The Davis Center for Portfolio Management

University of Dayton

U.S. Equity Outlook

Spring 2022 Outlook: Maneuvering in Unprecedented and Volatile Markets

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The opinions expressed herein are those of the student-managers of the Flyer Investments Fund and do not necessarily represent the views and opinions of the University of Dayton.

Living with COVID-19

Although COVID-19 continues to plague society, people are slowly reverting to their pre-pandemic lifestyles. It has been nearly two and a half years since COVID-19 was discovered in Wuhan, China. The World Health Organization cautions that the pandemic is still not over, but many people are starting to view COVID-19 as an endemic. The disease is becoming more predictable than it was initially, and it is widely circulating throughout the population. Even though the disease is becoming more predictable than before, variants prevent it from officially being classified as an endemic. In the last Outlook, Delta was the main variant of concern. Now, the Omicron variant is running rampant. Omicron is much more contagious than Delta, but it is also less likely to cause extreme illness. According to a study released by the CDC, those infected with Omicron are 53% less likely to be hospitalized and 91% less likely to die than those infected with the Delta variant. Patients experience similar symptoms, but Omicron symptoms are milder.

Our previous Outlook reported 251,795,660 active cases and 5,084,063 deaths worldwide. Since then, the number of active cases has nearly doubled to 482,811,946 cases, and the number of fatalities has increased to 6,151,003. Specifically, within the United States, there are over 79 million active cases and nearly one million deaths. The number of cases shot up dramatically between December 2021 and January 2022, mainly due to the resurgence of COVID-19 through the Omicron variant. However, in more recent months, from February to March, the CDC reported that the number of cases, deaths, and hospitalizations is trending negatively for both the United States and the world. The current case fatality rate for the U.S. is 1.2%, down from over 6% in May 2020. Since the Omicron variant is milder than previous variants and is starting to subside, the number of deaths and active cases continues to decline.

Vaccine and booster shots are widely accessible to the public at pharmacies, pop-up vaccine centers, universities, etc; 66% of the U.S. population is fully vaccinated. In comparison, 58% of the population is fully vaccinated worldwide. Everyone over the age of five is eligible for the vaccine, and those over the age of 12 are eligible for the booster shot as well. While approximately two-thirds of the U.S. population is vaccinated, only 29.5% of people have received a booster shot. The number of vaccinated and boosted individuals has not risen dramatically since the last Equity Outlook, and experts now say that we will probably never reach herd immunity because of the number of unvaccinated individuals, which allows the continued spread of infections. There has been much controversy about the vaccine, but places like New York and various institutions have implemented vaccine mandates. Anyone who works at a business in New York must show proof of vaccination. Otherwise, they can no longer work at the establishment. In addition, many bars, restaurants, and event venues in New York require proof of vaccination upon entry. Businesses around the

country have begun to allow their employees to return to the workplace in person, with either certain vaccine requirements or mask mandates. While many people are returning to in-person work, some businesses are still allowing employees to work from home.

The world has gone through many highs and lows regarding the COVID-19 pandemic, and although it is probably far from over, people have adapted and are slowly starting to return to their pre-pandemic life. For example, many places are beginning to lift mask mandates, a significant step for society. The University of Dayton, among many other universities, lifted its mask mandates for students and employees in March. Many feel that this is a monumental step toward returning to normal life. With the pandemic seeming to subside, many more people are traveling as compared to the previous two years. TSA checkpoint numbers were as low as 180,000 in 2020, and now these numbers are well above two million. While other variants may emerge, society has learned how to adapt and is better equipped to deal with new infections than at the beginning of the pandemic.

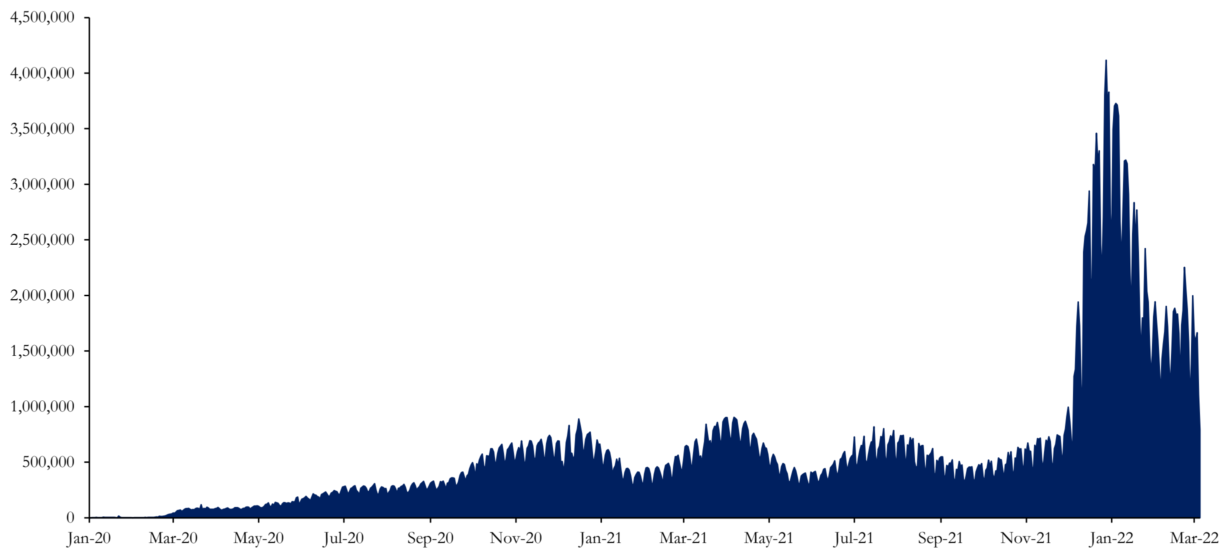

Figure 1: New Cases of COVID-19 Worldwide
Source: CDC | Data as of March 31, 2022

The Russia and Ukraine Conflict

On February 24, Russia invaded Ukraine with the supposed goal of achieving the demilitarization and de-Nazification of Ukraine and to protect people who have been subjected to abuse and genocide by the regime in Kyiv for eight years according to Vladimir Putin. He stated that it was not his intention to impose anything by force nor to occupy the Ukrainian territory. Putin has used the term "military operation" instead of "war" or "invasion" and requires Russian media to use the term as well. When looking at the conflict today, these claims have panned out to be false. The declaration of Nazism and genocide has been entirely baseless. While the invasion seemed to many like it would succeed in weeks or even days, the Russian military was hit with fierce resistance from the Ukrainian army. With the war being stretched to over four weeks now, 3.3 million people have fled the country, nearly 1,000 civilians have died, and infrastructure in various cities has been left in ruins. Sadly, the devastation appears to be far from over, causing Western allies to wage economic warfare on Russia through trade sanctions on foreign goods.

