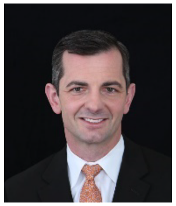
NorthCoast

Asset Management | A Connectus Partner

Quarterly Client Update

Q3 2023

September 30, 2023



"In the foggy seas of investing, it's not the absence of risk but the compass of wisdom that guides us to treasures."

~ Unknown

Navigating foggy seas: Imagine you're the captain of a sailboat on a vast ocean. Your goal is to sail to a distant island where treasures await. Under normal conditions, you use a combination of your map, compass, and clear skies to guide your way.

One day as you're sailing, a thick fog descends upon the water, reducing visibility. It's harder to see where you're going, other boats, and potential obstacles like rocks or shallow waters. You might still have a general sense of direction from your map and compass, but the clear landmarks and the distant view of the island are now obscured.

As you continue cautiously, you suddenly hear the sound of waves crashing against rocks. It's a sign that there are hazards nearby, but it's not necessarily a sign that your ship is about to be wrecked. You must be more attentive, make more frequent checks with your navigation tools, and possibly even slow down or adjust the course.

During this time, some sailors might choose to drop anchor and wait for the fog to lift—they prefer to avoid risk, even if it means their journey to the island might take longer. Others continue forward but at a slower pace, while some may use the fog as an opportunity, believing their knowledge of the seas will give them a navigational advantage.

However, it's essential to understand that while the fog and waves increase the level of difficulty and risk, they do not necessarily mean there is an imminent storm or that the boat will never reach its destination. It is a time for caution, informed decision-making, and possibly patience, but it's not a full-blown crisis (yet).

Just like a sailor navigating through difficult waters, investors navigating through high uncertainty and emerging risks require a balanced approach—keeping a close eye on indicators, adjusting strategies as needed, and remembering the long-term goals. But it also serves as a reminder that when risks are present, opportunities can also be found for those willing to navigate the challenges carefully.

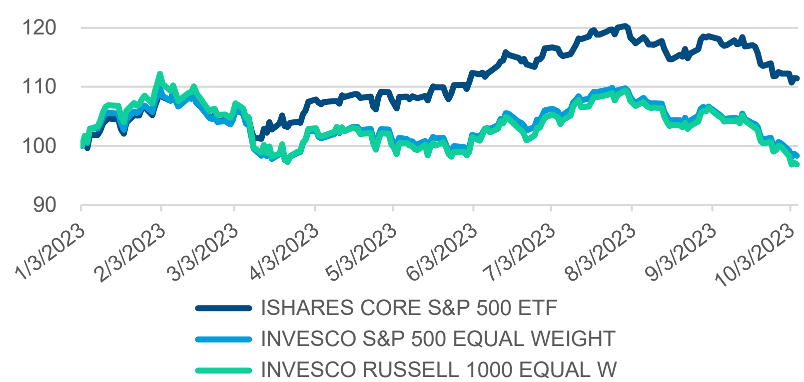
A CIO's View

Here are my summaries on several topics affecting markets, all monitored daily by our models. We regularly cover these topics in our monthly Navigator and quarterly Fixed Income Commentary.

Market Return: Historical Narrow Rally for Cap-Weighted Indices Only

We had mentioned in a previous newsletter the magnitude of the distortion of index returns caused by the top 10 stocks in the S&P500 representing 32% of the weight in the S&P500, a new high, while contributing to just 22% of the earnings. With the recent pull-back the distortion is more glaring: both the S&P500 Equal-weighted index and the Russell 1000 Equal-weighted index are below their levels from the beginning of the year, while the S&P500 Cap-weighted is still more than 10% above its 2023 starting level (Exhibit 1). That gap has increased during the Q3 pullback, with the S&P500 down 6.3% from the 7/31/2023 high, while the S&P500 Equal-weighted is down 8.1% over that same time period.

Exhibit 1: Cap-weighted vs. equal-weighted indices: a narrow rally eclipsing the broader reality



Source: Bloomberg

Recession: Slightly lower likelihood, with clouds on the horizon

Recession risks have continued to be pushed back for several months, forcing some with bearish positioning to adjust their stance. Looking at the short covering of bearish positions on the S&P500 puts the recent S&P500 pull back in perspective: at the end of September the non-commercial positioning in S&P500 E-mini futures contracts (overall net bets on the future direction of the market) was cut in half from its end of June level, as participants unwound half of their positions by buying back some of their contracts (Exhibit 2). This means traders were betting on a future decline in the market, but less so than the previous quarter. This activity had a net support effect for the market, leaving little support left from these participants.

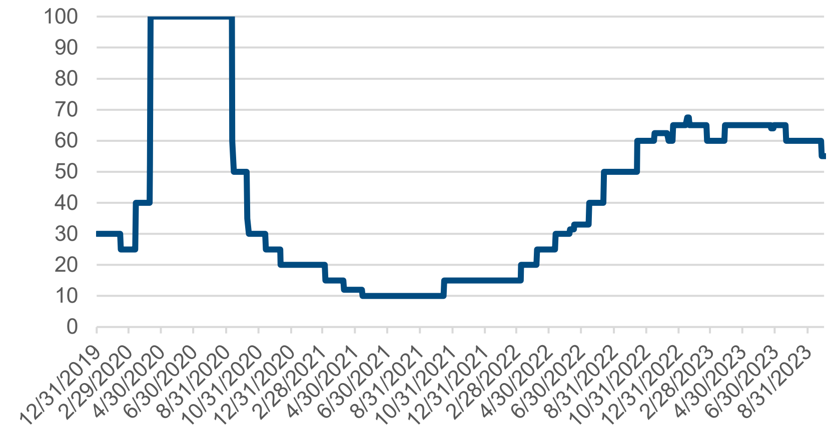
Exhibit 2: S&P 500 E-Mini Futures Contracts (50% reduction from June to September 2023)

Source: Bloomberg.

