January 30th, 2023

Weekly Market Guide

The equity market has been resilient to begin the new year (up 5% YTD), and we believe that it is attempting to turn.

When considering the equity market outlook, on one hand we have an economy that appears set to weaken. For example, the yield curve is deeply inverted, leading economic indicators are negative, banks are tightening lending standards, and demand surveys are pointing lower. We believe the odds of economic contraction are high, which will lead to lower corporate earnings. This view is supported by company comments regarding their earnings outlooks during Q4 earnings season. For example, the banks are increasing reserves on expectations of higher loan delinquencies, technology companies are citing broad-based weakness, and the rails are noting muted volume growth.

On the other hand, stocks discount the future and are likely to bottom well ahead of the economy and fundamentals. This is where technical analysis can help, and the positive developments are stacking up. Recent additions to the list are relative strength breakouts of high beta vs. low volatility and equal-weight consumer discretionary vs. consumer staples. This risk-on tone bodes well for the underlying backdrop of the market. Additionally, the percentage of Russell 3000 stocks making new 4-week highs recently moved above 50%. This bullish reading did not occur in the bear market rallies of the '01 dotcom bubble and '08 financial crisis, and adds further support that the worst of this bear market may be behind us.

That said, we do not believe that equities are ready for sustainable upside quite yet. A disconnect lies in Fed expectations in our view. The market-implied fed funds rate bakes in ~50bps worth of hikes left in the first half of 2023, followed by ~50bps worth of cuts in the second half. We believe that the Fed will be hesitant to begin cutting rates and risk disrupting the moderation in high inflation. They wish to avoid the stop-and-go policy of the 1970s that led to a prolonged period of high inflation and was very damaging to the economy. Thus, we believe they will be tighter for longer than the market currently expects, in order to bring inflation down to their target. *Updated Fed comments come at next Wednesday's FOMC meeting, which along with a full slate of economic data and Q4 earnings season, will be catalysts over the coming week.*

The result is a bottoming and recovery process that may be more elongated this cycle. We expect volatility to persist and for the S&P 500 to trade in more range-bound fashion over the coming months (potentially between ~3700-4300). Longer-term, we believe that equities present attractive risk/reward for investors and that stocks will be climbing by year-end. But for those investors trying to be timely, we recommend pragmatism and patience. Accumulate favored stocks over time as the trend evolves, refrain from chasing the rally periods, and use the weak periods as opportunity within a long-term perspective.

Equity Market Indices	Price Return Year to Date	Price Return 12 Months
Dow Jones Industrial Avg	1.8%	-1.6%
S&P 500	4.6%	-7.8%
S&P 500 (Equal-Weight)	5.6%	-2.2%
NASDAQ Composite	8.1%	-16.4%
Russell 2000	7.3%	-5.7%
MSCI All-Cap World	6.3%	-8.1%
MSCI Developed Markets	8.4%	-4.7%
MSCI Emerging Markets	8.9%	-14.0%
NYSE Alerian MLP	6.6%	18.8%
MSCI U.S. REIT	7.2%	-15.1%

S&P 500 Sectors	Price Return Year to Date	Sector Weighting
Communication Svcs.	11.9%	7.8%
Consumer Discretionary	9.7%	10.3%
Information Technology	7.6%	26.5%
Materials	7.2%	2.8%
Real Estate	7.0%	2.8%
Financials	5.3%	11.7%
S&P 500	***4.6%***	-
Energy	2.9%	5.1%
Industrials	2.0%	8.4%
Consumer Staples	-1.7%	6.8%
Health Care	-1.8%	14.9%
Utilities	-2.6%	3.0%

