



Q3 Economic & Market Outlook

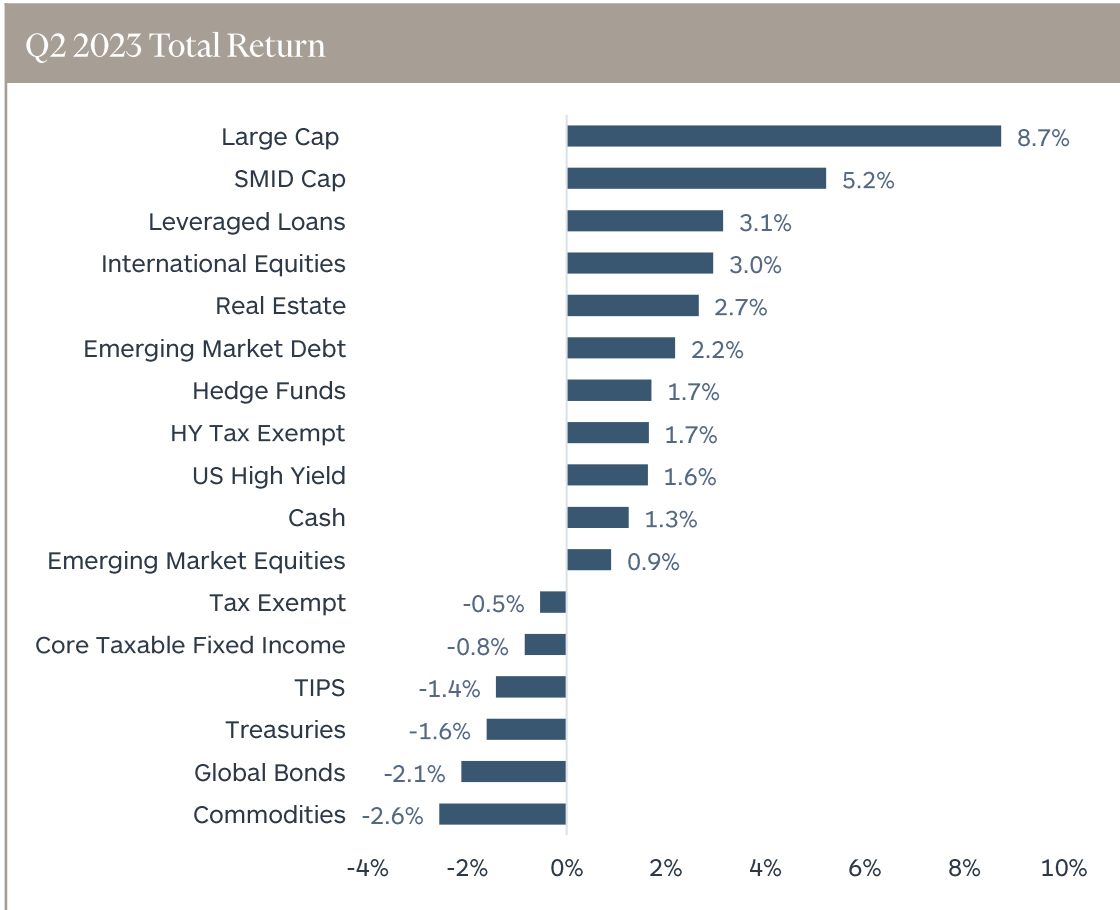
Unexpected Strength

Confidential & Proprietary

July 20, 2023

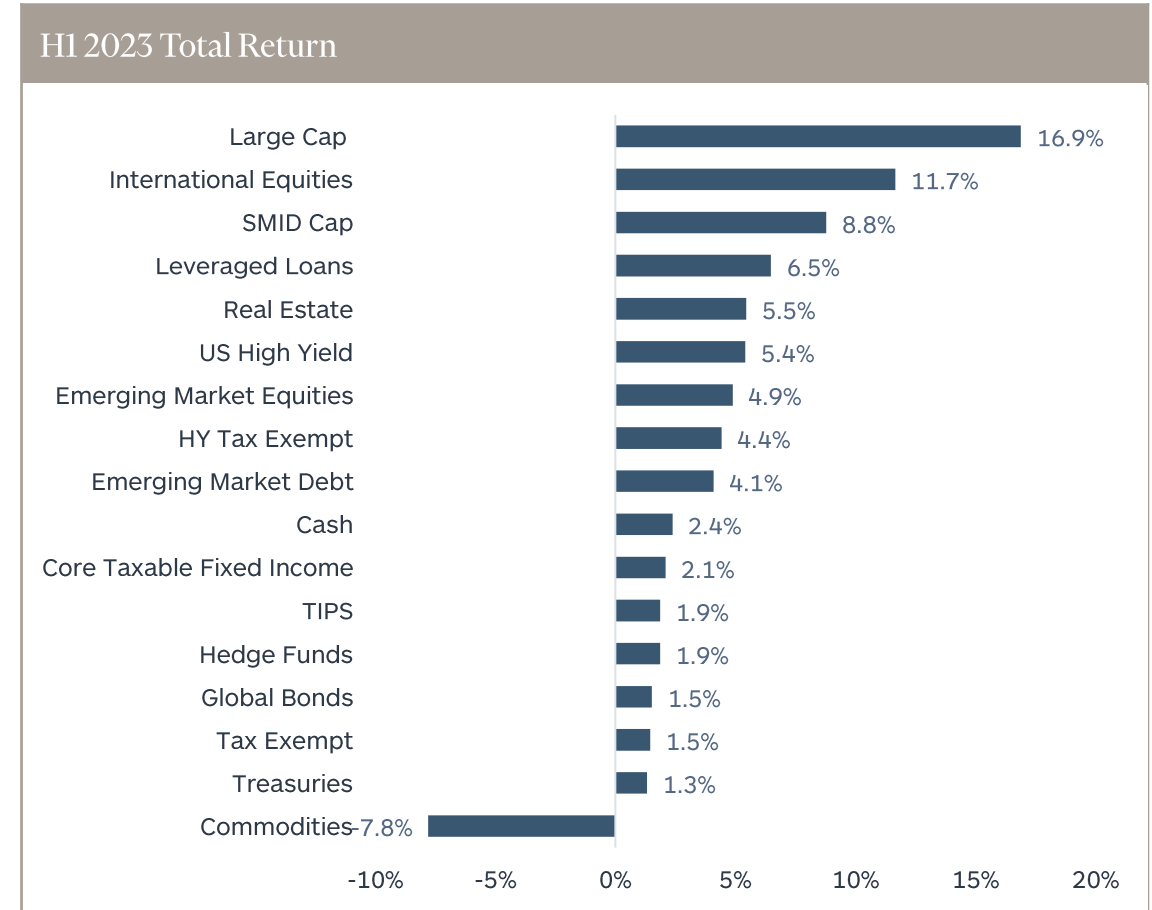
Q2 in Review

Continued strength in equities, but bond markets were timid.



As of 6/30/2023

Source: Morningstar Direct

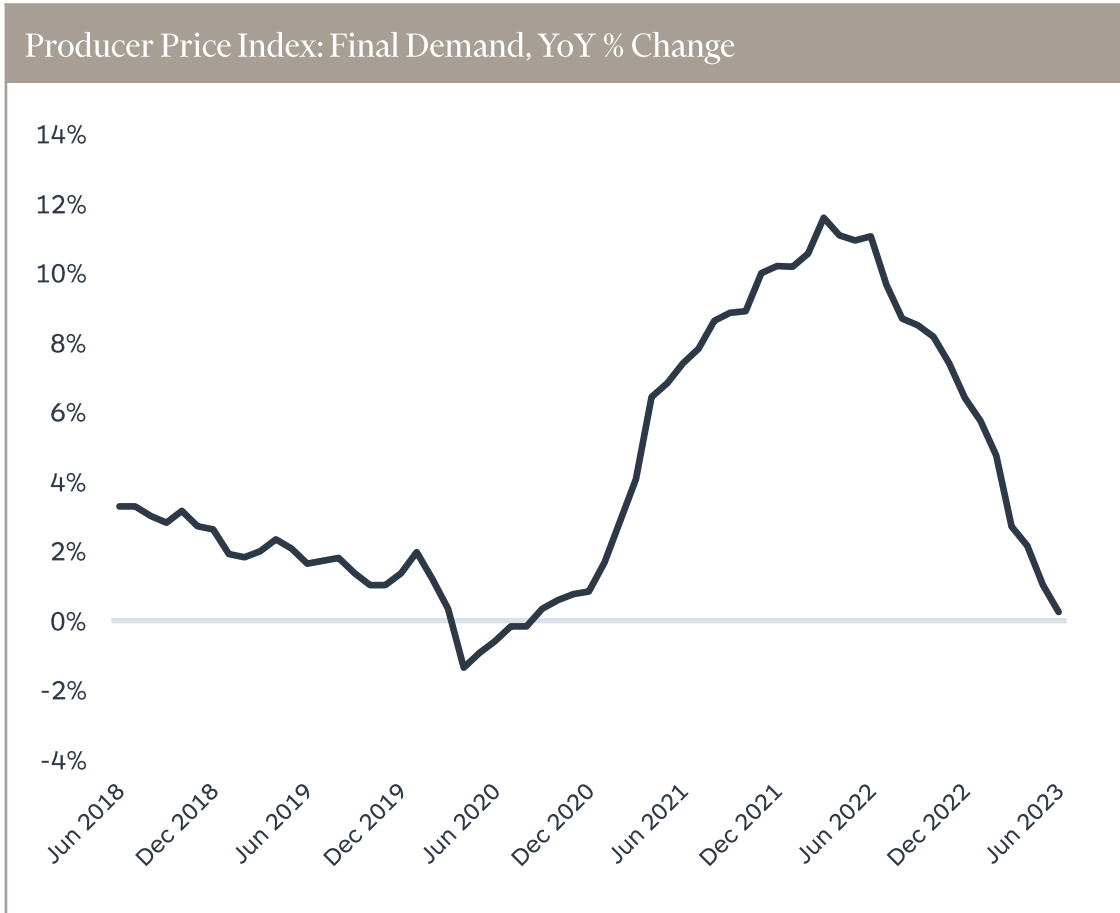


As of 6/30/2023

Source: Morningstar Direct

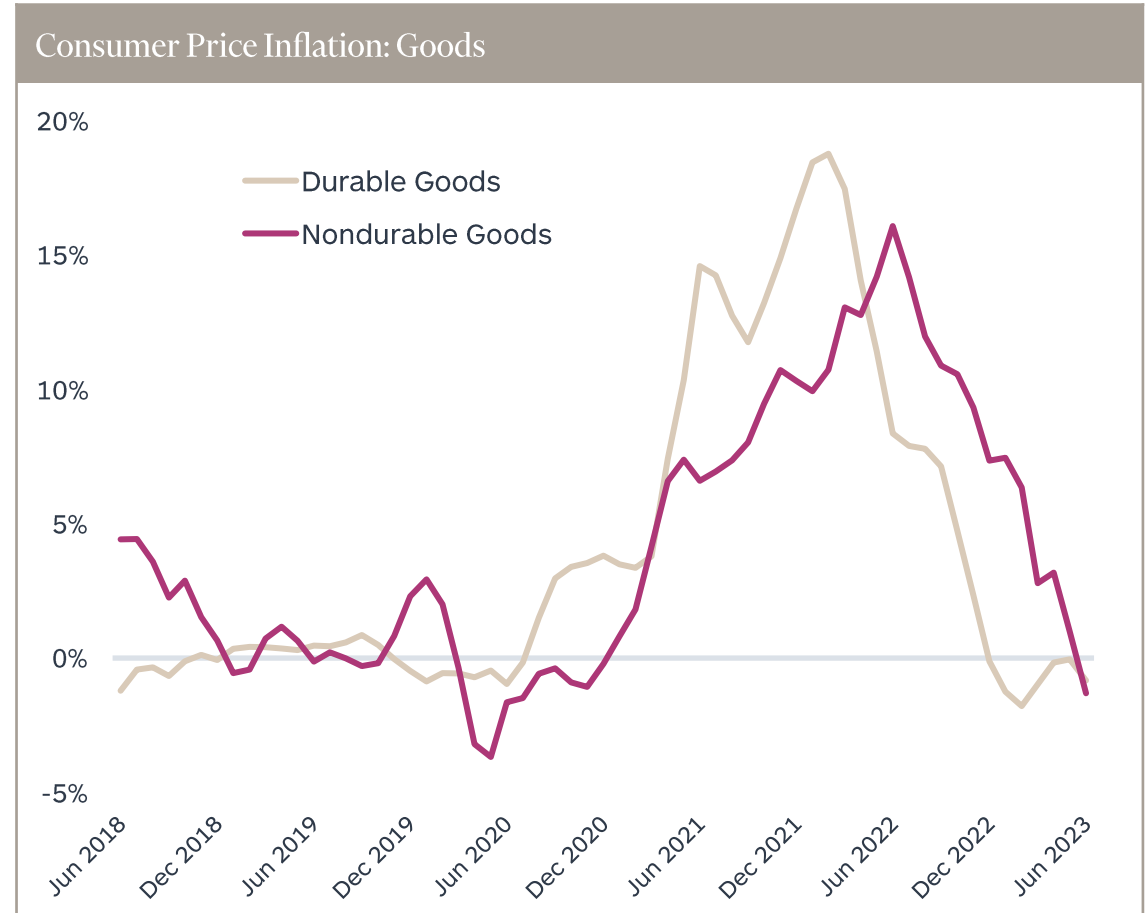
The Inflation Picture

Falling demand and input prices have quickly pulled down goods inflation...