On the positive side, the probability of a recession has improved slightly at an elevated 55% (Exhibit 3), since the economy has shown some resilience, and maybe emboldening the FOMC to continue its restrictive actions.

The risk-reward ratio still remains high for the remainder of 2023: the stock market continues to display expanded multiples despite a rise in policy rates and real rates with cash yielding 5%, and a decelerating economy due to the Fed's action along with softening consumer trends and other sources of uncertainty. The summer strikes contributed to a loss of more than 4 million work days, the excess savings from fiscal stimulus have mostly been spent, student loan repayments are restarting (with rising consumer delinquencies), oil prices hit a new high, and a strong dollar are all seen as drags on growth. The government shutdown has been temporarily averted, but at the price of the U.S. House losing its speaker and bringing more political uncertainty to an incoming election year. Additionally, the rising topic of reckless fiscal policies could lead to the necessary removal of some stimulating fiscal policies. This all contributes to lowering the potential for further appreciation.

Exhibit 3: Probability of a U.S. Recession (remains at 55%)



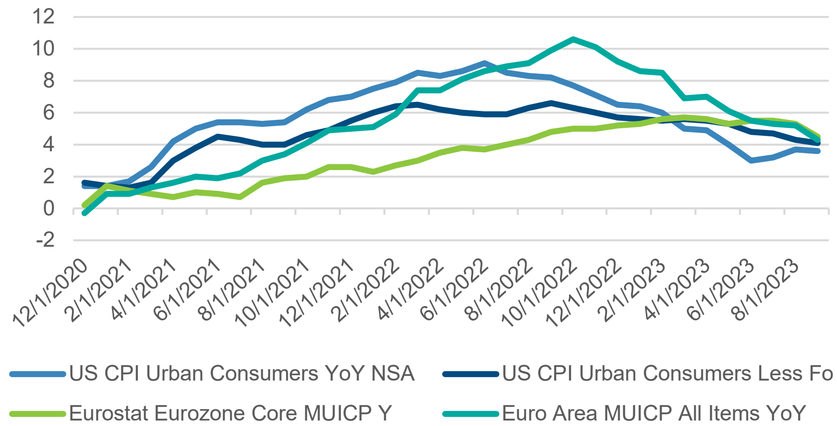
Source: Bloomberg.

Inflation: Improvements so far but resilience ahead

Updating our inputs from last quarter, while we continue to see the same pattern: core inflation is slowly coming down but still above 4%, while headline inflation has temporarily worsened to 3.6% due to an upward trend in energy prices which could continue over the next few months (Exhibit 4).

Core inflation above 3% for the remainder of 2023 and 2024 is a scenario which would trigger hawkish actions from the Federal Reserve and an additional rate hike.

Exhibit 4: U.S./Europe Core Inflation Rates

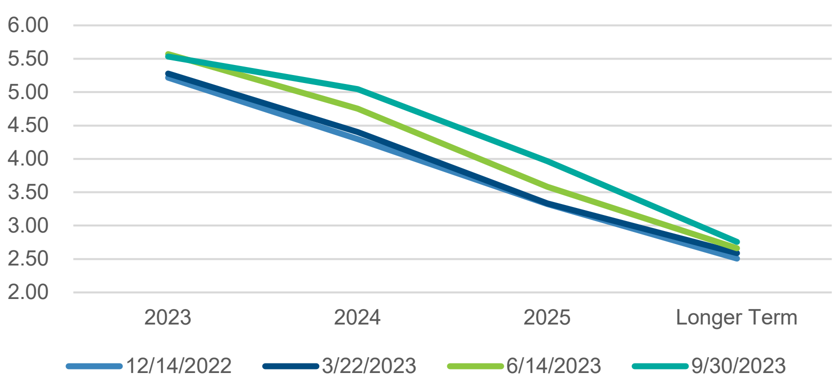


Source: Bloomberg.

Federal Reserve actions: Pause but another hike signaled

In September, the FOMC decided to pause, with additional context of higher real GDP growth for 2023, lower unemployment rates forecasts (from 4.1% to 3.8% in 2023 and from 4.5% to 4.1% in 2024), core inflation forecasts were lowered from 3.9% to 3.7% which was a positive sign. But the dot plots showed that most of the participants are still projecting another rate hike for 2023, with rates 50bps higher in 2024 and 2025, and a postponing of the first rate cut (Exhibit 5).