Source: FactSet, RJ Equity Portfolio & Technical Strategy

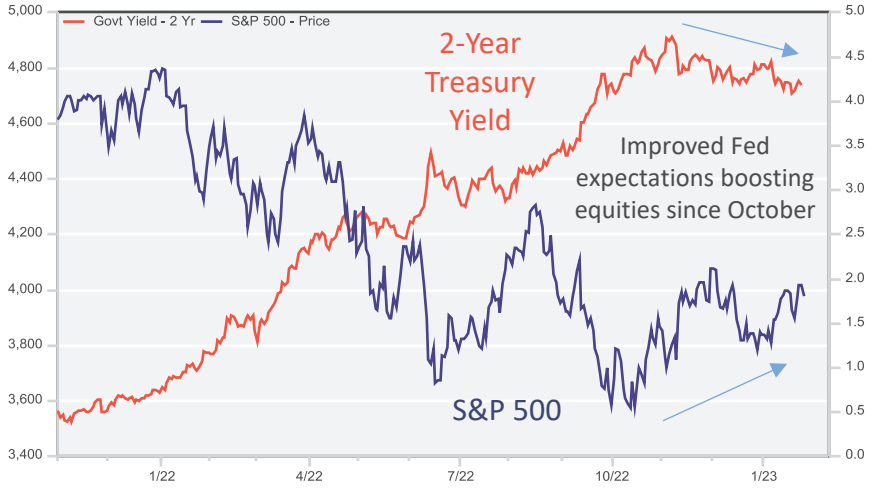
MACRO: US

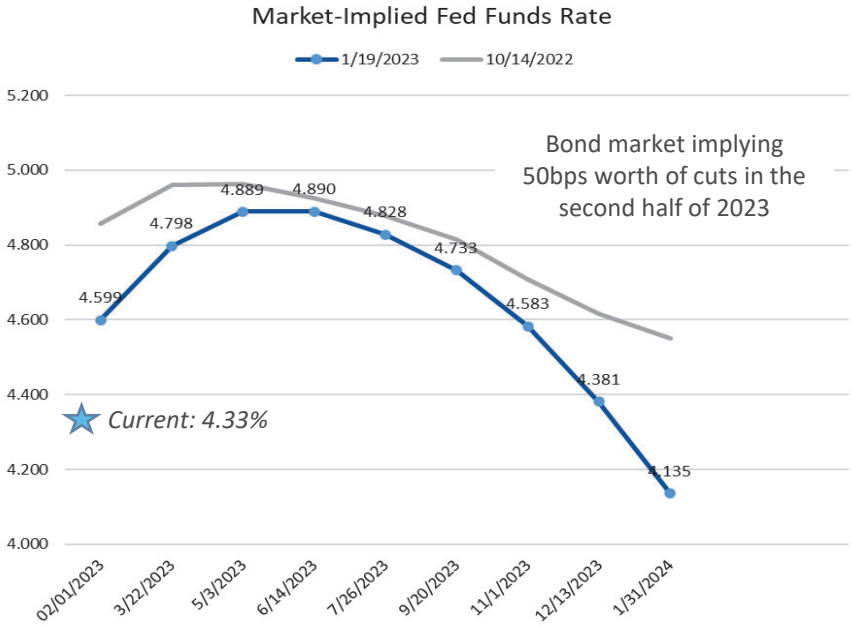
There is a full slate of economic data over the coming week, including:
1/27 Core PCE (Dec)- Fed's favored gauge of inflation
1/31 Employment Cost Index (Q4)
2/1 ISM Manufacturing (Jan), JOLTS Job Openings (Dec), FOMC Decision
2/2 Unit Labor Costs and Productivity (Q4)
2/3 Jobs Report (Jan), ISM Services (Jan)

This data, along with Fed commentary at next week's FOMC meeting, will be fresh catalysts for the market's interpretation of inflation moderation, Fed policy, and economic growth over the coming year. Market-implied expectations of Fed policy have eased since the market lows in October, now reflecting 50bps worth of cuts in the back half of this year. There is a good chance that the Fed talks down the market, as a ripping higher equity market would be inflationary. It is likely the language tilts hawkish, as they want to keep a lid on financial conditions to not stunt ongoing progress. This may be a headwind to equities, but we will also see if the market believes the Fed.