As of 6/30/2023

Source: FRED

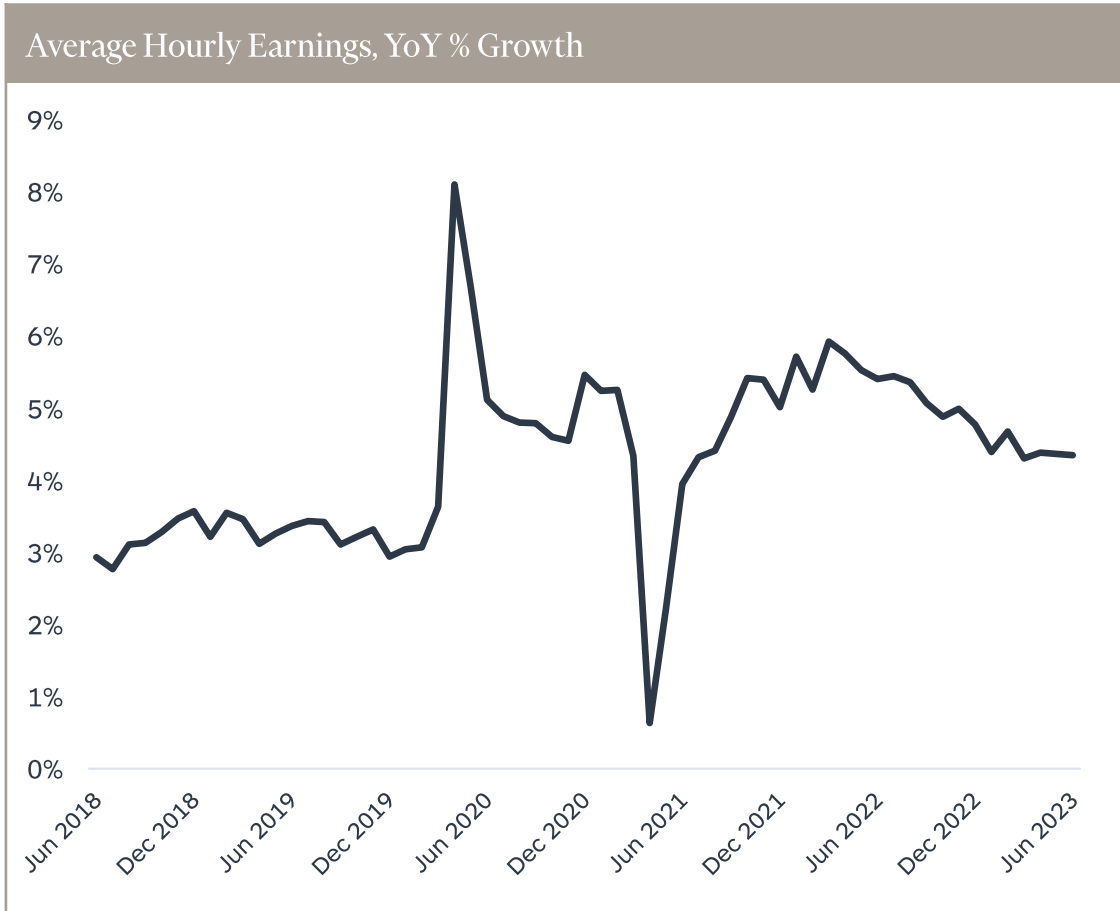


As of 6/30/2023

Source: FRED

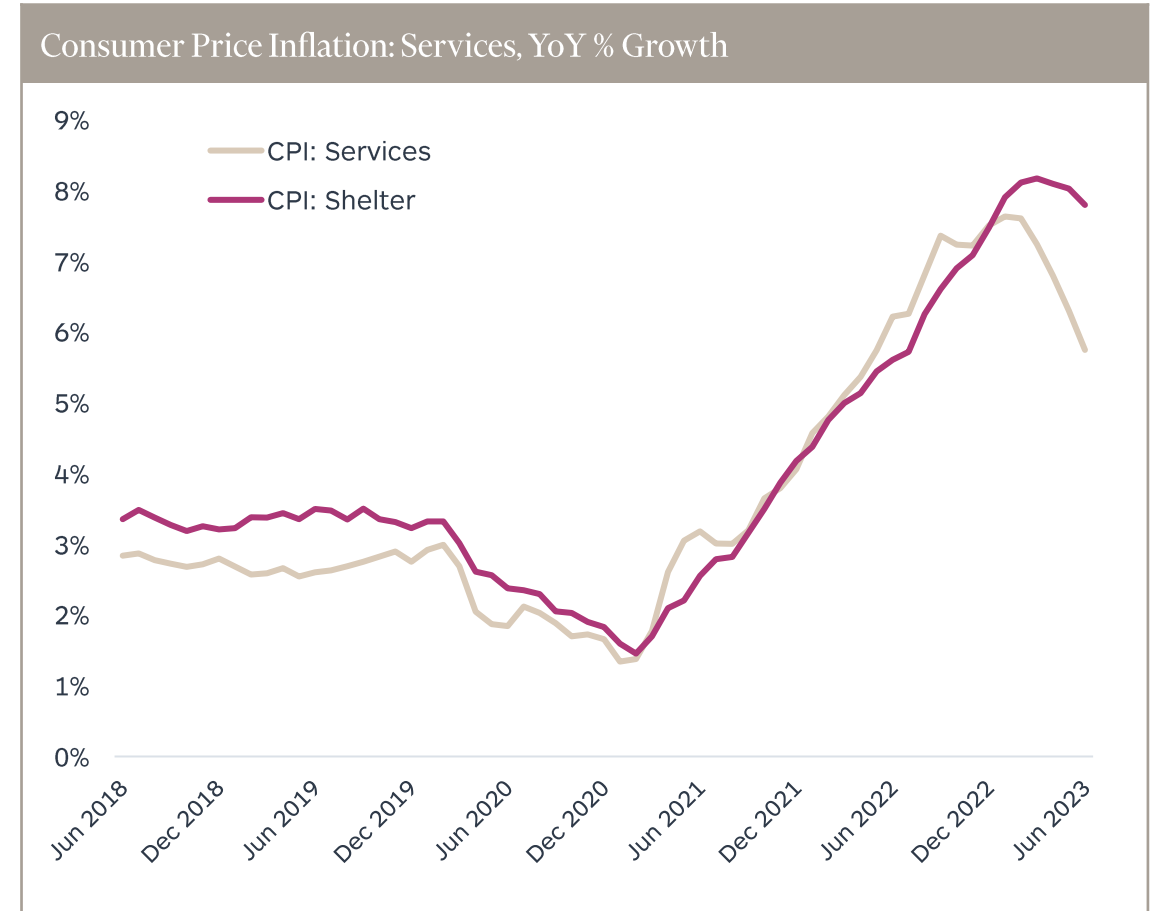
The Inflation Picture

...but strong demand and wage growth is keeping services inflation uncomfortably high.



As of 6/30/2023

Source: FRED

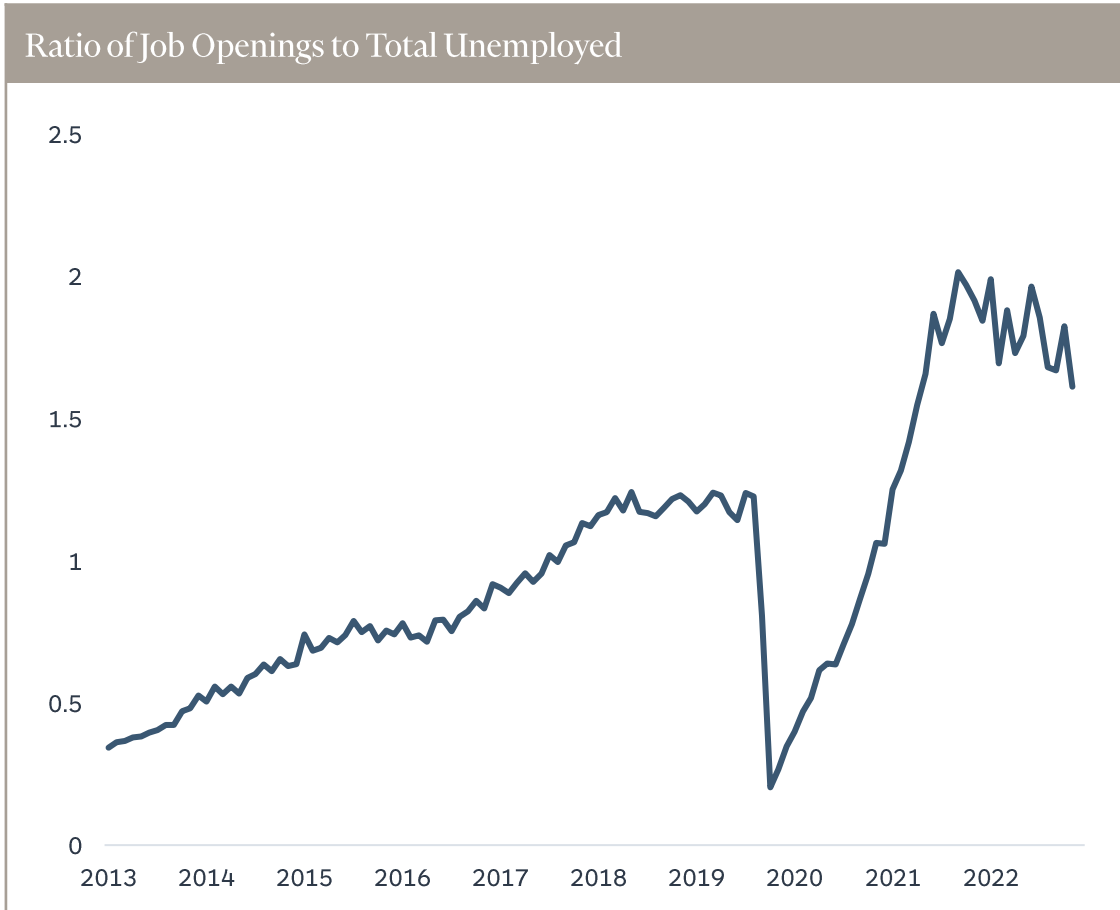


As of 6/30/2023

Source: FRED

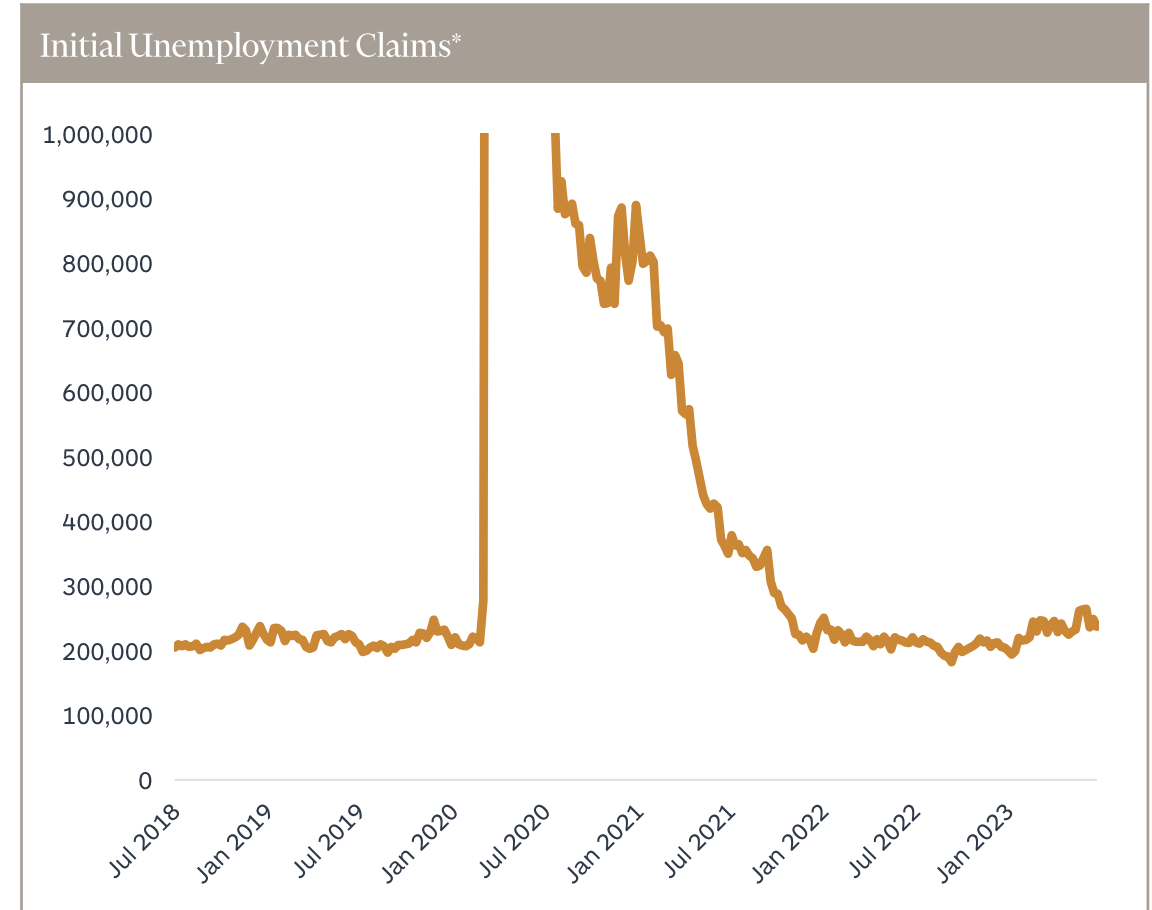
The Labor Market Remains Tight

Job openings are off a bit, but initial claims and the unemployment rate remain under control.



