MONTH IN REVIEW

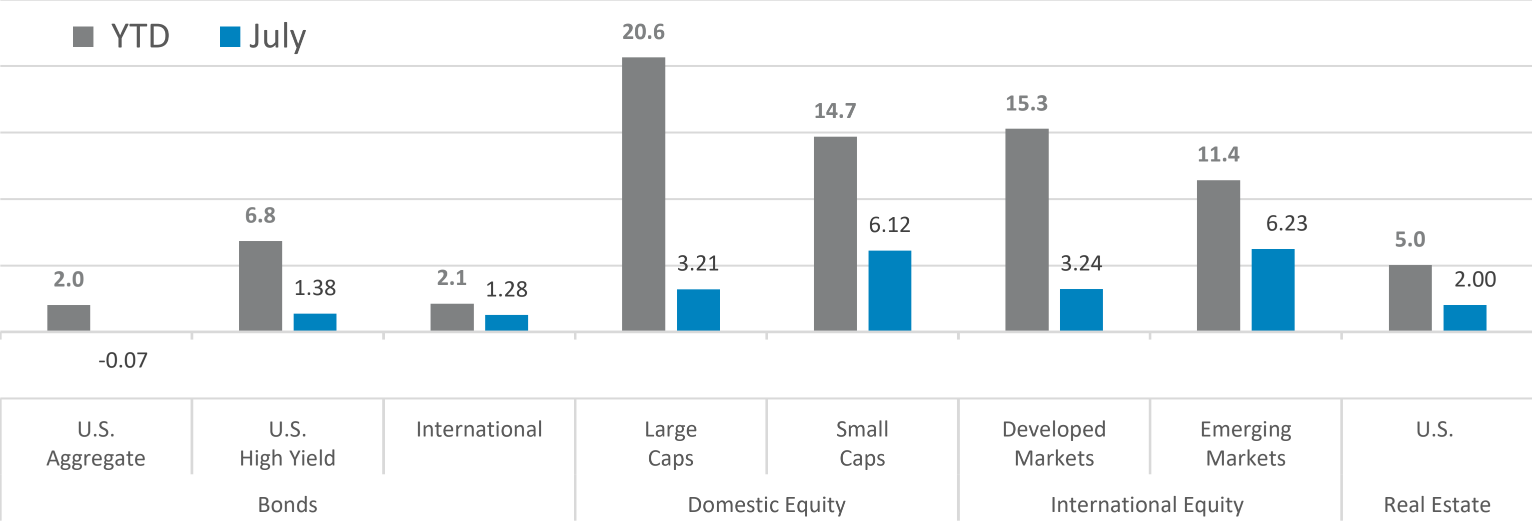
July 2023

Quick Takes

- **Risk Assets Grind Higher.** Risk assets continued their grind higher, adding to their already robust year-to-date gains.
- **Inflation Continues to Soften.** Inflation, as measured by the Fed's preferred data point of Core PCE Deflator, showed even furth signs of cooling off at the July reading with the data point landing below street estimates of +4.2% at +4.1% on the year-over-year metric. Despite this positive development, the FOMC elected to conduct yet another +25bps hike in interest rates during their July meeting.
- **Dollar Falls Then Recovers.** The greenback was in a downtrend for the first half of the month but began to trend upward as the FOMC's meeting approached and then continue climbing after their decision to increase interest rates. Despite this recovery in the back half of the month, the dollar still closed below where it started the month.
- **Robust Economic Production and Tight Labor Markets.** The first estimate of second quarter GDP came in well above consensus estimates of +1.8%, landing at +2.4%. Labor Markets remain tight with the Unemployment Rate falling to 3.6% at the reading towards the beginning of the month.

Asset Class Performance

July continued right where June left off with risk assets climbing higher and adding to their already stellar year-to-date return. At the end of the month, earnings season was in high gear with over half of S&P 500 companies having reported second quarter results. According to FactSet, 80% of companies have reported positive EPS surprise so far.



Source: Bloomberg, as of December 31, 2022. Asset-class performance is presented by using total returns for an index proxy that best represents the respective broad asset class. U.S. Bonds (Barclays U.S. Aggregate Bond TR), U.S. High Yield (Barclays U.S. HY 2% Issuer-Capped TR), International Bonds (Barclays Global Aggregate ex USD TR), Large Caps (S&P 500 TR), Small Caps (Russell 2000 TR), Developed Markets (MSCI EAFE NR USD), Emerging Markets (MSCI EM NR USD), Real Estate (FTSE NAREIT All Equity REITS TR).

