MONTHLY MARKET UPDATE

October 2023

OPAL WEALTH ADVISORS

Financial markets unfortunately kicked off the fourth quarter trending similarly as the third quarter where rising yields contributed to tighter financial conditions in what was a difficult environment for both stocks and bonds. Key drivers behind market activity in October included the move higher in interest rates, continuation of the higher for longer Fed narrative, third quarter earnings season, and a stark reminder of geopolitical risk stemming from the conflict crisis in the Middle East. Stock markets delivered a third consecutive down month, and a technical correction, after enjoying a healthy rally in the first seven months of the year. Bond markets, after a relatively benign first half, succumbed to stronger than anticipated economic data in the third quarter generating upside interest rate pressure on the long end of the yield curve.

The growth environment, while cooling, has generally surprised on the upside with strong labor markets and robust personal consumption leading the way to 'good news is bad news' concerns surrounding sticky inflation and tight monetary policy. Economic highlights in October included a robust U.S. GDP print of 4.9%, contractionary (but bottoming?) manufacturing sector activity, and slowing service sector growth

surveys. The labor market registered a below forecast 150,000 new jobs in October and a continuing but gradual cooling of wage gains. Disinflation trends continued with most recent headline and core PCE inflation readings of 3.4% and 3.7% respectively. The housing market (shelter) has been a stubborn inflationary component but high mortgage rates are clearly starting to impact activity. Third quarter corporate earnings season, now over 80% complete, is seeing bottom and top line growth of 3.7% and 2.3% respectively, with guidance skewed to the downside. Global investors received another dose of geopolitical risk, in what feels more like a secular trend, with the Hamas attack in Israel adding to Russia-Ukraine, and China-Taiwan as looming market relevant flashpoints with Russo-Chinese-Iranian conflicts mounting to challenge the U.S.-led world order. Despite a clear risk to global energy supplies, oil prices were down on the month suggesting falling global energy demand (falling growth) and/or limited risk of escalation in the Middle East.

Equity markets struggled in October with U.S. (-2.1%), developed international (-4.05%), and emerging markets (-3.89%) all losing ground. Large and mega-cap stocks continued to outpace small-caps and cyclical sectors (energy, materials, consumer discretionary). Equity markets ended October relatively oversold from a technical perspective and still sitting on gains of 10.7% for the year. Bond markets did not fare much better in October with a rise in longer dated interest rates taking the 10-year bond yield up 29 bps to 4.88%. The Barclays Aggregate lost 1.58%, taking year to date losses to 2.77%, the third worst 10-month start to the year on record (data back to 1976). Credit spreads widened slightly in October with high yield moving from 403 to 442 and investment grade from 125 to 132. Commodities were mixed with solid gains in gold (+7.38%) and natural gas (+13.5%) offset by falling WTI oil (-7.75%), copper (-1.9%), and aluminum (-4.5%).

Market Anecdotes

- The recent 3-month S&P losing streak marked just the 9th instance since 1928. The prior five times saw a positive print for November and five out of the last six times saw a positive return for the rest of the year.
- Geopolitical tensions remain very much a key point of financial/commodity market focus with Ukraine- Russia, Israel-Iran (Hamas/Hezbollah), and Taiwan-China all seeking to challenge the U.S.-led world order amidst pronounced divisions within the U.S.
- Significant federal budget deficits and corresponding UST issuance will be a material factor for some time as domestic/global strategic, growth, and market implications all factor into the fiscal policy debate. However, a Bianco analysis of supply, demand, and borrowing cost on marketable Treasury debt suggests inflation is the primary driver of yields, not UST supply.
- High and rising UST rates mean higher debt

service for businesses, government, and consumers as well as higher costs for projects and investments and mark to market losses on bond portfolios.

- The peak rate conversation lends itself well to a simple refresh in bond math and duration where, from today's levels, a 150bp rise in yields translates to a -5.8% total return where a 150 bps fall in yields translates to a +16.4% total return.
- An update from MCSI on commercial real estate illustrates widely differing expectations for distress in office and retail sectors relative to the industrial sector.
- Higher rates are logically impacting both the housing market and homebuilder sentiment. The 30yr mortgage rate marked a seventh consecutive weekly increase to 7.79%, the highest level since September 2000 but interestingly, only slightly above the long-term average of 7.74%.

Economic Release Highlights

- The October Employment Situation Report saw payrolls grow by 150,000, under the consensus call of 179,000 which took headline unemployment up one tick to 3.9%. Labor participation fell one tick to 62.7% while average hourly earnings cooled slightly to 0.2% MoM and 4.1% YoY.
- Headline PCE inflation registered 3.4% YoY alongside core readings of 0.3% MoM and 3.68% YoY. Personal Consumption grew 0.74%, an increase versus prior month and above the forecast and long-term average level of 0.54%. Personal Income grew 0.34%.
- Headline and core CPI registered 3.7%/4.1% YoY and 0.4%/0.3% MoM.
- Retail Sales grew 0.7%, above the 0.3% consensus estimate and forecast range of -0.1% to 0.5%. Ex-Vehicles (0.6% vs 0.2%) and Ex-Vehicles & Gas (0.6% vs 0.1%) also beat.
- The JOLT Survey registered 9.553M job openings, more than the 9.375M consensus estimate but down from the prior month's 9.610M.
- Third quarter U.S. GDP registered 4.9% growth, an increase from the prior quarter's 2.1%, well above the consensus estimate of 4.2%, and toward the higher end of the range (2.8% to 6.0%).
- Third quarter Personal Consumption Expenditures grew a very robust 4.0%, in line with spot consensus estimate of 4.1% and the range of 3.7% to 4.2%.
- Durable Goods Orders grew 4.7%, well above the spot 1.0% forecast and range of -0.5 to 3.6%. Ex-Transportation (0.5% vs 0.2%) and Core Capital Goods (0.6% vs 0%) beat as well.
- October U.S. Flash PMI (C, M, S) at 51.0, 50.0, 50.9 saw both services and manufacturing readings beat consensus forecasts. Flash PMIs (C, M, S) out of the EU (46.5, 43.0, 47.8), UK (48.6, 45.2, 49.2).
- The Consumer Confidence Index in October declined slightly from the prior month (102.6 vs 104.3) but beat the spot estimate of 100.0 and was above the high-end forecast range (99.5-102.0).
- Consumer Sentiment for October registered a five-month low of 63.0, below consensus estimate of 67.5 and the prior month's reading of 68.1.
- The NFIB Small Business Optimism Index declined slightly from 91.3 to 90.8, just short of the consensus forecast of 91.2.
- The Housing Market Index declined 5 points to 40, below the spot forecast of 45 and consensus range of 41 to 47. The Case Shiller Home Price Index grew more than expected on both the month (1.0% vs 0.7%) and year over year (2.2 vs 1.6%) readings.
- Housing Starts (1.358M vs 1.394M) and Permits (1.473M vs 1.450M) both registered within forecast consensus.
- Both New (759k vs 685k) and Pending (+1.1% vs -1.0%) Home Sales increased and beat expectations on the month. Existing Home Sales fell 2%, registering 3.96M, within the consensus forecast range and down 15.4% YoY.

Outlook

- We see evidence of higher interest rates finally beginning to exert their pressure resulting in a slowing economy beginning to take hold here in the fourth quarter. We believe this interest rate/policy-driven slowdown has the potential to result in recession sometime in 2024, likely in the latter half. This combined with the current manufacturing recession, Chinese property bust, and a tangible rise in oil supply risks (Russia/ Middle East) have us maintaining a moderately cautious view over our 12-24 month forecast horizon.

- That said, a marginal backtrack in interest rates alongside a 'peak cycle' policy narrative and a slowing but positive growth backdrop could translate to a short-term risk asset rally as we close out the year, bolstering a neutral policy stance on equity markets in the short term. Start-stop conditions should continue favoring periodic tactical (0-6 months) asset allocation shifts anchored at a neutral to slight underweight equity allocation rather than a decided pro-growth or defensive investment posture. We remain neutral on the growth/value style dimension, reflecting our view that we are nearing the end of an economic cycle and acknowledging the risks that persistently rising interest rates pose to growth stocks and the overall economy as we look forward. From a geography perspective, we are favoring quality U.S. markets over non-U.S. due to currency and relative growth dynamics.
- Upside interest rate pressure began to lose momentum as the 10-year approached 5%, a seemingly key psychological resistance point. Given the velocity and magnitude of the move in interest rates to date, we believe there is a limit to further meaningful upside in yields and expect risk markets to focus on the financial and economic impacts of the move higher in yields. Recommended fixed income positioning is neutral from a duration perspective and underweight below investment grade fixed income and bank loan markets over our forecast horizon.