As of 6/30/2023

Source: FRED



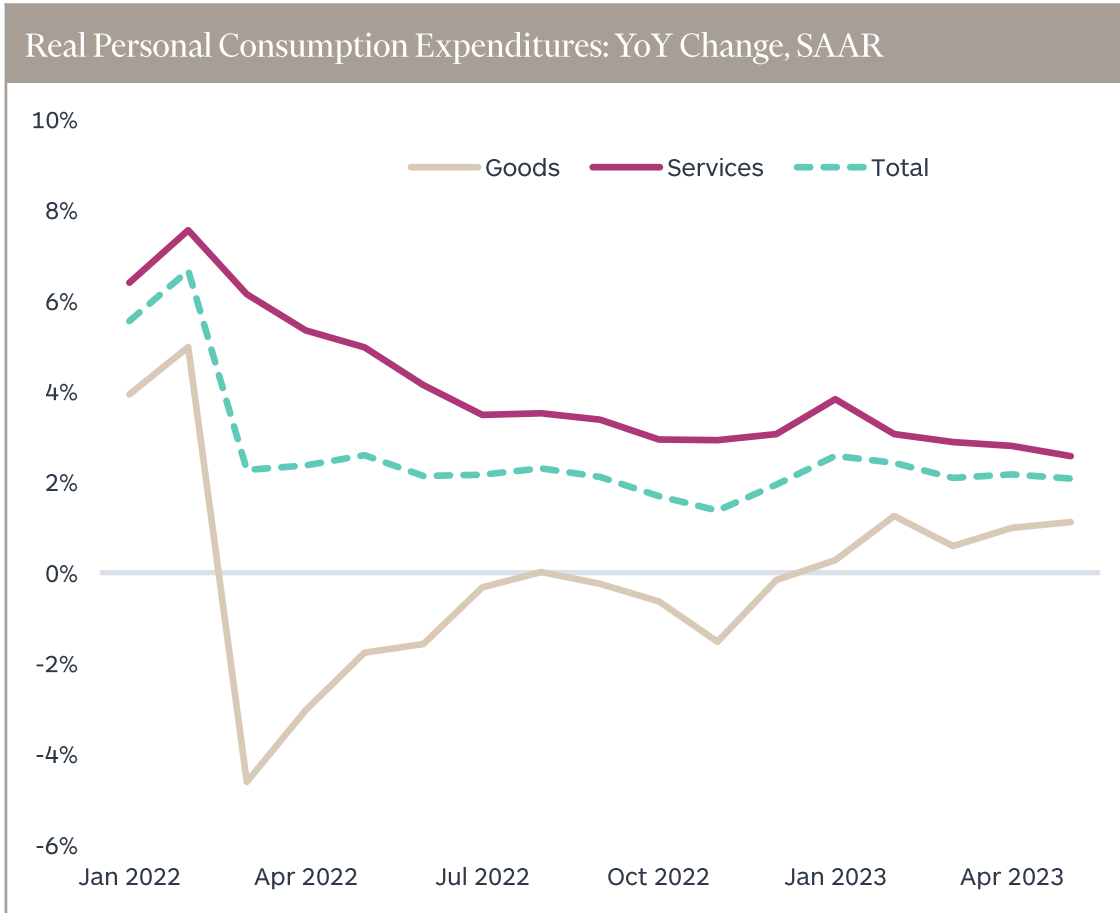
As of 7/8/2023

Source: Morningstar Direct

*Initial claims reached a high of 6.14 million in April 2020

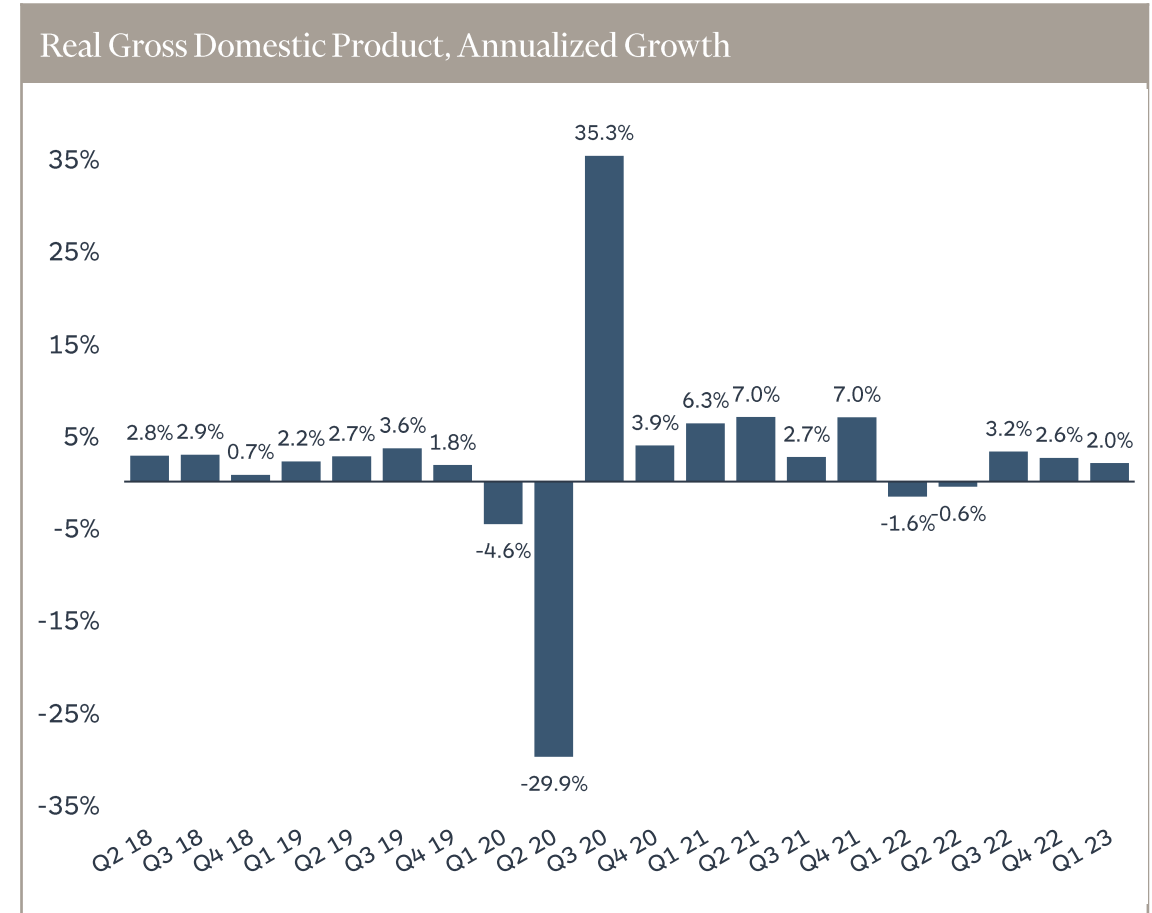
Wages Fuel Consumption, Consumption Fuels Growth

Despite growing recessionary concerns, consumers are employed, well-paid, and willing to spend.



As of 6/30/2023

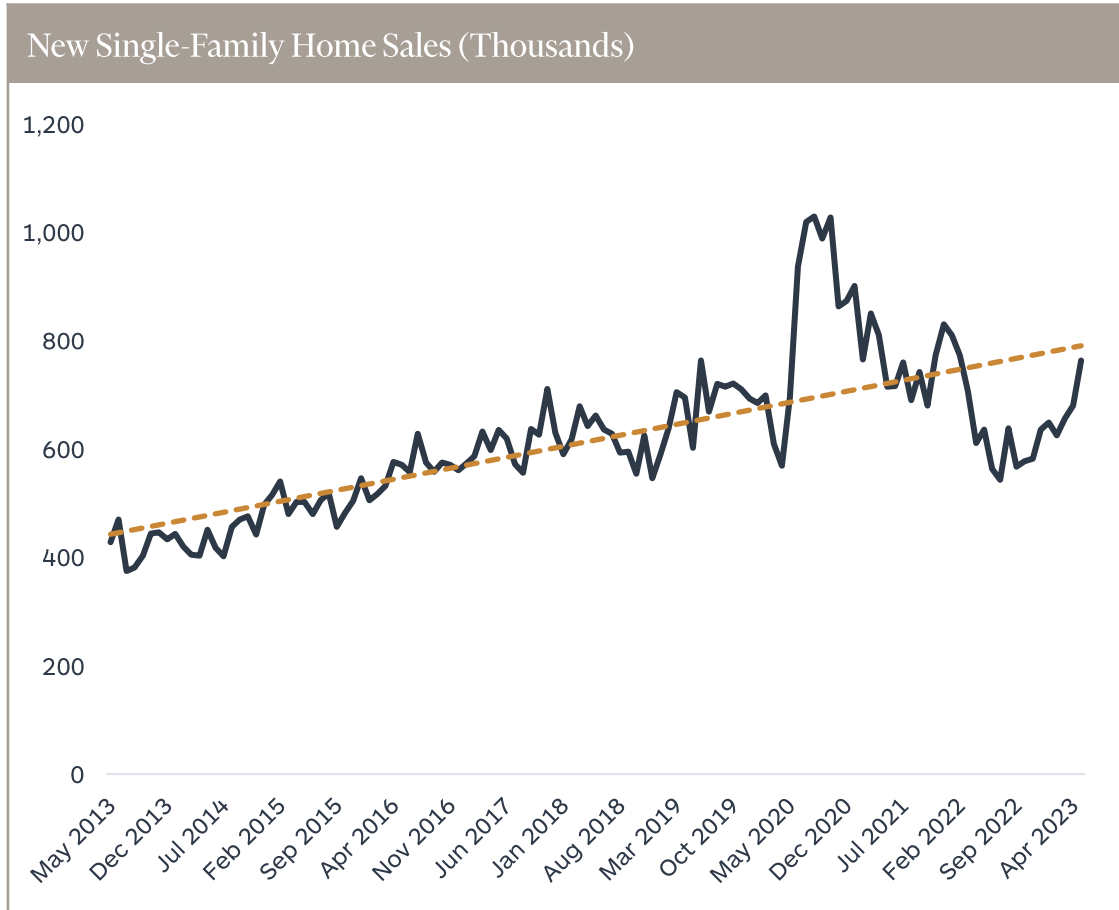
Source: FRED



Source: FRED

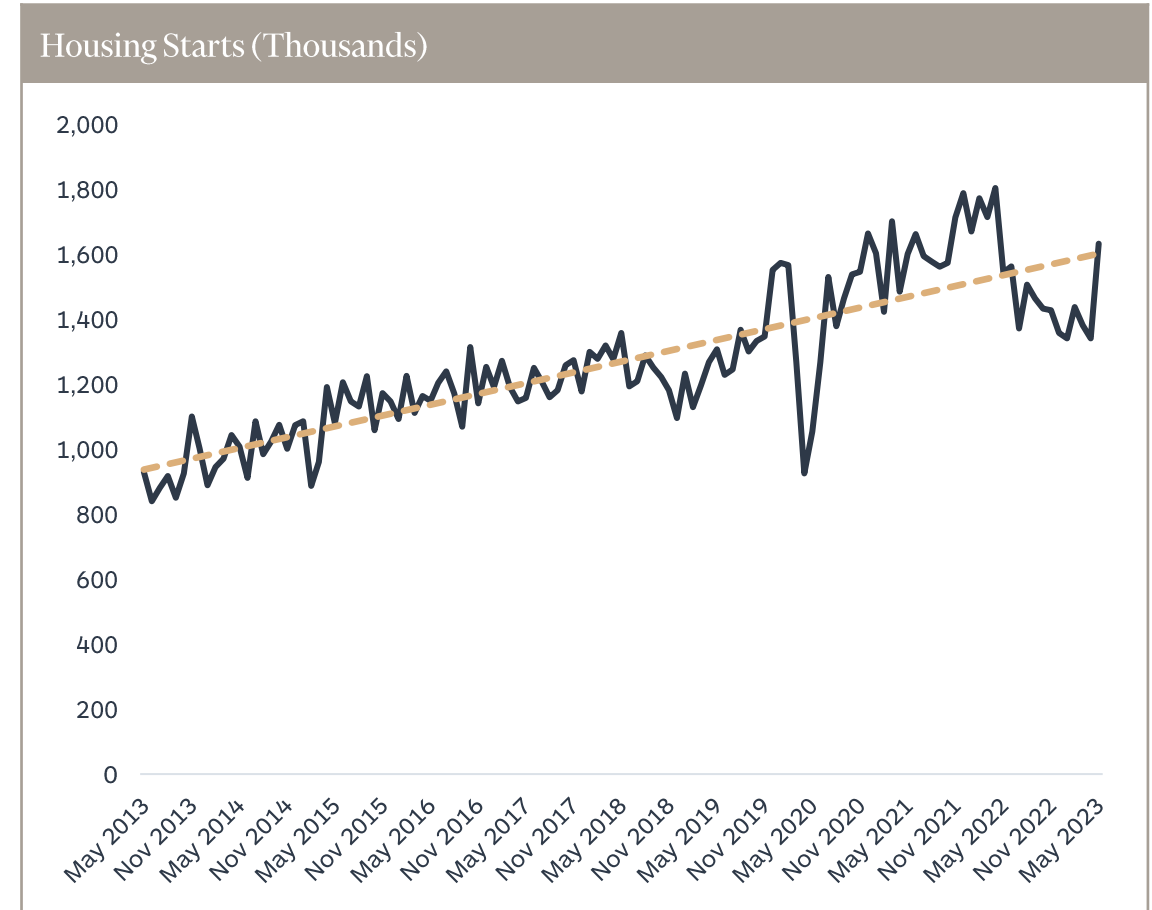
Housing Bottoming?

Still historically unaffordable, but there still seems to be enough demand for limited supply.



As of 6/30/2023

Source: FRED

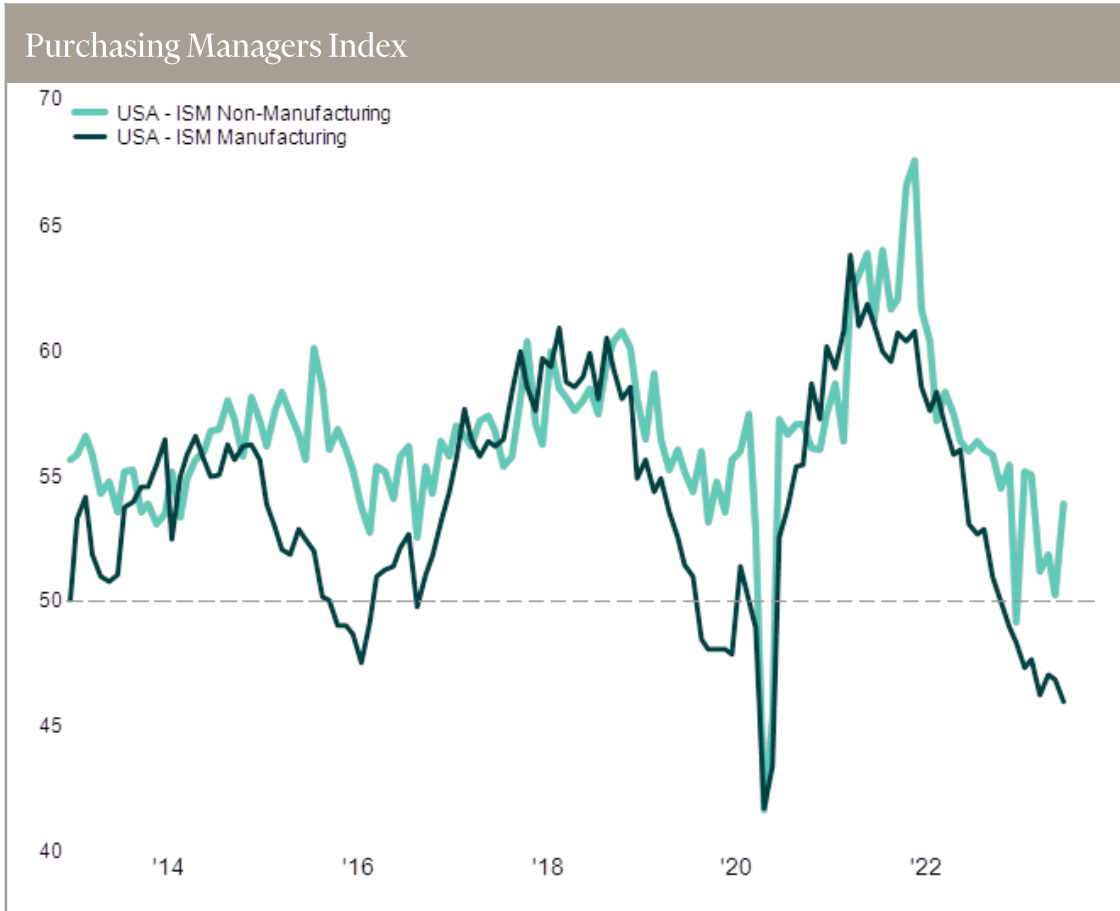


As of 6/30/2023

Source: FRED

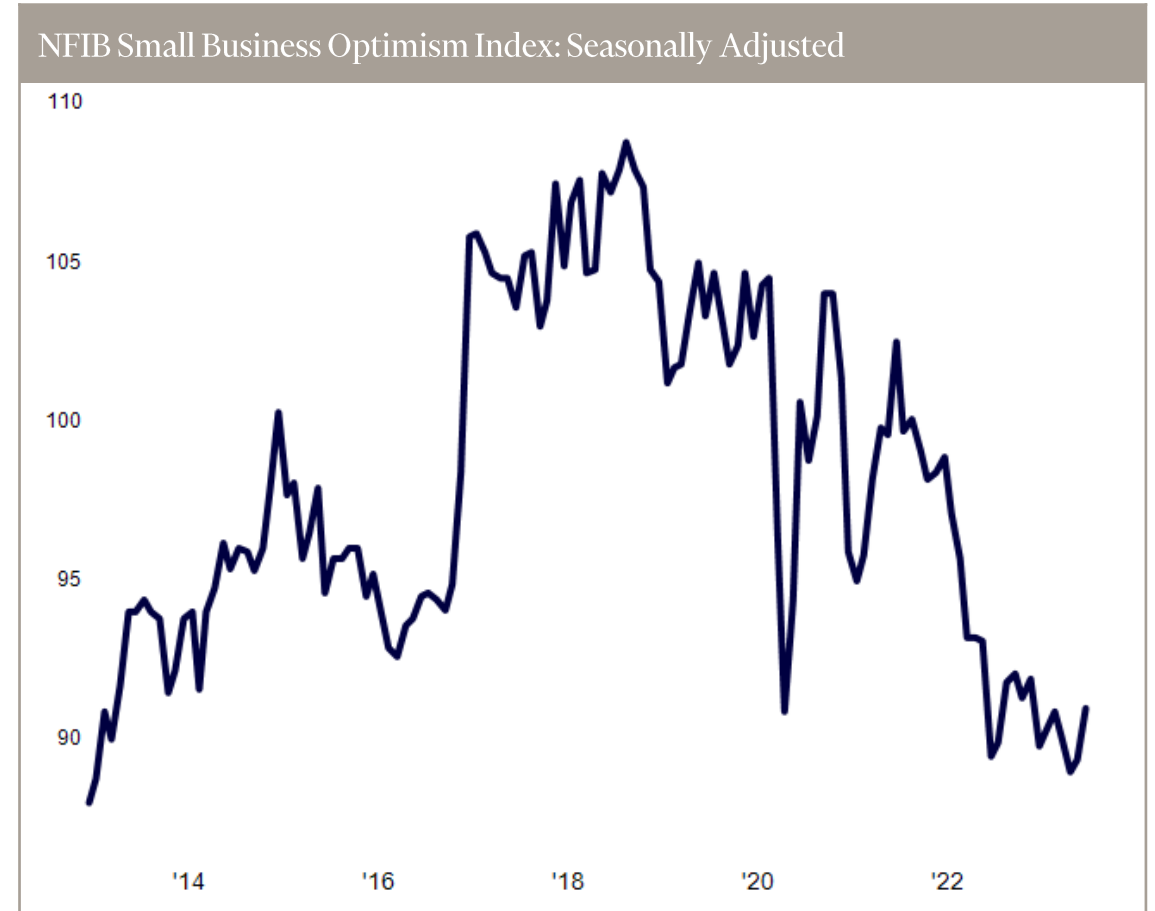
Survey Data Reflects Ongoing Pessimism

Particularly small businesses and the manufacturing industry.



