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MARKET REVIEW
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TRUST COMPANY of NORTH CAROLINA

CHINA COVID-19 LOCKDOWNS

After a strong start to the year, China's economy narrowly escaped a contraction in the second quarter as strict COVID-19 lockdown measures disrupted manufacturing production, consumer spending, and global trade. In contrast to the living with COVID-19 strategy of many developed countries, China has adhered to a Zero-COVID strategy where the country attempts to eliminate transmission of the virus and achieve zero new infections before returning to normal social and economic activities. China's strategy includes combatting new virus cases with a barrage of mass testing, contact tracing, travel restrictions, and in some cases banning people from leaving their homes. In one of the more extreme examples, China's largest city and financial and trading hub, Shanghai, experienced a two-month citywide lockdown in April and May. Almost all of Shanghai's 25 million residents were under some form of lockdown and most residents were not allowed to leave their homes. The more contagious Omicron variant has led to more frequent flare ups in virus cases in China which has caused some areas to endure multiple lockdowns this year including the technology manufacturing hub of Shenzhen.

The public backlash and economic fallout from stringent lockdowns such as the one in Shanghai appear to have led to China tweaking its Zero-COVID policy. Recent virus outbreaks in several cities were met with partial lockdowns targeting specific areas of cities or even individual housing complexes, rather than citywide lockdowns. Additionally, many manufacturing facilities have remained somewhat operational using closed loop systems. These systems attempt to segregate factories from surrounding areas by requiring employees to live and work on-site. Shenzhen, which produces a significant amount of the world's electronics, recently ended its seemingly successful closed loop system that included 100 large companies including iPhone assembler Foxconn. Skeptics of this strategy observe that many manufacturers do not have enough capacity to host their entire workforce.

Some market commentators have pointed to the lower efficacy of vaccines developed in China and the country's unwillingness to use vaccines from foreign countries as potential reasons behind President Xi Jinping's devotion to the Zero-COVID strategy. Clinical trials for China's inactivated-virus vaccines showed they are less effective at preventing infections and protecting against severe symptoms than the Pfizer-BioNTech and Moderna mRNA vaccines. China's government previously said production of its domestic mRNA vaccine would start by August 2021. However, Bloomberg's equity analysts believe China's mRNA vaccine is unlikely to be released before the end of 2022 because clinical trials have been disappointing and it caused more side effects compared to their inactivated-virus vaccines. Optimism for importing foreign made mRNA vaccines has also faded. Two Chinese companies reached an agreement with Pfizer in late 2020 to distribute Pfizer's mRNA vaccine in China, but the country's drug regulator has not granted approval yet. Yanzhong Huang, a global health specialist at the New York-based think tank Council on Foreign Relations, suspects the approval delay is likely due to political and nationalist reasons since Communist Party officials have touted self-reliance in fighting the virus.

ECONOMIC IMPACT

China's economy has taken an enormous hit from the Zero-COVID lockdown policies with some measures of economic activity hitting their lowest levels since the onset of the pandemic. Second quarter economic growth slowed to a meager 0.4% from 4.8% growth in the first quarter. That was the second worst quarter for GDP growth on record going back to the early 1990s, behind the first quarter of 2020. The two-month lockdown in Shanghai extracted a particularly heavy economic toll as the economy of the country's largest city contracted nearly 14% in the second quarter. Some areas of Shanghai's economy came to a complete halt, including the automotive retail industry which saw zero vehicle sales in April, compared to 26,311 sales in April last year.

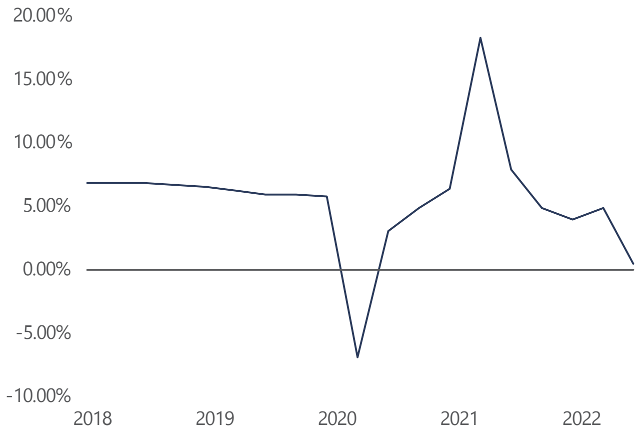
The sharp slowdown in economic growth was accompanied by a rise in the nationwide unemployment rate to 6.1% in April, which declined to 5.5% in June. The youth unemployment rate, covering workers aged 16 to 24, spiked to a record 19.3% in June from 14.3% in December. Fears are growing that youth unemployment may worsen as a record 10.76 million university students graduate this year and enter the weak labor market.

