CONGRESS ASSET MANAGEMENT COMPANY

A STORMY SEPTEMBER FOR FINANCIAL MARKETS

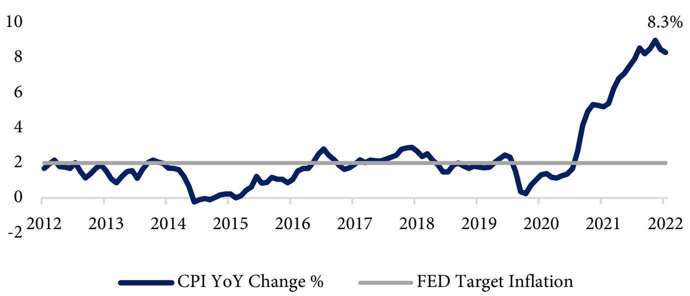
September 2022

The financial markets enjoyed a relatively quiet summer. September has not been as kind. Two reports from last week capture the concerns. First, the August Consumer Price Index, released on September 13, showed that YoY inflation increased 8.3%, despite gasoline prices falling 10.6%. Inflation remains higher than most anticipated and, importantly, has continued to broaden out – electricity prices are up 15.8%, household furnishing 10.6%, and shelter 6.2%. Shelter is particularly concerning given price increases tend to be "stickier" than other categories.

Two days later FedEx issued its preliminary August earnings statement, warning "Global volumes declined as macroeconomic trends significantly worsened later in the quarter, both internationally and in the U.S. We are swiftly addressing these headwinds, but given the speed at which conditions shifted, first quarter results are below our expectations." While some of FedEx's issues are self-induced, as one of the world's largest shippers, FedEx has unique insights into the global economy.

Consumer Price Index - Year over Year Change %

August 2012-August 2022



Source: US Bureau of Labor Statistics

Investors, politicians, businesses and consumers have come to rely on the Federal Reserve (Fed) to control inflation. Since the 1980's the Fed generally has been ahead of the game. That is not the case anymore - inflation is more widespread and entrenched than it has been in decades. To offset inflation the Fed has raised the short-term rates it controls and has begun to shrink its bond holdings. Both actions should raise market interest rates, indirectly slowing economic growth.

And that, in a nutshell, is the problem. The Fed is raising rates to offset inflation (with the intended consequence of slowing the economy) at the same time a bellwether company like FedEx is warning of a global slowdown.

Inflation presents a serious risk to long-term prosperity, so the Fed's aggressiveness is appropriate. But official inflation measures are likely to remain elevated until next year. Every inflation data point for the remainder of 2022, whether positive or negative, will carry heightened importance for both the stock and bond market.

2022 has been extremely volatile. In our view, the worst for bonds has past. While the ten-year U.S. Treasury Note yield currently trades near 3.5%, up from 1.5% earlier in the year, we expect more muted movements going forward. Stocks are likely to remain volatile, dependent on both inflation and growth. The path here is less certain but stocks are cheaper now than they have been and the outlook for earnings growth remains positive, in spite of FedEx's comments.

In the current environment, three things have an outsized impact on stock market volatility: first, the strength of the consumer measured by employment opportunities, compensation levels and consumer spending metrics; second, corporate earnings; and third, the level of market interest rates as measured by the ten-year U.S. Treasury Note.

We are all re-learning how inflation affects spending, investment, and growth. However, companies and consumers adapt quickly to new stimuli, presenting opportunities for growth after periods of market turmoil. In spite of the current travails, we believe U.S. equities are attractive on a longer-term basis.

Investment Oversight Committee
Daniel A. Lagan, CFA, President & CIO

CONGRESS ASSET MANAGEMENT COMPANY

2 Seaport Lane Boston MA 02210 800.234.4516 www.congressasset.com