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Wealth Advisory Market Update

November 3, 2022

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Market Update

Equities

The swings continued in October, with the S&P 500 rallying 8.1%. Year-to-date, the index is still down 17.7% for 2022 as of October 31st. The question remains, will this trajectory continue or is this just a bear market rally in an overall downward trend? For 3Q 2022, earnings were more positive than expectations overall, but forward guidance and tone was very mixed. With 52% of S&P 500 companies reporting results, 71% of those have reported positive EPS relative to consensus estimates and 68% have reported positive revenue relative to consensus. Despite this positivity relative to expectations, the blended 3Q 2022 earnings growth rate for the S&P 500 is currently 2.2%, the lowest in 2 years. In addition, market bellwethers like Amazon lowered expectations going forward and 28 S&P 500 companies have issued negative EPS guidance for 4Q 2022. Only 14 have issued positive guidance. The biggest earnings disappointments were from big tech as ad spend and margins continued to be pressured.

Regarding valuations, forward 12-month P/E for the S&P 500 is 16.3, below the 5-year average of 18.5 and the 10-year average of 17.1, but above the long-term trend of 15.5. We still believe valuations are frothy compared to long-term historical levels and that excess remains in the high-growth space, even after the major correction.

Monetary Policy and Economic Indicators

The labor market has remained stubbornly strong in the face of rate hikes and an overall slowing economy. This has given the Fed room to continue on their current path with another 75 basis point increase in November. This marks the fourth straight 75 basis point hike, pushing the Fed Funds rate up from 0 to 3.75-4.00% this year. The Fed signaled they are looking for a slower pace moving forward, however the terminal rate may be higher than original expectations. In his press conference following the announcement, Chairman Powell reiterated that any notion of a pause was premature. Friday's non-farm payroll numbers will be the next economic data to look at as the Fed positions their next move.

Inflation remains sticky and supply chain issues remain a major concern, although we think it will ease some by year end. Adding to concerns is a diesel shortage on the east coast which will further exacerbate inflation. The dollar has steamrolled every other currency so far this year. The month of October saw a slight reprieve which helped the markets rally globally. If the Fed continues its hawkish stance, we could see continued dollar strength moving forward, which means lower equity prices on the horizon.

Geopolitical risks are still a major concern. It seems rhetoric regarding Russia, China and Iran has continued its hawkish trend. Although yesterday, Russia agreed to rejoin the Ukraine grain deal which will allow grain to flow through the Black Sea again. Geopolitical turmoil can't be adequately forecasted, but is expected to continue to impact volatility.

Strategy

As we mentioned in our last letter, we still favor energy and that has paid off so far this year. We remain overweight value and quality over growth. This has been a good move so far this year and we believe it will continue. In times such as this we want to own companies with dominant market share and pricing power. As of now, we don't believe we've seen lows for the year, but a lot depends on future actions by the Fed. If they change their stance, we will change ours accordingly.

Fixed income continues to be under pressure, however, we have begun adding duration to our portfolios. We believe it is a great opportunity to start averaging new capital in. We still seek high quality in this space.

As always, we continue to navigate this difficult environment to the very best of our ability. We at AMB thank you for your support and for allowing us to partner with you in reaching your financial goals.

Matthew J. Roach, CFA®
Chief Investment Strategist