As of 6/30/2023

Source: Factset

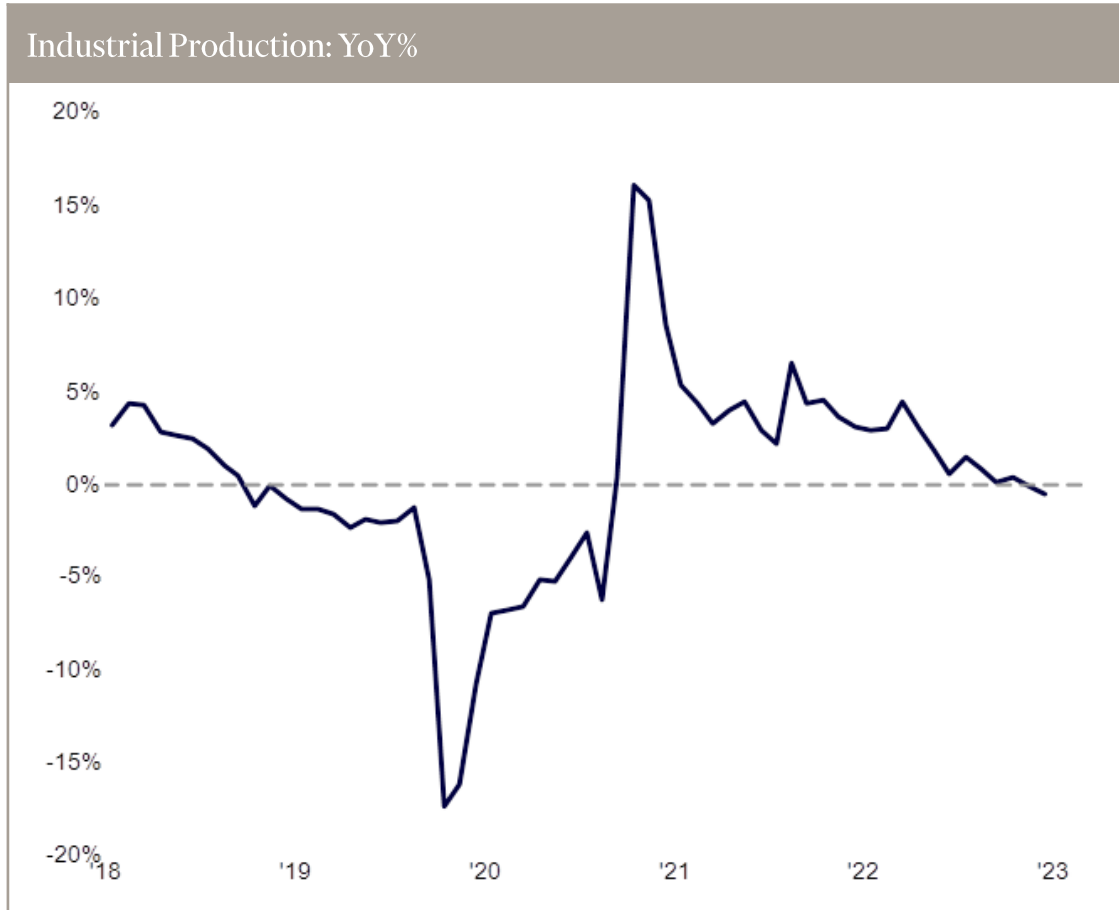


As of 6/30/2023

Source: Factset

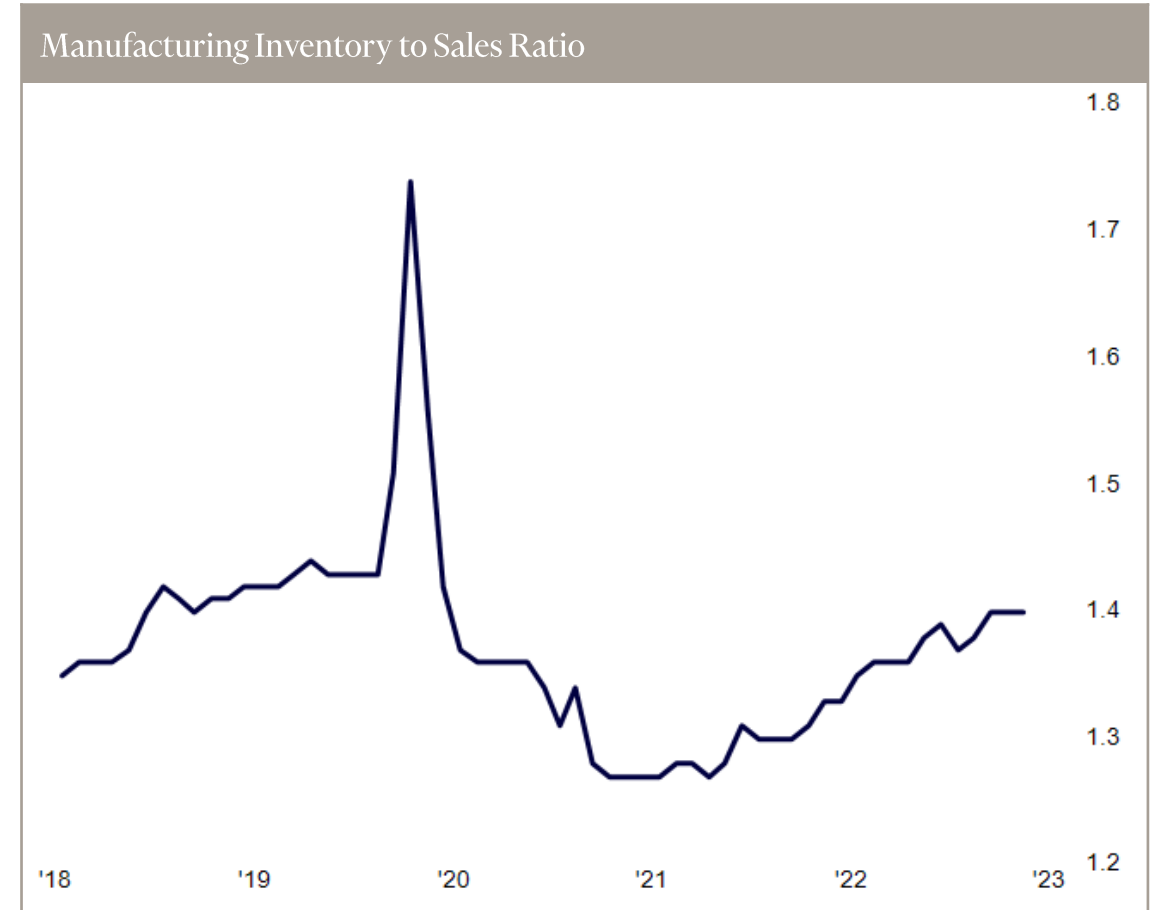
A Rolling Recession?

As housing begins its recovery, manufacturing appears to be the next sector to roll over.



As of 6/30/2023

Source: Factset

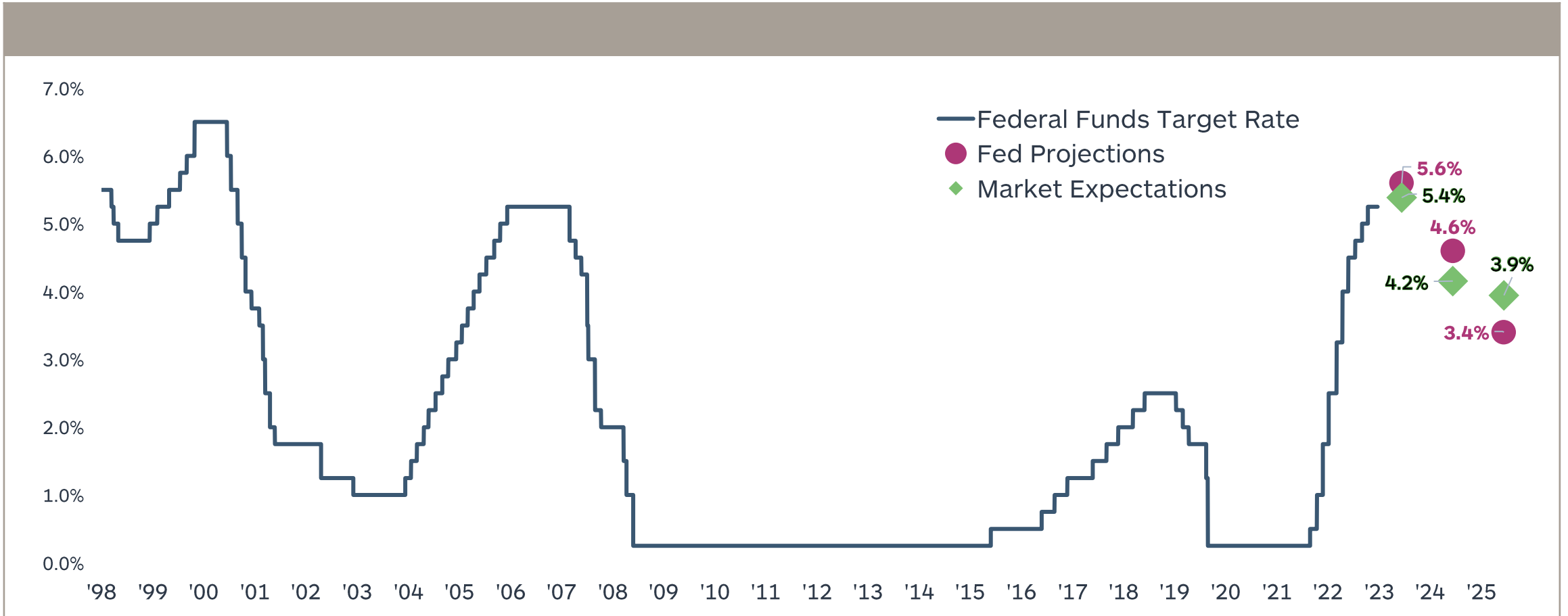


As of 6/30/2023

Source: Factset

The Fed Sees a Light at the End of the Tunnel

The Fed has squashed the notion of rate cuts in 2023. But still, one or two more hikes might be it.