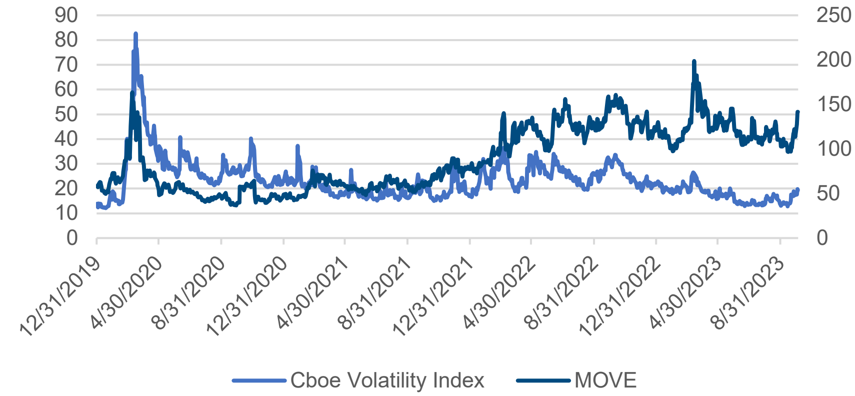
Exhibit 5: FOMC Dot plots signaling higher rates for a longer period



Source: Bloomberg.

The interest rate uncertainty has ticked up with the recent FOMC meeting, as can be seen in Exhibit 6: the MOVE Index (implied volatility of a basket of OTC options on US interest rate swaps) illustrates the foggy environment we are in.

Exhibit 6: The VIX Volatility Index and the MOVE Index indicate greater uncertainty in fixed income and higher interest rates

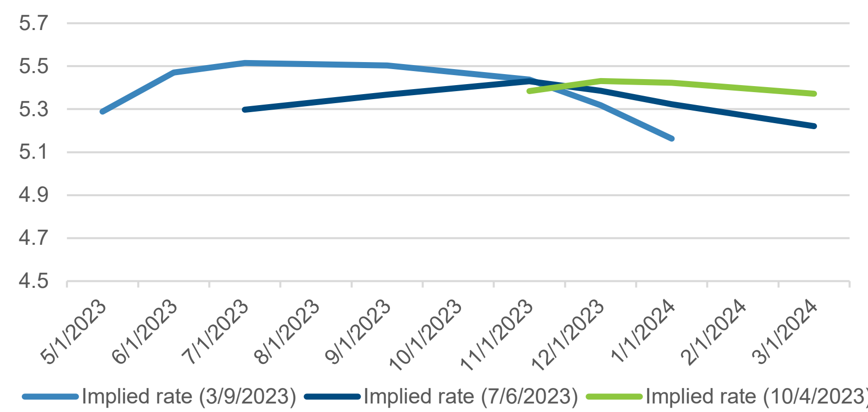


Source: Bloomberg.

The market has reacted to this information and incorporated most but not all of it (Exhibit 7): "Higher rates for longer."

The potential consequences would be twofold: more rate hikes down the road and later rate cuts as inflation could be more persistent than predicted.

Exhibit 7: Implied Rates now show higher rates for a longer period



Source: Bloomberg.

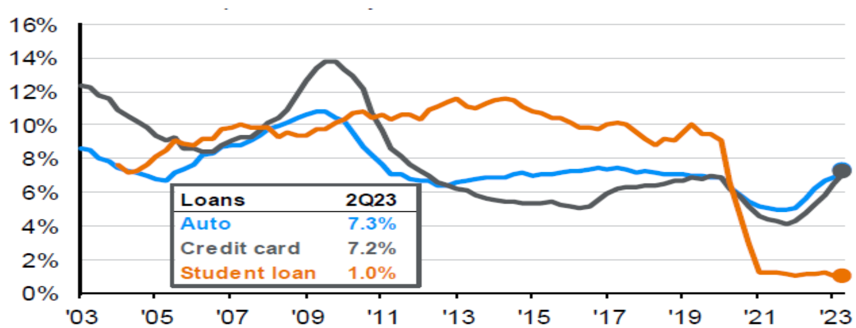
Economy: Resilient with some cracks

The persistent and surging higher bond yields are an adverse current for economic activity, which could lower financing activity, increase corporate debt burden, federal budget problems and have a negative impact on earnings which could reset market valuations.

Another impact is the rise of bankruptcies and delinquencies. We are seeing some of these effects manifesting themselves in the recent data (Exhibit 8).

Student loan repayments are restarting which will likely start showing an uptick in delinquencies within a few months.

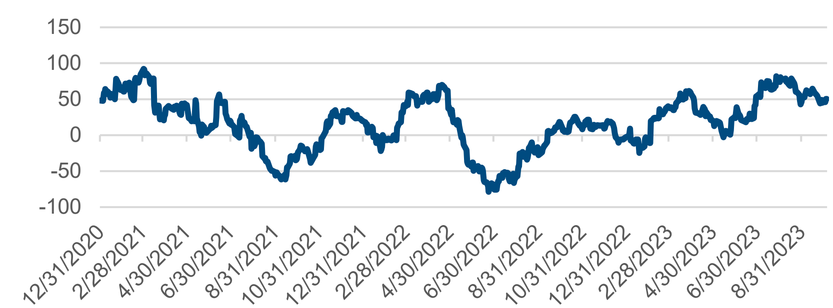
Exhibit 8: Debt delinquencies starting to rise (% of balance delinquent 30+ days)



Source: FactSet, JRB, J.P. Morgan Asset Management, BEA.

The Citigroup economic surprise index illustrates the resilience of the US economy: beating expectations, and almost as high as the end of 2020, but with a recent downtick (Exhibit 9).