The Russia-Ukraine crisis has created another driver for slow global growth and rising inflation rates as global growth risk is correlated to Russia's energy supply disruption. The risk to global growth has been materially altered since the launch of the full-scale invasion. The Russian ruble has reached all-time lows and continues to fall while the Russian equity market has remained closed since February 25. Oil has spiked to over $130 per barrel (bbl) for the first time since 2008, and gas prices have reached all-time highs in many countries. Major countries that have imposed global sanctions include the European Union, the U.S, the U.K, Canada, Switzerland, Japan, Australia, and Taiwan. President Biden signed an executive order that bans the import of Russian oil, natural gas, and coal to the United States while also forbidding new U.S, investment in Russia's energy sector. Due to the United States' reliance on Russia for these energy sources, the European Commission and the United States agreed to release 60 million barrels of oil from strategic petroleum reserves on March 1. Moreover, the International Energy Agency recently released a 10-Point plan to reduce the E.U.'s reliance on Russia for natural gas and natural gas products. The E.U. has also instituted a security policy that includes steps to move away from dependency on Russian energy, especially in gas markets.

Researchers at J.P Morgan say that the Russia-Ukraine crisis is a low earnings risk for U.S corporations. Still, an energy price shock during a time when the central bank is pivoting to curve inflation could lower investor sentiment. On a more positive side, U.S companies have low direct exposure to Russia; specifically, only 0.6% of the Russell 1000 Index, based on disclosed revenues. However, indirect risks include slower global growth and consumer spending because of increased oil and food prices, further supply chain disruptions, cybersecurity risks, and tightening monetary policy. Commodity prices are rising and are expected to continue to do so, due to the crisis. Nickel has

The Russia and Ukraine Conflict

risen nearly 100% since the beginning of the invasion as Russia is the largest exporter of this base metal globally, accounting for roughly 28% of all global exports. Coal had shot up to as high as 259 $ per ton, up from 140$ pre-invasion. Steel, Palladium, Aluminum, Iron, and Platinum have all seen increases and move in correlation with Russia's large corporations in each industry.

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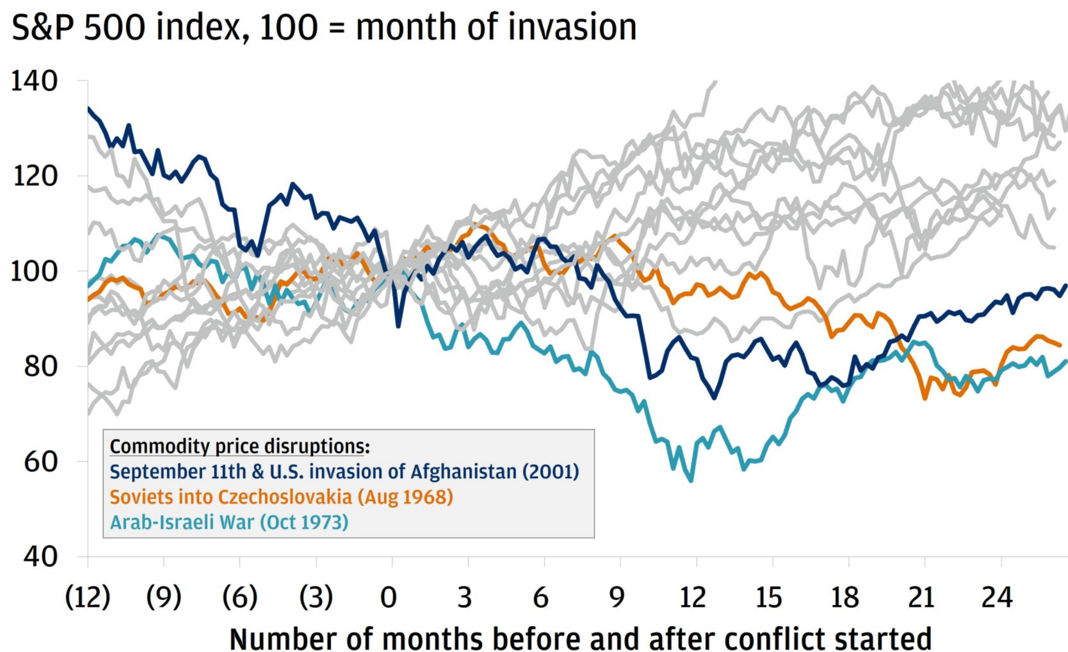

Figure 2: Geopolitical Events and Long-Term Market Impacts
Source: J.P. Morgan Asset Management

Macro Conditions

Real GDP Growth

Real GDP increased at an annual rate of 6.9% for Q4 of 2021. This significant increase was driven by private inventory investment, exports, business spending, and strong consume activity (many Americans still have relatively high savings and continue to spend). Despite this, companies still struggle to find workers while confronting supply chain issues. The problem that the economy faces is supply, not demand. Heading into 2022, there were already new threats that lay ahead. The invasion of Ukraine has already had a significant impact on the price of oil, and the sanctions that have been imposed on Russia could impact other economies throughout the world.

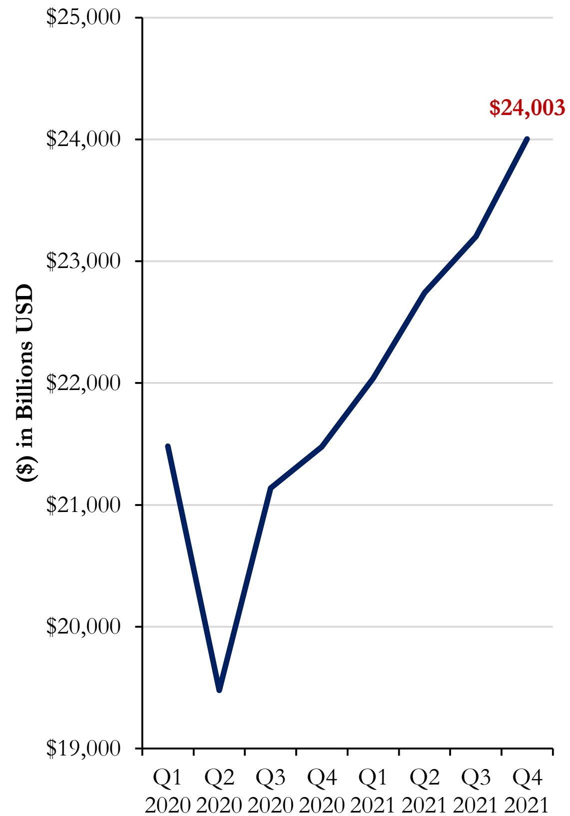

Figure 3: U.S. GDP; seasonally and inflation adjusted

Source: FRED. St. Louis Economic Data

Looking ahead, forecasts indicate that GDP growth will slow to 1.7% in Q1 of 2022. Adding to this, the U.S. economy is already experiencing high inflation, with an interest rate hike coming in March, the first since 2018. The most significant year-over-year price increases are expected to be seen in Q2 of 2022, which may inhibit consumer spending into Q3 of 2022. The impact of COVID-19 is beginning to diminish, but new variants could further damage this outlook. Likewise, the Russia-Ukraine conflict may have unexpected repercussions. Current sanctions are unlikely to be removed anytime soon. Russia supplies about 10% of the world's energy and the recent jump in gas prices, reduces consumers' spendable income. Higher oil prices, combined with the faster pace at which the Fed will be raising interest rates, have caused many GDP outlooks for 2022 to be cut. Despite all this, there are mixed outlooks on actual growth at the end of the year. Some expectations are as low as 3.0% year-over-year growth, while others are as high as 4.7%.