Commitment to the Zero-COVID strategy likely means China will miss its 5.5% economic growth target this year by the largest margin since 1998. China's Politburo, the Communist Party's top policymaking body, appears to have eased its

CHART 1

CHINA LOCKDOWN SLOWS THE ECONOMY

CHINA GDP GROWTH YOY



Source: Bloomberg.
Past performance does not guarantee future results.

CHART 2

RISE IN CHINA UNEMPLOYMENT AMID LOCKDOWNS

CHINA NATIONAL AND YOUTH UNEMPLOYMENT RATES

Source: Bloomberg.
Past performance does not guarantee future results.

commitment to this year's growth target. Local government officials have been told the growth target will not be used to evaluate their performance and there will be no penalties for failing to achieve policymakers' targets. Economists have steadily reduced their China GDP growth forecast for this year to 3.9% from 5.2% at the start of the year, according to the latest Bloomberg survey of over 70 economists. Some forecasters believe sporadic virus outbreaks combined with fresh lockdowns could pose a challenge for China's economic rebound in the second half of the year. The country's significant real estate slump poses another threat to the prospects of an economic rebound. We plan to revisit the real estate slump topic in a separate publication later this year.

GLOBAL IMPACT

The COVID-19 restrictions in China sent ripples through the global supply chain as idled factories, trucking shortages, and reduced capacity at ports disrupted the supply of raw materials, components, and finished products. According to data from the World Trade Organization and United Nations, China accounts for 15% of global exports and 29% of global manufacturing output, respectively. Supply chain disruptions in combination with weaker consumer demand in China have weighed on sales of multinational companies such as Apple and Tesla. The American Chamber of Commerce in China said a survey among its members, which includes many companies in the S&P 500 index, showed that 58% expect lower revenue this year due to China's lockdowns.

2022 NATIONAL PARTY CONGRESS

The direction of China's policies will likely remain somewhat uncertain until after this fall's National People's Congress of the People's Republic of China. The National Party Congress convenes every five years and elects the new members of the 376-member Central Committee. Candidates for the Central Committee are selected by the 25-member Politburo and seven-member Politburo Standing Committee (PSC). The new Central Committee, in turn, elects the new Politburo, PSC, and General Secretary (Communist Party leader, currently President Xi Jinping). The average turnover rate among Central Committee members during congress elections has been high at 62%. The Politburo's significant influence over the election process has historically enabled top leaders to consolidate power by promoting their supporters to key positions.

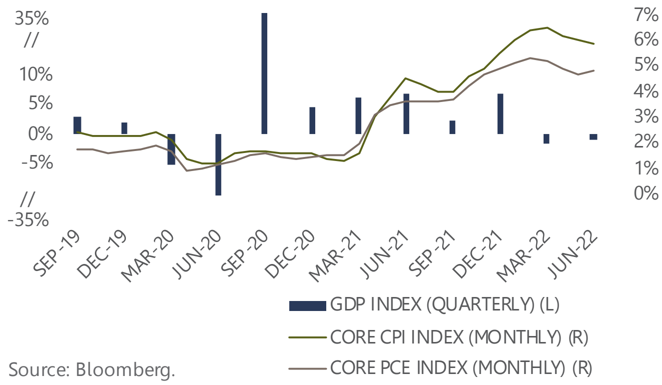
The National Congress held this fall marks a critical juncture for the Communist Party since President Xi Jinping will likely secure a third five-year term. Xi was originally supposed to step down this year due to the constitution's two-term limit, but his consolidation of power over the last decade enabled him to modify the constitution to remove the term limit. Global investment research firm BCA Research believes Xi will likely start his third term by easing fiscal, regulatory, and social policy to support the economy. However, BCA cautions that policy easing may be temporary, and the country will revert to the current leadership's long-term policy trajectory of using nationalism and hawkish foreign policies to boost China's self-sufficiency and global influence.