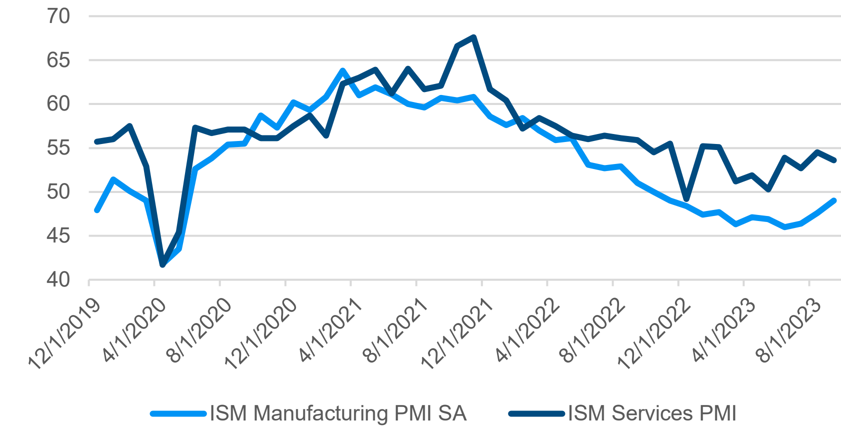
Exhibit 9: The Citigroup Economic Surprise Index indicates how economic data compares with consensus estimates



Source: Citigroup.

Similarly, the more restrictive monetary policies continue to show results: the ISM indices are still at a low (Exhibit 10), and the conference board leading indicators are in a recessionary phase.

Exhibit 10: ISM Manufacturing and Services Indices are still at a low



Source: Bloomberg.

Looking forward, we anticipate more weakness in the economy from the lagging effects of the Federal Reserve's tightening policy, combined with banks restricting credit. While we are not in a full-blown crisis like 2008, there are enough signs that invite us to caution and trim our sails.

Investment Implications

In summary, I have a few considerations for your portfolio given market conditions:

- Remain cautious in the current environment.
- Diversify your investments.
- Focus on active risk management and equal-weighted approaches.
- Consider getting paid to be on the sidelines with 5% cash yields.

Remember when you sail in the fog, trimming your sails and resisting the sirens' song will more likely lead you safely to your journey's destination. Thoughtful, measured consideration and diversity in your investment allocations according to your risk tolerance should be made with your advisor.

I hope this letter finds you and your family happy, healthy, and enjoying the last month of warm weather. If you have any questions about your portfolio or would like to discuss your current positioning, please contact your advisor at any time. Our team always has your interest at heart and stands ready to help you meet your goals with the proper allocations and financial planning. As always, we thank you for your business.

Enjoy the fall season and Happy Halloween!

Warm regards,

Patrick Jamin
President & CIO

Important Disclosure Information

The information contained herein has been prepared by NorthCoast Asset Management ("NorthCoast") on the basis of publicly available information, internally developed data and other third-party sources believed to be reliable. NorthCoast has not sought to independently verify information obtained from public and third-party sources and makes no representations or warranties as to accuracy, completeness or reliability of such information. All opinions and views constitute judgments as of the date of writing without regard to the date on which the reader may receive or access the information and are subject to change at any time without notice and with no obligation to update. This material is for informational and illustrative purposes only and is intended solely for the information of those to whom it is distributed by NorthCoast. No part of this material may be reproduced or retransmitted in any manner without the prior written permission of NorthCoast. NorthCoast does not represent, warrant or guarantee that this information is suitable for any investment purpose, and it should not be used as a basis for investment decisions.

NorthCoast Asset Management is a d/b/a of, and investment advisory services are offered through, Connectus Wealth, LLC, an investment adviser registered with the United States Securities and Exchange Commission (SEC). Registration with the SEC or any state securities authority does not imply a certain level of skill or training. More information about Connectus can be found at www.connectuswealth.com.

PAST PERFORMANCE DOES NOT GUARANTEE OR INDICATE FUTURE RESULTS.

This material should not be viewed as a current or past recommendation or a solicitation of an offer to buy or sell any securities or investment products or to adopt any investment strategy. The reader should not assume that any investments in companies, securities, sectors, strategies and/or markets identified or described herein were or will be profitable and no representation is made that any investor will or is likely to achieve results comparable to those shown or will make any profit or will be able to avoid incurring substantial losses. Performance differences for certain investors may occur due to various factors, including timing of investment. Investment return will fluctuate and may be volatile, especially over short time horizons.

INVESTING ENTAILS RISKS, INCLUDING POSSIBLE LOSS OF SOME OR ALL OF AN INVESTMENT.

The investment views and market opinions/analyses expressed herein may not reflect those of NorthCoast as a whole and different views may be expressed based on different investment styles, objectives, views or philosophies. To the extent that these materials contain statements about the future, such statements are forward looking and subject to a number of risks and uncertainties.

