November 6th, 2023

VERED WEALTH MANAGEMENT (CANADA) COMPANY LIMITED

Happy National Cliché Day! Who knew there was a day dedicated to celebrate the often vague (although sometimes useful) and frequently annoying catchphrases and buzzwords that have become part of everyday life? There are literally thousands of clichés that have infiltrated our media, popular culture and exist across all industries. And there is no shortage of these well-known expressions in the investing world. Our long-time readers know that we pride ourselves on going beyond these buzzwords when explaining our directional views on the financial markets and the economy. But one well-known financial market cliché that is apropos right now is "Don't Fight The Fed"—suggesting it is unwise to position against the direction of monetary policy. While Chairman Powell wants to keep open the possibility of another rate hike, below are three reasons we think the Fed is done with its tightening cycle:

Key Takeaways

Economic Growth Will Slow In The Coming Quarters

Labor Market Strength Is Easing

Disinflationary Trend Remains Intact

- **Economic Growth Will Slow In The Coming Quarters |** While 3Q23 growth showed the economy expanded at a 4.9% annualized rate, it is important to remember that the GDP report is backward looking. From our vantage point, many real-time indicators we follow suggest that economic growth is decelerating, and tighter financial conditions will only exacerbate this trend. Why? First, manufacturing activity remains sluggish. This week's ISM Manufacturing Survey reported that activity remained in contractionary territory for the 12th straight month, falling to its fourth lowest level (ex-COVID) since 2009. Second, consumer confidence fell for the third straight month to its lowest level since April. This downbeat sentiment is likely to spill over into consumer spending, with the National Retail Federation expecting holiday spending to rise 3-4%—its slowest pace in five years. Third, elevated interest rates are hampering the interest rate sensitive sectors of the economy. Housing affordability is at the lowest level since the early 1980s, existing home sales have slowed to the weakest level since 2010 and loan demand is likely to fall for the fifth consecutive quarter in next week's Senior Loan Officer Survey. As a result, we expect the economy to enter a mild recession in 1Q24.
- **Labor Market Strength Is Easing |** The labor market has remained resilient in the wake of the Fed's aggressive rate hikes. In fact, while job growth slowed in October (+150k), the US economy had added an average ~200k jobs/per month over the last three months and job openings remained elevated. However, there are cracks forming that signal weakness ahead. First, the employment subsector within ISM Manufacturing report declined into contraction territory for the third time in four months as commentary within the report suggested that businesses are having an easier time finding prospective employees. Second, while initial jobless claims hovered near cyclical lows, continuing claims have risen to a six-month high, and the duration of those unemployed is climbing, suggesting that it is taking longer to find jobs. Third, the percentage of consumers that viewed jobs as "plentiful" declined to the lowest level since March 2021. The slowdown in hiring should continue, with job growth turning negative in 1Q24. The cooling labor market should keep the Fed from tightening further.
- **Disinflationary Trend Remains Intact |** Inflation has eased considerably from its peak last year. While it's trending in the right direction, Fed policymakers are not ready to claim victory given 'core' inflation remains above their 2.0% target. The recent uptick in energy prices may slow the trend, but the disinflationary trend is likely to continue. Why? For starters, shelter inflation should ease considerably in the coming months as the lagged impact of falling rental prices starts to feed into the official statistics. In fact, core inflation less shelter was up 1.9% YoY in September, down from a peak of 10.6% in June 2022. Second, wage growth (+4.1%YoY) has eased. In fact, during this week's Fed press conference, Powell remarked that wage growth is nearing a level that is consistent with the Fed's inflation objective. The jump in productivity (+4.7% QoQ) should also keep inflation contained. Finally, the sharp rise in car prices, which drove inflation higher during the pandemic, is declining. Specifically, the Manheim Used Vehicle Index is down over 18% from its peak, the worst drawdown in the history of the Index. And the mid-month report suggests further declines are likely when the monthly data is reported next week. These dynamics suggest the Fed's work on inflation is largely done.

Bottom Line | While rising interest rates and aggressive monetary policy have been a headwind for the equity and bond market over recent months, the end of a Fed tightening cycle has historically been a positive catalyst for both asset classes. In fact, in the 12 months following the final Fed rate hike, the equity market is up ~14%, on average, and is positive ~75% of the time. From a fixed income perspective, 10-year Treasury yields typically decline ~100 bps in the 12 months following the final Fed rate hike. These historical relationships are embedded within our forecasts and are one reason why we see upside for equities and downside for interest rates (a positive for bond prices) into year end and over the next 12 months.

