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Wealth Advisory Market Update

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Market Update

The Federal Open Market Committee (FOMC) has been the main influencer of market behavior over the last few weeks with their policy opinions culminating at the annual Jackson Hole meeting a week ago. The more hawkish tone of the Federal Reserve speakers at the meeting created an immediate market response. Prior to the meeting, we saw a significant rally in the month of July, but after Jackson Hole, the rally reversed. Along with the FOMC's rhetoric, it's also important to note that economic data is trending stronger than anticipated, while inflation remains stubbornly high. To manage the rising inflation, the Federal Reserve continues to tighten financial conditions in an attempt to align demand more with current supply. In laymen terms, this means they will intentionally put the U.S. economy into a recession by increasing unemployment. This in turn, will lower demand. Engineering a soft economic landing is a difficult task, especially using the blunt tools that the Federal Reserve has at its disposal. As we move into the end of the year, our main focus will remain on the economy and how it is reacting to FOMC decisions.

A snapshot of the current equity markets, measured by the S&P 500, leads us to believe that risk remains elevated. Several factors influence our conclusion. After the recovery from the June lows, the index now sits at a multiple of over 19x. We still hold the belief that the market needs to hit a forward multiple of 12-14x earnings to mark a bottom, which would put the S&P between 3200-3400, depending on earnings. In our opinion, this will take place sometime in the fourth quarter, as the market will bottom before we enter a recession. Our continuing analysis led us to raise cash by selling into the most recent rally. Even with the overvaluation of the market, we remain overweight the energy sector which we believe to be undervalued. We believe the market will provide us opportunities in the coming months to put money to work elsewhere at better entry points. We remain focused on strong cash-flow generating companies with dominant market share while avoiding non-profitable names in highly competitive markets.

Fixed Income markets have been tough to navigate this year. Bonds are usually the safe haven when equity markets turn lower. However, in the stagflation-like environment we now find ourselves in, these same principals do not apply. We remain short in duration, taking advantage of the increase in rates on the front-end. In our opinion, now is not the time to take on duration risk. Credit markets have been showing some signs of cracking as the economy slows, which is why we will remain in strong balance-sheet companies. Once we believe the move in rates offers a more compelling risk/reward scenario, we will once again look to extend our maturities out and lock in higher interest rates.

It is an understatement to say that internationally, there is a lot going on. China is still implementing their "zero covid" policy, which continues to keep economic growth stunted and supply chains in disarray. They are also dealing with their own 2008, as their housing market is in utter collapse. Europe is heading for a major recession as their energy costs continue to sky rocket. The sanctions on Russia are definitely hurting Europe and their economies. If this dynamic continues, the EU is going to be in for a brutal winter. Japan's economy continues to shrink and will possibly be in a recession in the coming months. Their monetary policy has been an absolute disaster and we believe that they will soon be in a major currency crisis. Emerging markets around the globe are also going to struggle as the U.S. Dollar continues to strengthen. In summary, we are heading for a global recession and the US remains the cleanest dirty shirt and our allocations will continue to reflect that.

This is a snapshot of the current trend and it does not mean present conditions will remain. Economic data coming out in the near future could alter our outlook. If this occurs, we will be quick to assess and make adjustments to our portfolios. 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.

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