Economic Report	Period	Actual	Consensus	Prior
Existing Home Sales SAAR	DEC	4,020K	3,950K	4,080K
Leading Indicators SA M/M	DEC	-1.0%	-0.70%	-1.1%
PMI Composite SA (Preliminary)	JAN	46.6	46.4	45.0
Markit PMI Manufacturing SA (Preliminary)	JAN	46.8	46.5	46.2
Markit PMI Services SA (Preliminary)	JAN	46.6	45.3	44.7
Richmond Fed Index	JAN	-11.0	-5.0	1.0
Building Permits SAAR (Final)	DEC	1,337K	-	1,330K
Chicago Fed National Activity Index	DEC	-0.49	-	-0.51
Continuing Jobless Claims SA	01/14	1,675K	1,647K	1,655K
Durable Orders ex-Transportation SA M/M (Preliminary)	DEC	-0.10%	-0.10%	0.10%
Durable Orders SA M/M (Preliminary)	DEC	5.6%	2.5%	-1.7%
GDP SAAR Q/Q (First Preliminary)	Q4	2.9%	2.3%	3.2%
GDP SA Y/Y (First Preliminary)	Q4	1.0%	0.50%	1.9%
Initial Claims SA	01/21	186.0K	205.0K	192.0K
Wholesale Inventories SA M/M (Preliminary)	DEC	0.10%	0.75%	0.90%
New Home Sales SAAR	DEC	616.0K	610.0K	602.0K