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Labor Market Conditions

The U.S. labor market is steadily transitioning to a post-pandemic world with a strong stream of adults entering the labor force and overall employment nearing pre-pandemic levels. Total nonfarm payroll employment rose by 750,000 in the month of February while the unemployment rate stood at 3.8%, near its 50-year low of 3.5%, according to the U.S. Bureau of Labor Statistics. This was the largest gain in seven months, and the labor force even saw a decrease of 1.8 million people unable to work due to COVID-19. In addition, wage growth is easing the nationwide labor shortage as employers have finally been able to fill lower-wage positions that had persistently remained vacant. For February in particular, wage growth slowed slightly but continued to remain around its historically high levels. In the private sector, hourly earnings rose a seasonally adjusted 5.1% in February from the previous year, according to the Labor Department. Four of the past five months have seen annual wage growth exceed 5% compared to annual growth of 3.2% in the two years leading up to the pandemic. The industries that have experienced a surge in demand as the effects of the Omicron COVID-19 variant fade have exhibited the largest wage gains; in particular, 7.1% wage growth in retail, 7.7% growth in transportation, and 11.2% growth in the leisure and hospitality industries. However, these wage gains have added to inflationary pressures in what is referred to as the wage-price spiral. As wages increase, businesses tend to offset the incremental costs by raising prices, leading to even higher wage demands by employees and eventually resulting in even higher price markups on products. However, the rising wage trend does point to a recovering economy as more vacant positions continue to be filled. In terms of added jobs, the industries that have seen the highest gain are leisure and hospitality (+124,000), professional business services such as temporary care (+36,000), healthcare (+64,000), and transportation (+48,000). The least growth stemmed from utilities, mining and logging, and construction. Looking at those who have exited the workforce, February saw little change, with 1.6 million job leavers and 888,000 individuals being temporarily laid off. Regarding the remainder of the year, it is logical to assume that, as the effects from COVID-19 weaken, these numbers will show positive improvement as more jobs are added than lost. The labor force participation rate rose to 62.3% in February from 62.2% the previous month, still about 1.1% lower than pre-pandemic levels. Economists debate on when/if this rate will fully recover, considering that many older workers retired during the pandemic and immigration numbers are lower.

During the final months of 2021 and the very beginning of 2022, the economy saw continued additions of jobs, with an increase in nonfarm payroll employment of 249,000 in November, 199,000 in December, and 467,000 in January. The large additions in January 2022 are credited to the 11.3 million job openings throughout the month. Despite the dip in December, employment has been ro-

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bust leading up to March and is expected to remain so as the world continues to emerge from the pandemic. In February, 13% of those employed teleworked due to the pandemic according to the BLS household survey. Although this figure was down from 15.4% in the prior month, many companies have kept their work-at-home policies in place and plan to continue doing so, especially in densely populated cities. Economists are forecasting another strong month of labor market growth in March, but will watch closely should a tightening labor market (meaning more job openings than workers available) negatively affects the economy given current inflationary pressures. COVID-19 may have, however, left an indelible mark on the office environment in terms of work-from-home preferences.

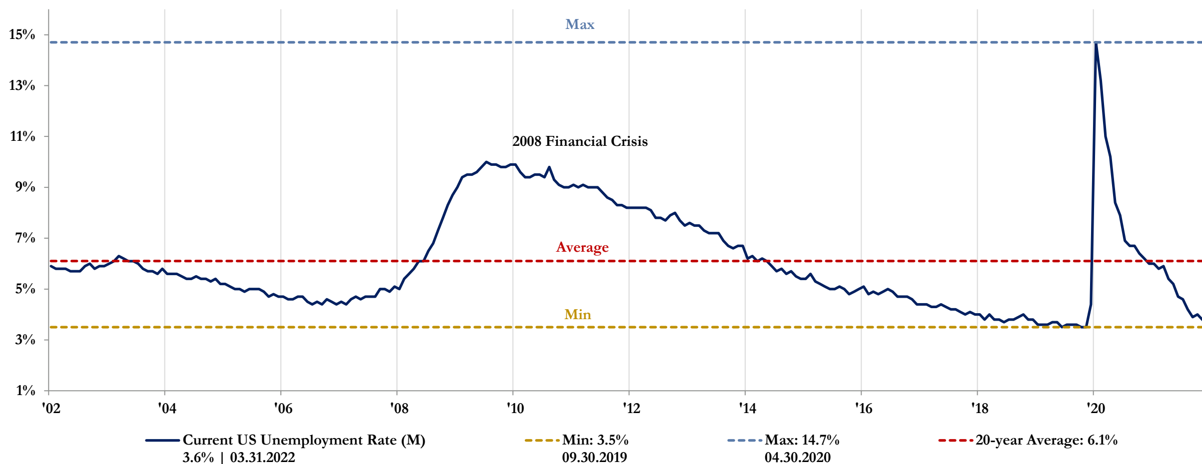

Figure 4: U.S. Unemployment Rate
Source: Bureau of Labor Statistics

Inflation Woes

For months, inflation has been rising at historical rates in the United States, with consumer prices being the highest in 40 years. Inflation rose 7.9% in February. Supply chain challenges, increasing oil prices, and changes in demand in relation to the pandemic have all been contributors. There are concerns that inflation will continue to worsen before it gets better due to Russia's war on Ukraine and additional pandemic-related lockdowns in China, a critical global manufacturer. Economists have closely monitored China's Purchasing Managers Index in both manufacturing and service to determine whether COVID-19 resurgences have further impacted supply chain issues.

