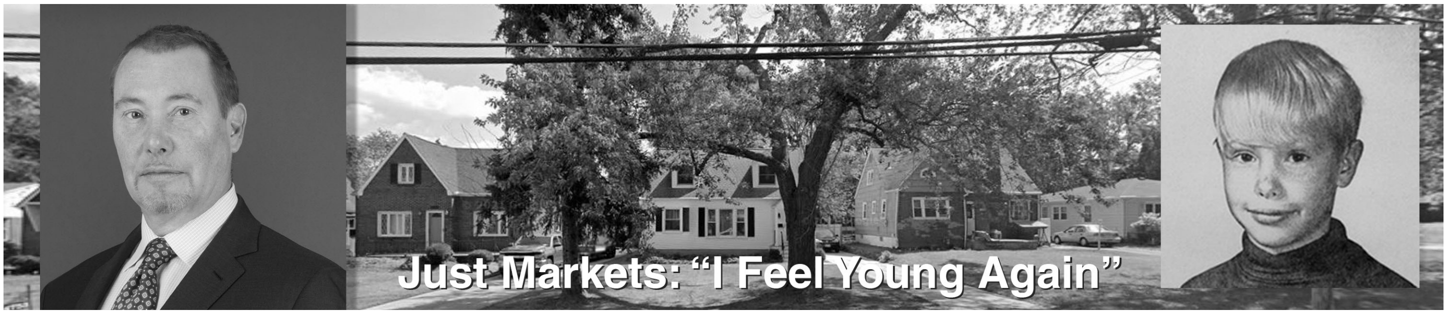
DoubleLine's Just Markets Webcast Recap

Originally aired on January 11, 2022



About this Webcast Recap

On January 11, 2022, Chief Executive Officer Jeffrey Gundlach held a webcast titled "I Feel Young Again," discussing the economy, the markets, and his outlook for what he believes may be the best investment strategies and sector allocations for 2022.

This recap is not intended to represent a complete transcript of the webcast. It is not intended as a solicitation to buy or sell securities. If you are interested in hearing more of Mr. Gundlach's views, please listen to the full version of this webcast on www.doubleline.com and click on the "Webcasts" menu item under the "Webcasts & Podcasts" section of the homepage.

Economic Data

- Since the onset of the pandemic, the magnitude of growth in consumer goods spending is similar to the growth observed from 2008 to February 2020.
  - Jeffrey Gundlach believes the upward acceleration in the S&P 500 Index and consumer goods spending since the pandemic has been supported by quantitative easing (QE) measures.
  - If QE measures come to an end in March, as planned, Mr. Gundlach believes risk assets will face more headwinds in 2022.
- U.S. household disposable income and income ex government transfers were growing in line with their longer-term trend until the start of the 2020 recession, when the gap, in the form of government transfers, grew to nearly $5 trillion.[1]
  - U.S. household income ex government transfers has nearly recovered to its pre-2020 trend while total disposable income remains elevated relative to its pre-2020 trend, indicating that government transfers remain elevated compared to pre-pandemic levels.
- Consumer sentiment has yet to recover to pre-pandemic levels even with relatively high U.S. nominal gross domestic product (GDP) growth.[2]
  - Rising auto and home prices likely contributed to the recent decline in consumer sentiment.
- Despite home prices increasing significantly over the past 18 months, affordability remains relatively favorable, driven in part by low mortgage rates.
  - Over the past 20 years, mortgage financing rates have outpaced consumer wage growth. Recently, this relationship has shifted, with wage growth higher than 30-year mortgage rates, further improving the affordability of homes.

[1] Government transfers account for government social benefits less personal social insurance contributions.
[2] Consumer sentiment as measured by the University of Michigan Consumer Sentiment Survey.

