DayMark
WEALTH PARTNERS

November 2022

Monthly Market Commentary

U.S. Treasury Interest Rates Trajectory

For 2-year U.S. Treasury securities, **yields** rose +29 basis points in October to 4.51% at month-end, where they **are up +378 basis points (+3.78%) since their closing level of 0.73% on December 31st, 2021**.

For 10-year U.S. Treasury securities, yields climbed +27 basis points in October and closed at 4.10% at the end of the month, where they **are up +258 basis points (+2.58%) since their closing level of 1.52% on December 31st, 2021.**

For 30-year U.S. Treasury securities, yields increased +43 basis points in October and reached 4.22% at the end of the month, where they **are up +232 basis points (+2.32%) since their closing level of 1.90% on December 31st, 2021.**

The lower right-hand chart depicts the recently inverted yield curve showing that the yield on the 3-month U.S. Treasury bill is above the yield on the 10-year U.S. Treasury bond, which is quite often an indicator of an impending economic recession. **With the 10-year U.S. Treasury bond yield (4.10%) already inverted -41 basis points (-0.41%) below the 2-year U.S. Treasury yield (4.51%), an economic recession in our opinion appears likely to ensue**, as restrictive monetary policy keeps short-term rates high and market participants—expecting GDP growth to slow—direct investment capital into longer-term issues (driving their prices up and their yields down).

Month-to-Month 2022 Yield Level Changes (in Basis Points)

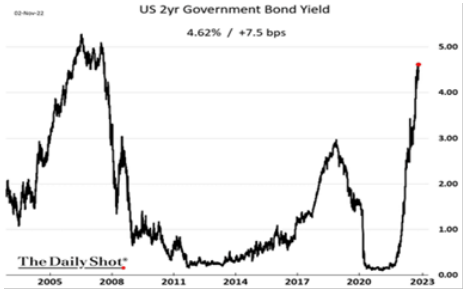
Security	Jan.	Feb.	Mar.	Apr.	May	Jun.	Jul.	Aug.	Sep.	Oct.	Nov.	Dec.
2-Year	+45	+26	+84	+42	-17	+39	-3	+56	+77	+29		
10-Year	+27	+4	+49	+57	-4	+13	-31	+48	+68	+27		
30-Year	+21	+6	+27	+52	+11	+7	-14	+27	+52	+43		

Source: The Wall Street Journal, and Yahoo Finance. October 31, 2022

2022 Month-End Treasury Securities Closing Yield Levels

Security	Jan.	Feb.	Mar.	Apr.	May	Jun.	Jul.	Aug.	Sep.	Oct.	Nov.	Dec.
2-Year	1.18%	1.44%	2.28%	2.70%	2.53%	2.92%	2.89%	3.45%	4.22%	4.51%		
10-Year	1.79%	1.83%	2.32%	2.89%	2.85%	2.98%	2.67%	3.15%	3.83%	4.10%		
30-Year	2.11%	2.17%	2.44%	2.96%	3.07%	3.14%	3.00%	3.27%	3.79%	4.22%		