Key economic indicators like the Core Personal Consumption Expenditure, the Fed's inflation gauge, can suggest how aggressive the Fed will be in its next interest rate bump. Meanwhile, con-

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sumers in the U.S. continue to spend. Still, household outlays have been slowing since the beginning of 2022 due to rising prices and concerns over Russia's invasion of Ukraine. Before the incursion, economists had been hopeful that inflation would peak this spring as the result of healing in the supply chain and rising interest rates from the Federal Reserve. However, the Ukrainian conflict has put upward pressure on the price of oil, wheat, and precious metals, further exacerbating already present inflation. In addition, despite annual wage growth rising at its fastest pace in two decades, it is still being outpaced by inflation, which erodes consumers' spendable income. Economists have predicted substantial employment gains; however, a tight labor market can push up wages and contribute to inflation.

Economists believe inflation will ease later in 2022 as supply chain constraints lessen and energy price increases slow. However, there is debate over the level at which price increases will stabilize. Fed officials predict that inflation will lower to 2.6% by the end of the year. This prediction factors in how aggressive the Fed will be in raising interest rates while avoiding pushing the economy into a recession. After raising rates 25 bps at its March meeting, the Federal Reserve is expected to continue to raise rates through the end of 2022. Federal Reserve Chair Jerome Powell has said that the central bank is ready to be more aggressive if inflation does not cool down as quickly as expected.

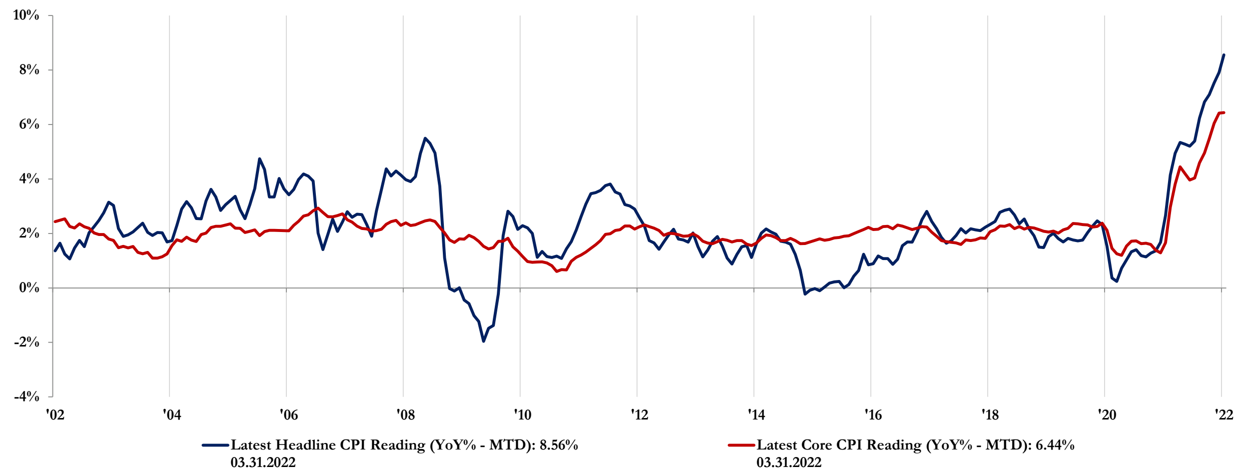

Figure 5: Headline vs. Core Consumer Price Index
Source: FactSet

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Federal Reserve Actions

During the Federal Open Market Committee (FOMC) meeting in March, officials voted to raise the federal funds rate and penciled in six more increases before the end of the year. This represents the most aggressive pace of rate hikes by the Federal Reserve in more than 15 years as the central bank escalates effort to slow down inflation, which is running at its highest levels in four decades. Officials will raise the federal funds rate by 25 bps to a range of 0.25% to 0.5%, the first rate hike since 2018. With its plan of raising rates six more times by year-end, the federal funds rate will be ~2%, slightly higher than the rate that prevailed before the pandemic hit the U.S. economy two years ago. Additionally, the Committee's median projections show the rate rising to 2.75% by the end of 2023, the highest since 2008.

The Fed's decision to raise its benchmark interest rate marks a sharp reversal from just two years ago when it lowered rates to near zero bound and launched a series of quantitative easing programs to support the economy. Since then, the economy has recovered tremendously amid federal stimulus, vaccinations, and surging inflation. As will be discussed later on in this Equity Outlook, inflation over recent months has reached multi-decade highs. Even before Russia's invasion of Ukraine, Fed officials appeared uneasy with the prospect that inflation was proving to be more sticky or less transitory than initially expected.

Fed officials now face three important questions. First, how quickly do they raise interest rates to a level that neither speeds up or slows down economic growth? Second, does raising the interest rates to an acceptable level reduce real or inflation-adjusted borrowing costs? Lastly, when or if will the Fed need to raise interest rates to a level that will slow down growth? How exactly the answers to these questions will play out remains very much a mystery, leading to increased market volatility and negative investor sentiment.

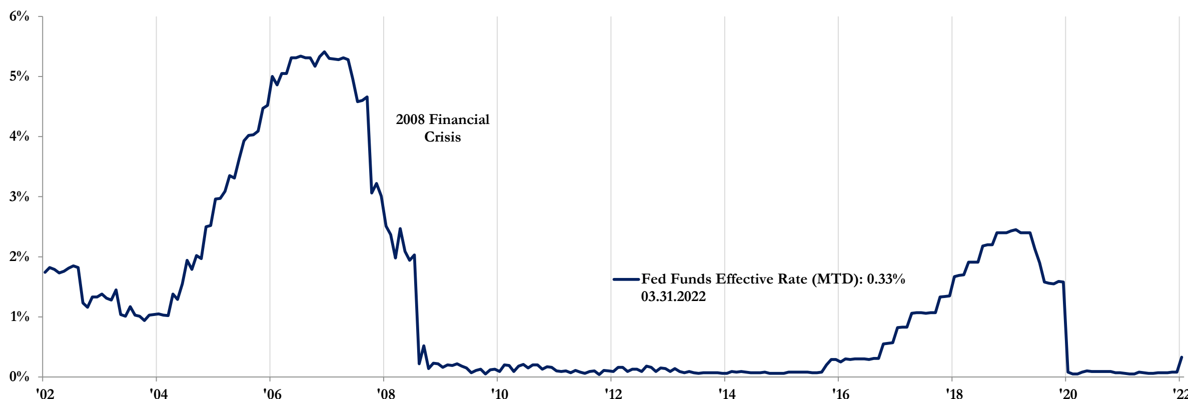

Figure 6: Effective Federal Funds Rate
Source: FactSet

Macro Conditions

Manufacturing and Services Activities

The most important metric for manufacturing activity is the Purchasing Managers' Index. The PMI is calculated from a survey of over 400 manufacturing companies conducted by the Institute for Supply Management to determine if the manufacturing sector is expansionary or contractionary. The metric is measured on a scale of 0-100, with a baseline of 50. A number over 50 indicates growth, while a number under 50 represents contraction. An expanding manufacturing sector suggests economic growth, and a shrinking manufacturing sector suggests economic decline. The ISM manufacturing index is a composite index that gives equal weighting to new orders, production, employment, supplier deliveries, and inventories. Finally, each factor is seasonally adjusted.