Inflation

- An example of the supply-chain bottlenecks contributing to inflation is the amount of container ships waiting at or near the Los Angeles and Long Beach ports.
  - In April 2020, there were nearly no container ships waiting at or near port. On Dec. 15, 2021, there was a backlog of 94 ships.
- The ISM Manufacturing Prices Paid Index, a leading indicator of the U.S. Consumer Price Index (CPI), recently peaked and started to decline.
  - Mr. Gundlach believes this could be an indication that the CPI could also move lower.
- Typically, there is a correlation between the National Federation of Independent Business (NFIB) Small Business Job Openings Hard to Fill Index and NFIB Small Business Compensation Plans Index, indicating that employers intend to raise wages.
  - Wages across all age cohorts have started to rise after remaining relatively stagnant over the last five years.
  - Workers 16 to 24 saw wage increases for much of the past 18 months as employers tried to hire entry-level workers.
  - Mr. Gundlach believes the Atlanta Federal Reserve Bank's Wage Growth Tracker is important to watch to see if the wage acceleration seen in the younger cohort will bleed through to more-seasoned workers.[3]
- Global inflation continued to surprise to the upside throughout 2021.
  - Over the past 10 years, there had always been at least one region of the world that surprised to the downside for inflation expectations, but now all regions of the world are surprising to the upside.

U.S. Dollar

- The U.S. Dollar Index (DXY) started 2021 near its lowest level in three years and was particularly strong in the second half of the year.
  - At these levels, Mr. Gundlach is neutral on the dollar.
- A leading indicator of moves in the dollar is the widening of the twin deficits. Widening budget deficits and current account deficits could indicate a lower dollar in 2022 on a technical basis.

[3] Seasoned workers are 25-54 and 55-plus, as followed by the Wage Growth Tracker.

Fed Funds Rate and Interest Rates

- As of Dec. 31, the real federal funds rate (FFR) was negative 673 basis points (bps) due to elevated inflation as measured by the CPI.[4]
  - The real Wu-Xia Shadow Federal Funds Rate, which accounts for the effects of QE, was negative 866 bps, far surpassing the negative interest rates of the Jimmy Carter era in the 1970s.
  - If the Fed were to stop QE and increase the FFR by 100 bps in 2022, that would equate to roughly 300 bps of tightening.
- Historically, the Fed has increased the FFR in line with wage growth.[5]
  - Currently, wage growth is north of 4% while the FFR is slightly above 0%. This is an indication to Mr. Gundlach that the Fed has fallen behind the curve.
- Short-term U.S. Treasury yields rose at a faster rate than longer-term yields in 2021, which led to a flatter yield curve across various tenors.
  - This trend has accelerated in 2022, and Mr. Gundlach believes if long-term yields were to decline while short-term yields continued to climb, that would be a recessionary signal.
- During the Carter era, the differential between two- and 10-year yields peaked near 150 bps. In this most recent economic expansion, the yield differential between the two is 86 bps after peaking near 150 bps at the end of the first quarter in 2021.
- The differential between the five- and 30-year yields has been shrinking since March 2021.
  - Historically, a convergence in yields between the long bond and the five-year note has been a recessionary signal.
- Over the last monetary cycle, the two-year yield has led the Fed and FFR in both tightening and easing monetary conditions.
  - Currently, the two-year yield is 68 bps higher than the upper bound of the FFR, signaling that the Fed should increase the FFR.

[4] The real FFR is the effective FFR minus the headline CPI year-over-year.
[5] Wage growth is measured by the Employment Cost Index quarterly percent change annualized.