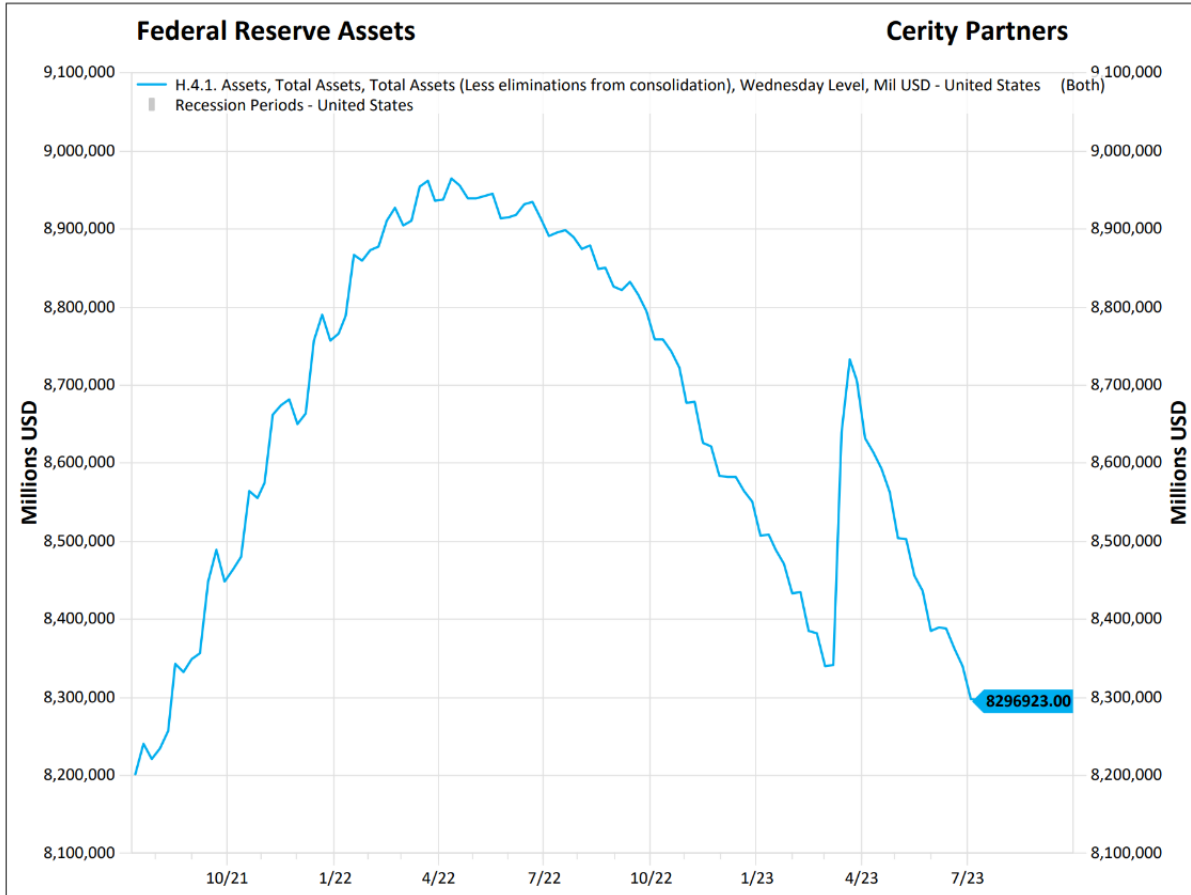


As of 6/30/2023. Market expectations are derived from Fed Funds futures pricing

Source: Factset

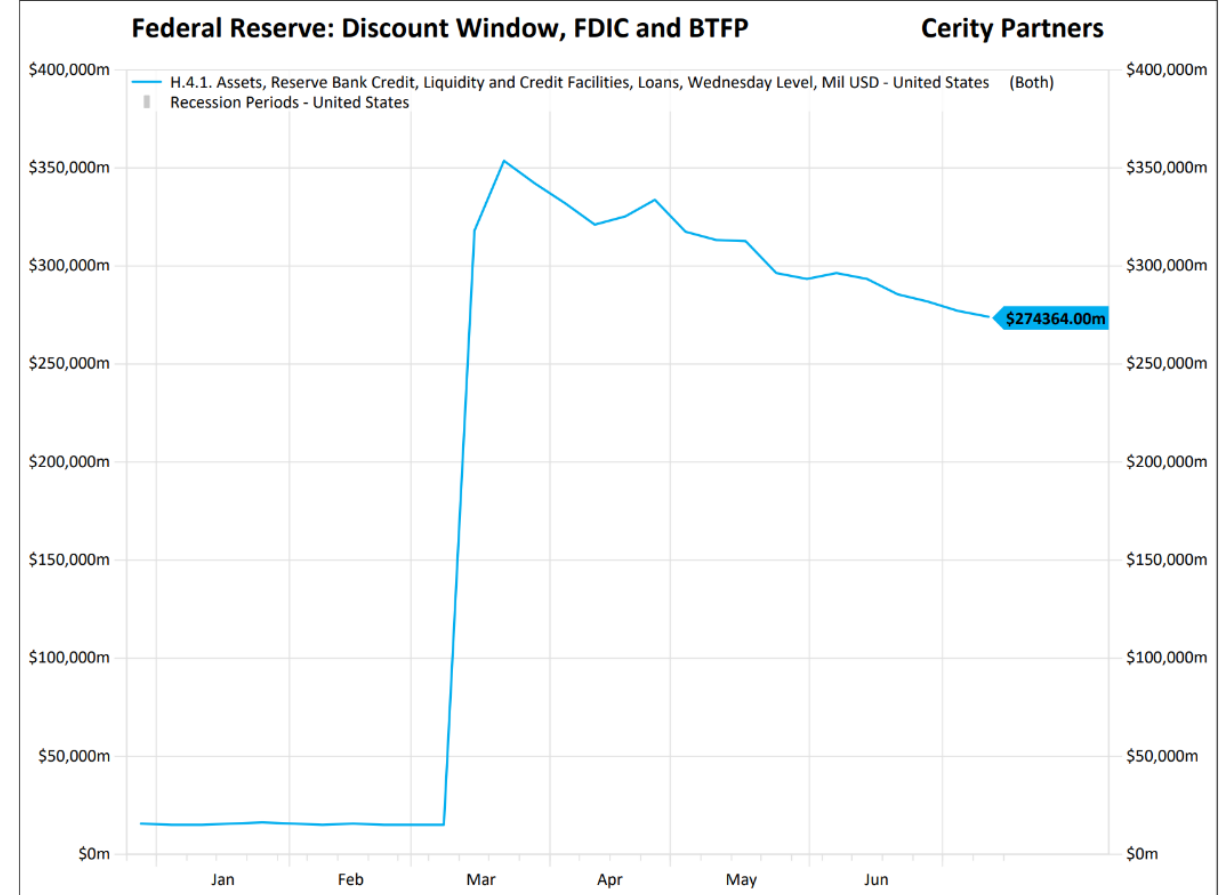
U.S. Banks: Crisis Averted

Swift action by the Fed seems to have resolved liquidity issues at most U.S. banks.



As of 6/30/2023

Source: Factset

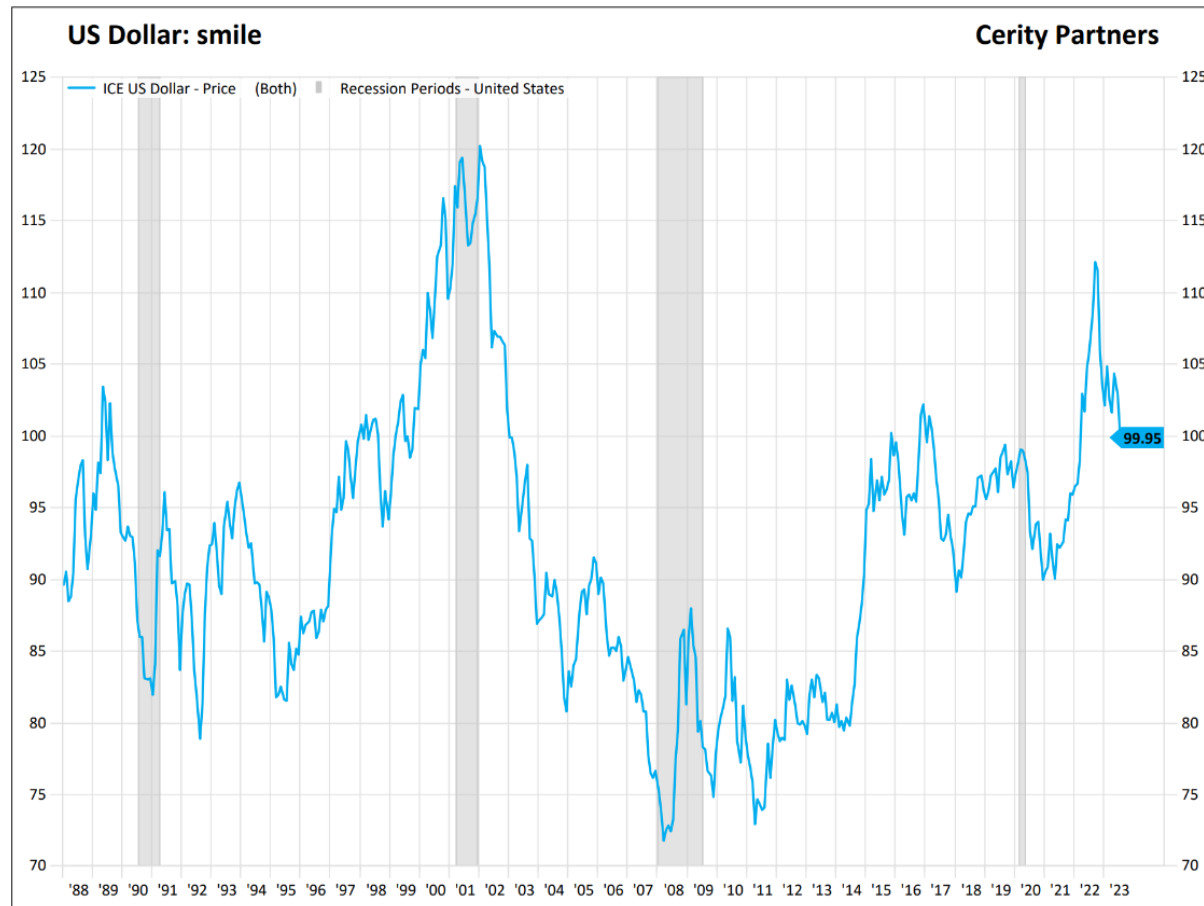


As of 6/30/2023

Source: Factset

The U.S. Dollar

A weak start to the year. But what does it mean?



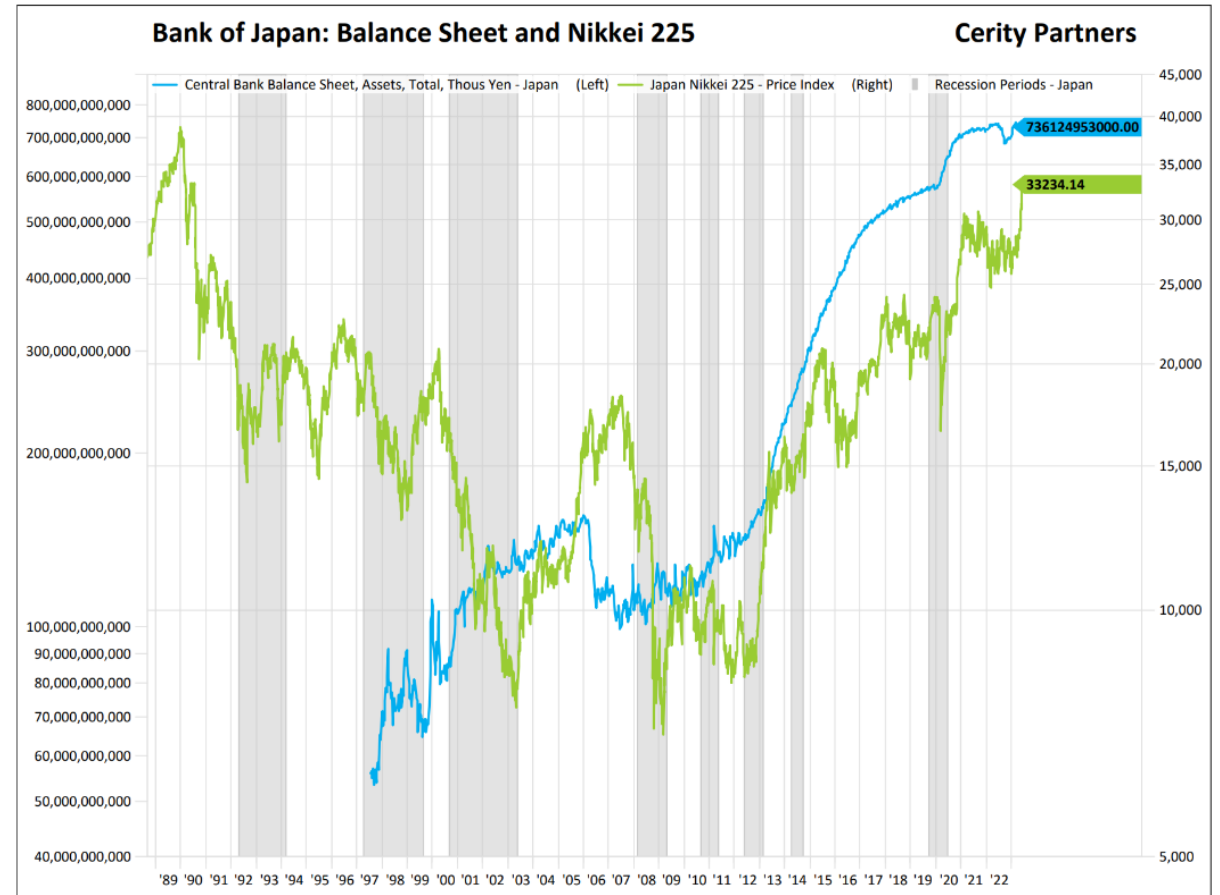
Source: Factset

As of 6/30/2023

The Case For Japan

Is it different this time?

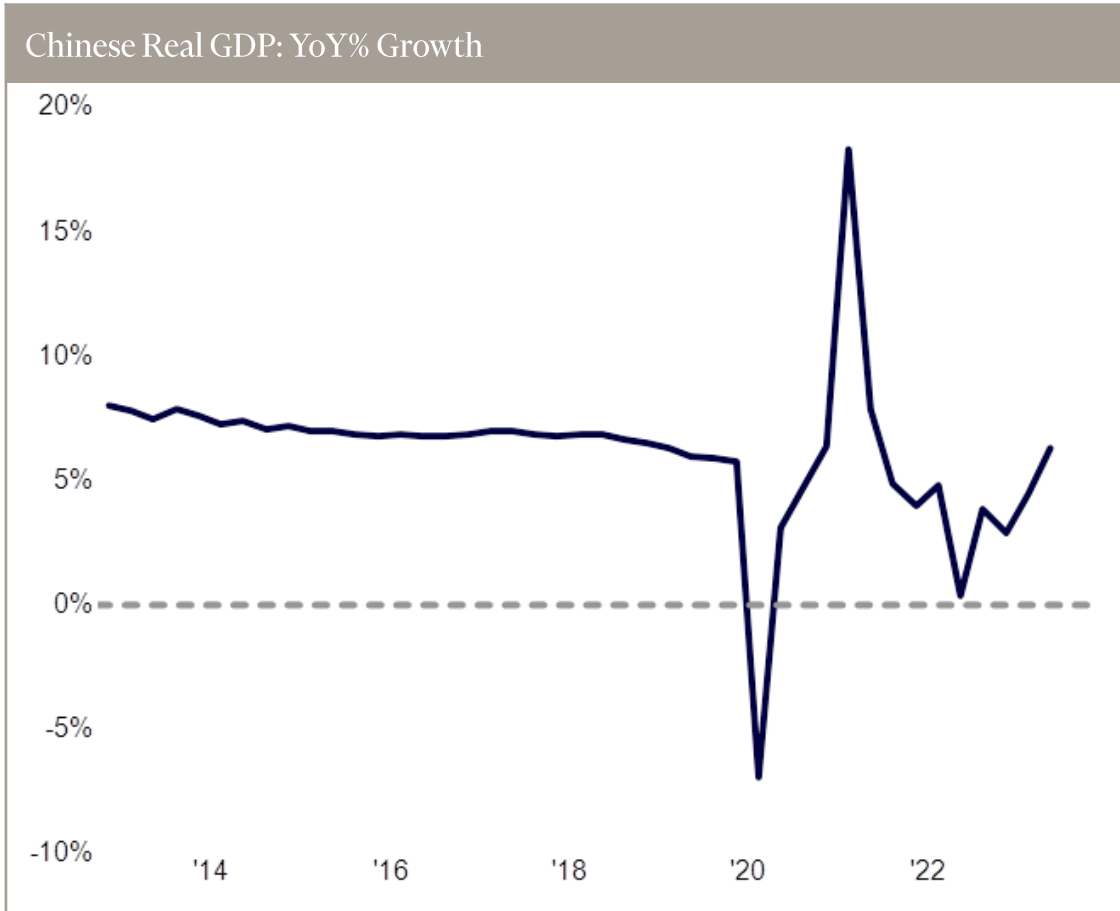
Pros	Cons
Valuation discount	No change in relative valuations for 8 years
Tailwind from considerable share buybacks	Fund managers have been getting burned for decades
Strong corporate governance laws and practices	Balance sheet unwind may be long and difficult
High corporate net cash positions	Deflation risk not over
Low wage pressure	Poor demographics
Weak Yen	
New BOJ regime	



Source: Factset

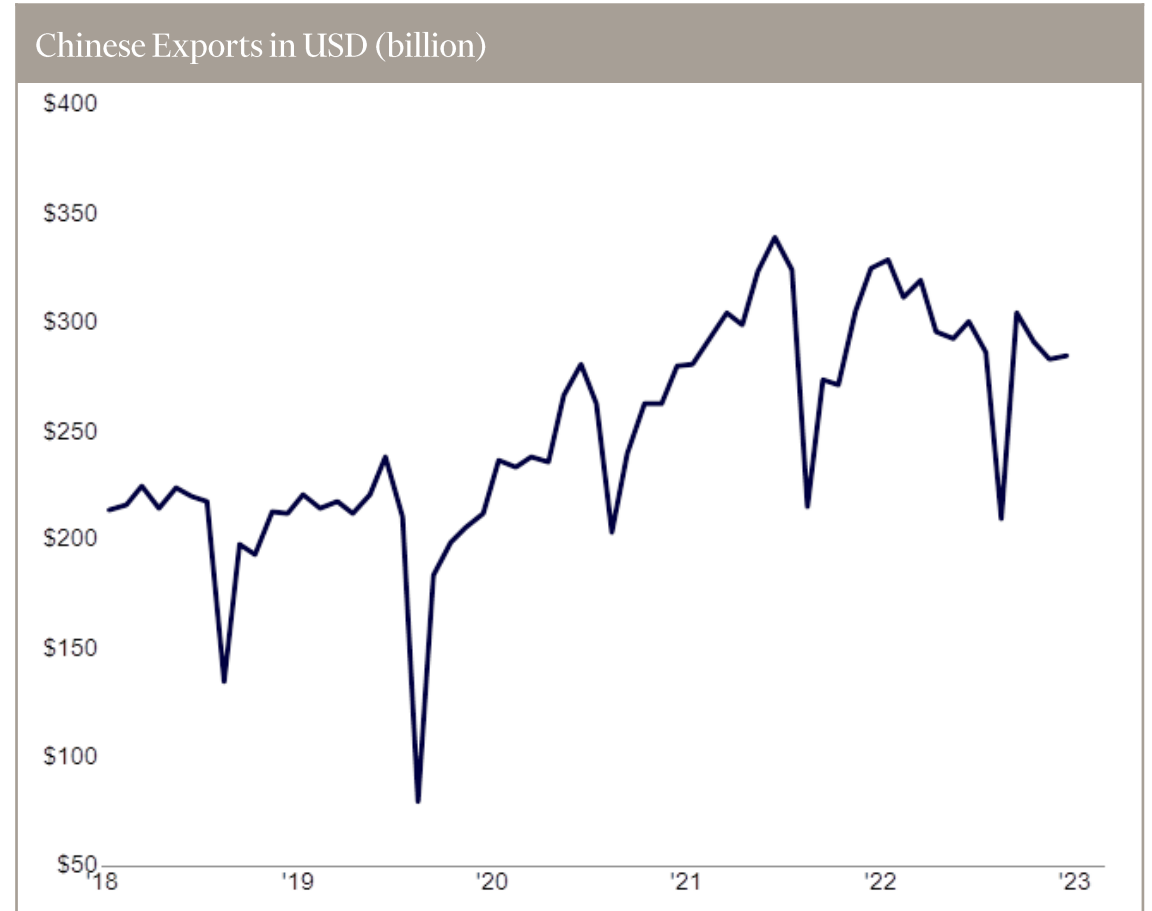
China

Growth is rebounding, but below expectations, thanks to weak exports and domestic spending.