The COVID-19 pandemic has resulted in severe short-term contractions and expansions in recorded PMI data, creating long-term ripple effects, which are being realized presently. As of February 2022, PMI registered at 58.6%, indicating economic growth for the 21st consecutive month following the April 2020 economic contraction, corresponding with a 3.5% growth in real GDP. The PMI for March 2021 was 63.7% and has been steadily declining to the present, but remains in growth territory. The further reduction in pandemic restrictions and the recovery of manufacturing-related supply chains have positively stimulated the supply-side to keep up with the recent uptick in consumer demand. The most significant growth has been seen in the following industries: Transportation Equipment, Machinery, and Computer and Electronic Products. These industries were almost perfectly predicted by experts to see the largest increase. The Transportation and Computer industries experienced an influx in consumer demand as travel for work and leisure continued to expand since March 2021, and the labor market's recovery resulted in excess consumer spending for luxury high-tech goods.

The outlook for PMI growth is pessimistic as the manufacturing sector, in particular, is heavily reliant on the health of supply chains. The economic consequences of Russia's invasion of Ukraine have caused natural gas prices to increase tenfold in most import-heavy economies. Given its industrial nature, the manufacturing sector will almost certainly see negative second-hand performance because of the collapse of supply chains for energy-related commodities. Gains in the service sector may potentially outweigh the losses in manufacturing, as it has seen some of the highest increases in employment in the recovery from the COVID-19 contraction.

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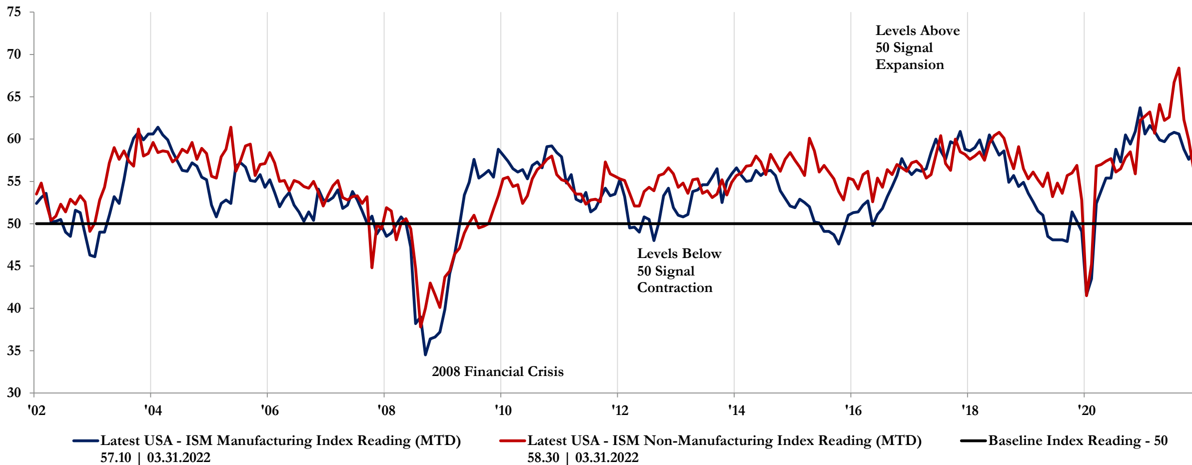

Figure 7: ISM Manufacturing PMI vs. Non-Manufacturing PMI
Source: FactSet

Global Economic Outlook

The International Monetary Fund, a worldwide financial organization consisting of 190 member countries, projected a more negative outlook for the global economy in its January 2022 World Economic Outlook report than reflected in its last report in October. This more pessimistic outlook, which has led to a 0.5% reduction in 2022 growth projections, is primarily due to developments in the world's two largest economies, the United States and China. The IMF is now assuming in its forecasts that the Build Back Better Act, a multi-trillion-dollar fiscal package addressing American infrastructure, will not be passed, dampening the United States' economic growth outlook. Additionally, the earlier than expected removal of monetary support by the Federal Reserve and persistent supply-chain delays further disrupt the United States' economic growth outlook. These factors culminate in a reduction of 1.2% in the IMF's economic growth projections for the United States. Meanwhile, the Chinese real estate sector, a major catalyst for economic growth over the last several decades, has seen a decline in growth due to new policies by the Chinese government intended to reduce leveraging by property developers. The slowdown in a key sector of the Chinese economy will likely cause a decline in the credit-lending ability of Chinese financial institutions, decreasing investment in the broader economy. In conjunction with China's zero-COVID policy, which will likely inhibit consumer spending, this trend culminates in a reduction of 0.8% in the IMF's economic growth estimates for China in 2022.

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The IMF anticipates that inflation will continue to persist throughout the world in 2022, with inflation projected to average 3.9% in advanced economies and 5.9% in developing economies. Oil prices nearly doubled in the second half of 2021, creating a critical catalyst for inflation throughout the world, particularly in Europe. The IMF projects fossil fuel prices will continue to escalate in 2022, with oil prices rising 12% and natural gas prices rising 58%. These increases are significantly lower than what transpired in the second half of 2021, contributing to the moderation of inflation levels in 2022. Supply chain bottlenecks also contributed to rising prices in 2021, with the IMF estimating that these logistic issues decreased global GDP growth by 0.5-1% and increased inflation levels globally by 1%. Although global supply chain congestions are expected to subside sometime in 2022, the longer they persist, the more they will contribute to surging product prices and, therefore, inflation. Rising inflation levels have caused the Federal Reserve to announce intentions to tighten monetary policy in 2022, with the tapering of asset purchases and the increases of interest rates by 75-100 basis points by the end of 2022. These moves are expected to put pressure on the currencies of many developing economies and countries with high foreign currency debt.

Although COVID-19 had begun to subside in the second half of 2021, with daily deaths from the virus decreasing from 10,000 in August to 7,000 in October, the Omicron variant could potentially disrupt this trend. The Omicron variant appears to be more transmissible but less severe than the Delta variant. Still, the effect of the Omicron variant on global deaths and hospitalizations is unknown. The IMF's global economic growth projections assume that COVID-19 cases, hospitalizations, and deaths will gradually decline throughout 2022 in most countries with increasing vaccination rates. More specifically, the hindrances caused by the Omicron variant, such as increased hospitalizations and social distancing restrictions, are forecasted to decrease global economic growth in the first quarter of 2022, with these effects fading in the second quarter of 2022 and beyond.