CONCLUSION

The potential for China's Zero-COVID strategy to cause another economic slowdown and hamper global supply chains remains a risk for the rest of the year. The country continues to implement rolling lockdowns to address sporadic virus outbreaks. Nomura's Chief Economist, Ting Lu, estimates that 41 cities with 264 million residents were undergoing full or partial lockdowns as of late July. The upcoming National Party Congress later this year adds another element of uncertainty since the country's policies could shift post-election. Widespread adoption of an effective mRNA vaccine would likely help the country move past the use of stringent lockdowns, although that appears to be a low probability outcome for the next several months.

ECONOMY

GDP AND CONSUMER PRICES
SEPTEMBER 2019 THROUGH JULY 2022



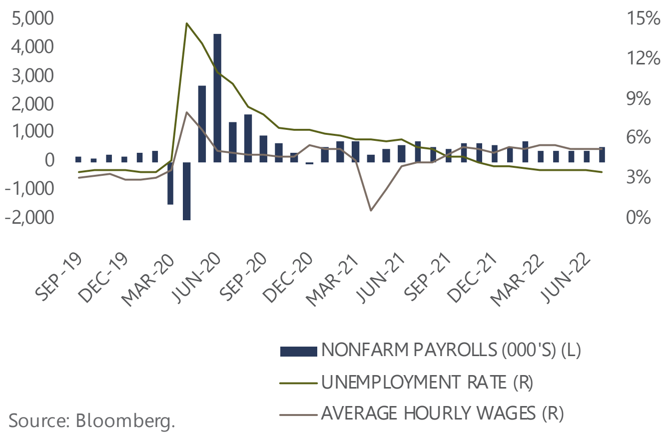
Source: Bloomberg.

The U.S. economy contracted at a 0.9% annualized rate in the second quarter, well below the median Bloomberg estimate of 0.4% growth. Despite the second straight quarter of negative growth (-1.6% in Q1), many commentators think the domestic economy is amid a mid-cycle slowdown rather than a sharp recession.

The core consumer price index (CPI) climbed 5.9% in July from a year prior and headline CPI was up 8.5% over the last twelve months. The Federal Reserve has been attempting to slow an overheated labor market and quell excess inflation with a series of aggressive rate hikes in recent months.

The core personal consumption expenditures (PCE) index, Fed policymakers' preferred inflation gauge, rose at a 4.8% year-over-year clip in June, down from a 39-year high of 5.4% in February.

LABOR MARKET
JULY 2019 THROUGH JULY 2022



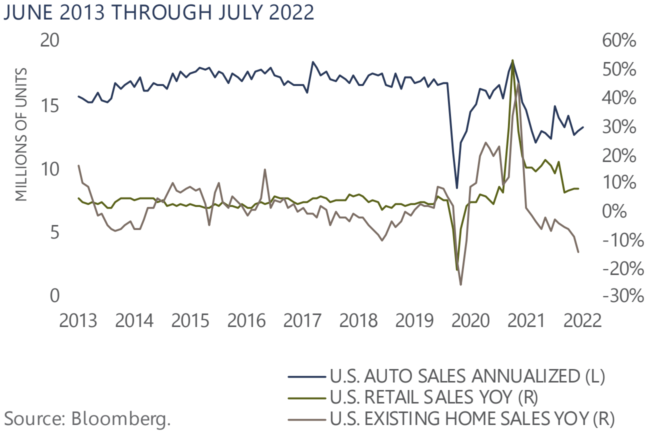
Source: Bloomberg.

Employment in the U.S. surged in July as nonfarm payrolls rose 528,000, more than double the estimate of 250,000. Job gains were widespread across sectors, with leisure and hospitality adding the most new positions.

The unemployment rate ticked down to 3.5% from 3.6% the month prior. Strong job growth over the last two years has brought both the unemployment rate and total nonfarm payrolls back to their pre-pandemic levels.

The evidence of continued labor market strength seen in the July payrolls report should alleviate fears the U.S. economy is on the verge of falling into a sharp recession, but it may also allow the Federal Reserve to proceed with its aggressive tightening campaign.

HOUSING, AUTO AND RETAIL SALES
JUNE 2013 THROUGH JULY 2022



Source: Bloomberg.