ECONOMY

- October ISM Manufacturing (46.7) remained in contraction territory (a level below 50) and experienced its sharpest monthly drop (-4.7%) since June 2022. The main driver of this decline was the New Orders subindex which printed a weak 45.5. While this sector has been in contraction for the past 12 months, the services sector continued to expand, with the ISM Services index printing 51.8 in October. Despite being in expansion—driven by strong New Orders (55.5), most of the subindices (7/10) were weaker in October.
- Turning to the US labor market, job openings (9.55 million) were almost unchanged from the prior month which was revised down (9.6 to 9.5 million). Larger establishment sizes (5000+ employees) saw the biggest fall in job openings. Meanwhile, the US economy added 150k jobs in October, and September jobs added were revised downward by 39k. Also highlighting cracks in the labor market was the unemployment rate, which increased to 3.9%, and the fact that multiple job holders almost reached an all-time high.
- **Focus of the Week:** While a relatively slower week, we will be paying close attention to the Q3 Household Debt and Credit report, which is likely to show rising household debt led by higher credit card balances. In addition, the Michigan Consumer Sentiment report will be of interest, particularly the Inflation Expectations component which experienced a meaningful uptick last month.

November 6 – November 10

MON	Senior Loan Officer Survey	WED	Wholesale Inventories	FRI	Michigan Sentiment
TUE	Trade Balance Consumer Credit	THU	NFIB Small Business Index Jobless Claims	FUTURE EVENTS	11/14 CPI 11/15 PPI 11/16 NAHB Housing Market Index

US EQUITY

- At the end of 3Q23, we wrote that the S&P 500 Index could see the low 4,000s—a level consistent with a pre-recessionary drawdown, albeit mild, in the low double digits. Last week, the stock market entered correction territory with a 10% decline from its July peak of 4,589 to its October trough of 4,117. Given depressed technical indicators (e.g., oversold RSI, year-to-date high in the % of bearish investors), however, the S&P 500 posted its best week since November 2022 as the loss of momentum in both the labor market and the manufacturing sector signaled the prospect of the Fed being done with rate hikes
- After its busiest two weeks, earnings season is set to quiet down next week with an additional 49 S&P 500 companies (representing 5% of S&P 500 market capitalization) scheduled to report. With 75% of index market cap having already reported, earnings season has improved with bottom-line growth coming in at 4% year-over-year (YoY), thereby ending the earnings recession. 79% of companies have beaten estimates by an average magnitude of 7.4%, which is above the previous ten-year average results.
- **Focus of the Week**: Of the 49 companies reporting next week, 13 (27%) are in the Health Care sector. Despite the recent weakness of Health Care earnings, we remain optimistic on the segment for the following reasons: 1) People spend on health care goods and services regardless of the economic environment. Health Care earnings growth typically outperforms in recessions, which we expect to occur next year; 2) Health care spending has the added tailwind of an aging population; 3) Producer pricing power is strong in the health care industry (3% YoY); 4) Health Care boasts the strongest EPS growth expected by consensus of any sector in 2024 (27% YoY) which is aggressive, but we agree the segment should be a key anchor for index-level earnings next year; and 5) The stocks are out of favor amongst investors, given their poor performance year-to-date (-7%).