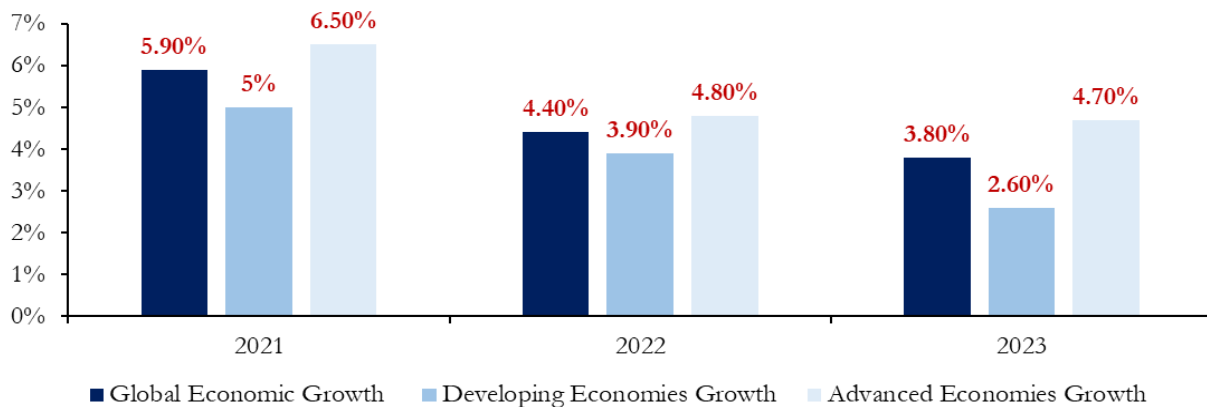

Figure 8: IMF Gross Domestic Product Growth Estimates
Source: International Monetary Fund (IMF)

S&P 500 Outlook & Fundamentals

S&P 500 Outlook

Just as we watched COVID-19 batter economies, we now observe new global factors, such as the Russian invasion of Ukraine and rising inflation, heavily impacting the world economies. Investors turn to the S&P 500 Index to examine how these factors affect markets and judge how Wall Street will react to them. The consensus on the Street is that the S&P 500 will see a price increase of 16.8% over the next 12 months. This is based on the median target price estimates for all companies within the S&P 500 Index as of March 14, 2022. The bottom-up target price for the index is 5,278.60 based on company-level estimates submitted by industry analysts. Several factors are to be considered when understanding this valuation. In early February, the Street consensus was slashed down to 4,900 points from 5,100 points following uncertainty regarding the path of inflation and Fed policy. Initially, many expected around seven rate hikes by the Federal Reserve this year; however, following Russia's invasion of Ukraine, there has been too much uncertainty surrounding the geopolitical tension's effects on Fed policy to implement immediate rate hikes. Regardless, strong expected price increases in the Communication Services, Consumer Discretionary, and Information Technology sectors are driving upside, with these sectors having the largest differences to date between their bottom-up target price and the closing price on March 24. Communications Services is expected to see a price increase of 27.9%, Consumer Discretionary is expecting a 21.1% increase, and Technology is expecting a 19.9% increase. The sectors expecting the smallest price increases are Energy at 4.5% and Utilities at 5.0%. It is apparent that the Street is expecting the Fed to adjust policy in response to market turbulence caused by the Ukraine-Russia conflict and rising inflation. Consensus on the Street is also that inflation will decelerate but remain high. Rising corporate bond yields and a strengthening dollar may underlie this deceleration, but strong corporate profits are needed to remain at manageable levels. There are 10,785 ratings of individual stocks in the S&P 500 Index of which 56.8% are buy ratings, 37.2% hold ratings, and 6.0% sell ratings. Analysts are most optimistic about Energy (67%), Communications Services (62%), and Information Technology (62%), as

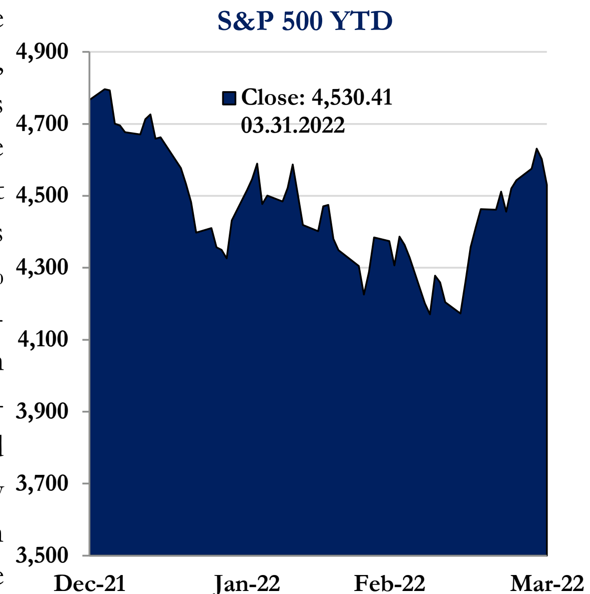

Figure 9: S&P 500 Price Index
Source: FactSet

S&P 500 Outlook & Fundamentals

these sectors have the highest percentages of buy ratings. Consumer Staples (42%) has the lowest percentage of buy ratings and also has the highest percentage of hold (48%) and sell (10%) ratings. The target price of 5,270 for the S&P 500 Index is attainable, but the road to get there may not be easy as it will require careful action by the Federal Reserve and investors to endure market uncertainty regarding global macroeconomic conditions.

Earnings

In Q4 of 2021, approximately 76% of S&P 500 companies reported a positive EPS surprise, and 78% reported a positive revenue surprise, despite the fact that 57% of S&P 500 companies had provided negative EPS guidance for Q4, the highest number since Q1 of 2020. The blended earnings growth rate for the S&P 500 in Q4 of 2021 came in at 31%, marking the fourth straight quarter of growth above 30%. Leading the charge with the highest earnings growth was the Industrials sector at 94%. Positive earnings surprises in the Consumer Discretionary, Information Technology, Healthcare, and Financials sectors were the top contributors to the overall increase in earnings in Q4. A hot topic of that quarter was the multitude of supply chain disruptions that caused production bottlenecks across many industries, especially within automobile and semiconductor businesses. The term "supply chain" was mentioned at least once in 341 S&P 500 companies' earnings calls from December 15 through February 28.

For the first quarter of 2022, the estimated earnings growth rate for the S&P 500 is 4.8%. If this is realized, it will mark the lowest earnings growth rate since the 3.8% reported for the fourth quarter of 2020. Also, for Q1 2022, 66 S&P 500 companies have issued negative EPS guidance, and 29 have issued positive. Thus far, only 13 companies have reported actual results, with eight S&P 500 companies reporting a positive EPS surprise and ten companies reporting a positive revenue surprise.