As of 6/30/2023

Source: Factset

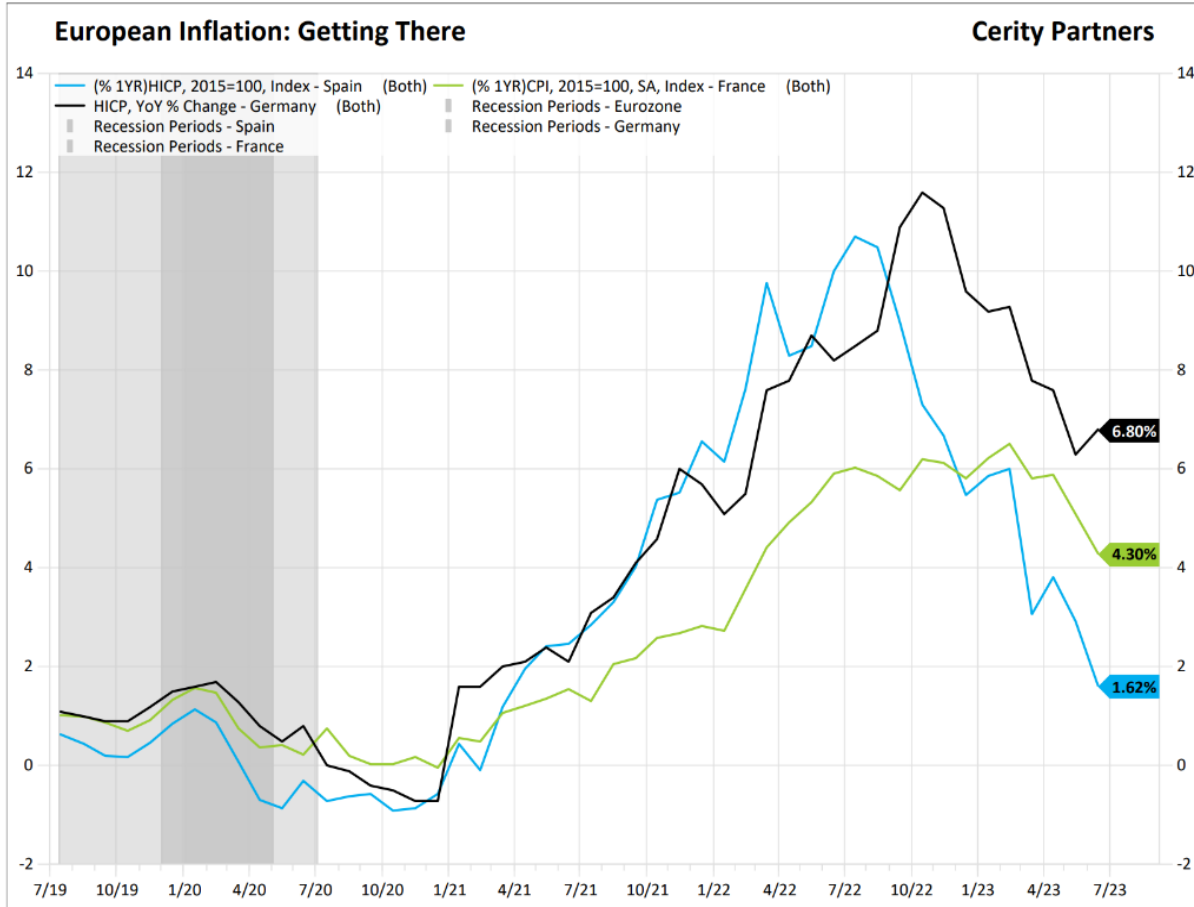


As of 6/30/2023

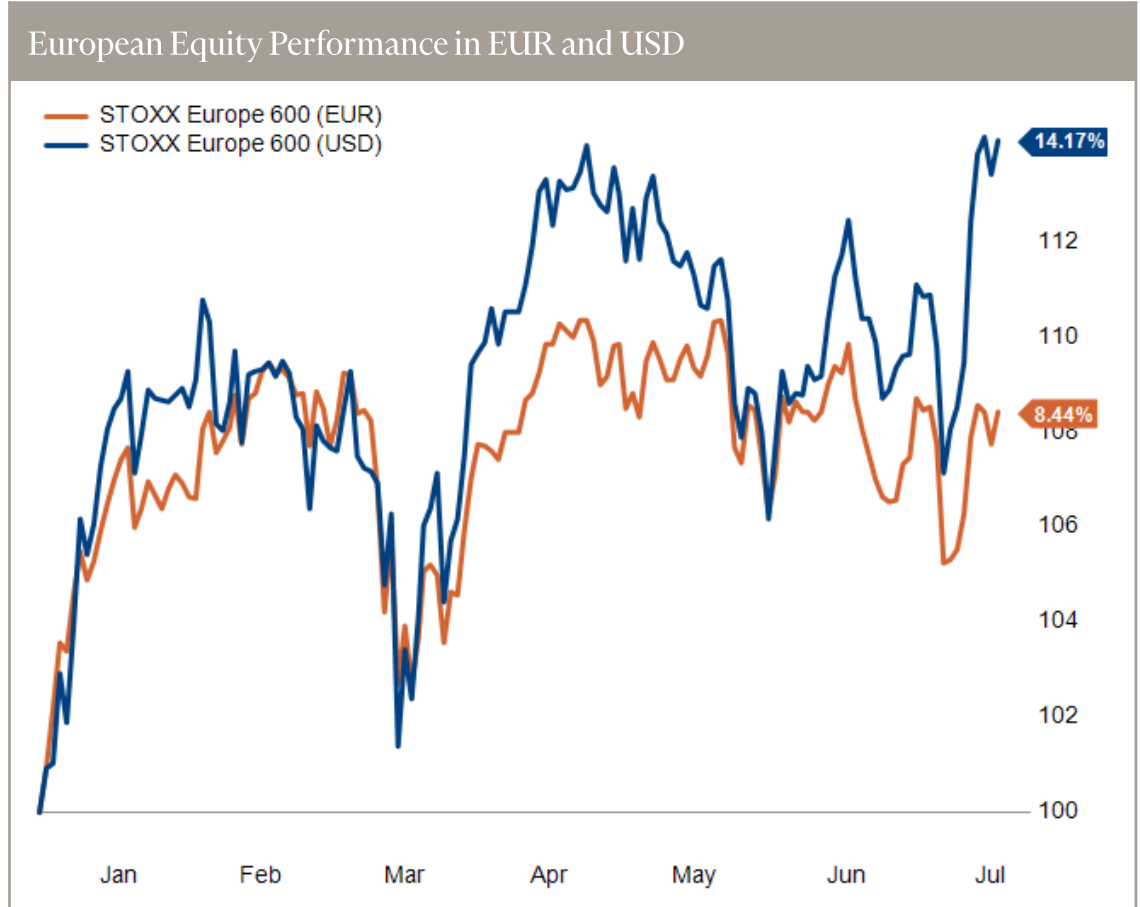
Source: Factset

Europe

Inflation is coming down, but the ECB is still pressing ahead.



Source: Factset



Source: Factset



U.S. Equities

How Is 2023 Going?

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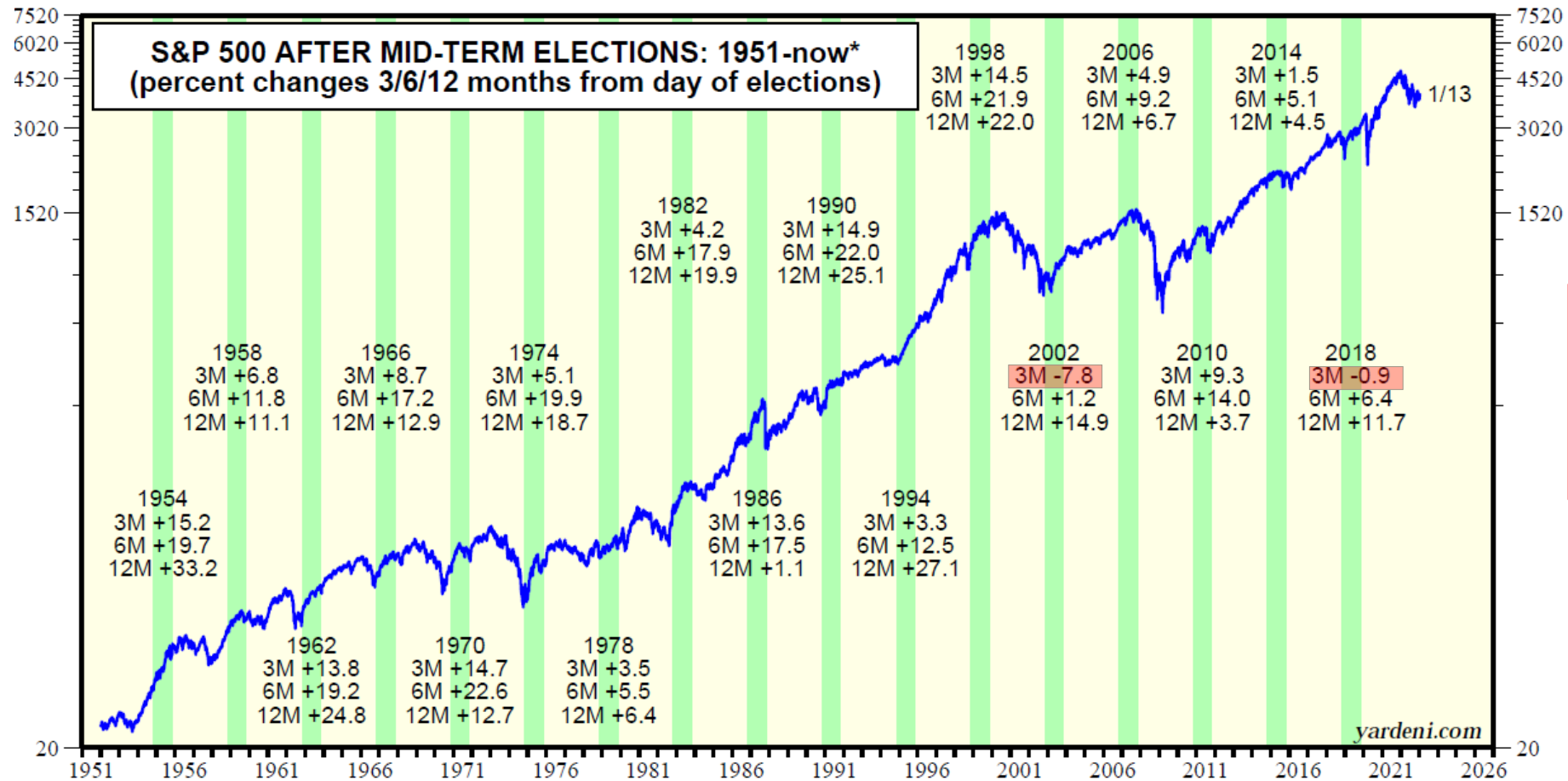
We Made Some Predictions at the Beginning of the Year

Let's look at how they've turned out



Post Mid-Term Elections Markets Tend to Rally

Current returns are in-line with historical precedent after mid-term elections.



2022
3M +8.2%
6M +8.7%
12M ???

Source: Yardeni Research

Technical Analysis in Early 2023 Was Positive

The 200-day moving average turned up in late March and a Golden Cross was reached in February.



Source: Factset

Technical Predictions Came to Fruition

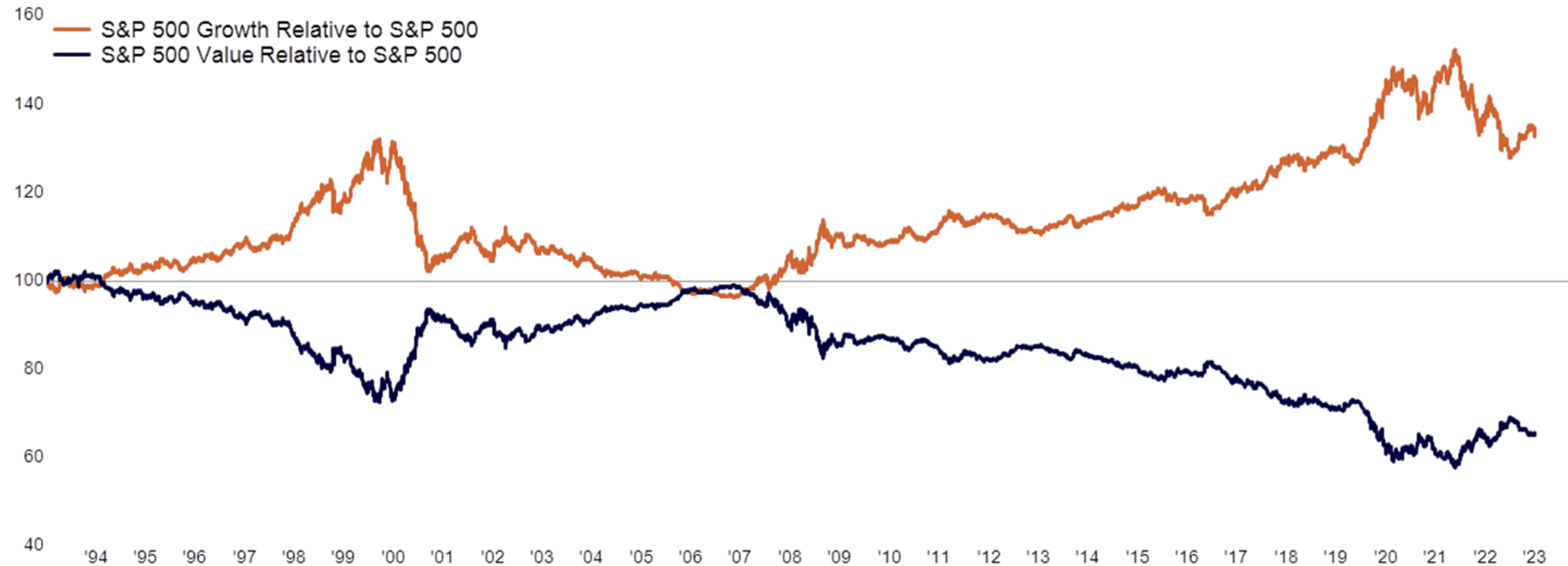
A look at the moving averages shows a bit of a stretched market; not an invitation to market time.