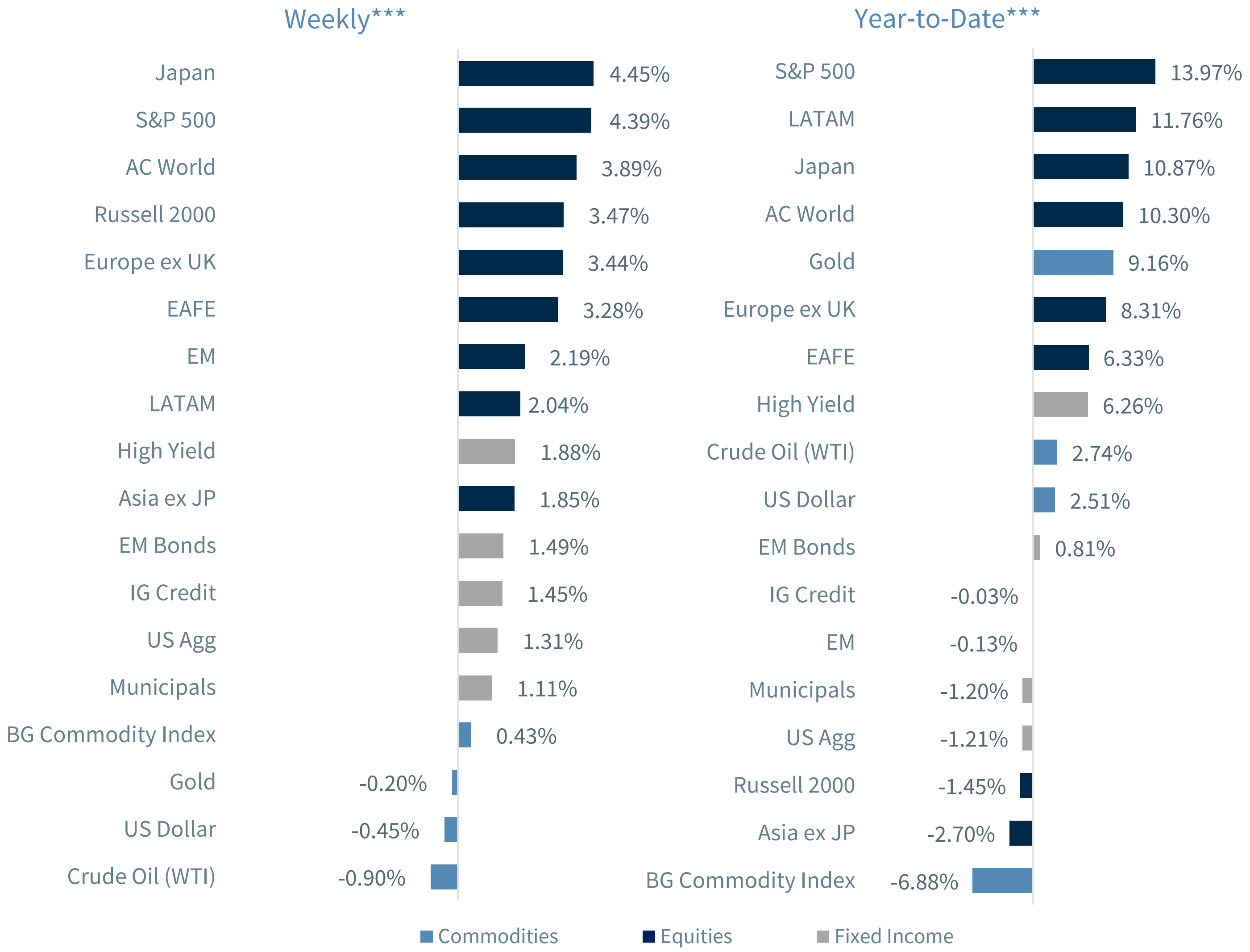
FIXED INCOME

- The Federal Reserve left interest rates unchanged this week, as expected. Powell tried to walk a fine line in his post-meeting press conference, balancing between the need to remain vigilant on the inflation front, while also being attentive to the sharp tightening in financial conditions over the last few months. While Powell kept open the possibility for further rate hikes, his comments about the September dot plot projections suggested that policymakers may be less confident about the need for one additional rate hike this year. With the market now anticipating that the Fed is done with its tightening cycle, Treasury yields tumbled across the curve.
- After the brutal rise in longer maturity yields over the last few months, the market was keenly focused on the Treasury's quarterly refunding announcement (i.e., borrowing estimates for the next quarter and debt sale plans). While the market was expecting additional longer-term debt sales, the Treasury Department slowed the ramp up in longer duration issuance, favoring more supply in shorter-maturities (where there has been strong demand). This added to the positive tone in the markets. It also may be a sign that Treasury expects yields to move lower and does not want to get locked into these higher long-term interest rates.
- The Bank of Japan maintained its negative interest rate policy but made another adjustment to its yield curve control policy—essentially scrapping the 1% hard cap on the 10-year JGB yield. The market immediately pushed longer-maturity yields higher, with the 10-year hitting its highest level in over a decade.
- **Focus of the Week:** The Fed's quarterly release of the Senior Loan Officer Survey will be the key event to watch next week. With borrowing rates up sharply since the end of last quarter, banks are likely to report tighter lending standards and weakening demand for loans. High yield spreads tend to be very sensitive to deteriorating credit conditions. However, there has been a disconnect during this cycle, likely due low overall borrowing needs.

POLITICS

- The White House released its long-awaited AI executive order (EO) on Monday, which is unlikely to be a major damper on the AI industry in the short term but could shape some of the behaviors in the sector in the long term. Comprehensive regulation of AI will likely take several years for Congress to develop, but the EO can be viewed as setting the stage for Congressional action—with funding measures as a likely first mover. We would remind investors that EOs tend to have more bark than bite when it comes to near-term market impact; however, this EO's national security focus and use of the wide-ranging authorities of the Defense Production Act could act as the starting point for more expansive federal action on AI long term. Key provisions include new requirements for firms to submit advanced AI models that could pose a national security concern to the Commerce Department, with the government then deciding whether it can be exported or restricted. We would also highlight provisions on international cooperation, which we view as in line with other coordinated technology restrictions undertaken by the Biden administration.