NorthCoast
Asset Management | A Connectus Partner

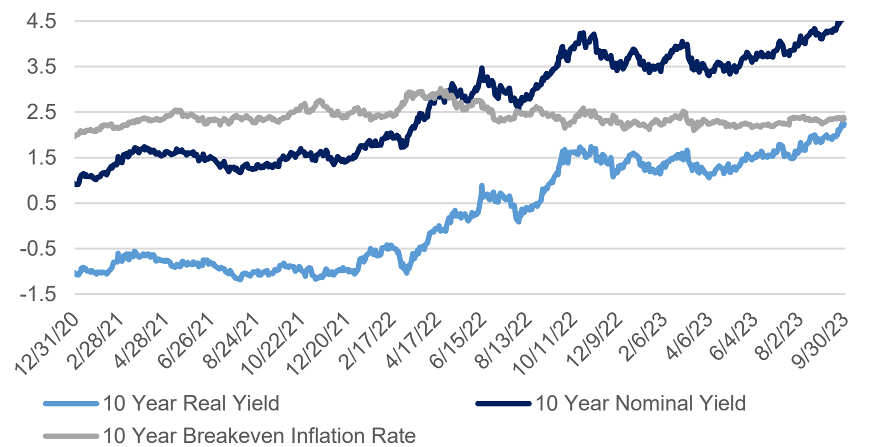
Continued US Economic Resilience with Challenges Ahead

Julia Zhu
Senior Vice President, Market and Security Research

Market Recap

U.S. government bond yields climbed significantly during the third quarter, with yields on benchmark Treasurys hitting 16-year highs. This surge was primarily prompted by a series of robust economic data and speculations that central banks will keep interest rates high for longer to quell inflation. Part of the move is also due to the U.S. Treasury's decision to increase its long-term debt issuance driven by significant budget deficits and an unexpected adjustment in the Bank of Japan's Yield Curve Control policy. The nominal 10-year U.S. yields ended the quarter at 4.57%, up from 3.84% at the end of the previous quarter. The primary factor behind this shift was the increase in real yield (by 65 basis points), while inflation expectations, measured by the 10-year inflation breakeven rate, saw a slight increase from 2.22% at the end of the second quarter to 2.35% (refer to Exhibit 1).

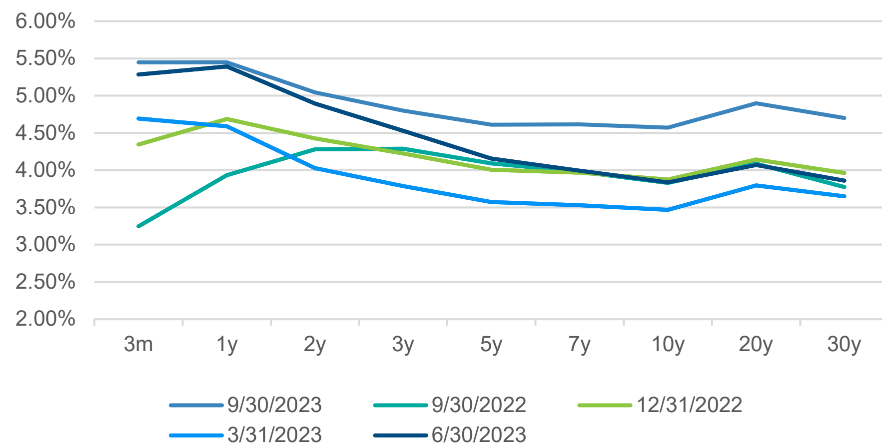
Exhibit 1: Treasury Yields rose significantly in the third quarter of 2023



Source: Bloomberg.

Treasury yields across all maturities increased for the third quarter, with longer-term yields moving up the most, leading to a less inverted yield curve. The 2-year yield, which is highly sensitive to the expectation of the Fed funds rate, rose from 4.90% to 5.04%, a level 47bps higher than the 10-year yields (compared with 1.1% higher than the 10-year yields at the end of last quarter, see Exhibit 2). The 30-year bond yield, which is more sensitive to changes in long-term economic prospects, increased more significantly from 3.86% to 4.70% at the end of third quarter.

Exhibit 2: U.S. Treasury Yields Curve



Source: Bloomberg.

Macro Picture: resilient US economy with higher probability of soft landing

This year, a notable surprise has been the resilience of the US economy despite the Fed's aggressive interest rate hikes. Forecasts for an upcoming recession have consistently been postponed and toned down. The markets swiftly adjusted their expectations towards a U.S. soft landing in late August and early September. In our view, various factors support this resilience, with the durable labor market and the stability of the US housing sector standing out as potentially the most crucial ones.

While it's true that the rate of job creation has slowed down, the unemployment rate remains close to historically low levels. Strong job market and higher real wages supported by decelerating inflation have continued to bolster consumer spending, which accounts for one-third of the total GDP.

The recent resilience is also partly attributed to the robust U.S. housing market. Although existing home sales experienced a significant drop due to rising mortgage rates, there has been a sustained high level of employment in the construction sector. This sector holds significant importance in the U.S. labor market, as it is one of the primary areas where job losses usually occur during a hiking cycle. Various factors have contributed to the housing market's performance this cycle, including a historical trend of insufficient home construction in the U.S. and an uptick in household formation. Cyclical factors, such as a reduced supply of existing homes due to potential sellers holding onto low mortgage rates, have also driven more demand for new homes.

Despite the recent better-than-consensus activity data in the U.S., our view is that the U.S. economy is not heading for a re-acceleration. Rather, we anticipate a mild slowdown with lagged impacts of elevated interest rates, sustained credit restrictions, surging energy costs, and the start of student loan repayments. Several leading indicators, such as decreasing leading economic index, contracting PMI index, and continued tightening of bank lending standards, all point towards a potential downturn on the horizon.

