

VITAL SIGNS

The State of the Markets

ECONOMY

Consumer sentiment lowest since 2011. More consumers mentioned reduced living standards due to rising inflation than at any other time, except during the two worst recessions in the past fifty years. Most prominent on the mind of consumers is the rising price of gasoline. According to AAA, U.S. gasoline prices increased 24% to \$4.33 per gallon compared with a month ago (February). Further increases are likely after the ban on imports of Russian oil into the United States.

Inflation rate highest since 1981. Current price increases are running at the fastest pace in roughly 40 years. The consumer price index, which has steadily increased for each of the last six months, rose to 8.6% annual rate in March fueled primarily by rising prices in food and gasoline. Supply constraints related to geopolitical unrest and unprecedented spending of more than \$10 trillion in fiscal and monetary stimulus are the main drivers behind this inflation surge.

Unemployment close to pre-pandemic rate. The U.S. economy added 431K jobs in March (1.7M jobs added in 1Q22) pushing the unemployment rate down to 3.6%. This is close to the pre-pandemic rate of 3.5% achieved in February 2020. Unsurprisingly, leisure and hospitality led the payroll gains, followed by professional and business services and retail trade.

Indicator	Latest Available Data (eop)	Change			
		Average Last 5 Years	YoY	YTD	QoQ
Consumer Sentiment	● 59.4 Mar	↘	↓	↓	↓
Inflation (CPI)	● 8.6% Mar	↑	↑	↗	↗
Unemployment	● 3.6% Mar	→	↓	↓	↓

CAPITAL MARKETS

The S&P 500 index declined 4.9% in 1Q22. Equities closed their first losing quarter in two years with rising inflation and the war in Ukraine dampening investors' mood. The start of a rate hiking cycle from the Fed also contributed to the decline. Rising rates have an effect on valuations because stocks are valued based on expectations of their future cash flows. Higher interest rates affect the cost of debt thus impacting the rate at which cash flows are discounted to a present value.

A hawkish Fed. The Federal Reserve announced in mid-March that it is raising the Fed Funds rate by 0.25% with at least six more hikes forecasted later this year. Raising interest rates is aimed at reducing demand. However, current price pressures, particularly with food and gasoline, are due largely to supply issues rather than excess demand. Hence, it will be harder for interest rates to have the desired effect of reducing inflation.

U.S. VC activity is recalibrating. Last quarter, VC investments were down 28% compared to 4Q21 (about flat when compared to 1Q21). Public market performance and economic uncertainty caused a pause in VC activity in 1Q22. Investors are seeing initial downward corrections in the market pricing, valuation, and the speed at which deals are closing. In terms of fundraising, VC funds were able to raise \$73.8B in 1Q22. This represents 56% of the \$131.5B raised in 2021.

S&P 500	● 4,391 Mar	↗	↗	↓	↓
10-yr. T-Bond Rates	● 2.1% Mar	→	↗	↑	↑
VC - Investments (\$bn)	● 70.7 1Q22	→	→	↓	↓
VC - Exits (\$bn)	● 31.6 1Q22	→	↘	↓	↓
VC - Fundraising (\$bn)	● 73.8 1Q22	→	↑	↑	↑

M&A ACTIVITY

U.S. M&A down 17% in 1Q22. Although the first quarter of a year is typically slow for M&A, market instability and interest rate hikes have compounded the situation in 2022. According to FactSet, U.S. M&A value dropped 17% from 4Q21 and 19% from a year ago. Dealmaking in the technology and real estate sectors led the way while healthcare activity, which typically accounts for a big share of deals, dropped by more than 50%.

M&A multiples continued to decline in 1Q22. The median EBITDA multiple fell 18% to 6.8x in 1Q22 from 8.0x reached at the end of 2021. On an annual basis, deal multiples are down 31%. Deal multiples are reflecting the expectation of rising inflation and higher interest rates, which in turn will affect corporate cash flows and lead to lower valuations.

U.S. M&A (\$bn)	● 127.8 Mar	↗	↘	↘	↘
M&A EBITDA Multiples	● 6.8x 1Q22	↘	↓	↓	↓