Source: FactSet, Gibbs Capital Management

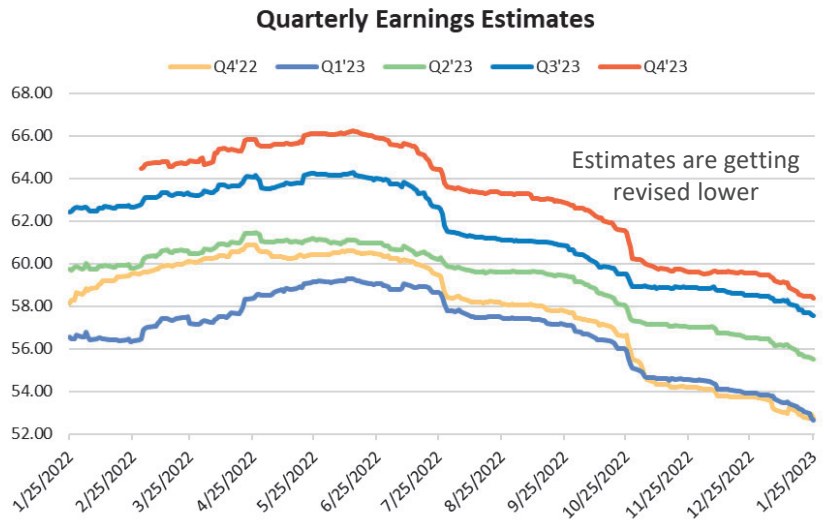


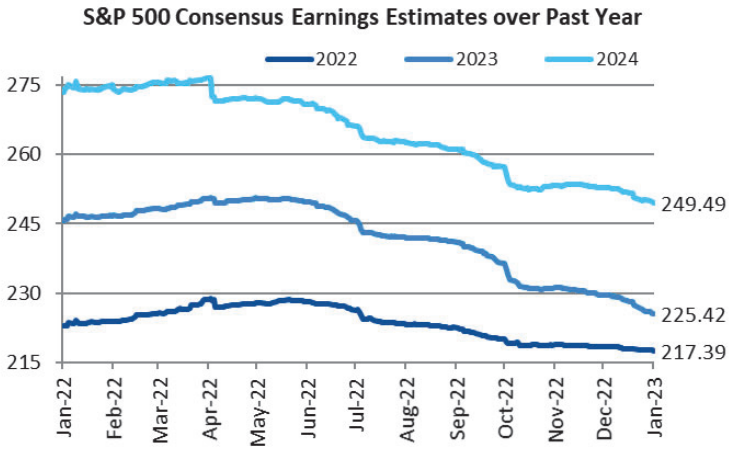


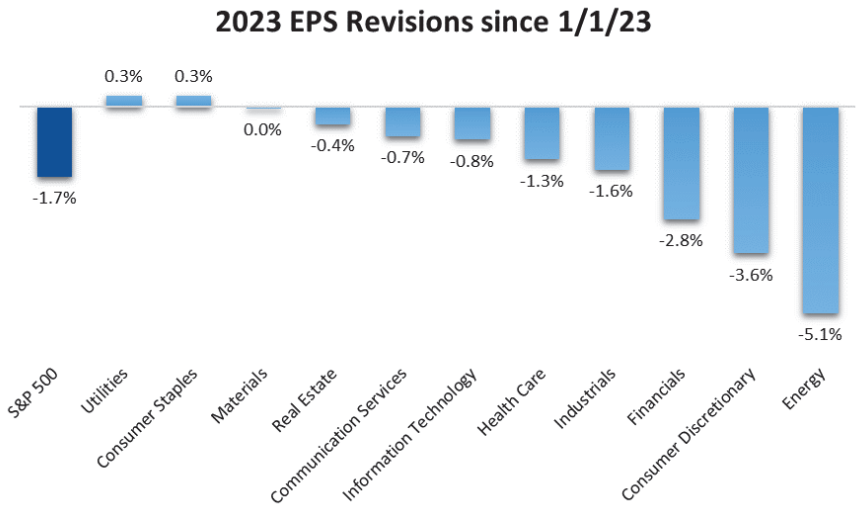
Q4 EARNINGS SEASON

Q4 earnings season is ramping up- 30% of the S&P 500's market cap has reported Q4 earnings season with an additional 123 S&P stocks reporting by the end of next week. Results have been decent, though below historic averages. 67% of companies so far have beaten their quarterly earnings estimates by an aggregate 1.5% (vs. 70% and 5.4% 15-year averages, respectively). Roughly half of those reporting have traded higher and the other half lower following results for an average 3-day price reaction of 0.8%.

Company comments on the earnings outlook have continued to steer increasingly cautious. For example, the banks are increasing reserves on expectations of higher loan delinquencies, technology companies are citing broad-based weakness, and the rails are noting muted volume growth. Earnings estimate revision trends are pointing lower, and we use a $215 S&P 500 earnings estimate for 2023 (vs. bottom-up analyst consensus at $225). Despite our expectations for an earnings contraction this year, we do believe equity markets will be higher by year-end 2023 due to valuation multiple expansion as investors gain clarity on inflation, Fed policy, and the economic damage done.







Source: FactSet, Gibbs Capital Management

TECHNICAL: S&P 500

Source: FactSet, Gibbs Capital Management

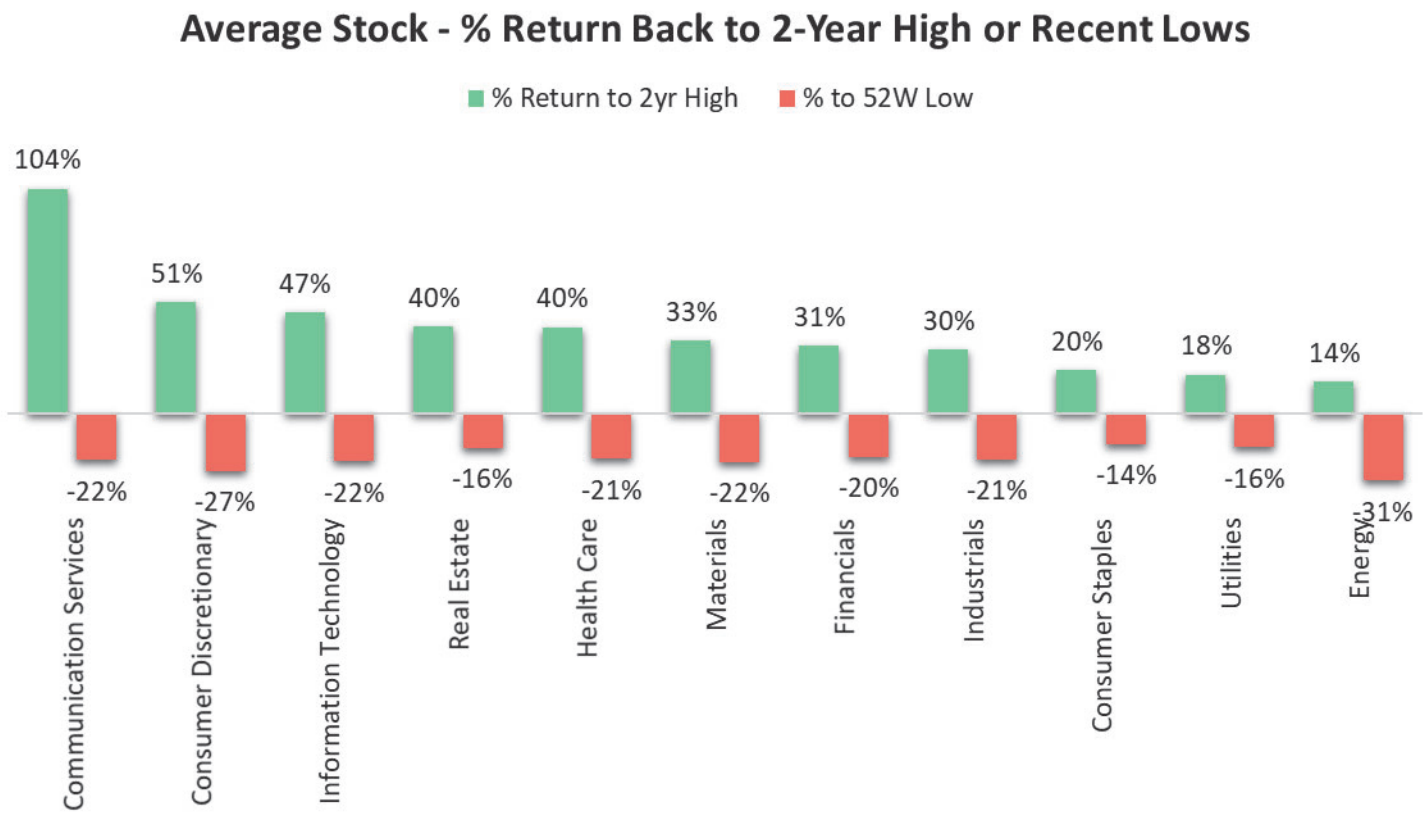
Despite an economic and earnings picture that appears to be deteriorating, stocks discount the future. Oftentimes, equity markets will bottom well ahead of the economy and fundamentals. This is where technical analysis can help, and the positive developments are stacking up.