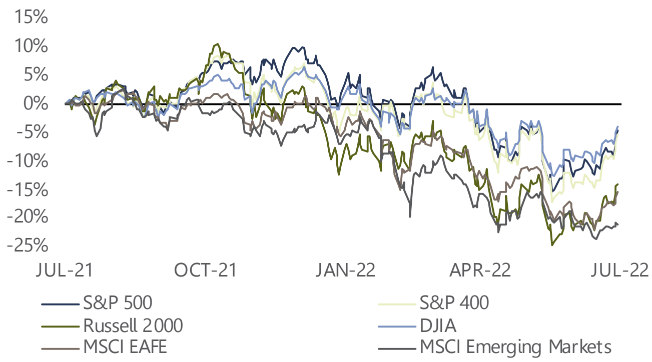
U.S. vehicle sales rebounded 2.5% in July to a seasonally adjusted annualized rate of 13.35 million units from the June reading of 13.00 million units. Although signs of a rebound are emerging, higher prices and low incentive offers have made it more difficult to purchase a new vehicle.

In June, retail sales increased 8.4% from a year prior as consumers continued to find ways to cope with surging prices. Services spending offset lower goods consumption, while higher prices for gas and groceries weighed on real spending.

Sales of previously owned homes fell for the fifth straight month to a two-year low in June, as higher borrowing costs and limited housing supply weighed on affordability. Existing home sales were down 5.4% in June from the prior month.

EQUITY

TRAILING 12-MONTH EQUITY RETURNS
PRICE APPRECIATION, JULY 2021 THROUGH JULY 2022



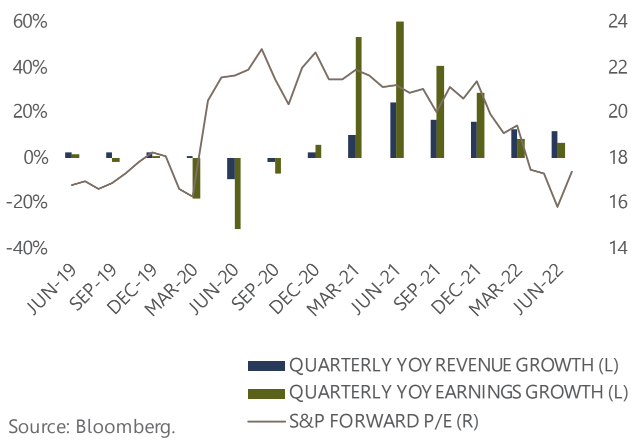
Source: Bloomberg. Past performance is no guarantee of future results.

U.S. stocks rebounded sharply in July as second quarter earnings results were better than feared. Stocks also benefitted from hopes that the slowing economy might lead to a less aggressive Fed rate hike cycle.

The S&P 500 gained 9.22% in the month, clawing back a large part of its losses this year. July was the index's strongest month since November 2020 when the COVID-19 vaccines' positive clinical trial data was first announced.

The MSCI Emerging Market index posted a negative 0.16% return in July. The decline was driven by the MSCI China index falling 9.44% in the month. The rising number of COVID-19 cases in China fueled fears that lockdowns could return.

S&P 500 YOY EARNINGS & REVENUE GROWTH
BY QUARTER, JUNE 2019 THROUGH JULY 2022



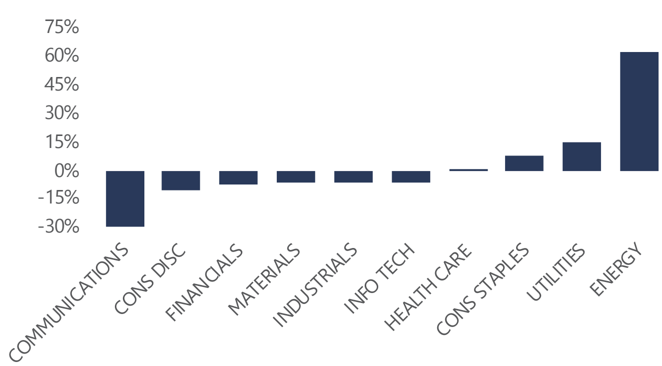
Source: Bloomberg.

S&P 500 companies are on track for 8.7% earnings growth in the second quarter, the weakest since the fourth quarter of 2020. Earnings have been well received in aggregate, however, since they are outpacing analysts' forecast for 4.1% growth.

S&P 500 earnings received a large boost from the energy sector, while earnings contractions in financials and technology were drags. Index-level net income margin of 13.2% is below analysts' forecast for 13.9% and is down for a second consecutive quarter.

S&P 500 revenues are on pace for 14.8% growth compared to analysts' forecast for 9.9% growth. All 11 sectors have positive revenue growth, and four sectors have double-digit growth.