Source: The Wall Street Journal, and Yahoo Finance. October 31, 2022

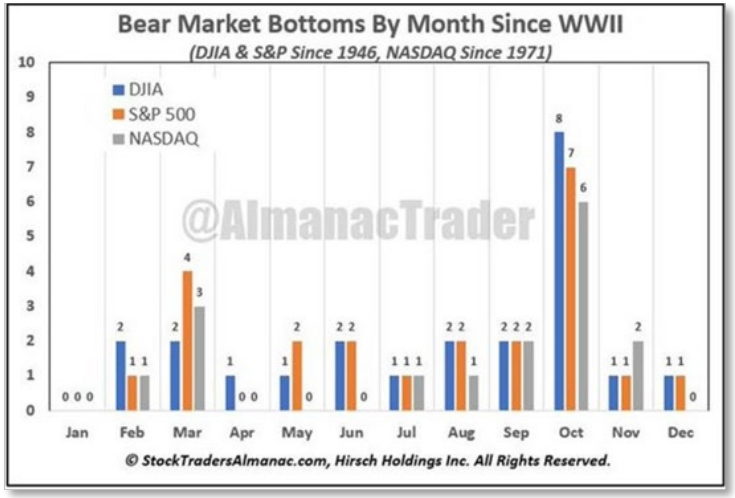


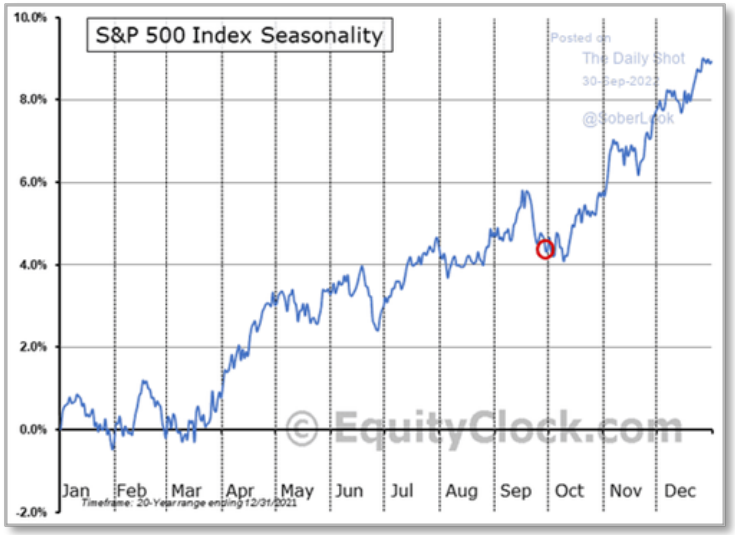
Equity Market Seasonal and Election Year Dynamics

Recognizing that (i) "past performance does not necessarily predict future outcomes," and (ii) "while history does not repeat itself, it nevertheless does rhyme sometimes," the nearby charts may provide some perspective as investors approach the last two months of 2022 and the year ahead.

The top chart shows that by a significant margin, **October more than any other month has tended to feature bear market troughs for the Dow Jones Industrial Average** (eight since 1946), the S&P 500 index (seven since 1946), and the NASDAQ Composite (six since 1971).

As far as seasonality, the bottom chart depicts the average seasonality of the S&P 500, in which **on average over the past 20 years, equity prices have tended to rise during the last quarter of the calendar year.**



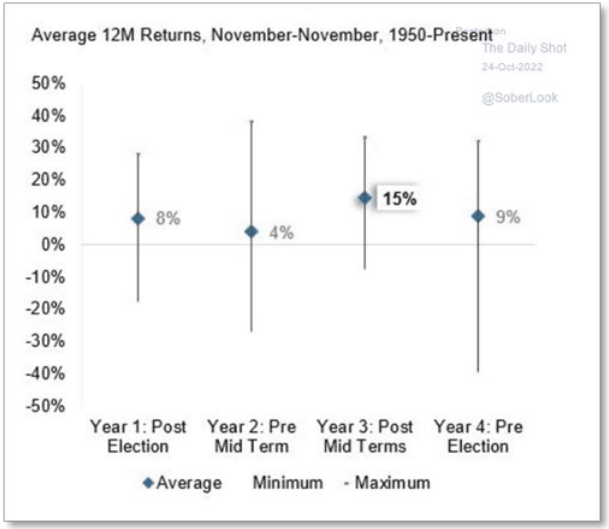


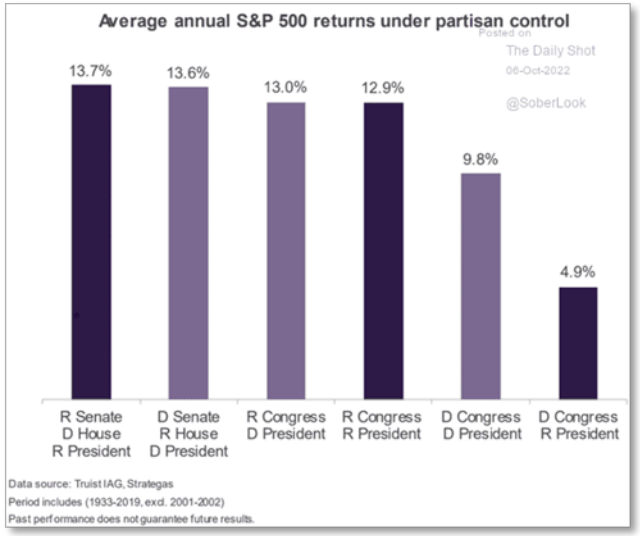
Equity Market Seasonal and Election Year Dynamics Cont.

Recognizing that (i) "past performance does not necessarily predict future outcomes," and (ii) "while history does not repeat itself, it nevertheless does rhyme sometimes," the nearby charts may provide some perspective as investors approach the last two months of 2022 and the year ahead.