- S&P 500 held 200-Week MA and 50% Fib retracement (so far)
- Investor Sentiment reached depressed levels
- Net Positioning very negative
- Equity Put/Call ratio spiked (though at odds with Composite and VIX)
- HY CDS Spreads have receded
- Advancers vs. Decliners has experienced some elevated readings
- Declining number of new lows as index made new lows
- % of stocks above their 50 DMA reached >90% twice
- % of Russell 3000 stocks making new 4-week highs recently moved above 50% (never occurred in ’01 and ’08 bear market rallies)

But ultimately, we need to see the downtrend end. The S&P 500 is right on its downtrend line at ~4032. We view this level as initial resistance, followed by 4083-4100. Initial support could be found around the 21DMA, which currently comes in at 3911. Below the 21DMA watch 3800, 3700, and then 3518.

POSITIONING

It is important to find the right balance in portfolio positioning- managing risk while also keeping an eye on the long-term opportunity. Longer-term, we believe that equities present an attractive risk/reward for investors and that stocks will be climbing by year-end. In fact, the average S&P 500 stock ex-Energy/Utilities/Staples would return 43% to get back to its post-Covid high. However, these same stocks would also experience a -22% decline on average if they go back to their recent lows. Given our expectations for volatility to persist, we recommend pragmatism and patience for those investors attempting to be timely. Accumulate favored stocks over time as the trend evolves, refrain from chasing the rally periods, and use the weak periods as opportunity within a long-term perspective.



Source: FactSet, Gibbs Capital Management (M23-108536)

Disclaimer

1. *The particulars contained herein were obtained from Raymond James we believe to be reliable but are not guaranteed by us and may be incomplete. The opinions expressed are based upon our analysis and interpretation of these particulars and are not to be construed as a solicitation or offer to buy or sell the securities mentioned herein.*

2. *The securities or sectors mentioned herein are not suitable for all investors and should not be considered advice. Please consult your investment advisor to verify whether this security or sector is suitable to you and to obtain the information, including the risk factor completely.*

3. *Vered Wealth Management (Canada) Company Limited provides comprehensive investment services, including managed accounts and advisory services. We have access to a wide range of investment products, including mutual funds, stocks, fixed income products, various alternative investment products and more. We offer registered and non-registered investment accounts, such as cash and margin accounts, corporate accounts, RRSPs & RRIFs, LIRAs & LIFs, RESPs and TFSAs.*

4. *Vered Wealth Management (Canada) Company Limited is a member of the Investment Industry Regulatory Organization of Canada (IIROC) and is registered in BC and ON. Vered is a member of the Canadian Investor Protection Fund (CIPF).*

5. *The contents herein are not intended and shall not be constructed as a solicitation of customers or business in any jurisdiction in which Vered is not registered as a dealer in securities.*