Equities

- The Nasdaq 100 Index outperformance relative to the S&P 500 has exceeded the highs of the 1999-2000 dot-com era.
  - Over the past year and a half, this relative outperformance has stopped. If the Nasdaq 100 outperformance of the S&P 500 were to fall below its dot-com peak, it would send a technical signal that the S&P 500 could start to outperform the Nasdaq 100.
- Since the start of the pandemic, growth names have been outperforming value names by a wide margin on a price basis.
  - Historically, the earnings per share (EPS) of growth names have similarly outpaced EPS growth of value names, but this relationship has become disconnected in the wake of substantial price gains of growth relative to value.
  - This disconnect between price outperformance relative to EPS outperformance of growth versus value is one reason Mr. Gundlach favors value names.
- The S&P 500 has outperformed the MSCI All Country World Index ex U.S. by a wide margin since the Global Financial Crisis (GFC). Over the same time, U.S. equities have grown increasingly expensive relative to the rest of the world, as measured by price-to-earnings (P/E) ratios.
  - Similarly, the S&P 500 has strongly outperformed European stocks, as measured by the MSCI Europe Index, until the past 18 months.
  - On a technical basis, Mr. Gundlach believes this recent stall in outperformance could mean the momentum of S&P 500 outperformance of European stocks is waning.
- The S&P 500 has strongly outperformed emerging market (EM) stocks since March, largely due to a stronger dollar and greater strain on many EM healthcare systems caused by the pandemic.
  - The outperformance of the S&P 500 relative to EM stocks has historically exhibited cyclicality, usually peaking around 4.5 times outperformance. At the current level of 3.8 times outperformance, EM stocks could look attractive in the coming years.
- Given the commodity-dependent nature of some EM economies, EM stocks tend to trade in the same direction as industrial metals.
  - In 2021, industrial metals recorded significant gains while EM stocks finished the year with negative returns.
    - Mr. Gundlach believes this divergence is either very bullish for EM stocks or bearish for industrial metals.
- The impact of negative interest rates in Europe and Japan is exemplified by the performance of each regions' bank stocks:
  - The Bank of Japan (BOJ) initiated a sub-1% interest rate policy in 1995, which eventually lead to the BOJ adopting negative interest rates in 2016. Since 1995, Japanese bank stocks are down nearly 83%, as measured by the Tokyo Stock Exchange TOPIX Banks Index.
  - From 1995 to the GFC, European and U.S. banks significantly outperformed Japanese banks.
    - To stimulate the eurozone economy post-GFC, the European Central Bank (ECB) introduced negative interest rates in 2014.
    - Since the GFC, the Stoxx Banks Price EUR Index has significantly underperformed U.S. banks, as measured by the KBW Bank Index.
  - Federal Reserve Chair Jerome H. Powell has stated that he does not want to implement negative interest rates. In the next economic decline, Mr. Gundlach believes the Fed will have a difficult decision in regard to the level at which the FFR should reside.

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Definitions

Below Investment Grade/Non-Investment Grade – Term indicating a security Basis Points (BPS) – Basis points (or basis point (bp)) refer to a common unit of measure for interest rates and other percentages in finance. One basis point is equal to 1/100th of 1%, or 0.01% or 0.0001, and is used to denote the percentage change in a financial instrument. The relationship between percentage changes and basis points can be summarized as: 1% change = 100 basis points; 0.01% = 1 basis point.

Consumer Price Index (CPI) – This index, compiled by the U.S. Bureau of Labor Statistics, examines the weighted average of the prices of a basket of consumer goods and services, such as transportation, food and medical care. It is calculated by averaging price changes for each item in the basket. Changes in the CPI are used to assess price changes associated with the cost of living. The CPI is one of the most frequently used statistics for identifying periods of inflation or deflation.

Earnings Per Share (EPS) – Calculated as a company's profit divided by the outstanding shares of its common stock. The resulting number serves as an indicator of a company's profitability.

Employment Cost Index (ECI) – Survey of employer payrolls conducted by the U.S. Bureau of Labor Statistics that measures the change in total employee compensation each quarter. It is used by a wide variety of stakeholders – economists, investors, employers – to track the state of the economy or set pay scales for their employees.

Federal Funds Rate (FFR) – Target interest rate, set by the Federal Reserve at its Federal Open Market Committee (FOMC) meetings, at which commercial banks borrow and lend their excess reserves to each other overnight. The Fed sets a target federal funds rate eight times a year, based on prevailing economic conditions.

Growth Stock – Any share in a company that is anticipated to grow at a rate significantly above the average growth for the market. These stocks generally do not pay dividends. This is because the issuers of growth stocks are usually companies that want to reinvest any earnings they accrue in order to accelerate growth in the short term. When investors invest in growth stocks, they anticipate that they will earn money through capital gains when they eventually sell their shares in the future.