A Look Beneath the S&P 500 Tells a Story

We expected value to outperform growth this year; we have been wrong . . . so far.

S&P 500 Growth and Value: Relative Price Performance



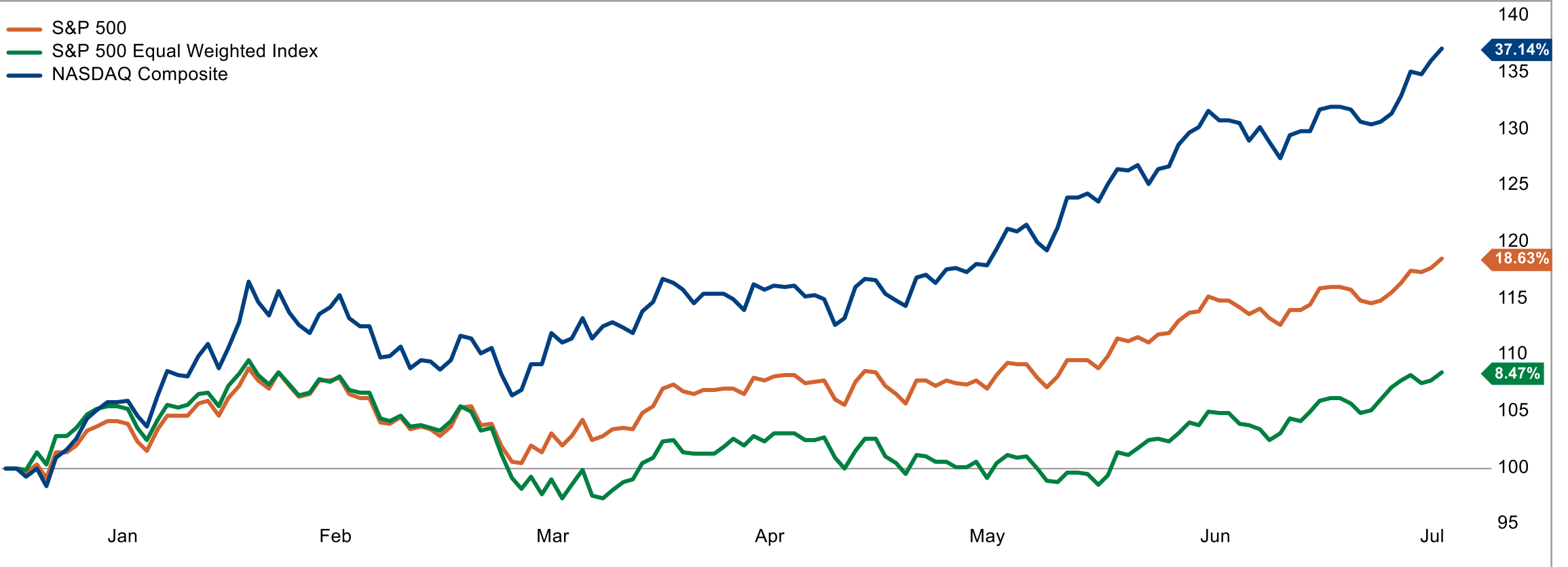
As of 6/30/2023

Source: Factset

Which Leads to the Big Discussion About Breadth

Technology/AI stocks' divergence from the rest of the market does not seem sustainable.

S&P 500 Growth and Value: Relative Price Performance



As of 7/18/2023

Source: Factset

A Close-Up Look at the Contest

Tuesday, July 18th's market action shows how the market narrows.

FINANCIAL TIMES

Microsoft to charge \$30 per month for generative AI features



Richard Waters in San Francisco

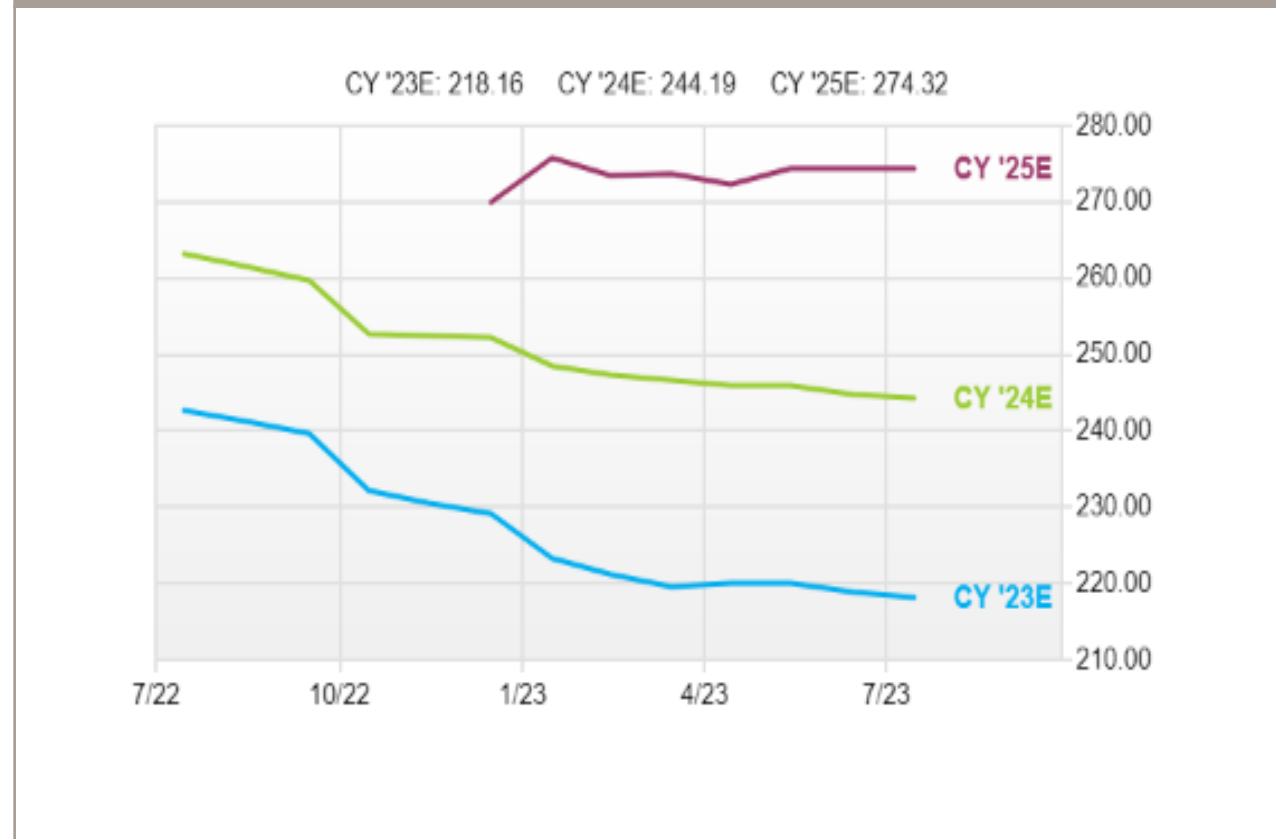
Tue, July 18, 2023 at 11:30 AM EDT



The Next Battleground

After the market has weathered inflation, the Fed, elections, and recession fears . . . now we get to earnings.

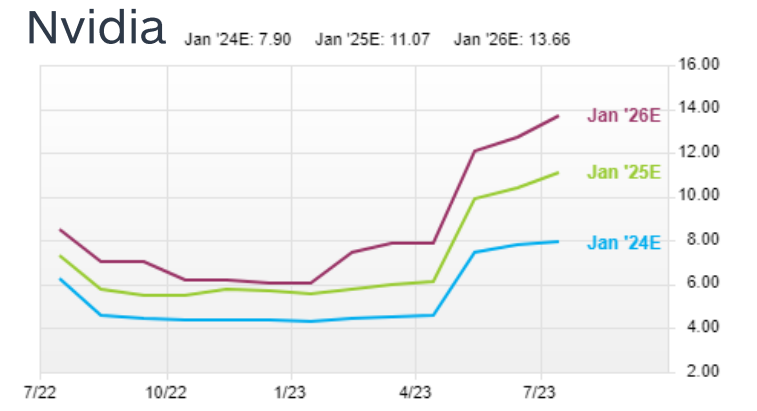
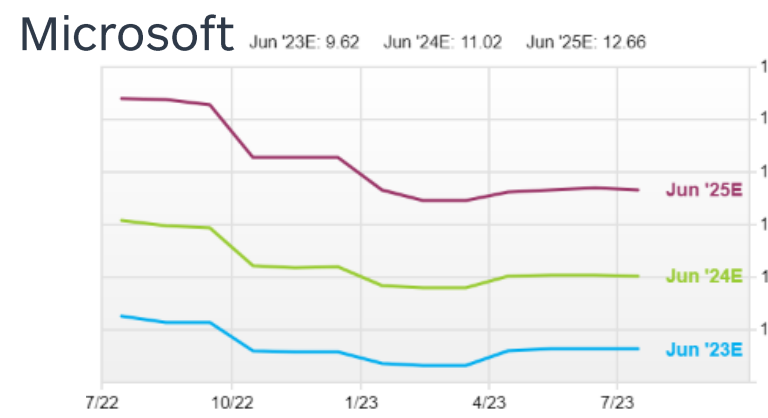
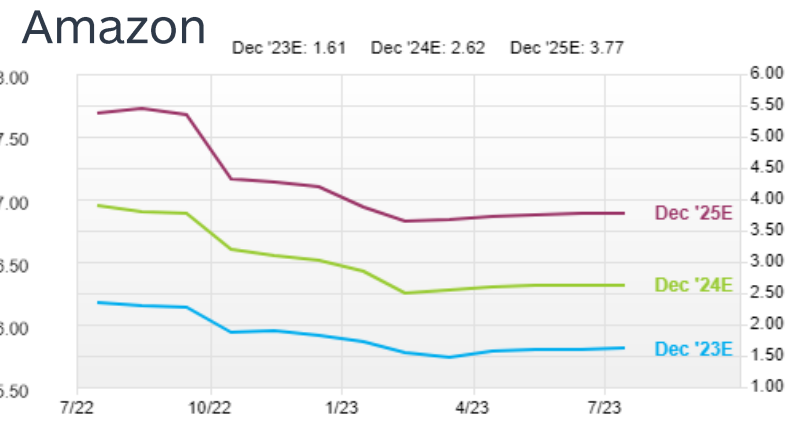
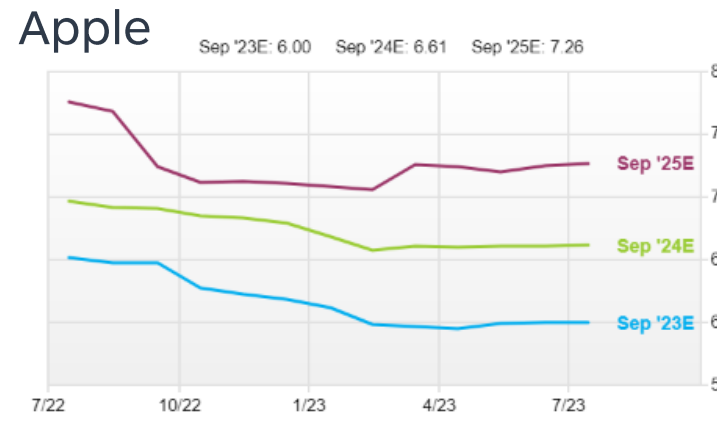
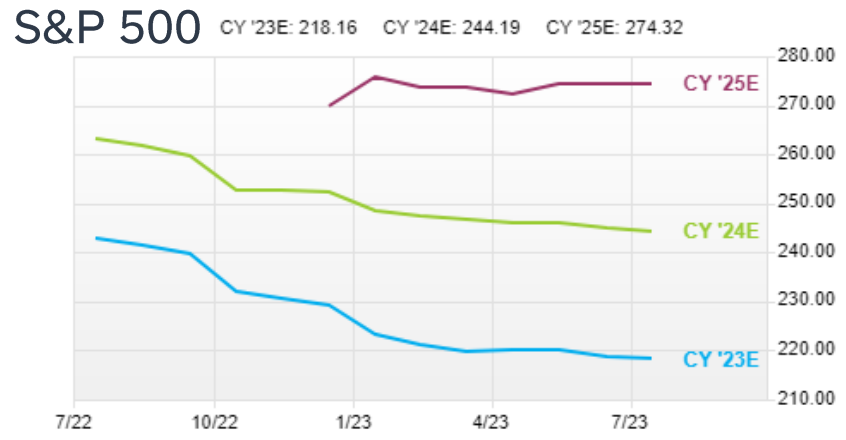
Changes in S&P 500 EPS Estimates Through 2023



Source: Factset

Why We Think Earnings Will Surprise to the Upside

There is a dichotomy between top-down macro analysts and company-specific analysts



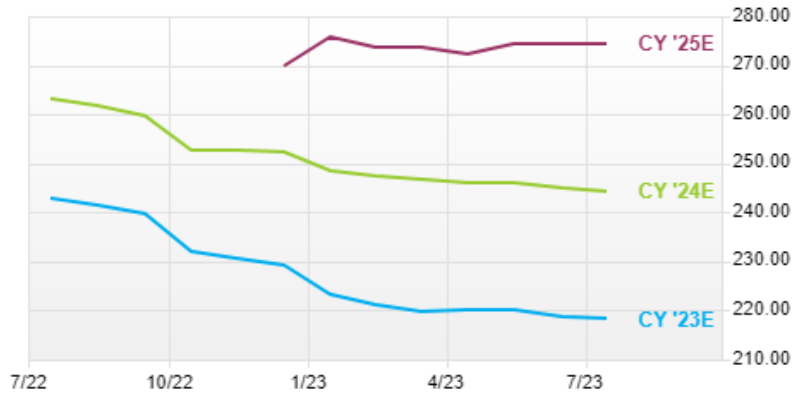
Source: Factset

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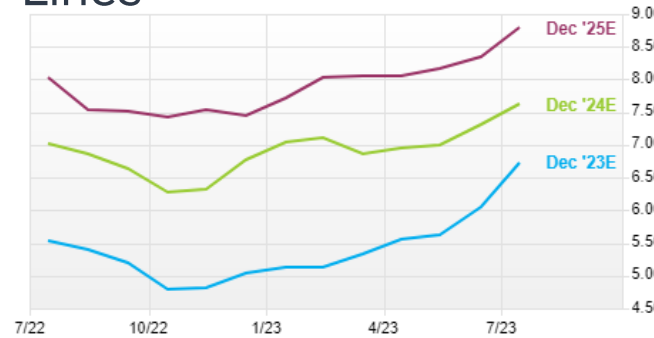
S&P 500