S&P 500 SECTORS 12-MONTH PRICE RETURNS
JULY 2021 THROUGH JULY 2022



Source: Bloomberg.

All S&P 500 sectors had positive returns in the month for the first time this year. Consumer discretionary and technology were the strongest sectors with double-digit returns. Higher growth stocks benefitted from lower interest rates and second quarter's earnings being more resilient than expected.

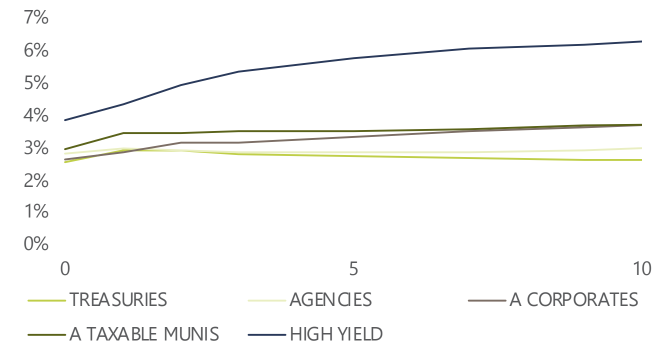
The energy sector posted a 9.72% return in the month, despite the price of West Texas Intermediate (WTI) crude oil falling 6.75%. The sector's strong performance was driven by better-than-expected second quarter earnings.

Defensive sectors posted more pedestrian performance in July with the consumer staples and health care sectors returning less than 4%.

FIXED INCOME

CURRENT YIELD CURVES

YIELD CURVES AS OF JULY 2022



Source: Bloomberg. Past performance is no guarantee of future results.

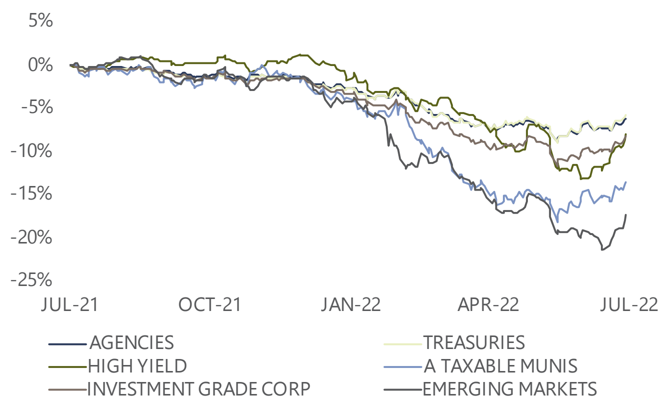
The 2-year-to-10-year portion of the U.S. Treasury curve bull-flattened in July in response to the steep trajectory of Fed rate hikes. The yield on the 2-year note dipped 0.08% to 2.87%, while the yield on the 10-year maturity declined 0.35% to 2.67%. The front end of the yield curve flattened dramatically as the 3-month Treasury bill yield climbed 0.69% to 2.32%

The 1-year, 2-year, and 5-year U.S. Treasury notes outyielded the 10-year maturity by 0.26%, 0.27% and 0.07% respectively on the final day of July. An inverted yield curve is atypical and frequently precedes periods of slowing economic growth.

Single A-rated taxable municipal bonds significantly outyielded single A-rated corporates out to seven years despite possessing similar credit quality and taxability status.

12-MONTH RETURNS, TAXABLE BOND SEGMENTS

JULY 2021 THROUGH JULY 2022



Source: Bloomberg. Past performance is no guarantee of future results.

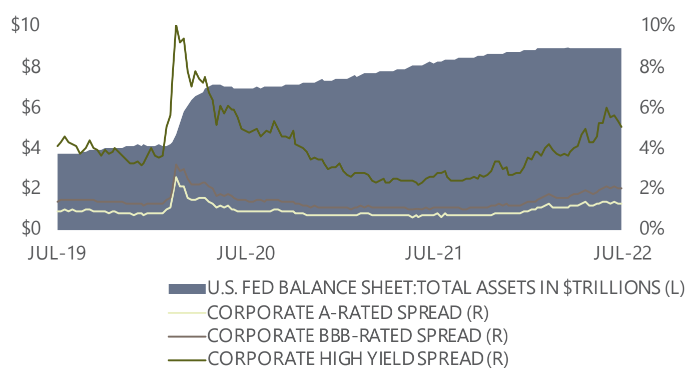
Declines in intermediate and longer term rates in July allowed every bond segment shown in the accompanying chart to claw back at least 1% of its 12-month negative return during the month. At the end of July fed funds futures markets projected the Fed's policy rate will be 2.94% in July 2023, compared to a projection of 3.24% one month ago.

