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2022 Midyear Market Outlook

Transitioning to a New Paradigm

Four Themes to Follow

1. Navigating Challenging Currents
2. Fundamentals Matter
3. Flexible Fixed Income
4. Managing Through Geopolitical Risks

1 Navigating Challenging Currents

For years markets have experienced historically low volatility and ample liquidity.

In 2022, that's changed: **Inflation is now a central factor** determining where markets might go from here.

3 ways inflation can threaten economic growth:

- Less consumer spending due to higher prices
- Forced interest rate hikes
- Lower corporate earnings due to higher input costs

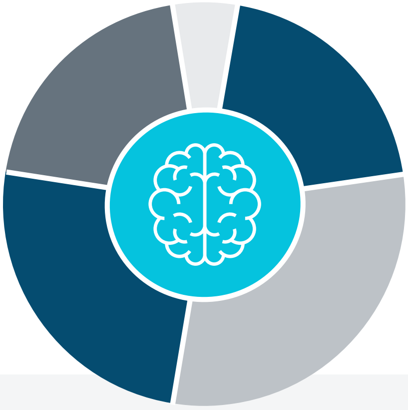
Key Takeaway

Understanding your risk tolerance, staying active, and remaining diversified could be critical to navigating these challenging currents.

> We're going through a regime shift from low growth, low inflation, and low rates to something that looks different. Fortunes can be made and lost during regime shifts.
>
> **— Sébastien Page**
> Head of Multi-Asset
> and Chief Investment Officer

2 Fundamentals Matter

A potential shift in market leadership means that **fundamentals are likely to matter more.**



We believe it's wise to **diversify intelligently, avoiding extreme allocations.**

Tactical Opportunities

- Expect less tolerance for unprofitable, speculative stocks.
- Dividends and earnings growth could become more critical to equity performance.
- A deep understanding of companies and industries could be key to consistently strong performance.

A risk to watch: Rising interest rates have already punished equity valuations. The question now is whether an earnings slowdown may be the next shoe to drop.

Key Takeaway

Cap-weighted indexes may be poorly positioned for structural change, making skilled active management a critical tool for identifying risks and opportunities.

"In volatile markets, active management can be your friend."

— **Justin Thomson**
Head of International Equity
and Chief Investment Officer

3 Flexible Fixed Income

U.S. Treasuries and other sovereign bonds have been a poor diversifier of equity risk, suggesting investors may need a more **flexible approach to fixed income** allocations.

How Do We Navigate This Shift?

- Consider your time horizon and your position on the yield curve. (For example, two-year yields have performed very differently than 10-year yields.)
- Actively manage duration.
- Globally diversify to mitigate interest rate risk.
- Utilie liquidity to stay nimble.
- Consider opportunities within credit sectors, particularly high yield bonds.

Key Takeaway

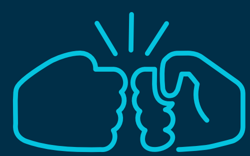
We believe fixed income investors could be rewarded in 2022 for being nimble.

> This may be the best point to buy bonds that we've seen for several years. Valuation is much more attractive than it has been.
>
> **— Arif Husain**
> Head of International Fixed Income and Chief Investment Officer

4 Managing Through Geopolitical Risks

New risks for global markets have emerged, triggered by geopolitical **shocks to agriculture, digital security, defense, and energy**

The Ukraine conflict: Potential global fallout



Shorter-term

- Profound humanitarian tragedy
- Higher food prices
- Market volatility

Longer-term

- Sanctions could disrupt a broad range of industries from energy to agriculture to the international payments system.
- The push for energy independence could accelerate the green transition.
- Greater potential for conflict between NATO and non-NATO nations.

Key Takeaway

The war has worsened global inflation, highlighted energy security, and created agricultural shortages. Elections in a number of countries and China's upcoming Party Congress also could have significant market implications.

> Some countries may be looking at [financial sanctions against Russia] and thinking, "We need to find another way of moving our money and transacting on a global basis."
>
> — **Arif Husain**
> Head of International Fixed Income and Chief Investment Officer

Take the Next Step

Get strategies to help you respond to these investment themes. Speak to your financial adviser for more information or call your T. Rowe Price Relationship Manager.

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