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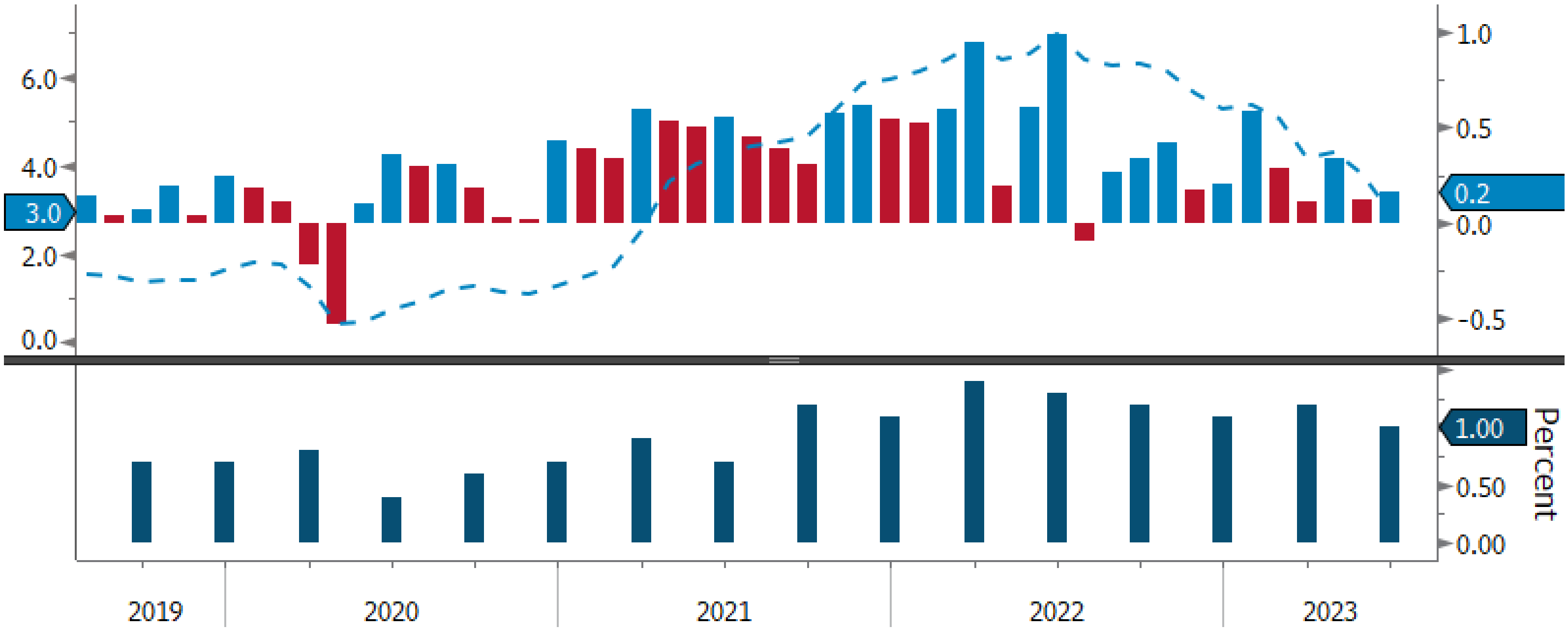
July 2023

Markets & Macroeconomics

Inflation Further Softens and So Does Consumer Spending

Inflation Eases and Labor Costs Soften

PCE Price Index MoM & YoY (Top), Employment Cost Index YoY



Source: Commerce Department, Bureau of Labor Statistics, Bloomberg

As the effects of the Fed's rapid tightening in financial conditions continue to work their way through the economic system, inflation, as measured by the Fed's favored methodology of Personal Consumption Expenditure ("PCE") index, continued to show signs of softening with the topline data reading landing in-line with street estimates of +3.0% and the Core metric (which excludes the volatile categories of food and energy) came in below survey estimates of +4.2%, landing at +4.1% on the year-over-year metrics. Despite the recent positive trend in inflation metrics over the course of the year so far, an area that has showed persistent tightness has been the labor markets. However, the July reading of the Employment Cost Index, which is a broad metric of the cost of wages and benefits, showed signs of softening for the second quarter with the reading landing below expectations of +1.1% coming in at +1.0%. Tight labor markets have plagued the Fed's battle against inflation as the robust job markets have led to increased competition for available workers, which has led to increased upward pressure on wages and benefits. With consumers benefiting from these higher wages and benefits, this has allowed consumer spending to remain robust throughout the Fed's tightening cycle. While consumers have increased pools to spend from, they are not immune to the effects of higher inflation, for the July reading of Real Personal Spending (i.e., inflation adjusted levels of Personal Spending) came in above expectations of +0.3%, landing at +0.4%, while Personal Income came in softer than expected at +0.3% versus estimates of +0.5%. This indicates that consumers ultimately spent more than they took in, likely tapping into dwindling levels of savings or credit card balances. This trend is not sustainable in the long-run, which would indicate that households will either need to cut back on spending or re-enter the labor market.

Bottom Line: Inflation, as measured by the PCE Core Deflator continued to show signs of moderating as the effects of the Fed's tightening of monetary policy works its way through the economic system. While Labor Markets have remained resiliently tight throughout the Fed's tightening campaign, market participants are continuing to see signs that softening is entering the jobs market with the Cost of Employment Index moderating in the second quarter. Furthermore, consumers appear to be increasing Personal Spending above levels of increasing Personal Income. While increased Personal Spending has helped prop up economic production, it's not sustainable in the long-run which should lead to slackening in the Labor Markets as Participation increases.

July 2023

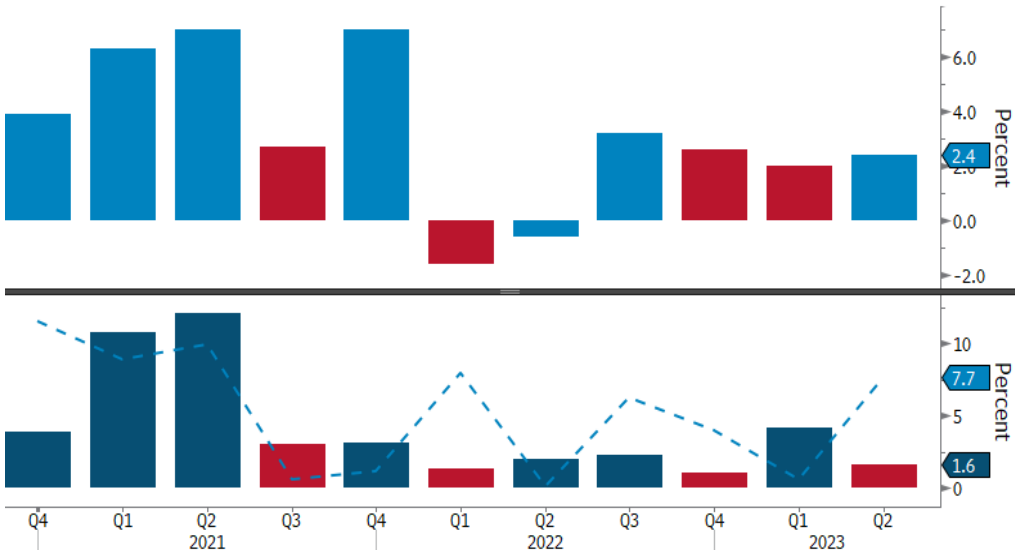
What's Ahead

Economic Production Surprises to the Upside Despite FOMCE Hikes

Surprising to the upside in a big way, the initial reading of GDP for the US Economy landed at +2.4%, well above estimates of +1.8% and Q1's final number of +2.0%. While the initial estimate will go through multiple revisions over the next several months as more data becomes available, this initial reading suggests that the economy may not have to go through a recession while the Fed combats inflation back to a more sustainable level. One major contributor to economic production's robust initial reading of second quarter data was Personal Consumption. Consumers have thus far been able to offset most of the Fed's monetary tightening with their spending activities, while other areas of the economy have shown signs of stagnation. While the topline number of Durable & Capital Goods Orders, a metric of US factory investment, came in screaming above expectations, this surprise was mostly due to a large order of aircraft. When excluding for defense and aircraft order, i.e., the Core metric, factory investment rose a mere +0.2% for the July reading. This indicates that manufactures are continuing to moderate investment which typically happens during times of economic slowdown. While Goods Orders came in slightly positive, Shipments were effectively flat, which also hints at a slowdown. While manufacturing investment on the goods side has been stagnating, one area of spending has been on structures, which have been buoyed by a slew of government programs encouraging investment in domestic production. Nonresidential fixed investment increased at breakneck speed in the second quarter of the year, suggesting that production facilities are seeing investment and should lead to increased capacity in the future, despite the lackluster investment in current output. Combing all this together, and it appears that there is a path forward for the Fed to tame inflation while keeping economic production positive on the backs of consumers, but the threading of the needle leads to little room for error on the Fed's tightening campaign with producers preparing for a slowdown.

QoQ GDP & Personal Consumption Lands Well Above Estimates

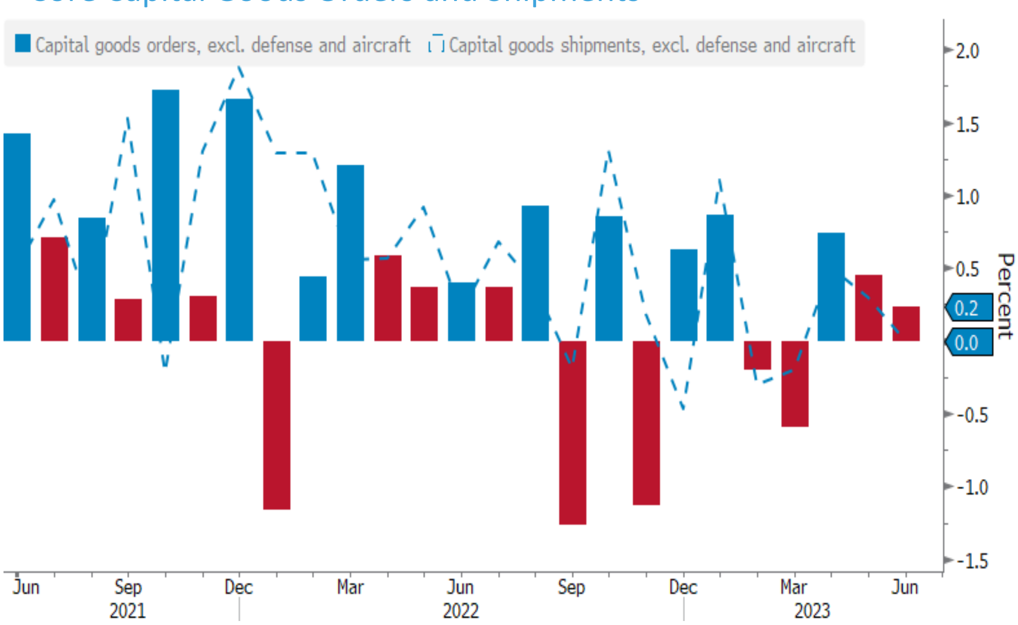
GDP Annualized (Top), Personal Consumption, Nonresidential fixed Investment



Source: Bureau of Economic Analysis, Bloomberg

Durable Goods Orders Spike, Core Capital Goods Stall

Core Capital Goods Orders and Shipments



Source: US Commerce Department, Bloomberg

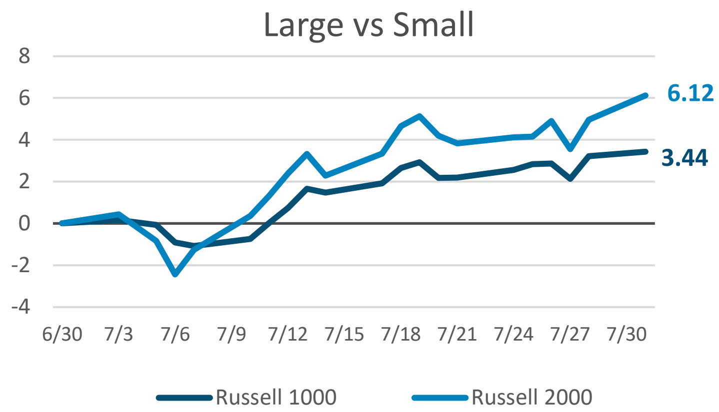
<u>Bottom Line</u>: Consumer Spending has propped up second quarter economic production, while current manufacturing output investment has continued to show signs of stagnating in preparation for economic slowdown. However, it appears that manufactures are increasing future capacity with investment in infrastructure spending that has been bolstered by a slew of government programs. With the push and pull between consumers' robust spending and producers' lackluster investment, it's possible that the Fed may be able to slowdown the economy enough to get inflation under control while avoiding a recession, however, any misstep by the Fed could have dire consequences with many areas of the economy already hunkered down for a potential recessionary environment.