Acute U.S. dollar strength over the last 12 months has enabled domestic high yield corporate bonds to significantly outperform emerging market bonds despite both segments' similar credit quality.

The two highest quality bond segments in the accompanying chart, U.S. Treasuries and U.S. Agencies, have held up best so far in 2022 as market interest rates climbed and credit spreads widened.

FED BALANCE SHEET EXPANSION AND CREDIT SPREADS

JULY 2021 THROUGH JULY 2022



Source: Bloomberg.

The Fed's balance sheet has shrunk by about $80 billion over the last four months after expanding by 112% from $4.2 trillion in February 2020 to nearly 9.0 trillion in April 2022.

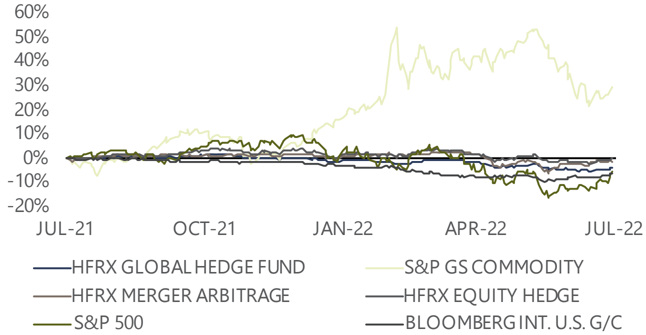
According to the Fed's projections, its balance sheet will be reduced by $522.5 billion this year to roughly $8.375 trillion, a modest 5.87% decrease. In 2023, the balance sheet is projected to shrink by $1.14 trillion to around $7.235 trillion, a 13.6% decrease.

U.S. corporate high yield, BBB-rated, and single A-rated credit spreads compressed in July in response to a strong start in second quarter corporate earnings results. However, all three spreads remain wider than their highest levels in all of 2019.

ALTERNATIVES

ALTERNATIVES, 12-MONTH RETURNS

JULY 2021 THROUGH JULY 2022



Source: Bloomberg. Past performance is no guarantee of future results.

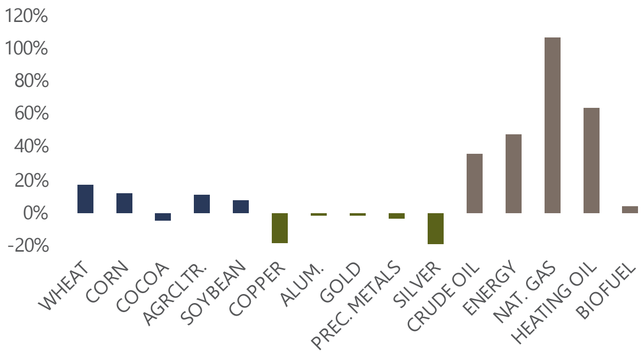
The broad commodities asset class, as measured by the S&P GSCI Spot Index, declined 2.34% in July after falling 9.82% in June. Despite recent weakness, the benchmark is still up nearly 30% over the last 12 months.

Growing fears of global economic slowdown, pressure from a strong U.S. dollar, and overextended bullish positioning in futures markets have weighed on most commodities over the last two months.

Through the first seven months of 2022, the HFRX Equity Hedge Index (-3.57%) and HFRX Event Driven Merger Arbitrage Index (-2.66%) have held up better than both the S&P 500 (-12.59%) and the Bloomberg Intermediate Government/Credit Index (-5.25%).

COMMODITIES, 12-MONTH SPOT RETURNS

JULY 2021 THROUGH JULY 2022



Source: Bloomberg. Past performance is no guarantee of future results.

U.S. natural gas prices climbed nearly 27% in July as warmer-than-expected temperatures swept over most of the lower 48 states. European natural gas prices spiked by an even steeper magnitude due to tightening Russian supplies and concerns about an extended shutdown to the Nord Stream 1 pipeline.

A tentative deal between Russia and Ukraine to resume global shipments of various grains from Black Sea ports put downward pressure on wheat and corn prices in July.

Gold fell 6.91% over the last three months despite levels of inflation in the U.S., U.K. and other major economies not seen since the 1980s. Gold's relative weakness has been attributed to a very strong U.S. dollar and aggressive Fed rate hikes.

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NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY			