MONTHLY MARKET UPDATE

September 2023

OPAL WEALTH ADVISORS

The “September Effect” was on display last month where the U.S. economy felt like a lose-lose situation in which weak growth could tip it into recession while accelerating growth could initiate a second wave of inflation leaving the Fed no choice but to tighten their way toward recession. That is, unless goldilocks comes along (still entirely possible), and everything lands just right. That said, the consensus call today is that a global recession can be deferred but not denied with timing still very much up for debate.

Key drivers of market volatility in September included a ‘higher for longer’ Fed, looming government shutdown, UAW strike, resumption of student loan payments, and sharply rising bond yields and oil prices. Monetary policy was a key driver last month with the FOMC meeting serving to cool market expectations for any dovish pivot in policy by pushing a clear higher for longer fed funds narrative - not necessarily welcome news for the stock market. It was however, the rise in market interest rates that posed the key challenge to both global stock markets and the overall economy. It will most certainly take some time for consumers and companies to figure out how they are going to borrow and finance themselves in an environment with materially higher interest rates that, when viewed over the long term, are really just back to normal levels. All that said, a bottoming in the global manufacturing cycle, resilient personal consumption/economic growth, and a tight U.S. labor market are forces pushing what may be an inflation/policy driven recession a bit further out into the future.

Financial markets in September continued to consolidate with global equity markets losing 4.3% and rising bond yields translating to bond market losses of approximately 2.5%. This wrapped up a difficult third quarter where most financial assets lost ground. The S&P 500 fell 4.8% in September, leaving the year to date return up 13%. Non-U.S. developed (-3.4%) and emerging (-2.6%) performed marginally better on the month but are well behind the U.S. for the year to date. While the 10yr UST yield rose from 4.09% to 4.59%, pressuring bond market returns, credit spreads remained relatively sanguine with high yield spreads widening from 3.85% to 4.03%, still well below the historical average spread of 5.39%.

Commodities were generally higher with oil prices surging 9.8% in September, fueling concerns that central banks will have to maintain tight monetary policy for longer.

Market Anecdotes

- While we’ve seen some consolidation in the equity market here in the third quarter, a Bianco Research chart reminds us just how frequently this happens and of the sizable dispersion of returns within both stock and bond markets so far in 2023.
- Goldman Sachs made note the market’s most difficult month (September) is behind us but also that turning the calendar to October leads us into historically the best season of the year where, since 1985 Q4 has averaged 6.1% while Q1, Q2, and Q3 have all been less than 3%.
- The move higher in interest rates from a 0.52% yield in the summer of 2020 to 4.6% today is remarkable but a research note from Deutsche Bank reminds us we’re finally now back to the long-term average price of money.
- An interesting data point to gauge economic growth and the health of the labor market is to monitor Federal income and employment tax receipts which shows a healthy 4.5% growth rate through late September when compared to 2022.
- Individual investor bullish sentiment has waned, falling from a peak 51.4% two months ago to 31.3% in the most recent release - now back below its long-term average of 37.5%.
- The NY Fed Survey of Market Participants showed only a 5% chance of peak Fed funds surpassing 6%, relatively in line with futures market pricing.
- Eaton Vance published LCD data illustrating S&P’s default forecasts for the coming six months with the current rate of 1.7% either rising to 4.5% (pessimistic), falling to 1% (optimistic), or leveling off to 2.5% (base case). Distressed loan data is also signaling some turbulence ahead.
- A research note from Goldman on the U.S. equity market concentration issue painted a stark

contrast between U.S. and non-U.S. markets while an unrelated note from J.P. Morgan illustrated the cost of higher rates hitting smaller companies disproportionately harder as well.

- Tightening lending standards leading to a credit cycle across commercial credit and real estate is becoming clear with regional, international, and local banks alongside the CMBS market holding the lion's share of real estate loans and buy side investors of all colors holding commercial loans.
- Apollo made note of the estimated $7.6trn in US government debt maturing over the next year which logically should translate to persistent upward pressure on interest rates.
- The impact of high mortgage rates on mortgage applications and existing home sales is clear while renting as an alternative is being accommodated by record high multi-family construction.

Economic Release Highlights

- The September Employment Report firmly beat expectations (336k vs 170k), accelerating from 187k last month. The unemployment rate and average hourly earnings remained unchanged at 3.8% and 0.2% respectively.
- Headline PCE inflation registered 3.9% YoY alongside core readings of 0.1% MoM and 3.9% YoY. Personal Consumption grew 0.4%, a decrease relative to the prior month and slightly below consensus forecast of 0.5%. Personal Income met consensus at 0.4%.
- Headline and core CPI registered 3.7%/4.3% YoY and 0.6%/0.3% MoM. Headline and core PPI registered 1.63%/2.16% YoY and 0.74%/0.19% MoM.
- Retail Sales of 0.56% (+2.5% YoY) came in higher than the 0.1% expected and above the prior two months' pace, but gasoline sales seem to have played a large part in the report.
- The JOLT Survey revealed a sizable increase in job openings at 9.610mm, well above the consensus estimate of 8.75mm and last month's 8.827mm.
- The final 2Q GDP (third release) was revised downward from 2.3% to 2.1%, right at the bottom end of consensus forecasts.
- Durable Goods Orders (MoM) in August rose 0.2%, way above the spot consensus of -0.3% and Ex-Transportation (+0.4%) also exceeded estimates while Core Capital Goods (+0.9) improved versus the prior month.
- The September flash U.S. PMI reported Manufacturing (48.9a vs 47.8e), Services (50.2a vs 50.2e), and a Composite of 50.1.
- Eurozone and U.K. flash PMIs (C, M, S) registered (47.1, 43.4, 48.4) and (46.8, 44.2, 47.2) while China's S&P PMI reading (C, M, S) for September came in at 50.9, 50.6, and 50.2.
- Consumer Confidence Index in September registered 103.0, below the 105.8 spot forecast and range of 103.5 to 107.2.
- UofM Consumer Sentiment fell from 69.5 to 67.7 (-2.6%) in September. It is up 15.53% from this time in 2022 but remains well below its historical average of 86.
- The NFIB Small Business Optimism Index declined 0.6 to 91.3, slightly below consensus call of 91.5.
- The Housing Market Index declined from 50 to 45, well below consensus estimate of 50 and the forecast range of 49-52. The Case Shiller Home Price Index increased 0.9% MoM and 0.1% YoY, both slightly ahead of consensus estimates.
- Housing Starts (1.283m vs 1.435m) and Permits (1.543m vs 1.440m) missed and beat consensus expectations respectively with strong permits and weak starts data on the month.
- New (675k vs 699k) and Pending (-7.1%) Home Sales were down on the month. Existing Home Sales registered 4.040mm, slightly under consensus forecast for 4.100mm but within the forecast range.

Outlook

- The second half 2023 interest rate pressure we projected came into focus very quickly with the 2yr (5.15%) and 10yr (4.80%) yields gapping out 20bps and 100bps, respectively since June 30th. Given the velocity of the move to date, we believe there is a limit to further upside in yields and expect risk markets to focus on the financial and economic impacts of the move higher in yields with an increased probability of some form of 'financial accident' as a result.
- Stocks may well outperform bonds in the coming months, supporting our neutral stance in the short term, but we expect risks for equity markets and bond yields are skewed to the downside when

viewed over a 12-24 month horizon. 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. 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	33508	(3.42)	(2.10)	2.73	19.18	8.62
NASDAQ	13219	(5.77)	(3.94)	27.11	26.11	6.60
S&P 500	4288	(4.77)	(3.27)	13.07	21.62	10.15
Russell 1000 Growth		(5.44)	(3.13)	24.98	27.72	7.97
Russell 1000 Value		(3.86)	(3.16)	1.79	14.44	11.05
Russell 2000		(5.89)	(5.13)	2.54	8.93	7.16
Russell 3000		(4.76)	(3.25)	12.39	20.46	9.38
MSCI EAFE		(3.37)	(4.05)	7.59	26.31	6.28
MSCI Emg Mkts		(2.57)	(2.79)	2.16	12.17	(1.34)
Fixed Income	**Δ Yield**	**1 Mo**	**3 Mo**	**YTD**	**1 Yr**	**3 Yr**
US Aggregate	2.86	0.13	0.28	0.47	0.89	0.74
High Yield	6.15	0.18	0.23	0.08	0.95	1.11
Municipal	2.18	0.13	0.25	0.31	0.48	0.35

Commodities	9/30/23	7/31/23	4/30/23	1/31/23
Oil (WTI)	88.81	81.80	76.78	78.95
Gold	1870.50	1970.70	1982.60	1923.90
Currencies	**9/30/23**	**7/31/23**	**4/30/23**	**1/31/23**
USD/Euro ($/€)	1.06	1.10	1.10	1.08
USD/GBP ($/£)	1.22	1.29	1.26	1.23
Yen/USD (¥/$)	149.43	142.18	135.99	130.17
Treasury Rates	**9/30/23**	**7/31/23**	**4/30/23**	**1/31/23**
3 Month	5.55	5.55	5.10	4.70
2 Year	5.03	4.88	4.04	4.21
5 Year	4.60	4.18	3.51	3.63
10 Year	4.59	3.97	3.44	3.52
30 Year	4.73	4.02	3.67	3.65

Style Returns

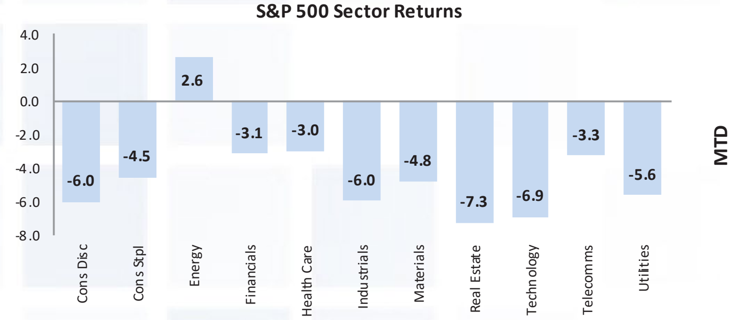
MTD

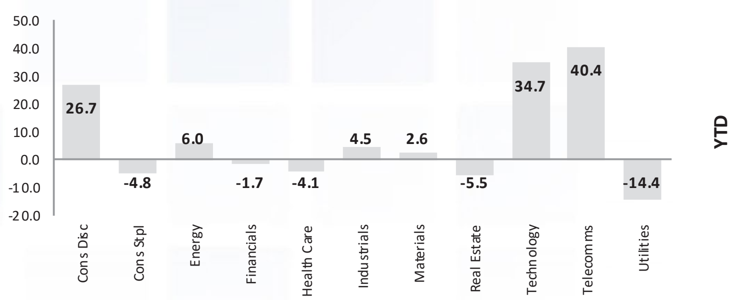
	V	B	G
L	-3.86	-4.70	-5.44
M	-5.09	-5.02	-4.87
S	-5.21	-5.89	-6.60

YTD

	V	B	G
L	1.79	13.01	24.98
M	0.54	3.91	9.88
S	-0.53	2.54	5.24

S&P 500 Sector Returns





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