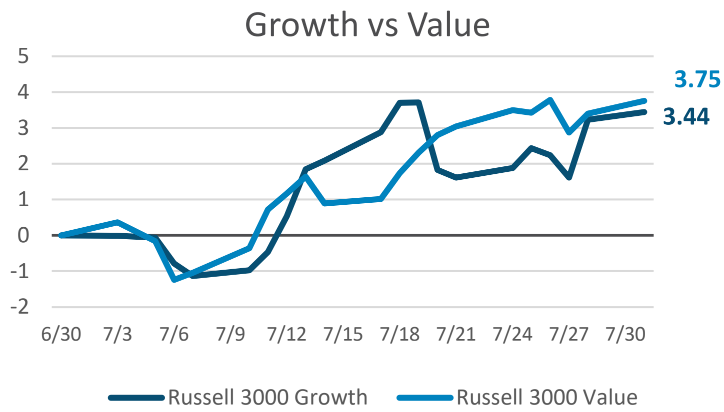
July 2023

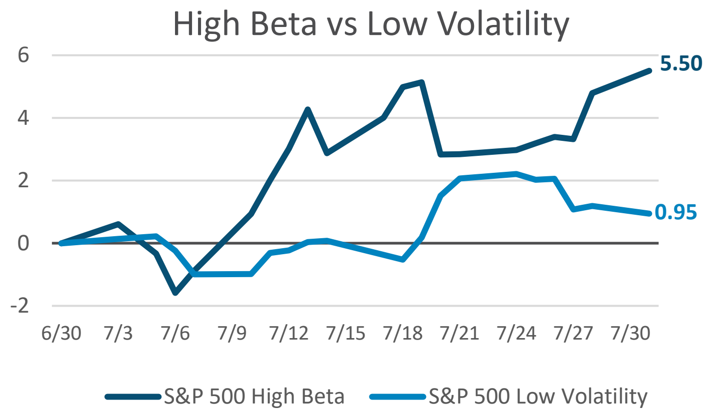
Equity Themes

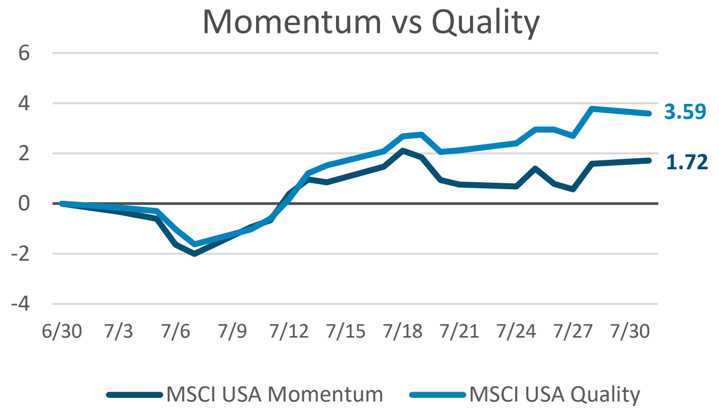
What Worked, What Didn't

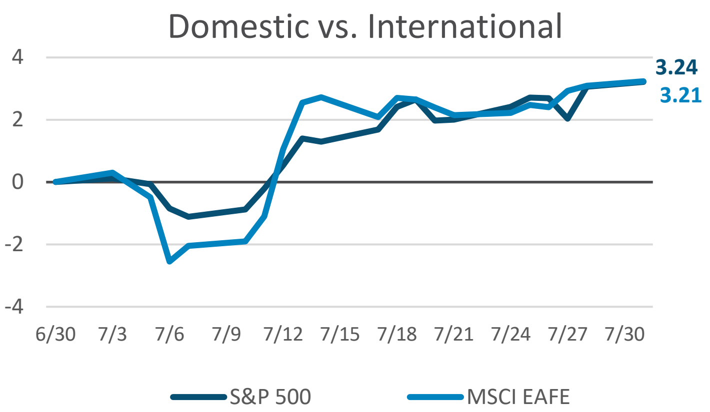
- **Small Over Large, Value Over Growth.** Small Cap equities continued their run of outperforming their Large Cap peers and Value styled equities slight outperformed their Growth Styled peers, but both had strong performance in July.
- **High Beta and Quality Outperform.** High Beta equities crushed their Low Vol peers, and the Quality factor was in favor for the month of July while Momentum lagged for the month of July.
- **Domestic over International, Emerging over Developed.** Domestic Equities eked out slight margin of outperformance for the month of July, but Emerging Markets were the winner for the month of July on the back of the Chinese government encouraging more stimulative policies for their stagnating economy.

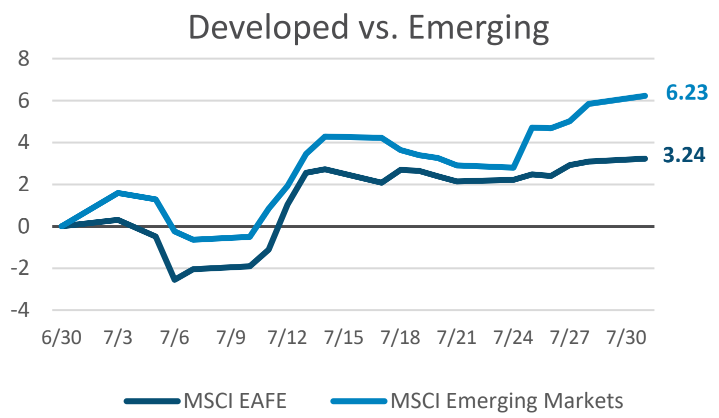












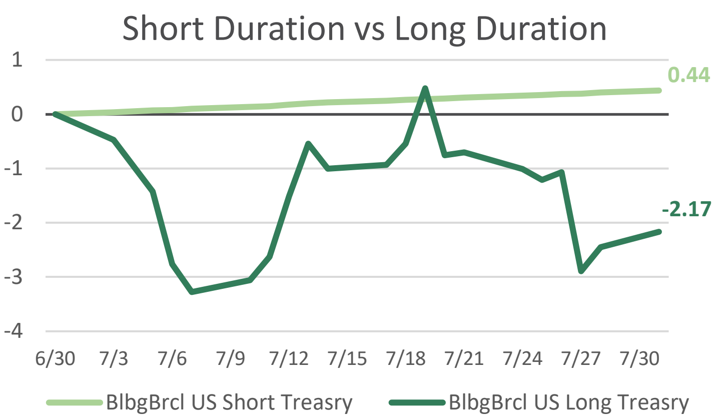
Source: Bloomberg.