Election years have in the past tended to feature interesting paths for equity prices. In the top chart, according to the hedge fund and credit market analysis firm SoberLook, **U.S. equity prices — on a November-to-November basis since 1950 —have tended on average to rise**: +8% in the 12 months immediately following a presidential election; +4% in the 12 months pre-midterm elections; **+15% in the 12 months immediately following midterm elections:** and +9% in the 12 months immediately preceding presidential elections.

The bottom chart sets forth the average annual S&P 500 returns under partisan control, for all but two years of the 1933–2019 timeframe. These returns range from an average +13.7% during years which featured a Republican majority in the Senate, a Democratic majority in the House of Representatives, and a Republican President, to +4.9% in years in which Democrats controlled the Senate and the House of Representatives with the White House occupied by a Republican President. Perhaps our politicians would be well advised to be mindful of the sentiments expressed by Caius Titus in an oft-quoted speech delivered to his peers in the Roman Senate: *Verba volent, scripta manent* ("words fly away, writings remain").





Consumer and Producer Price Inflation

Even as M-2 money supply growth and the prices of gasoline, vehicles, medical services, and numerous goods have begun (or continued to) exhibit weakness in recent reporting periods, these declines have so far generally been more than offset by rising prices for many services and especially, shelter costs. **Shelter costs have been a principal driver of the core Consumer Price Index, with owners' equivalent rent in September reaching +6.7% year-over-year, the largest annual increase ever.**

Moreover, the shelter measure tends to lag increases in home prices and rents, making it uncertain how quickly the incipient cooling in many housing markets will begin to meaningfully tilt consumer price indices in a downward direction. Housing prices make up nearly 40% of the monthly CPI report and represent a chief reason why the CPI has not yet begun to meaningfully decline. **The inertial character of shelter costs represents a key factor in our expectation of a modest downward trajectory in inflation price indices for the time being.**

Despite Personal Consumption having proven resilient so far this year — in nominal terms, rising +0.6% month-over-month in September despite high inflation rates and borrowing costs — real wages (nominal wages less inflation) have been declining in nine of the past 12 months, and are down -3.0% over the past year. **As household liquidity continues to be drawn down, weakness in real wages tends to constrain personal consumption, itself one of the avenues by which the Federal Reserve is seeking to bring down the rate of inflation.**

