MONTHLY MARKET UPDATE

October 2022

OPAL WEALTH ADVISORS

Most global financial assets rebounded from the oversold conditions of August/September with the notable exception of Chinese equities. Capital market narratives for the month were centered around monetary policy and the inflation backdrop while also acknowledging a clearly decelerating global economy which generally moves in lockstep with the corporate earnings landscape. Other market attention grabbing headlines included China's 20th Party Congress confirming President Xi Jinping for an unprecedented 5-year term, the shortest ever tenure for a British Prime Minister, and continued anxiety surrounding the Russian invasion of Ukraine.

Global equities surged to begin the fourth quarter with Europe and developing markets (ex-China) leading the way. U.S. equity markets were led by value and small caps with cyclicals (energy, industrials, financials, materials) and health care names driving returns. The capitalization-weighted S&P 500 (+8.1%) again underperformed the equal-weighted S&P 500 (+9.77%), with a year to date return differential of 4.4%. Bond markets continued to post losses in a record down year with only senior bank loans and high yield bonds managing gains for the month. October saw the Barclays Aggregate (-1.3%) and Intermediate Aggregate (-0.8%) continue to grind lower leaving both down double digits for the year-to-date.

The U.S. Dollar (USD) weakened slightly in October but remains up nearly 17% for the year. Since 1967, only 1981 and 1982 posted stronger year-to-date returns for the USD through the first three quarters. Commodities were mixed but generally higher in October: energy (+4%), ag commodities (+1%), metals (-0.56%), and precious metals (-1.4%).

Market Anecdotes

- Through the end of October, FactSet noted blended third quarter earnings for the S&P 500 of 2.5% growth with blended net margins of 12% which would represent a fifth consecutive QoQ margin decline, still above the five-year average margin of 11.3%.
- Bespoke notes that there have been 5 months so far this year when the S&P 500 has been up or down 7.5%. You have to go back to the 1930s to find another such instance.
- The future of the richly-valued USD depends very much on the direction of the U.S. economy while also factoring in geopolitics, technical conditions, and foreign rate differentials.
- While recessions clearly impact demand for goods and services, Arbor Data Science highlighted demand for oil declines as well—a dynamic that is not lost on FOMC policy-makers.
- The ECB delivered another 75bp rate hike as expected, and announced changes to the TLTRO facility, while the BoJ left policy rates unchanged.
- Nearly half of Americans have looked for a second job to keep up with inflation in what is likely a significant midterm election cycle consideration.
- Death of the goldbug? October marked a seventh straight negative month for gold, its longest consecutive monthly losing streak on record amid record inflation levels.
- Goldman Sachs made note of emerging market forward P/E multiples at 10.5x. This is somewhere between the 2018 and 2008 bear market levels. Meanwhile, many emerging market central banks are considering rate cuts with much more manageable inflation levels. U.S. small cap P/E ratios also look very cheap relative to their large cap peers.
- The pain that 20-year high mortgage rates have inflicted on the housing market is clear with prices, transaction volume, and home builder sentiment all falling significantly.
- A look at narrow market leadership and average correlations among stocks within the S&P 500 illustrate some of the primary headwinds for active managers in place since the GFC and era of central bank intervention policies.
- The pain of rising interest rates is clear and translates to rising mortgage rates (30yr (5.66%), 15yr (4.98%), and 5/1 adjustable (4.51%))

exerting pressure on the housing market. Rates are also pressuring P/E multiples which sit near the midpoint of the range over the last ten years.

- Softness in the housing market from exuberant levels of late 2021 to early 2022 is apparent. Bianco Research examined several alternative measures also illustrative of both pricing trends and the technical backdrop.
- With midterms approaching, political analysts are stepping up their forecasts with projections of a divided Congress and a plethora of Trump 2.0 storylines. Key takeaways are limited legislative pathways translating to ample executive agency and debt limit/shutdown debates.
- The EU energy crisis with December and February sanctions looming has EU bound Russian gas being flared, the EU buying gas at any price, and a G7 agreement of a price cap on Russian oil.
- Housing market dynamics, weak domestic demand, a contraction in exports, and persistent zero Covid public health policies are seemingly limiting the modest stimulus measures undertaken in China, leaving strategists with an underwhelming outlook for Chinese equity markets.

Economic Release Highlights

- Third Quarter U.S. GDP accelerated to 2.6% from -0.6% the prior quarter and came in slightly higher than the consensus forecast of 2.3% thanks to higher-than-expected Personal Consumption Expenditures of 1.4% versus the forecast of 0.8%.
- The Personal Income and Outlays report showed YoY headline and core inflation of 6.2%a vs 6.1%e and 5.1% vs 5.2% alongside MoM readings of 0.3% vs 0.3% and 0.5% vs 0.5%, all in line with expectations.
- Personal Consumption Expenditures (0.6%a vs 0.4%e) and Personal Income growth (0.4%a vs 0.3%e) came in stronger than expected.
- The October jobs report revealed 261,000 new jobs, well above the consensus forecast of 210,000 but lower than the prior month. The unemployment rate moved up one tick to 3.7%.
- Average hourly earnings increased MoM (0.4%a vs 0.3%e) and YoY (4.7%a vs 4.7%e).
- The Job Openings and Labor Turnover survey revealed 10.717mm job openings, in excess of the consensus estimate of 9.875 and an increase over the prior month.
- October's ISM Manufacturing Index (50.2a vs 50.0e) softened slightly while ISM Services (54.4a vs 55.4e) missed consensus and fell two points relative to the prior month.
- The PMI report came in below consensus on both manufacturing (49.9 vs 51.2) and services (46.6 vs 49.3) fronts and saw the composite reading decline two points to 47.3.
- The Case Shiller Home Price Index came in slightly under consensus forecast with prices MoM (-1.3% vs -0.8%) and YoY (13.1% vs 14.1%) softening more than expected. New Home Sales declined (603k vs 685k) but did not fall as much as was expected (585k). Pending Sales fell 10.2% versus estimates of -3.8%.
- The Housing Market Index fell from 46 to 38, well below consensus forecast of 44. Housing Starts (1.439M) and Permits (1.564M) were relatively in line with expectations while Existing Home Sales in September of 4.71M came in slightly higher than the 4.695M consensus estimate.
- Consumer Confidence registered 102.5 versus consensus forecast of 106.0.