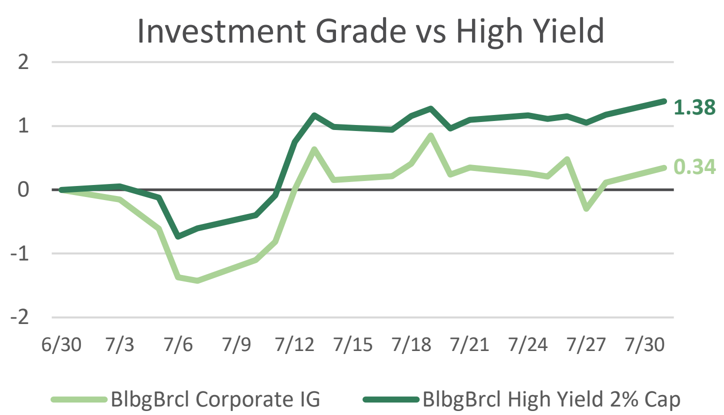
July 2023

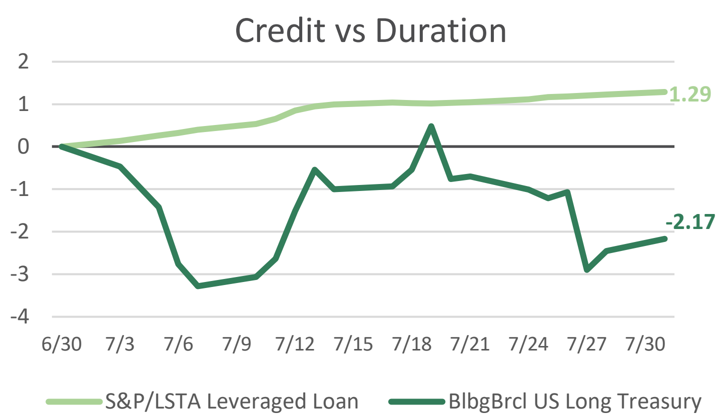
Bond Themes

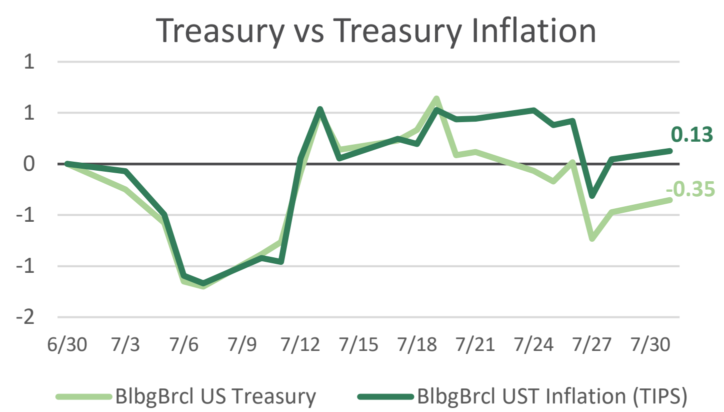
What Worked, What Didn't

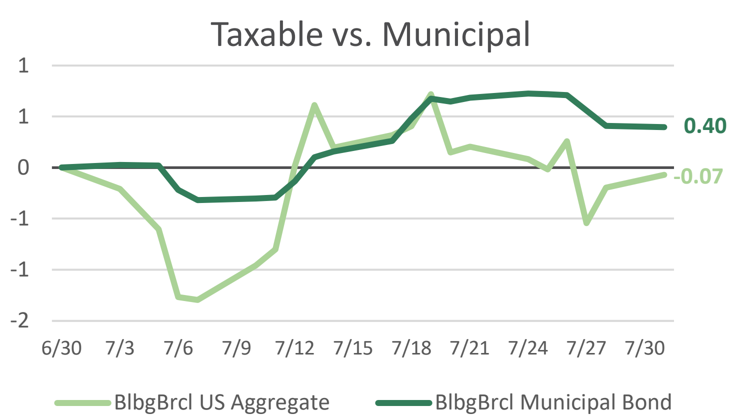
- **Short Duration and High Yield Outperform.** Long Duration bonds had a rough ride for the month of July on the back of the Fed conducting yet another rate hike, on the flip side, this buoyed Short Duration bonds for the month and High Yield was a benefactor of better-than-expected economic news.
- **Credit Beat Duration and TIPS Underperform.** TIPS lagged for the month with softer Inflation numbers and Leveraged Loans posted a wide margin of outperformance for July with Duration lagging.
- **Munis and International Outperform.** Munis posted a respectable month versus the Aggregate Bond Index for the month of July as did International Bonds as the Aggregate Index lagged for the month.