CY '23E: 218.16 CY '24E: 244.19 CY '25E: 274.32



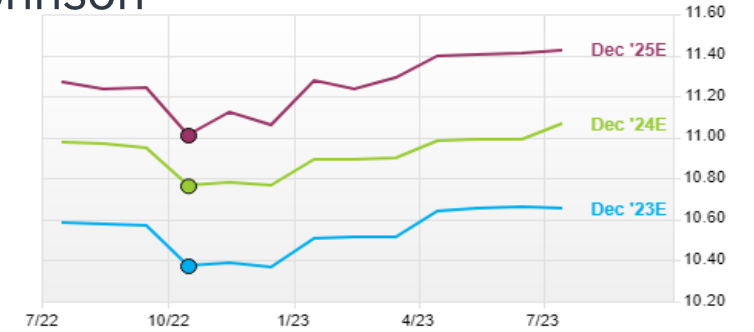
Delta Air Lines

Dec '23E: 6.72 Dec '24E: 7.61 Dec '25E: 8.78



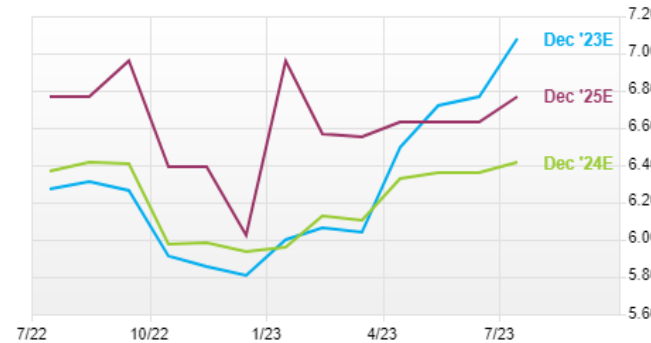
Johnson & Johnson

Dec '23E: 10.37 Dec '24E: 10.76 Dec '25E: 11.01



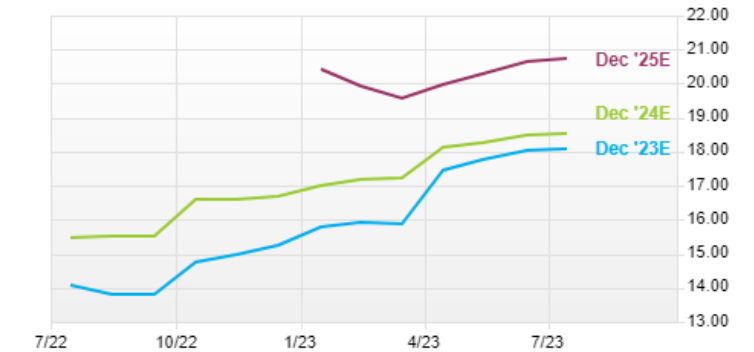
General Motors

Dec '23E: 7.08 Dec '24E: 6.41 Dec '25E: 6.76



Caterpillar


Dec '23E: 18.07 Dec '24E: 18.50 Dec '25E: 20.70



Source: Factset

Early 2Q Earnings Commentary is Positive


Very early in earnings season, there's something for the bulls and something for the bears

 The New York Times


JPMorgan, Citigroup and Wells Fargo Report Better-than-Expected Profits

 CNBC

Delta posts record quarterly earnings, hikes full-year outlook on travel boom

 Barron's

PepsiCo Stock Rises After Earnings Beat and Guidance Boost. Thank Potato Chips.

 Yahoo Finance

Lockheed Martin stock trends higher on earnings beat, strong demand

Source: Barron's, CNBC, Marketwatch

Many of the Worst Prognostications Still Look Unlikely

Fears from the summer of 2022 – These were off the mark.

F Forbes

Jamie Dimon Warns Of A 'Hurricane' Coming Our Way ...

Jamie Dimon, the CEO of JPMorgan and one of the most respected Wall Street leaders, gave a stern warning to investors. He advised people to...

Jun 2, 2022

Morgan Stanley | RESEARCH

July 11, 2022

US Equity Strategy | North America

Weekly Warm-up: Strong Dollar
Just Another Headwind for
Earnings, Leaving Unfinished
Business for the Bear

B Bloomberg.com

JPMorgan Sees Oil at \$380 on Worst-Case Cut by Russia

Global oil prices could reach a "stratospheric" \$380 a barrel if US and European penalties prompt Russia to inflict retaliatory crude-output...

Jul 1, 2022

PIPER | SANDLER

US Economics | Macro Research

July 27, 2022

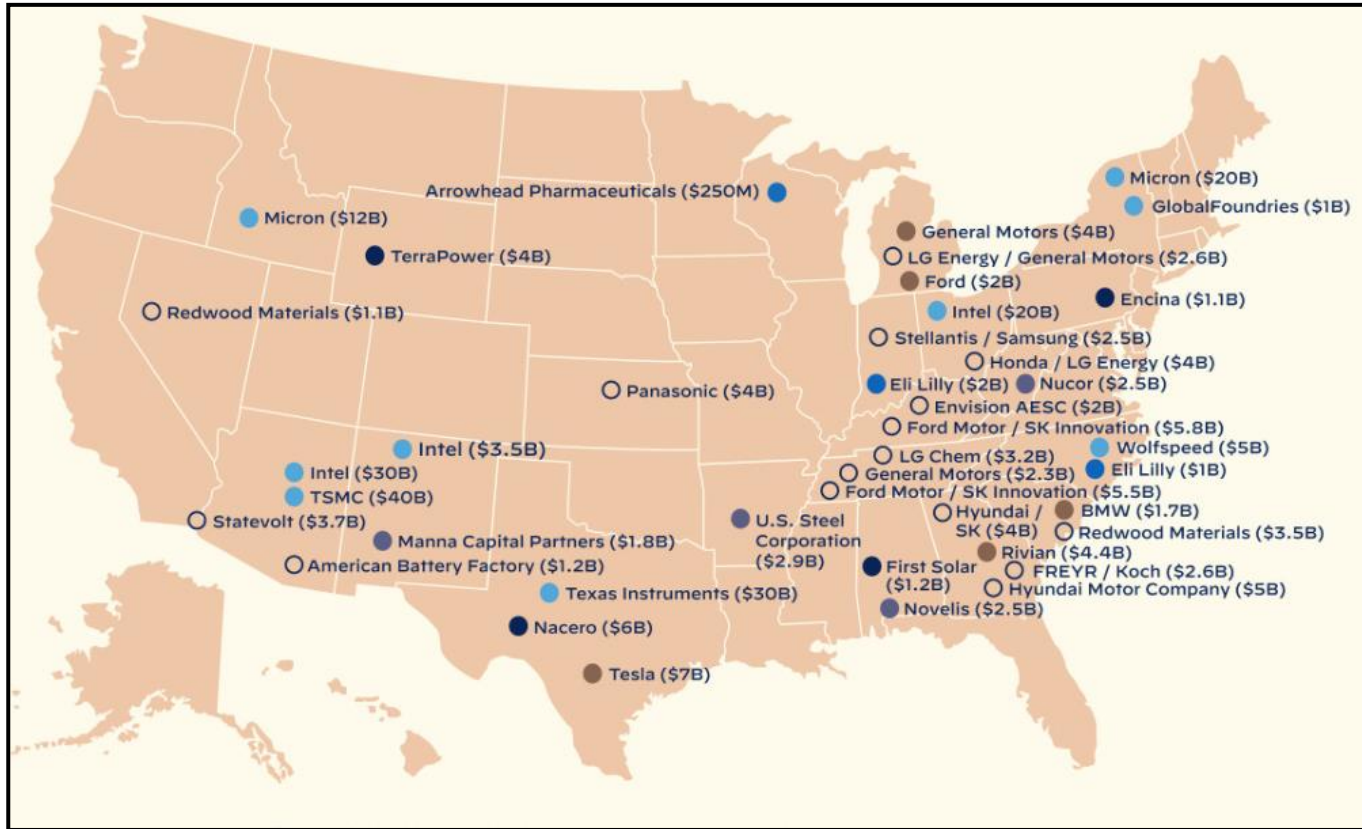
The Profit/EPS Downturn Is Here.

[Report Link](#)

Conclusion: Profits always fall in recessions, and we're moving into one now. On average, in recessions profits & EPS decline -12%, and -24%, respectively. We're now forecasting S&P EPS to decline -8% cumulatively in 2022 & 2023 – to \$200 in 2022, and \$190 in 2023. (pgs 2-4)

Source: Bloomberg, Morgan Stanley, Piper Sandler

U.S. Manufacturing is on the Rise



OTHER \$1B+ INVESTMENTS
(Sites to be determined)

- SK Group (\$22B)
- Cytiva / Pall Corp (\$1.5B)
- CubicPV (\$1B)

LEGEND

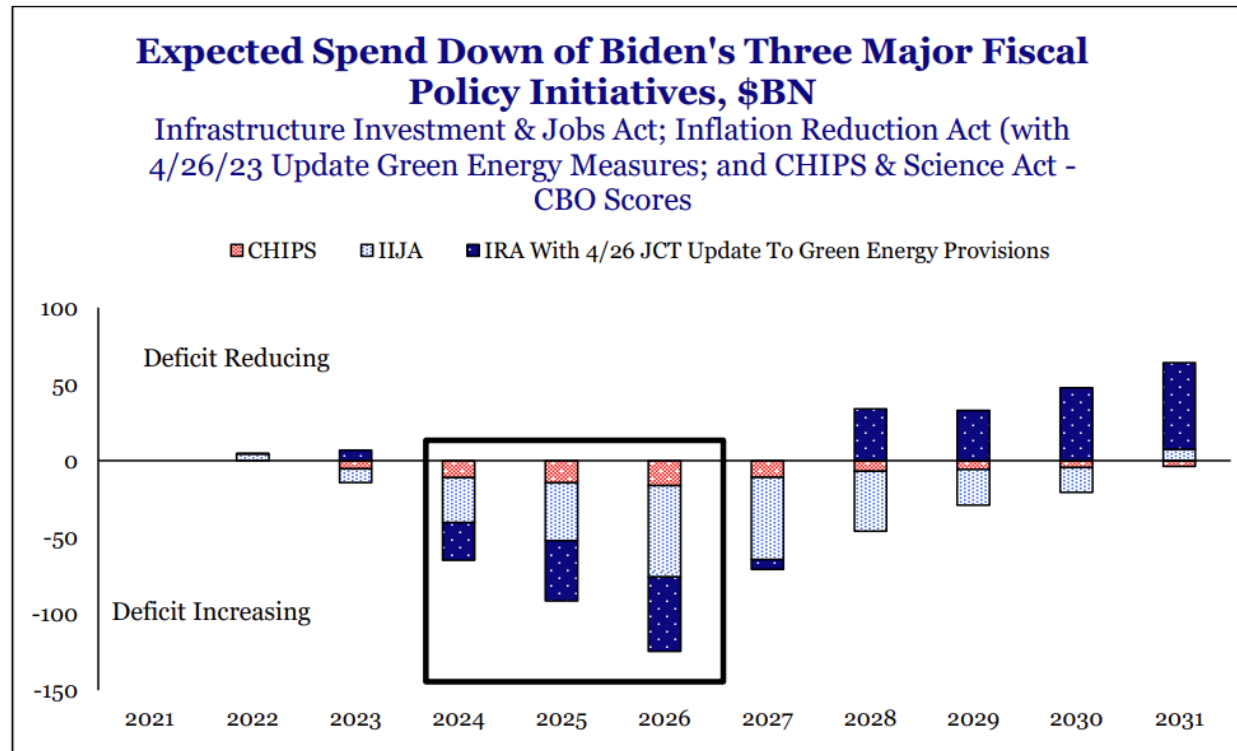
- Battery Factory (\$53B)
- Auto/Electric Vehicle Plant (\$26.2B)
- Volkswagen (\$7.1B)
- Semiconductor Fab (\$183.5B)
- Biomanufacturing Facility (\$4.75B)
- Steel and Aluminum (\$9.7B)
- Other Clean Energy (\$13.3B)

Source: Reshoring Initiative, ZETA, SIA, and Alliance for Automotive Innovation
Note: Initial snapshot of just some of the companies announcing major investments in the U.S. since 2021.

Infrastructure Spending: A Structural Tailwind

Lots of announcements so far, but the real spending will happen over the next few years.

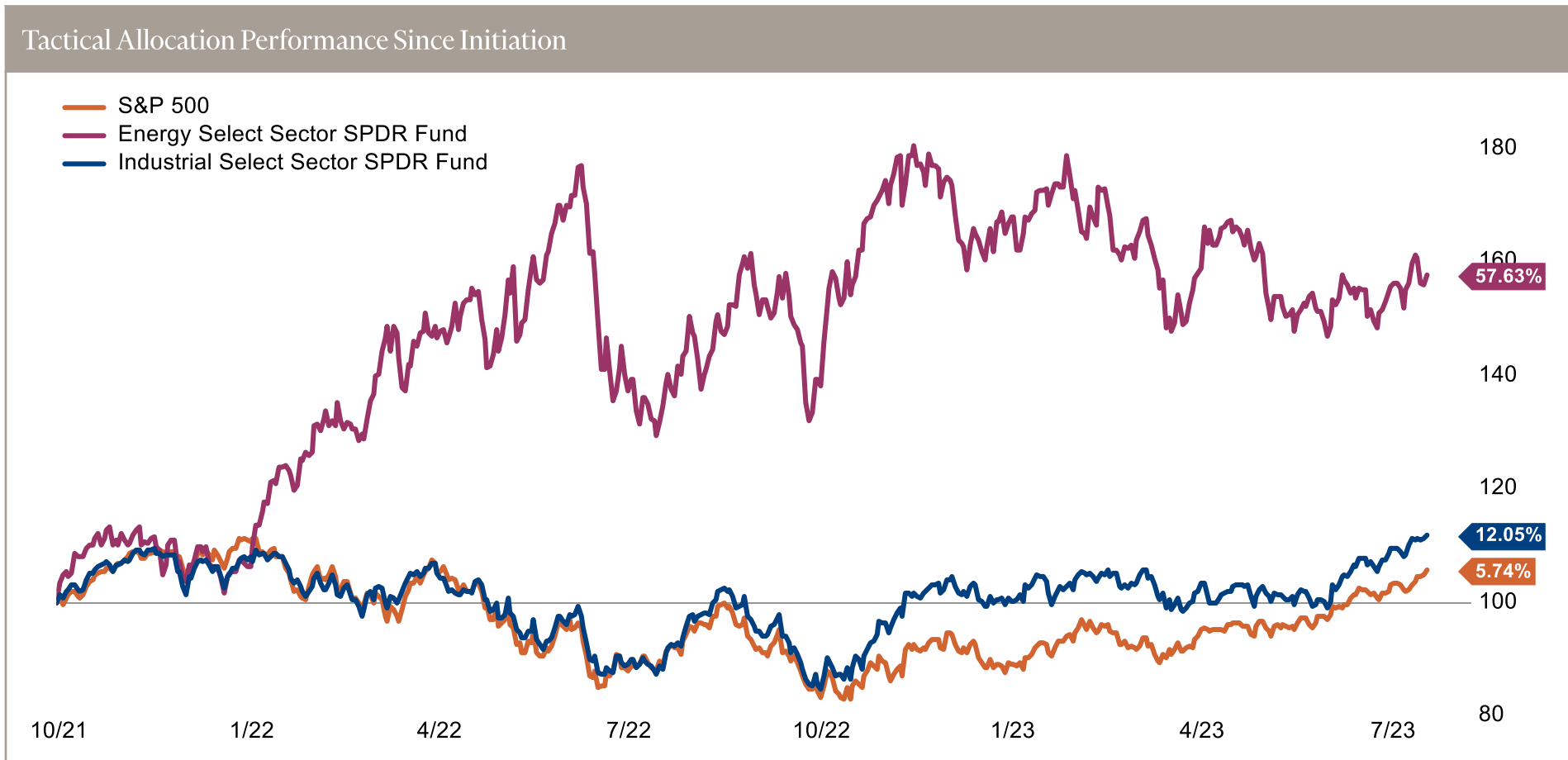
LONG LAG TIME OF INFRASTRUCTURE SPENDING: THE EFFORT REALLY DOES NOT START UNTIL 2024



Source: Strategas

What Does Leadership Shift Imply?

Our tactical allocations currently favor two of the primary value industries.



As of 7/18/2023

Source: Factset

Important Notes

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