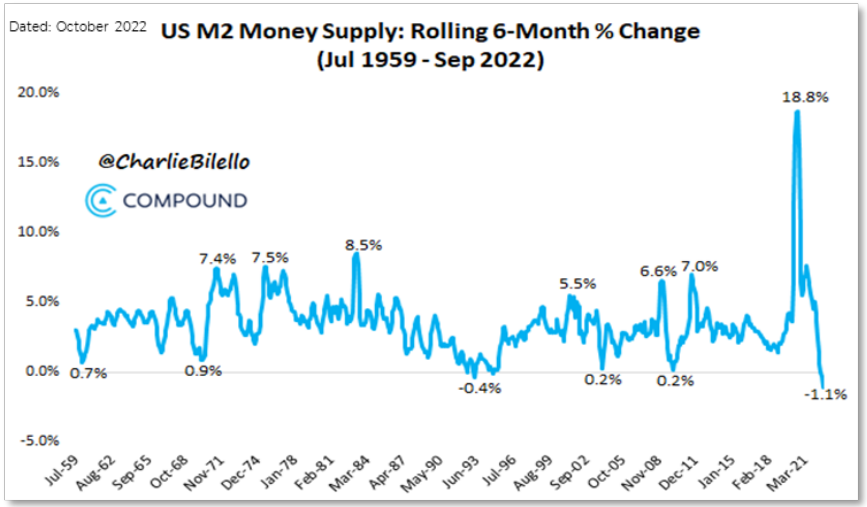
Comparative Inflation

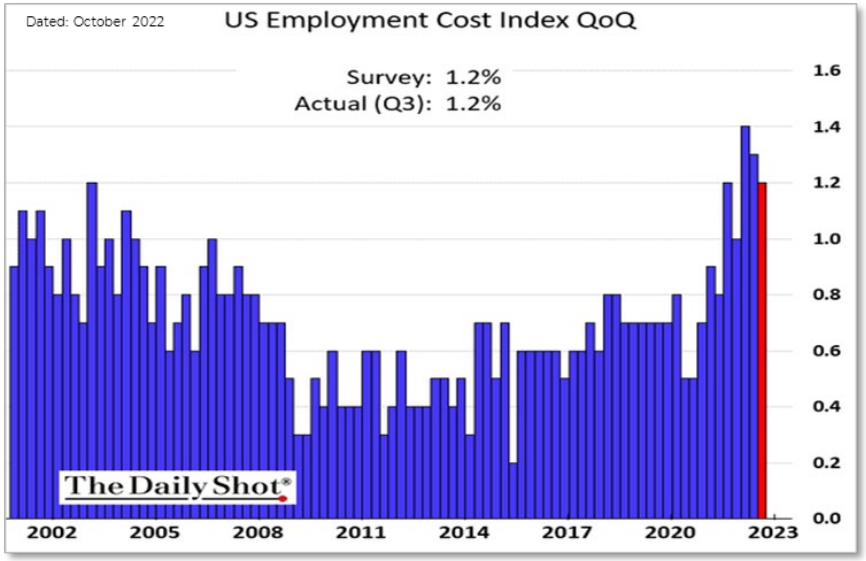
	September				August			
	Release Date	Mo.-Over-Mo.		Yr.-Over-Yr.	Release Date	Mo.-Over-Mo.		Yr.-Over-Yr.
Headline CPI	10/13	+0.4%	Sep	+8.2%	9/13	-0.1%	Aug	+8.3%
Core[1] CPI	10/13	+0.6%	Sep	+6.6%	09/13	+0.6%	Aug	+6.3%
Headline PPI	10/12	+0.4%	Sep	+8.5%	09/14	-0.2%	Aug	+8.7%
Core[1] PPI	10/12	+0.4%	Sep	+7.2%	09/14	+0.4%	Aug	+7.3%
Headline PCE	10/28	+0.3%	Sep	+6.2%	09/30	+0.3%	Aug	+6.2%
Core[1] PCE	10/28	+0.5%	Sep	+5.1%	09/30	+0.6%	Aug	+4.9%

Inflation Influences

The significant decline in the 3-Month Percentage Change in the U.S. M-2 Money Supply is frequently a reliable several-months-ahead precursor of future price trends. To us, such a trajectory – with some as-yet-unknown time lag – **appears to foretell downward-sloping headline consumer price inflation.**

Labor costs have exhibited a meaningful upward trend in recent quarters. Such costs have historically tended to be asymmetrically stickier to the upside than to the downside. **We believe the Federal Reserve needs to see softening labor market conditions as a key prerequisite to achieving their inflation-fighting goals.**



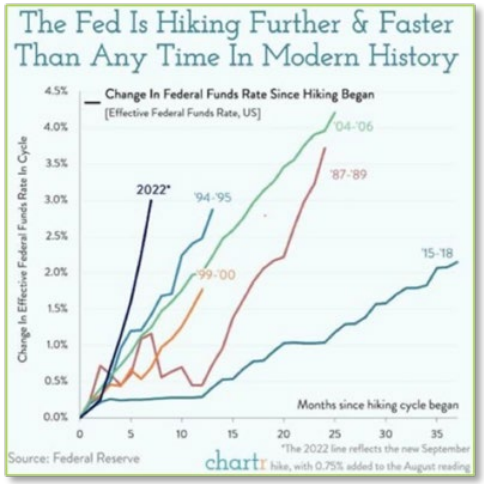


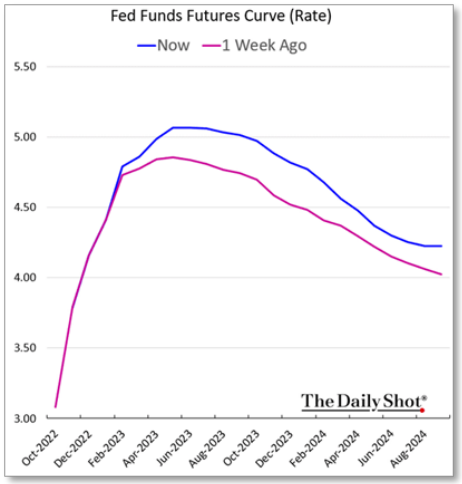
Monetary Policy & Fed Funds Interest Rates