Fed Policy: Higher for Longer

As widely expected, at its September meeting the FOMC chose to keep the fed funds rate unchanged at the range of 5.25% to 5.5%. At the same time, there were notable shifts in the FOMC's economic forecast in the September Summary of Economic Projections, predicting higher real GDP growth (from 1% in June to 2.1%) and lower unemployment (from 4.1% to 3.8%) in 2023, while core inflation forecasts were trimmed from 3.9% to 3.7% for 2023. However, the FOMC's stance was generally viewed by the market as a hawkish pause as it maintains a bias toward tightening, with dot plots 50bps higher (the Fed dot plot is a chart showing projections for the fed funds rate) and a postponed timeline for the first rate cut.

While the Federal Reserve currently pivots to a soft-landing narrative, we believe that the rates will be high for longer due to at least the following factors:

- In the near term, we see two headwinds for the Fed policymakers, including surging energy prices and the ongoing United Auto Workers strike. Hence, we anticipate one more potential uptick in headline inflation next month, followed by a subsequent decline. Should this materialize, it increases the probability of an additional rate hike in 2023.
- The robustness in economic activity presents a double-edged sword, as a stronger economy could reignite inflationary pressures.
- Although inflation has moderated, it is still well above the target, and the risk of inflation remains elevated until further softening of the labor market.
- The Fed has affirmed its commitment to the 2% inflation target. We believe major central banks will take necessary measures to maintain longer-term inflation expectations in line with their established targets.

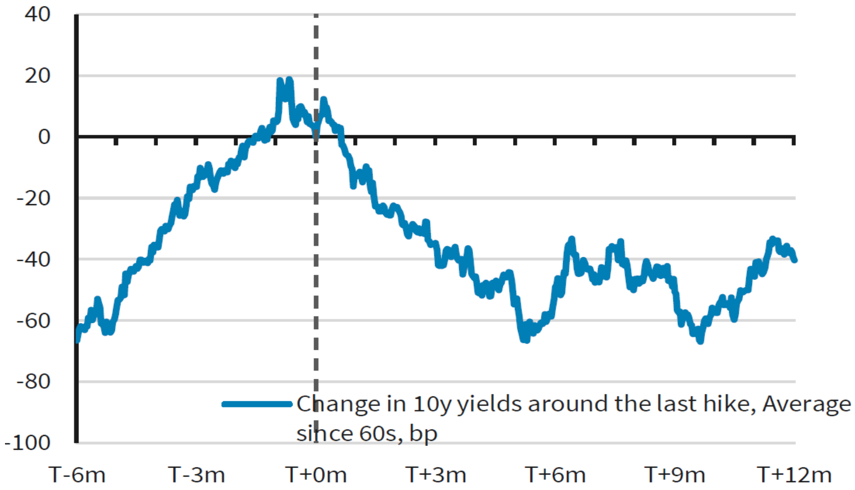
As a result, we have increased confidence in our belief that the Fed will be cautious in cutting rates, and we anticipate that the lagging effects of rate hikes will precipitate a mild slowdown. While there is an elevated level of uncertainty for market conditions, we believe that this backdrop favors extended high short-term interest rates and provides appealing opportunities for high-quality investments across our various strategies.

Bonds have historically done well after the Fed stops raising interest rates.

The current higher yields act as a cushion against market volatility, and ultimately, the end of the hiking cycle could improve fixed income performance. Historically, bonds have shown strong performance after the Federal Reserve stopped raising interest rates. Data in Exhibit 3 illustrates that, on average, the 10-year yield has decreased by approximately 60 basis points in the twelve months following the final rate hike in a cycle since the 1960s. In addition, Exhibit 4 highlights the impressive outperformance of various fixed income sectors 12 months after the end of hiking cycles since 1995.

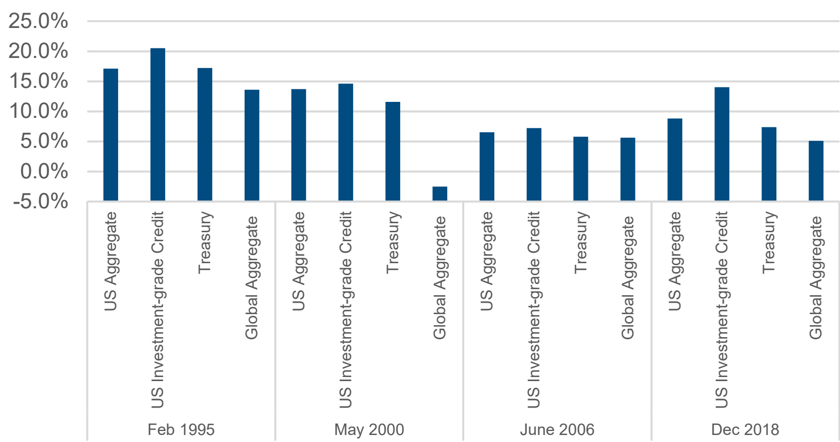
We understand that different factors can differentiate each rate hiking cycle, and the inflation data in the upcoming quarters will ultimately determine when the first rate cut occurs. However, due to the recent steepening of the yield curve, the initial conditions have become more favorable, with the 10-year U.S. treasury yield over 4.8%, trading above the expected average policy rate. With a fed funds rate heading into restrictive territory, there is potential for fixed income to deliver equity-like returns as policy rates ultimately normalize.