Equity	Level	1 Mo	3 Mo	YTD	1 Yr	3 Yr
Dow Jones	33053	(1.26)	(6.55)	1.44	3.17	9.84
NASDAQ	12851	(2.76)	(10.24)	23.61	17.99	6.42
S&P 500	4194	(2.10)	(8.25)	10.69	10.14	10.36
Russell 1000 Growth		(1.42)	(7.62)	23.20	18.95	8.70
Russell 1000 Value		(3.53)	(9.75)	(1.80)	0.13	10.21
Russell 2000		(6.82)	(16.69)	(4.45)	(8.56)	3.95
Russell 3000		(2.65)	(9.08)	9.41	8.38	9.19
MSCI EAFE		(4.04)	(10.82)	3.24	15.01	6.26
MSCI Emg Mkts		(3.87)	(12.09)	(1.80)	11.26	(3.30)
Fixed Income	**Δ Yield**	**1 Mo**	**3 Mo**	**YTD**	**1 Yr**	**3 Yr**
US Aggregate	2.95	0.10	0.32	0.56	0.92	0.87
High Yield	6.30	0.16	0.38	0.24	1.13	1.29
Municipal	2.27	0.09	0.29	0.39	0.54	0.44

Commodities	10/31/23	8/31/23	5/31/23	2/28/23
Oil (WTI)	83.03	83.55	68.11	76.88
Gold	1996.90	1942.30	1964.40	1824.60

Currencies	10/31/23	8/31/23	5/31/23	2/28/23
USD/Euro ($/€)	1.06	1.09	1.07	1.06
USD/GBP ($/£)	1.21	1.27	1.24	1.21
Yen/USD (¥/$)	151.46	145.68	139.78	136.09

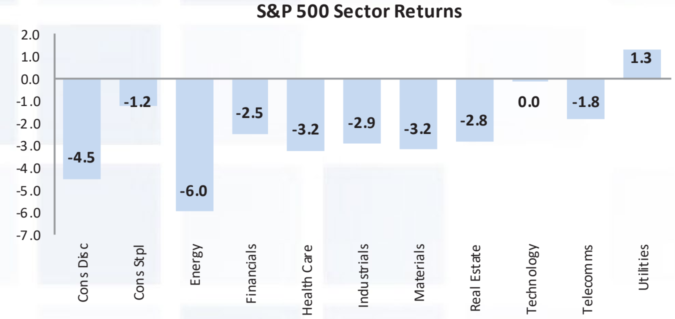
Treasury Rates	10/31/23	8/31/23	5/31/23	2/28/23
3 Month	5.59	5.56	5.52	4.88
2 Year	5.07	4.85	4.40	4.81
5 Year	4.82	4.23	3.74	4.18
10 Year	4.88	4.09	3.64	3.92
30 Year	5.04	4.20	3.85	3.93

Style Returns

MTD

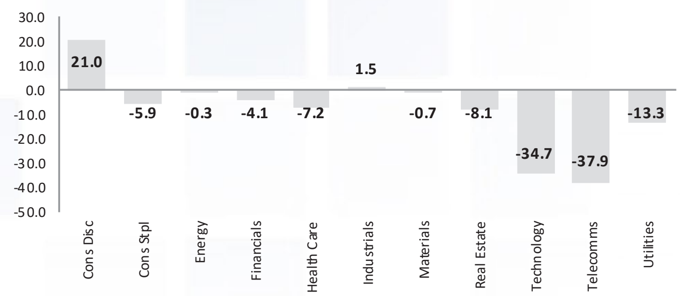
	V	B	G
L	-3.53	-2.42	-1.42
M	-4.95	-4.99	-5.10
S	-5.97	-6.82	-7.71

S&P 500 Sector Returns



YTD

	V	B	G
L	-1.80	10.28	23.20
M	-4.44	-1.28	4.28
S	-6.46	-4.45	-2.87



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