Valuation

With rising long-term yields, a continued storyline this semester, and the expectation that the Fed will increase interest rates this summer, there have been multiple contractions in the overall market relative to recent pandemic highs. The 10-Year Treasury Note has increased 82 bps YTD. It sits at 245 bps, sinking S&P 500 multiples to a pre-pandemic level of 21.1x price-to-earnings (~9 turns lower than pandemic highs) and dropping higher-priced growth sectors such as Consumer Discretionary (~14.5 turns lower) even further. Geopolitical issues, such as Russia's invasion of Ukraine and world powers' response to the actions of the oil giant, have exacerbated uncertainties, leading to worries of even higher commodity prices affecting companies' ability to generate profit. Valuation analysis will remain crucial in the months ahead as markets tolerate both persistently high inflation numbers and the Fed's playbook in dealing with current economic conditions. As a result, the Flyer Investments Team emphasizes valuation metrics that measure a firm's ability to generate earnings power and leverage operations to improve cash flow.

Valuation Matrix	March 31, 2022	3 Month Median	5-Year Median	10-Year Median	20-Year Median	Current vs 10-Year Median Difference	Premium (Discount) vs 10-Year Median
S&P 500 (LTM)							
P/E	**21.6x**	21.6x	20.8x	18.6x	17.3x	3.0x	16.4%
P/B	**4.5x**	4.5x	3.5x	3.1x	2.9x	1.4x	45.9%
EV/Sales	**3.4x**	3.4x	2.7x	2.4x	1.9x	1.0x	40.9%
EV/EBITDA	**16.1x**	16.0x	13.6x	12.5x	10.7x	3.6x	28.8%
S&P 500 Sectors (Forward P/E)							
Energy	**11.4x**	12.4x	16.9x	16.6x	13.2x	(5.2x)	(31.4%)
Materials	**15.8x**	15.6x	17.0x	16.0x	15.2x	(0.2x)	(1.5%)
Industrials	**20.0x**	19.8x	18.0x	16.0x	15.7x	4.0x	25.1%
Consumer Discretionary	**29.5x**	28.8x	23.8x	20.9x	17.5x	8.7x	41.6%
Consumer Staples	**21.2x**	21.1x	20.0x	19.4x	17.4x	1.8x	9.4%
Healthcare	**16.5x**	16.0x	16.4x	16.1x	16.0x	0.4x	2.5%
Financials	**14.1x**	14.3x	13.6x	12.5x	12.2x	1.6x	12.4%
Technology	**24.4x**	24.2x	19.8x	16.4x	17.0x	8.0x	48.8%
Communication Services	**18.5x**	18.6x	20.2x	18.6x	17.9x	(0.2x)	(0.9%)
Utilities	**21.3x**	20.0x	18.5x	17.1x	14.9x	4.1x	24.1%
Real Estate	**22.0x**	21.5x	19.6x	18.3x	18.1x	3.7x	19.9%
Macroeconomic Enviroment							
10-Year US Treasury Yield (Nominal)	**2.32%**	1.94%	1.84%	2.18%	2.77%	0.1%	6.4%
Effective Federal Funds Rate	**0.33%**	0.08%	1.16%	0.15%	0.41%	0.2%	120.0%
Core CPI (YoY)*	**6.42%**	6.04%	2.13%	1.97%	2.00%	4.4%	225.5%