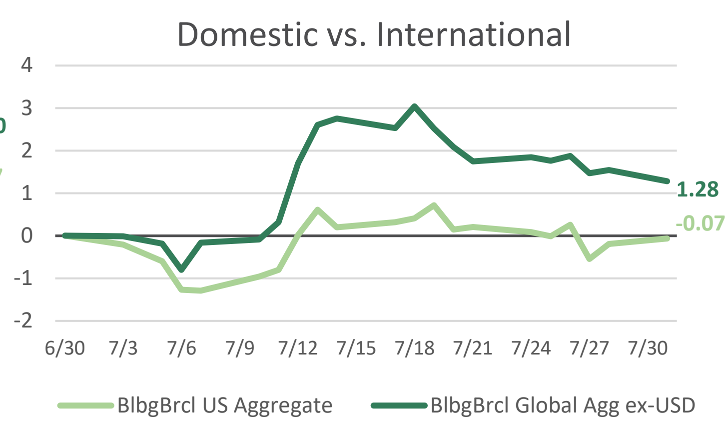












Source: Bloomberg.

July 2023

Asset Class Performance

The Importance of Diversification. From period to period there is no certainty what investment will be the best, or worst, performer. Diversification mitigates the risk of relying on any single investment and offers a host of long-term benefits, such as less portfolio volatility, improved risk-adjusted returns, and more effective compounding.

	Jul-03	Jul-05	Jul-06	Jul-07	Jul-10	Jul-11	Jul-12	Jul-13	Jul-14	Jul-17	Jul-18	Jul-19	Jul-20	Jul-21	Jul-24	Jul-25	Jul-26	Jul-27	Jul-28	Jul-31	Jul	YTD	
High	EM 1.11	RE 0.34	IBD -0.50	SCV 1.44	SCG 1.92	RE 1.34	EM 2.24	IEQ 1.60	LCG 0.26	SCG 1.20	SCV 1.58	RE 1.10	LCV 0.55	RE 0.46	EM 1.36	EM 0.83	SCV 1.26	IEQ -0.23	EM 2.42	SCG 1.30	SCV 7.41	LCG 33.35	High
	RE 0.86	LCG 0.13	USB -0.65	EM 1.13	MCG 1.75	MCV 1.33	IEQ 1.91	EM 1.30	IBD -0.14	MCG 0.93	SCG 0.91	SCV 0.99	MCV -0.18	LCV 0.27	RE 0.81	LCG 0.57	EM 0.58	LCG -0.57	LCG 1.58	SCV 0.94	EM 6.04	MCG 19.36	
	SCV 0.84	MCG -0.29	LCG -0.67	IBD 1.00	SCV 1.38	SCV 1.08	IBD 1.62	LCG 1.28	RE -0.15	SCV 0.86	LCG 0.84	LCV 0.55	RE -0.30	HYB 0.25	SCV 0.62	MCG 0.44	RE 0.52	HYB -0.79	SCG 1.36	MCV 0.58	SCG 4.69	SCG 18.85	
	MCV 0.60	HYB -0.31	HYB -0.73	SCG 0.87	MCV 0.88	LCV 1.07	SCV 1.27	IBD 1.28	60/40 -0.48	LCG 0.74	MCV 0.69	MCV 0.54	HYB -0.44	IEQ 0.20	LCV 0.42	SCG 0.31	HYB 0.40	60/40 -0.84	SCV 1.28	RE 0.57	MCV 4.41	IEQ 15.54	
	LCV 0.38	IBD -0.42	RE -0.80	IEQ 0.75	LCV 0.67	MCG 1.05	60/40 1.11	SCG 1.01	USB -0.48	MCV 0.38	LCV 0.68	USB 0.31	IEQ -0.51	USB 0.07	LCG 0.33	IEQ 0.11	USB 0.33	LCV -0.84	MCG 1.07	MCG 0.49	LCV 3.52	EM 11.56	
	SCG 0.09	USB -0.45	MCV -0.91	MCV 0.72	HYB 0.50	EM 1.01	LCG 1.03	60/40 0.95	MCG -0.49	HYB 0.19	IEQ 0.65	60/40 0.19	USB -0.52	MCG 0.07	MCV 0.25	MCV 0.11	SCG 0.32	USB -0.86	IBD 1.01	LCV 0.31	LCG 3.44	60/40 10.94	
	60/40 0.09	LCV -0.51	60/40 -1.05	60/40 0.32	60/40 0.43	SCG 0.90	SCG 0.84	MCG 0.90	EM -0.56	60/40 0.18	IBD 0.58	HYB 0.08	60/40 -0.61	60/40 0.06	60/40 0.08	60/40 0.08	MCV 0.31	MCV -1.10	60/40 0.81	HYB 0.24	MCG 3.00	SCV 10.13	
	LCG -0.10	60/40 -0.53	LCV -1.07	MCG 0.25	RE 0.42	IEQ 0.90	USB 0.81	SCV 0.70	IEQ -0.57	EM 0.12	MCG 0.47	MCG 0.00	SCV -0.70	IBD 0.00	SCG -0.13	LCV -0.05	IBD 0.30	MCG -1.19	IEQ 0.72	60/40 0.20	IEQ 2.70	MCV 9.79	
	IEQ -0.11	EM -0.60	MCG -1.10	LCV 0.12	IEQ 0.28	60/40 0.67	HYB 0.78	RE 0.70	SCG -0.69	USB 0.11	60/40 0.36	LCG 0.00	EM -0.74	MCV -0.03	IBD -0.17	HYB -0.07	LCV 0.30	EM -1.23	MCV 0.65	LCG 0.20	60/40 2.33	LCV 8.75	
	USB -0.12	MCV -0.64	SCG -1.47	HYB 0.09	USB 0.28	HYB 0.54	MCV 0.59	USB 0.62	LCV -0.71	LCV 0.06	HYB 0.28	IEQ -0.05	SCG -0.95	EM -0.15	HYB -0.17	USB -0.11	60/40 0.30	SCG -1.27	HYB 0.57	USB 0.12	RE 1.74	RE 5.67	
	HYB -0.16	IEQ -1.12	IEQ -1.73	USB 0.02	IBD 0.21	LCG 0.50	MCG 0.58	MCV 0.60	HYB -0.73	IBD -0.10	USB 0.08	IBD -0.17	IBD -1.13	SCG -0.30	USB -0.18	IBD -0.20	IEQ 0.27	SCV -1.33	LCV 0.43	EM 0.05	IBD 1.74	HYB 5.65	
	IBD -0.18	SCV -1.18	SCV -1.77	RE -0.26	LCG 0.09	IBD 0.35	RE 0.54	HYB 0.60	MCV -1.01	IEQ -0.12	RE -0.59	EM -0.20	MCG -1.36	LCG -0.31	IEQ -0.24	SCV -0.32	MCG 0.10	IBD -1.35	USB 0.39	IEQ 0.03	HYB 1.12	IBD 5.00	
Low	MCG -0.27	SCG -1.33	EM -2.04	LCG -0.44	EM 0.08	USB 0.22	LCV 0.42	LCV 0.43	SCV -1.24	RE -0.67	EM -0.73	SCG -0.20	LCG -1.81	SCV -0.42	MCG -0.39	RE -0.70	LCG -0.21	RE -2.20	RE -0.19	IBD -0.22	USB -0.02	USB 2.24	Low