Exhibit 3: Change in 10yr yields at the end of the last hike



Source: Bloomberg, Barclays Research.

Exhibit 4: Fixed Income performance one year after end of rate hikes



Source: Bloomberg.

Investment Implications

With the recent substantial repricing of the fixed income market, investors may be able to achieve the highest real yields in over a decade without assuming uncomfortable risks. Given the current starting yield levels, which are typically highly correlated with subsequent total returns, high quality fixed income could potentially deliver equity-like returns with less volatility and greater downside protection. We believe that in this time of increased uncertainty, it is crucial to prioritize high quality investment and diversification while maintaining portfolio flexibility. Thus, we continue to emphasize high-quality fixed income sectors, while also preparing to take opportunities in other sectors as prices adjust to reflect changes in underlying fundamentals. We slightly underweight duration in our tactical portfolios and maintain our neutral stance on duration in less dynamic portfolios. For YTD ending September 30, 2023, our Tactical Income strategy returned -0.7% net of fees, outperforming the Global Aggregated Bond Index and U.S. Aggregate Bond Index by 1.5% and 0.5%, respectively. In the third quarter, we focused on several key themes in our strategies, outlined below:

- **Short-term treasuries still preferred:** We lean towards short-term government bonds over credit. Driven by aggressive Fed interest rate hikes, the yields on short-term government bonds have increased together with the long-term yields, making the short-term U.S. treasury deliver comparable yields as high-quality credit without assuming any credit risks. We overweight the short-term treasury and hold our 6% cash in a money market mutual fund, which earns a 5% yield.
- **Neutral for investment grade credit:** We reduced our exposure to investment grade corporate bonds from overweight to neutral. We have observed early indications of a shift in the credit cycle, as downgrades are surpassing upgrades for corporate credits. We believe that high-quality corporate bonds offer limited compensation for any possible lower return due to wider spreads and sensitivity to economic downturns.
- **Cautious to add duration:** Investors are now finally getting modest compensation for term premium after the recent significant rise in long-term yields. Nevertheless, we still hold a cautious stance and are not yet ready to take more duration risks given the challenges from massive budget deficits and our view of a mild economic slowdown down the road.
- **Continued to hold bank loans and added high-quality CLO:** With a coupon rate standing at 9%, the highest since 2001, we believe that bank loan yields adequately compensate for the increasing credit risk. In our portfolio, we have allocated 5% to the Invesco Senior Loan ETF (BKLN), which has generated a YTD return of 9.1% as of 09/30/2023. Regarding collateralized loan obligations (CLOs), we foresee a restrained issuance and expect the spreads to remain relatively stable for the rest of the year. We prefer senior CLO tranches due to their appealing carry and higher credit ratings. We recently added a modest position of the BlackRock AAA CLO ETF (CLOA), which primarily invests (92%) in AAA-rated tranches and currently offers a yield of 6.6%.

Important Disclosure Information

The information contained herein has been prepared by NorthCoast Asset Management ("NorthCoast") on the basis of publicly available information, internally developed data and other third-party sources believed to be reliable. NorthCoast has not sought to independently verify information obtained from public and third-party sources and makes no representations or warranties as to accuracy, completeness or reliability of such information. All opinions and views constitute judgments as of the date of writing without regard to the date on which the reader may receive or access the information and are subject to change at any time without notice and with no obligation to update. This material is for informational and illustrative purposes only and is intended solely for the information of those to whom it is distributed by NorthCoast. No part of this material may be reproduced or retransmitted in any manner without the prior written permission of NorthCoast. NorthCoast does not represent, warrant or guarantee that this information is suitable for any investment purpose, and it should not be used as a basis for investment decisions.

NorthCoast Asset Management is a d/b/a of, and investment advisory services are offered through, Connectus Wealth, LLC, an investment adviser registered with the United States Securities and Exchange Commission (SEC). Registration with the SEC or any state securities authority does not imply a certain level of skill or training. More information about Connectus can be found at www.connectuswealth.com.

PAST PERFORMANCE DOES NOT GUARANTEE OR INDICATE FUTURE RESULTS.

This material should not be viewed as a current or past recommendation or a solicitation of an offer to buy or sell any securities or investment products or to adopt any investment strategy. The reader should not assume that any investments in companies, securities, sectors, strategies and/or markets identified or described herein were or will be profitable and no representation is made that any investor will or is likely to achieve results comparable to those shown or will make any profit or will be able to avoid incurring substantial losses. Performance differences for certain investors may occur due to various factors, including timing of investment. Investment return will fluctuate and may be volatile, especially over short time horizons.

INVESTING ENTAILS RISKS, INCLUDING POSSIBLE LOSS OF SOME OR ALL OF AN INVESTMENT.

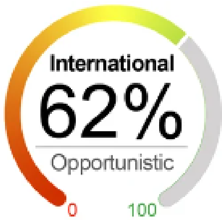
The investment views and market opinions/analyses expressed herein may not reflect those of NorthCoast as a whole and different views may be expressed based on different investment styles, objectives, views or philosophies. To the extent that these materials contain statements about the future, such statements are forward looking and subject to a number of risks and uncertainties.