Data as of 03.31.2022 | Source: FactSet

** CPI Data as of 2.28.2022*

Figure 10: S&P 500 Price Valuation Matrix
Source: FactSet

Valuation

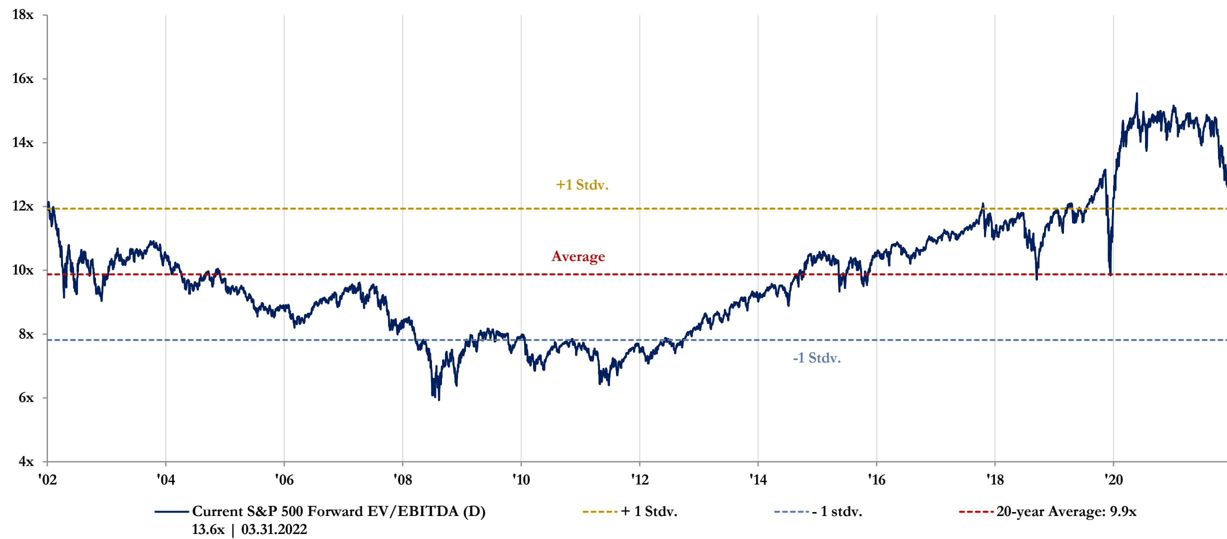

Figure 11: S&P 500 Forward EV/EBITDA
Source: FactSet

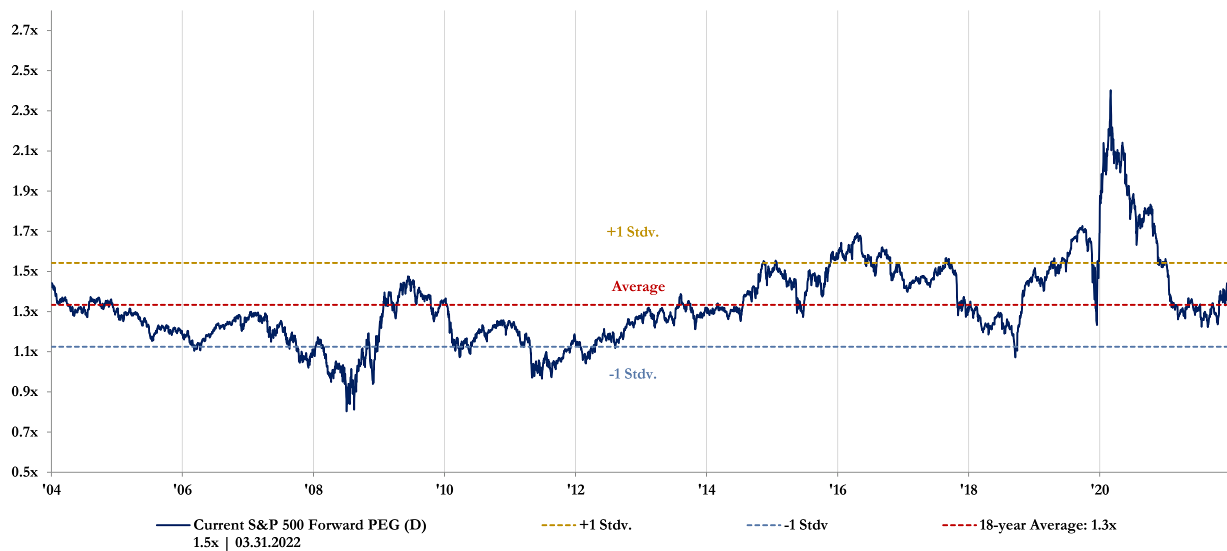

Figure 12: S&P 500 Forward P/E
Source: FactSet

Sector Positioning

The Russian invasion of Ukraine in late February, ongoing and rising geopolitical tensions, increasing signs of stagflation, tightening of financial conditions, and likely Federal Reserve interest rate hikes have clouded the Team's view on equity sectors. Thus, the Team feels it is prudent to maintain sector allocations in line with the overall market.

Information Technology

The Economic Analysis Team recommends a neutral weight position in the Information Technology sector relative to the S&P 500 Index for the upcoming semester. Long-term fundamentals--such as the continued rollout of 5G cellular networks, higher spending on technology infrastructure, overall strong balance sheets, and earnings growth potential with low funding costs--remain intact, making the sector very attractive. Counterbalancing strong fundamentals, however, overall investor optimism for the sector has stretched valuations beyond historical averages, and the ongoing semiconductor shortages have dramatically reduced the available supply of finished technology goods.

Health Care

The Economic Analysis Team recommends a neutral weight position in the Health Care sector relative to the S&P 500 Index for the upcoming semester. There are many factors that prove positive for the sector, such as its historically defensive nature in peaking economic growth environments, an aging global population and a growing middle class in emerging markets who are in high demand for drugs and medical treatments, and the resumption of elective care. There are still risks and negatives associated with the sector, however, such as the prospect of prescription drug price controls and regulations regarding anticompetitive contracting practices and the threat of new COVID-19 variants that will once again postpone elective medical care.

Financials

The Economic Analysis Team recommends a neutral weight position in the Financial sector relative to the S&P 500 Index for the upcoming semester. The sector has many favorable fundamental attributes, with economic growth, interest rates, and investor and consumer sentiment acting as drivers. While macro conditions remain strong, we have likely seen a peak in the growth rate for the economy, although rising long-term interest rates should aid in the expansion of the net interest margins for banks. Valuations remain relatively attractive as compared to other sectors, but forward earnings estimates have flattened out. If the Federal Reserve can tame inflation without inadvertently slowing down economic growth, interest rates and loan growth will likely translate to earnings and price increases.

Sector Positioning

Consumer Discretionary

The Economic Analysis Team recommends a neutral weight position in the Consumer Discretionary sector relative to the S&P 500 Index for the upcoming semester. With virtually all of the economy reopened, many of the beaten-up equities in the sector have recovered, such as those in the apparel and hotel industries. Long-term trends toward e-commerce platforms and electrical vehicle growth are likely to support the fundamentals in the space. However, similar to our thoughts from the previous semester, supply chain and labor shortages will continue to weigh heavily on companies' ability to meet demand. Additionally, valuations seem relatively stretched compared to historical averages.

Communication Services

The Economic Analysis Team recommends a neutral weight position in the Communication Services sector relative to the S&P 500 Index for the upcoming semester. Since the launch of the Communication Services sector in late 2018, the Team has consistently underweighted it relative to the S&P 500 Index due to a secular decline in "old media" and the shift away from traditional and cable T.V. The Team has come to realize that it is foolish to continue underweighting a sector composed of companies that are in the process of transitioning toward online mediums instead of relying on a dying business model. Despite the highly concentrated nature of the sector's market capitalization, the Team feels a neutral weight in the sector is warranted.

Industrials

The Economic Analysis Team recommends a neutral weight position in the Industrials sector relative to the S&P 500 Index for the upcoming semester. A few positives for the sector include the continued introduction of a new CAPEX cycle, solid fundamentals and marginal increases in earnings expectations, and strong domestic and global trade that will aid in transportation demand. However, the sector faces negatives such as peaking economic growth, historically a headwind for this cyclical sector, and higher fuel costs for the transportation and air freight industries.

Consumer Staples

The Economic Analysis Team recommends a neutral weight position in the Consumer Staples sector relative to the S&P 500 Index for the upcoming semester. While the sector tends to outperform during the late stages of the business cycle due to its defensive nature and stable earnings power, many companies within the sector are currently facing higher input costs. Any inability to pass those along to consumers will cause profit margins to contract.

Sector Positioning

Materials

The Economic Analysis Team recommends a neutral weight in the Materials sector relative to the S&P 500 Index for the upcoming semester. The sector typically performs well during the expansion stages of the business cycle since economic growth and spending support the demand for raw materials and chemicals. Although prices for major metals and chemicals remain elevated amid strong demand and supply constraints, global economic growth is at risk of easing amid peaking U.S. growth and tighter financial conditions resulting from the threat of inflation and the Russia/ Ukraine war.

Energy

The Economic Analysis Team recommends a neutral weight in the Energy sector relative to the S&P 500 Index for the upcoming semester. Amid the ongoing global energy crisis and the Russia/ Ukraine war, the Energy sector has outperformed the overall market, with supply shortages driving up the price of a barrel of oil past $100 in March of 2022. Although this is an excellent environment for Oil & Gas operators, the Flyer Investments Fund is precluded from owing ~90% of the companies within the sector in keeping with the University's prohibition against investing in the fossil fuel industry.

Real Estate

The Economic Analysis Team recommends a neutral weight in the Real Estate sector relative to the S&P 500 Index for the upcoming semester. Components of this sector are very sensitive to increasing interest rates and have historically underperformed most other sectors when the Fed raised rates, as illustrated in the aftermath of the 2008 Financial Crisis. However, in counterbalance to this risk, certain REITs can act as a strategic hedge against inflation since they can quickly increase their revenue streams to adapt to an inflationary environment.

Utilities

The Economic Analysis Team recommends a neutral weight in the Utilities sector relative to the S&P 500 Index for the upcoming semester. This sector performs relatively better when concerns about slowing economic growth resurface and underperform when those worries fade. Recent signs of peaking economic growth provide a tailwind for this sector. However, expectations of higher short- and long-term interest rates counterbalance the defensive attributes somewhat since the sector acts as a bond proxy.