2022 2Q OUTLOOK SUMMARY

SOFTENING EXPECTATIONS

The investment environment to begin the year was clouded by uncertainties tied to the pandemic, inflation, and the prospect of slowing growth on the back of the Federal Reserve's plans for policy tightening. The military conflict in Ukraine added a dangerous new dimension of uncertainty, leaving a humanitarian crisis and tragedy in its wake. For investors, it's a difficult environment to navigate, and the following are some diverse perspectives from across PGIM's autonomous asset management businesses, highlighting the opportunities available in such a tumultuous climate, along with a reminder about some of the risks.

- **A softening expansion:** The US economy remains healthy and should continue to generate stronger growth than other developed regions. However, with interest rates moving higher to combat persistent inflationary pressures, the pace of US growth is set to moderate, even before factoring in the effects of the war in Ukraine. Signs of cooling have begun to emerge in the level of mortgage applications, housing turnover, and used car prices. With the fourth quarter earnings season coming to an end, it is clear that reported profit growth remained robust through 2021 and generally in line with forecasts. Our forecasts for 2022 suggest a meaningful moderation in US profit growth, following last year's dynamic rebound from the worst effects of the pandemic. We also anticipate a passing of the baton from outsized demand for goods to services, particularly travel and leisure spending. Trends to date remain supportive of these expectations.

- **The US isn't cheap:** Equity markets corrected during the quarter, with some market declines meeting the technical definition of a bear market. Assuming the war with Russia does not extend beyond Ukraine's borders, we expect equity markets to recover lost ground, but calendar-year returns are likely to be weak, though positive, in 2022. Moves in bond markets were also substantial, with yields repricing upward given the significant change in central bank policy expectations, particularly for the Fed. In an environment of rising interest rates, stocks have experienced notable multiple compression from 2020's elevated levels. Some markets look very attractively valued (e.g. Latin America and UK), with forward PE ratios significantly below their 10-year averages. The US market, however, still trades at an above-average valuation multiple.

- **Splintered global growth:** The world's largest economies face vastly different conditions. The US is experiencing above-trend growth and uncomfortably high inflation, while China lumbers under COVID lockdowns and a real estate overhang as Europe confronts the threat of an energy embargo that could almost certainly push the economy into recession and/or stagflation. Central banks around the world stand at different phases of removing their virus-induced policy accommodation. The slow movers, such as the ECB and the Fed, are just wrapping up QE and starting to tighten policy, respectively, while the faster moving EM countries in Eastern Europe and Latin America remain way ahead in taking action to address inflation. The unpredictable course of the Russia/Ukraine conflict, the global response, and the associated impacts on the world's geopolitical order and financial system will continue to drive market dynamics. The disconcerting backdrop may render beta an ineffective generator of returns, reinforcing the need for an expanded micro focus on bottom-up research and relative-value positioning as a reliable way to generate alpha.

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