NorthCoast
Asset Management | A Connectus Partner

NorthCoast Navigator

Q3 2023 | September 30, 2023

The NorthCoast Navigator is a market barometer displaying current equity outlook. The aggregate metric is determined by multiple data points across four broad dimensions including macroeconomic, sentiment, technical and valuation indicators. The daily result determines equity exposure in our tactical strategies. As of 9/30/23. Data provided by Bloomberg, NorthCoast Asset Management.



Current Equity Exposure

Summary: US stocks ended September with their biggest monthly decline since last December 2022, with the S&P 500 and Dow dropping by 4.8% and 3.4%, respectively, while the technology-heavy Nasdaq lagged by losing 5.8%. The expectation of "higher for longer" interest rates put pressure on markets. With a hawkish hold in September's FOMC meeting and hawkish commentary from several Fed policymakers, investors are worried that a pivot toward lower rates will not happen any time soon. The US long-term interest rates surged due to the uncertainty in the macro landscape. Also contributing to the negative sentiment was a series of modestly adverse events in the US, such as an escalation of the UAW strike, a looming government shutdown, and a recent upswing in oil prices. We continue to hold the view that the resilient economy and persistent inflation call for sustained restrictive monetary policy, which could lead to narrower profit margins, weakened balance sheets, and a mild economic slowdown. Given this backdrop, we have maintained a cautious approach to equities, reducing our US equity exposure to 40% and international exposure to 62% during the month.

Fed – higher for longer: As widely expected, at its September meeting the FOMC chose to keep the fed funds rate unchanged at the range of 5.25% to 5.5%. At the same time, there were notable shifts in the FOMC's economic forecast in the September Summary of Economic Projections (SEP), driven by the resilient U.S. economy data in the summer. The SEP predicted higher real GDP growth for 2023 (from 1% in June to 2.1%) and 2024 (from 1.1% to 1.5%). The estimate for unemployment rates was also revised lower from 4.1% to 3.8% in 2023, and from 4.5% to 4.1% in both 2024 and 2025. Core inflation forecasts were trimmed from 3.9% to 3.7% for 2023, indicating that the FOMC believes that inflation can be controlled without a significant rise in unemployment. However, the FOMC's stance was generally viewed by the market as a hawkish pause as it maintains a bias toward tightening, with the dots (the Fed dot plot is a chart showing projections for the fed funds rate) for 2024 and 2025 moving 50bp higher. Also, 12 out of 19 participants have projected another hike by 2023 year-end, and participants have postponed their timeline for the first rate cut.

Surging yields weighed on markets: Bond yields are experiencing a significant upswing this month, putting pressure on the equity market. Due to a volatile macroeconomic environment, rising oil prices, and a substantial fiscal deficit, Treasury yields across various maturities reached their highest levels in over ten years. Specifically, the 10-year U.S. Treasury yield has surged to 16-year highs at 4.69%. While major central banks have paused rate hikes, they have left the possibility open for future hikes, which aligns with our long-held view that interest rates will likely remain high. We believe that the treasury markets are more reasonably priced after the recent rise in yields, as the increase in long-term bond yields indicates that markets are adapting to the heightened risks associated with the new era of amplified macroeconomic and market volatility.

Oil prices: Crude oil prices have surged by approximately 30% since midyear. This rise is primarily attributed to a disruption in the oil supply, stemming from Saudi Arabia's coordinated decision with OPEC to reduce oil production in late June. This action set off a steady upward trend in energy prices. Additionally, there has been a notable rebound in demand from China, evidenced by recent production and refinery activity data in the country. The rising oil prices resulted in the fastest monthly rise in headline CPI in August since June 2022, largely driven by a 10.6% rise in gasoline prices. Furthermore, investors are concerned that the supply cuts may continue, possibly in conjunction with other relatively modest adverse events in the US, such as an escalation of the UAW strike, a potential government shutdown, and the recent increase in US long-term interest rates. Hence, we anticipate one more potential uptick in headline inflation next month, followed by a subsequent decline. Should this materialize, it increases the probability of an additional rate hike in 2023.

Macroeconomic

- Nonfarm payrolls rose by 187,000 in August, slightly higher than consensus forecasts. The four-week moving average of initial jobless claims dropped to 211,000 as of Sep 23, the lowest level since February.
- Retail sales grew 0.6% in August after rising 0.5% in July, supported by a healthy labor market and real wage growth.
- U.S. industrial production increased solidly by 0.4% in August.

Sentiment

- U.S. manufacturing activity contracted for the 10th consecutive month, with the ISM manufacturing index edging up 1.2 points to 47.6 in August.
- The University of Michigan Consumer Confidence Index fell again in September, dipping to 68.1, with rising gasoline prices and the declining equity market weighing on confidence.
- The NAHB index fell from 50 to 45 in September, below the neutral level.

Technical

- Technical indicators were positive overall, with positive momentum and fear signals outweighing neutral reversal signals.
- The S&P 500 was 2% above its 200-day moving average, 2% below the 100-day average, and 4% below the 50-day average.
- The VIX index spiked after mid-month with market volatility, hitting its highest level since May before retreating and settling at 17.5 at the end of the month.

Valuation

- Valuation metrics for equity remained negative. P/E decreased from 22.1 at the end of August to 21.1 at the end of September.
- Forward P/E decreased to 19.9 at the end of September from 20.6 at the end of August.
- Inflation-adjusted valuation metrics continued to be negative.
- Equity valuation metrics relative to bonds remained negative with high bond yields.