Outlook

Whether the recovery rally in October will ultimately be categorized as a bear market rally or something with more staying power remains to be seen. What underpinned the rally was increasing sentiment that the Fed tightening cycle is nearing its end thanks to emerging signs of inflation abating coupled with an indisputably healthy U.S. consumer. We do feel the global tightening cycle is at an inflection point but also acknowledge the Fed's specific need to see a slowdown in the U.S. labor market along with decelerating inflation trend data to substantiate a pause. This leaves the FOMC in a very difficult position as it attempts to engineer a 'soft landing.' Looking forward, we see recession risks more prevalent in the spring/early summer next year but still not a foregone conclusion.

With equity markets currently down 20% and likely only 4-6 months of tightening financial conditions, we feel this warrants a tight neutral position toward equities relative to respective benchmarks. Routine rebalancing into short-term strength is a focal point due to our view that the worst of the rise in interest rates is behind us and strength in real wages may force the Fed's hand once inflation does begin to cool down.

From a geography perspective, although valuations are dramatically cheaper overseas, persistent strength in the USD, high geopolitical tensions, and severe supply side issues in Europe have us maintaining a tempered short-term outlook for developed non-U.S. markets. China's dominance across emerging markets tempers our view on developing markets even more so. Fixed income investors should maintain a slightly short duration bias and remain overweight credit sectors—especially within floating rate issues.

Equity	Level	1 Mo	3 Mo	YTD	1 Yr	3 Yr
Dow Jones	32733	14.07	0.20	(8.42)	(6.74)	8.83
NASDAQ	10988	3.94	(11.13)	(29.32)	(28.56)	10.71
S&P 500	3872	8.10	(5.86)	(17.70)	(14.61)	10.22
Russell 1000 Growth		5.84	(8.90)	(26.61)	(24.60)	11.75
Russell 1000 Value		10.25	(2.41)	(9.32)	(7.00)	7.31
Russell 2000		11.01	(1.68)	(16.86)	(18.54)	7.05
Russell 3000		8.20	(5.50)	(18.44)	(16.52)	9.79
MSCI EAFE		5.39	(8.95)	(22.81)	(22.62)	(0.82)
MSCI Emg Mkts		(3.09)	(14.01)	(29.15)	(30.73)	(4.07)
Fixed Income	**Δ Yield**	**1 Mo**	**3 Mo**	**YTD**	**1 Yr**	**3 Yr**
US Aggregate	2.22	0.07	0.29	0.45	0.40	(0.49)
High Yield	5.60	(0.04)	0.66	1.33	1.19	0.02
Municipal	1.89	0.02	0.14	0.17	0.09	(0.27)

Commodities	10/31/22	8/31/22	5/31/22	2/28/22
Oil (WTI)	91.80	90.09	114.38	96.13
Gold	1639.00	1715.90	1838.70	1909.90

Currencies	10/31/22	8/31/22	5/31/22	2/28/22
USD/Euro ($/€)	0.99	1.00	1.07	1.12
USD/GBP ($/£)	1.15	1.16	1.26	1.34
Yen/USD (¥/$)	148.63	138.69	128.53	115.11

Treasury Rates	10/31/22	8/31/22	5/31/22	2/28/22
3 Month	4.22	2.96	1.16	0.35
2 Year	4.51	3.45	2.53	1.44
5 Year	4.27	3.30	2.81	1.71
10 Year	4.10	3.15	2.85	1.83
30 Year	4.22	3.27	3.07	2.17

Style Returns

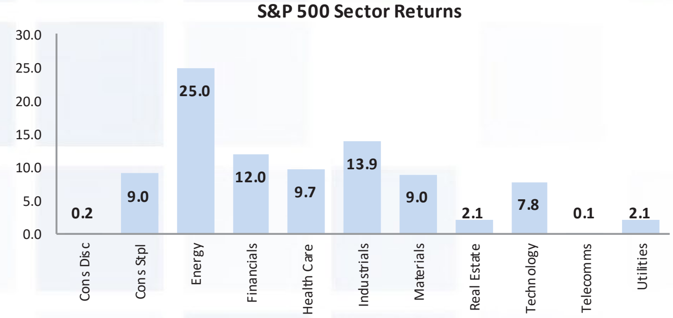
MTD

	V	B	G
L	10.25	8.02	5.84
M	9.45	8.88	7.86
S	12.59	11.01	9.49

YTD

	V	B	G
L	-9.32	-18.54	-26.61
M	-12.83	-17.55	-26.06
S	-11.19	-16.86	-22.57

S&P 500 Sector Returns



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