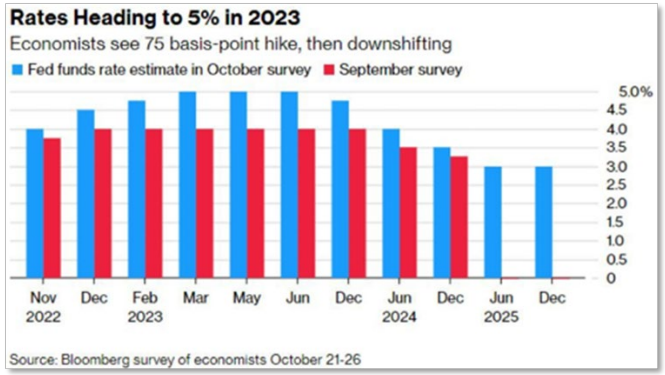
Financial market participants have taken note of the speed and intensity of the increases in the federal funds monetary policy rate since the Federal Reserve began hiking interest rates: +25 basis points in March 2022; +50 basis points in May 2022; +75 basis points in June 2022; +75 basis points in July 2022; +75 basis points in September 2022; and +75 basis points at the conclusion of the Federal Open Market Committee's November 1-2 meeting.

In our opinion, it is important to distinguish between: (a) a Fed pivot (indicating that policy interest rate increases have ceased during the current policy cycle); and (ii) a reduced magnitude — less than markets have been anticipating — of policy interest rate increases. Looking forward to the next three FOMC sessions, **we currently anticipate an increase of +50 basis points after the December 13-14 meeting; +25 basis points after the January 31–February 1 meeting; and +25 basis points after the March 21-22 meeting**.

Such a pattern of policy rate increases are consistent with: (i) fed funds futures rate pricing curves (shown in the lower left-hand chart); as well as (ii) the Higher for Longer policy rates persisting through much of 2023, before beginning a step-down pattern late in the year (as also estimated in the October Bloomberg Survey of Economists, shown in the lower right-hand chart).