Legend

- 60/40 Allocation (60/40)
- Large Growth (LCG)
- Large Value (LCV)
- Mid Growth (MCG)
- Mid Value (MCV)
- Small Growth (SCG)
- Small Value (SCV)
- Intl Equity (IEQ)
- Emg Markets (EM)
- U.S. Bonds (USB)
- High Yield Bond (HYB)
- Intl Bonds (IBD)
- Real Estate (RE)

Source: Bloomberg. Asset-class performance is presented by using market returns from an exchange-traded fund (ETF) proxy that best represents its respective broad asset class. Returns shown are net of fund fees for and do not necessarily represent performance of specific mutual funds and/or exchange-traded funds recommended by the Prime Capital Investment Advisors. The performance of those funds June be substantially different than the performance of the broad asset classes and to proxy ETFs represented here. U.S. Bonds (iShares Core U.S. Aggregate Bond ETF); High-Yield Bond (iShares iBoxx $ High Yield Corporate Bond ETF); Intl Bonds (SPDR® Bloomberg Barclays International Corporate Bond ETF); Large Growth (iShares Russell 1000 Growth ETF); Large Value (iShares Russell 1000 Value ETF); Mid Growth (iShares Russell Mid-Cap Growth ETF); Mid Value (iShares Russell Mid-Cap Value ETF); Small Growth (iShares Russell 2000 Growth ETF); Small Value (iShares Russell 2000 Value ETF); Intl Equity (iShares MSCI EAFE ETF); Emg Markets (iShares MSCI Emerging Markets ETF); and Real Estate (iShares U.S. Real Estate ETF). The return displayed as “Allocation” is a weighted average of the ETF proxies shown as represented by: 30% U.S. Bonds, 5% International Bonds, 5% High Yield Bonds, 10% Large Growth, 10% Large Value, 4% Mid Growth, 4% Mid Value, 2% Small Growth, 2% Small Value, 18% International Stock, 7% Emerging Markets, 3% Real Estate. 080223006 - MAH

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