Asset Class Performance | Weekly and Year-to-Date (as of November 2)**



Weekly Data**

Data as of November 2

US Equities

Index	Price	Weekly	MTD	YTD	1 Year	3 Year	5 Year	10 Year
S&P 500	4317.8	4.4	3.0	14.0	16.8	11.0	11.6	11.5
DJ Industrial Average	33839.1	3.2	2.4	2.1	5.3	7.9	6.0	8.0
NASDAQ Composite Index	13294.2	5.5	3.4	27.0	26.3	6.7	12.6	13.0
Russell 1000	4536.2	4.3	2.9	13.5	9.5	9.5	10.7	10.9
Russell 2000	4260.2	3.5	3.1	(1.5)	(8.6)	3.9	3.3	5.6
Russell Midcap	6942.4	3.2	2.8	1.5	(1.0)	6.0	7.1	8.1

Equity Sectors

Sector	Price	Weekly	MTD	YTD	1 Year	3 Year	5 Year	10 Year
Materials	488.3	3.4	2.0	1.3	9.5	8.1	9.9	8.1
Industrials	852.0	3.5	2.4	3.9	10.7	10.8	9.3	9.4
Comm Services	223.8	5.2	2.8	41.7	46.5	5.3	9.5	6.5
Utilities	312.0	2.8	3.0	(10.7)	(4.3)	1.9	6.4	8.3
Consumer Discretionary	1253.7	7.7	3.9	25.7	18.7	3.0	9.0	10.9
Consumer Staples	726.0	1.8	1.2	(4.8)	0.5	6.5	8.0	8.1
Health Care	1476.6	1.2	1.8	(5.5)	(1.3)	8.8	9.3	11.0
Information Technology	3014.8	6.3	3.8	39.8	42.0	16.6	21.5	20.3
Energy	670.0	1.0	2.8	2.5	2.0	50.2	10.7	4.3
Financials	554.1	4.1	3.1	(1.1)	1.2	13.3	7.1	9.4
Real Estate	215.2	4.3	3.7	(4.6)	(0.1)	2.9	5.0	6.7

Fixed Income

Index	Yield	Weekly	MTD	YTD	1 Year	3 Year	5 Year	10 Year
3-Months Treasury Bill (%)	5.4	0.1	0.0	4.2	4.9	1.9	1.8	1.1
2-Year Treasury (%)	5.0	0.2	0.2	1.7	2.6	(1.0)	0.9	0.7
10-Year Treasury (%)	4.7	1.5	1.9	(3.7)	(1.1)	(8.2)	(0.4)	0.4
Bloomberg US Corporate HY	9.1	1.9	1.6	6.3	7.9	1.6	3.3	4.0
Bloomberg US Aggregate	5.4	1.3	1.6	(1.2)	1.8	(5.1)	0.3	1.1
Bloomberg Municipals	--	1.1	1.1	(1.2)	3.2	(2.2)	1.3	2.2
Bloomberg IG Credit	6.1	1.5	1.9	(0.0)	4.4	(4.9)	1.3	2.1
Bloomberg EM Bonds	8.2	1.5	1.4	0.8	8.1	(4.2)	0.4	2.1

Commodities

Index	Price	Weekly	MTD	YTD	1 Year	3 Year	5 Year	10 Year
WTI Crude ($/bl)	82.5	(0.9)	1.8	2.7	(8.4)	30.8	5.5	(1.4)
Gold ($/Troy Oz)	1993.5	(0.2)	(0.0)	9.2	20.8	1.7	10.1	4.3
Bloomberg Commodity Index	105.0	0.4	0.4	(6.9)	(8.7)	13.4	4.6	(1.6)

Currencies

Currency	Price	Weekly	MTD	YTD	1 Year	3 Year	5 Year	10 Year
US Dollar Index	106.1	(0.4)	(0.5)	2.5	(4.7)	4.1	1.9	2.8
Euro	1.1	0.7	0.5	(0.5)	7.6	(3.0)	(1.4)	(2.4)
British Pound	1.2	0.4	0.3	1.2	6.2	(1.9)	(1.2)	(2.6)
Japanese Yen	150.5	(0.1)	0.6	(12.3)	(2.2)	(11.4)	(5.6)	(4.1)

International Equities

Index	Price	Weekly	MTD	YTD	1 Year	3 Year	5 Year	10 Year
MSCI AC World	655.0	3.9	2.9	10.3	15.9	7.8	8.4	7.7
MSCI EAFE	2006.1	3.3	3.0	6.3	17.5	6.8	5.0	4.0
MSCI Europe ex UK	2224.5	3.4	2.9	8.3	20.9	7.9	6.5	4.7
MSCI Japan	3400.4	4.4	4.0	10.9	19.9	3.0	4.0	4.8
MSCI EM	930.6	2.2	1.7	(0.1)	9.9	(3.1)	1.5	1.8
MSCI Asia ex JP	588.6	1.8	1.3	(2.7)	11.4	(5.0)	1.7	3.2
MSCI LATAM	2262.8	2.0	3.5	11.8	5.5	15.4	1.8	0.1
Canada S&P/TSX Composite	14232.8	4.0	4.0	1.2	1.8	7.7	5.4	3.9

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