ISM Manufacturing PMI – This index (which used to be called the ISM Manufacturing Purchasing Managers Index) is compiled by the Institute for Supply Management and tracks the economic health of the manufacturing sector. The index is based on five major indicators: new orders, inventory levels, production, supplier deliveries and employment environment.

ISM Manufacturing Prices Paid Index – This index tracks input price data from the Institute for Supply Management's ISM Manufacturing PMI.

KBW Bank Index – Benchmark stock index of the banking sector that includes a weighting of 24 banking stocks selected as indicators of this industry group.

Morgan Stanley Capital International All Country World Index (MSCI ACWI) – This market capitalization-weighted index is designed to provide a broad measure of stock performance throughout the world. It comprises stocks from 23 developed countries and 27 emerging markets.

Morgan Stanley Capital International (MSCI) Europe Index – This index is U.S. dollar denominated and represents the performance of large- and mid-cap equities across 15 developed countries in Europe. It covers approximately 85% of the free float-adjusted market capitalization in each country.

Nasdaq 100 Index – This index comprises the 100 largest U.S. and non-U.S. nonfinancial securities based on market capitalization listed on the Nasdaq stock exchange. The index reflects companies across major industry groups including computer hardware and software, telecommunications, biotechnology and retail/wholesale trade.

NFIB Small Business Compensation Plan Index – This seasonally adjusted index, compiled by the National Federation of Independent Business (NFIB), is based on a survey of 800 companies and tracks the net percentage of business owners planning to increase compensation during the next three-month period.

NFIB Small Business Job Openings Hard to Fill Index – This index compiled by the National Federation of Independent Business (NFIB) is based on the NFIB's survey of 800 small companies and tracks the number of job openings that owners are seeking to fill.

Price-to-Earnings (P/E) Ratio – This ratio for valuing a company measures current share price relative to earnings per share (EPS). The P/E ratio is also sometimes known as the "price multiple" or the "earnings multiple." A high P/E ratio could mean that a company's stock is overvalued, or investors are expecting high growth rates in the future.

S&P 500 Index – This unmanaged capitalization-weighted index of the stocks of the 500 largest publicly traded U.S. companies is designed to measure performance of the broad domestic economy through changes in the aggregate market value of the 500 stocks, which represent all major industries.

Stoxx Banks Price EUR Index – This index tracks the stock prices of the eurozone banking sector.

Tokyo Stock Exchange TOPIX Banks Index – Capitalization-weighted index of all the banks listed on the First Section of the Tokyo Stock Exchange and is one of the 33 industry sectors of the Tokyo Stock Exchange Price Index (TOPIX), which tracks all domestic companies of the exchange's First Section.

Quantitative Easing (QE) – An unconventional monetary policy used by central banks to stimulate the economy when standard monetary policy has become ineffective. A central bank implements quantitative easing by buying specified amounts of financial assets from commercial banks and other private institutions, thus raising the prices of those financial assets and lowering their yield, while simultaneously increasing the monetary base.

University of Michigan Consumer Sentiment Index – This index rates the relative level of current and future economic conditions through monthly surveys of about 500 U.S. households (ex Alaska and Hawaii). There are two versions of this data released two weeks apart, preliminary and revised. The preliminary data tends to have greater impact. A higher-than-expected reading should be taken as positive/bullish for the U.S. dollar; a lower-than-expected reading should be taken as negative/bearish.

U.S. Dollar Index (DXY) – A weighted geometric mean of the U.S. dollar's value relative to a basket of six major foreign currencies: the euro, Japanese yen, British pound, Canadian dollar, Swedish krona and Swiss franc.

Value Stock – Shares of a company that appear to trade at a lower price relative to its fundamentals, such as dividends, earnings or sales, making it appealing to value investors.

Wage Growth Tracker – Measure of the nominal wage growth of individuals published by the Federal Reserve Bank of Atlanta. It is constructed using microdata from the Current Population Survey and is the median percent change in the hourly wage of individuals observed 12 months apart.

Wu-Xia Shadow Federal Funds Rate – Shadow rate model, by economists Jing Cynthia Wu and Fan Dora Xia, to characterize the term structure of interest rates that is not bounded below by zero percent.

You cannot invest directly in an index.

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