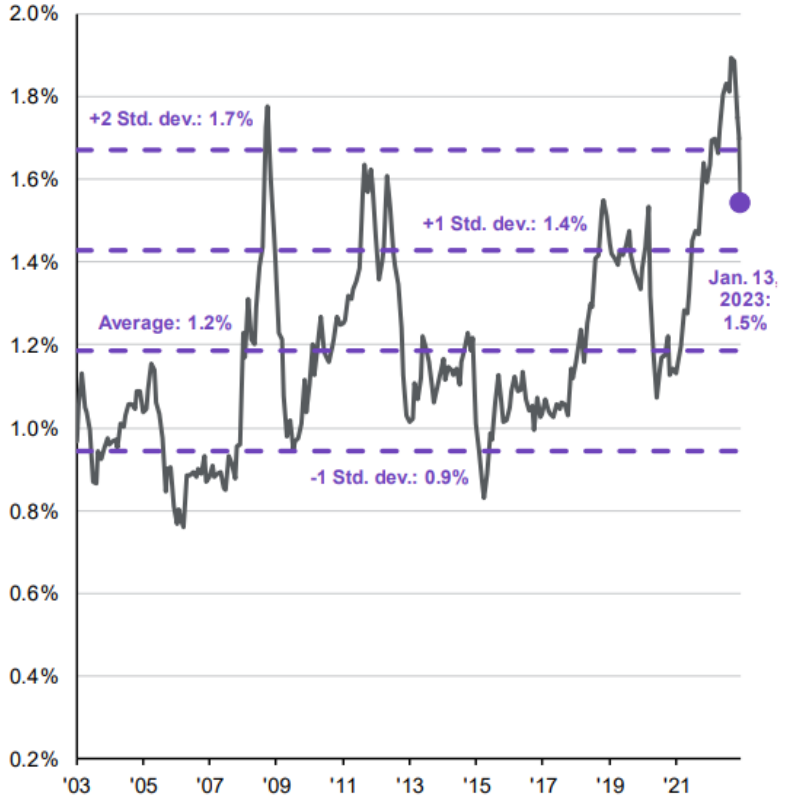
International: Price-to-earnings discount vs. U.S.

MSCI AC World ex-U.S. vs. S&P 500 Indices, next 12 months



International: Difference in dividend yields vs. U.S.

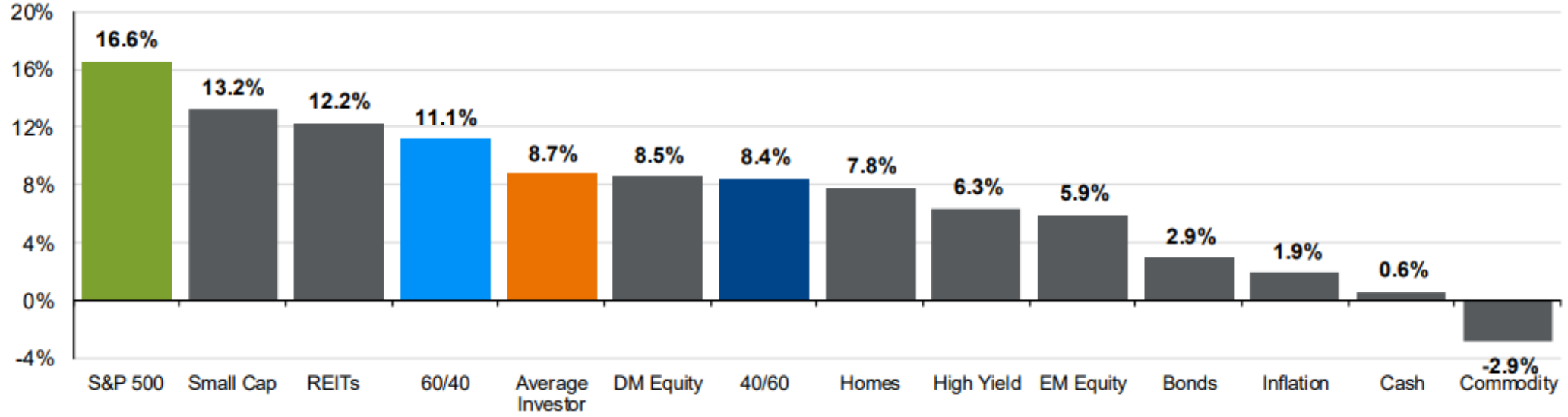
MSCI AC World ex-U.S. minus S&P 500 Indices, next 12 months



Source: FactSet, MSCI, Standard & Poor's, J.P. Morgan

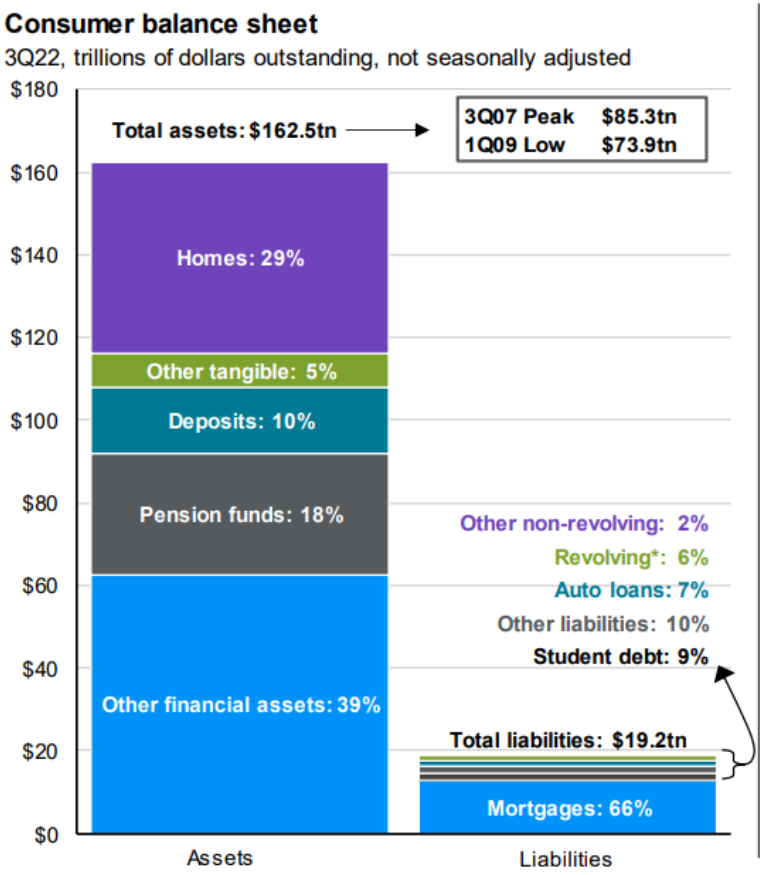
Market Overview: Returns by Asset Class

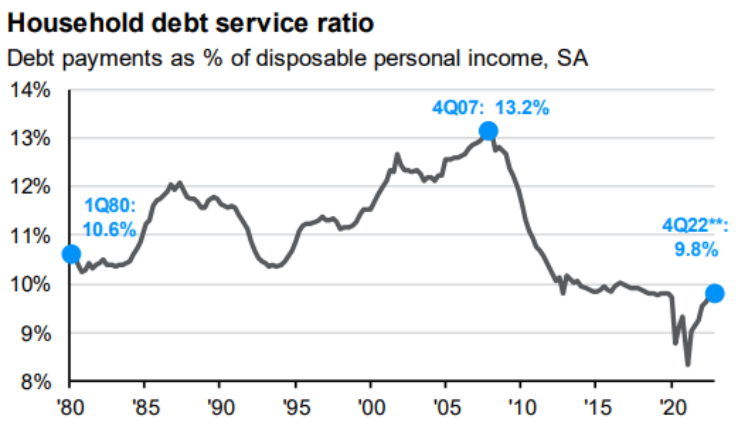
10-year annualized returns by asset class (2012 – 2021)

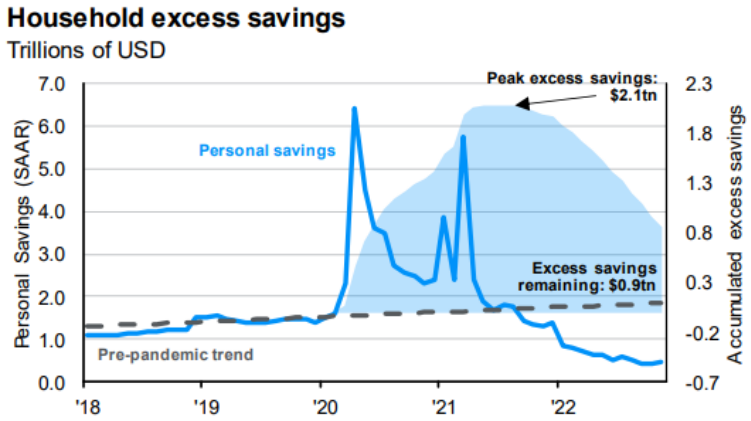


Source: Bloomberg, FactSet, Standard & Poor's, J.P. Morgan

Market Overview: Consumer Balance Sheet



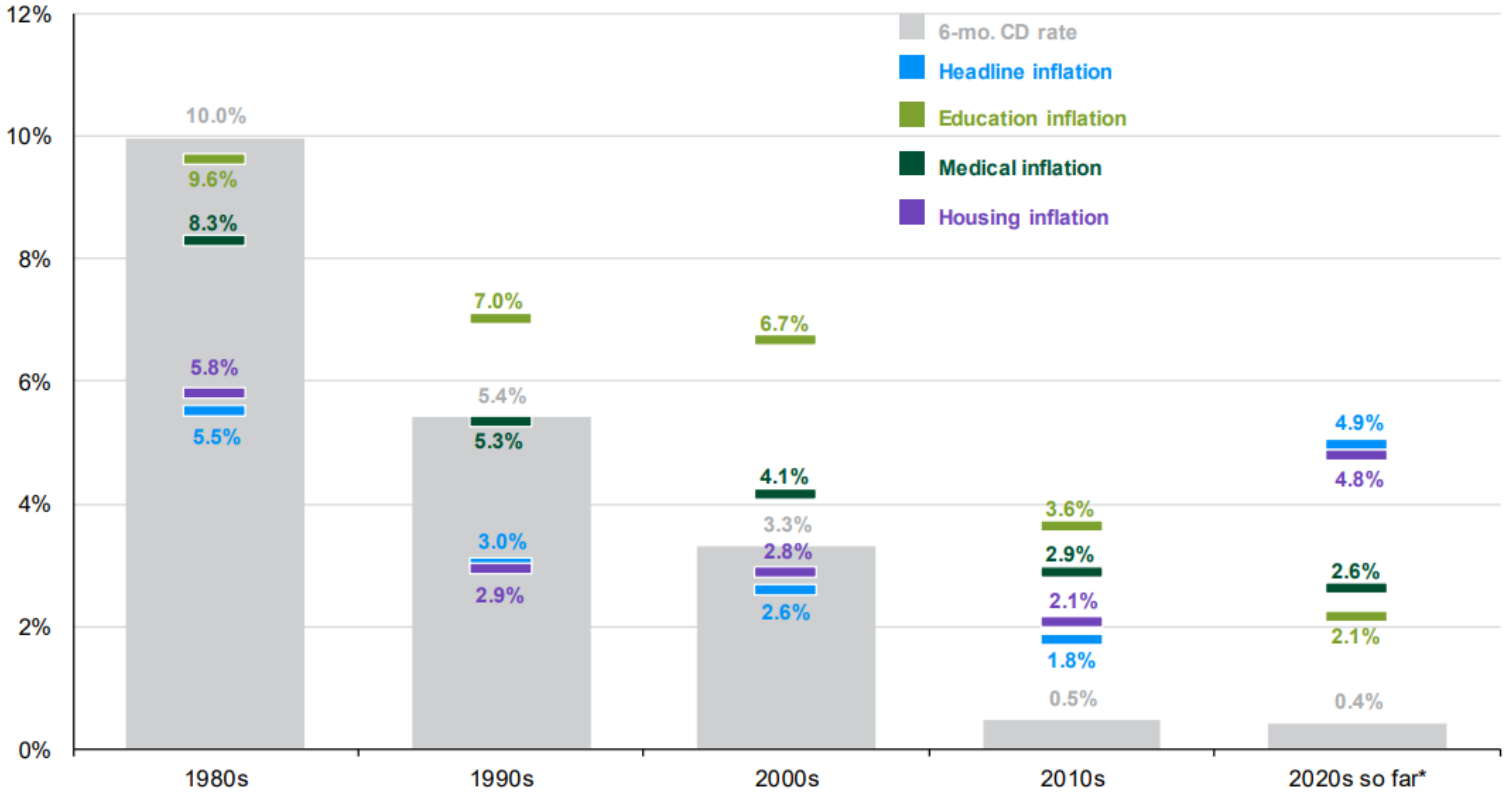




Source: J.P. Morgan

Market Overview: Savings Rate

Average annualized return on 6-month CD vs. annualized CPI inflation and subcomponents
By decade, derived from subcomponents of the consumer price index



Source: J.P. Morgan

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