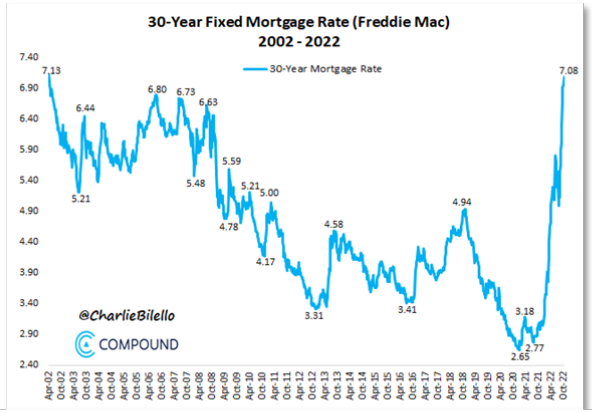


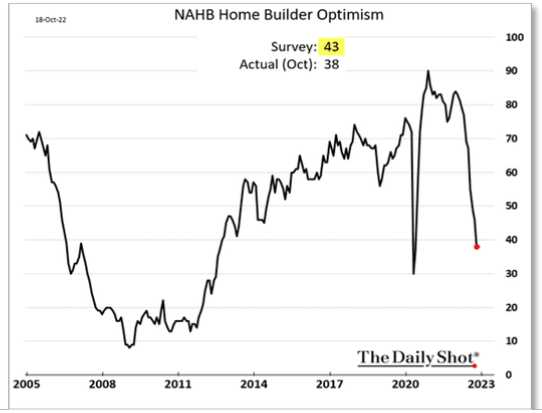


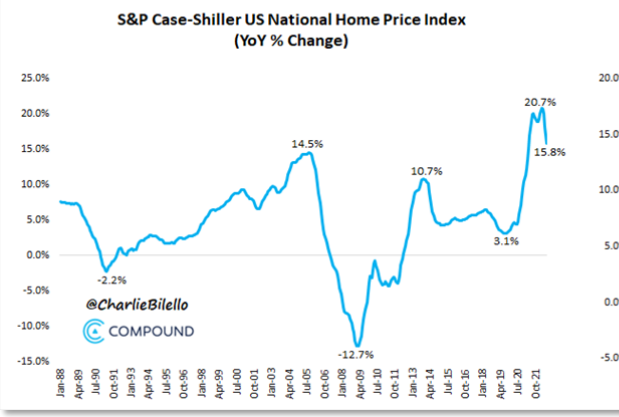


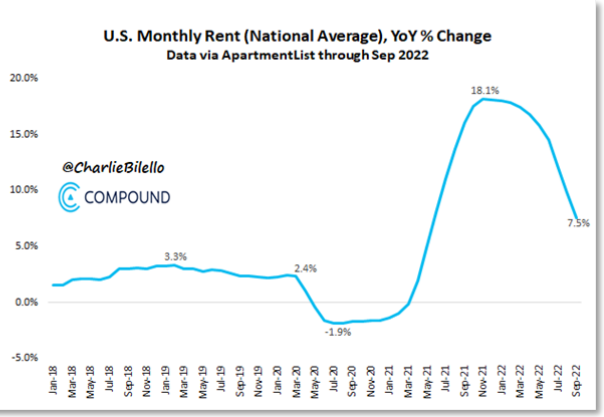
The Housing Sector

A chief factor underlying our (and numerous others') call for an anemic 2023 U.S. economic performance is expected weakness in the housing market. Housing represents a key driver of investment, employment, and consumption. Hindering the economic contribution of the housing sector have been: (i) sharply escalating mortgage financing costs (as depicted in the nearby chart); (ii) constrained demand as potential home buyers choose to wait and see where the housing market ends up; (iii) a slowdown in home building (with homebuilder optimism falling in October to levels last experienced at the height of the coronavirus pandemic, as shown in the upper right-hand chart); and (iv) declining new home sales (-17.6% year-over-year in September) and existing home sales (-23.8% year-over-year in September). **Slowing monthly rental costs (+7.5% year-over-year through September as depicted in the lower right-hand chart) should begin to exert decelerating force on the significant shelter component of the Consumer Price Index**







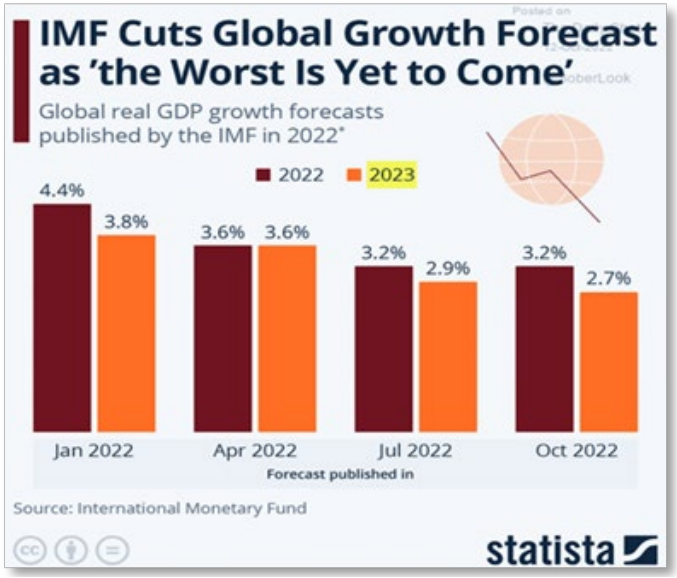


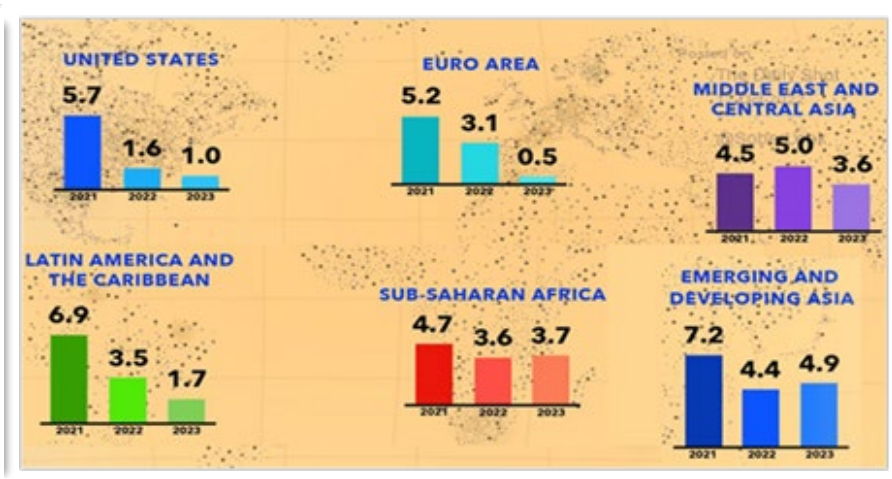
[1] NAHB: National Association of Home Builders is one of the largest trade associations in the US representing the interests of home builders, developers, contractors, and associated businesses.

The U.S. Economy & Corporate Profits

As depicted in the upper left-hand chart, in its October 2022 Global Real GDP Forecast, the **International Monetary Fund (IMF) is projecting +3.2% in global real GDP growth for calendar year 2022** (down from a 2022 projection of +4.4% global real GDP growth in January of this year), **followed by projected global real GDP growth of +2.7% for calendar year 2023** (reduced from a 2023 projection of +3.8% global real GDP growth in January of this year).

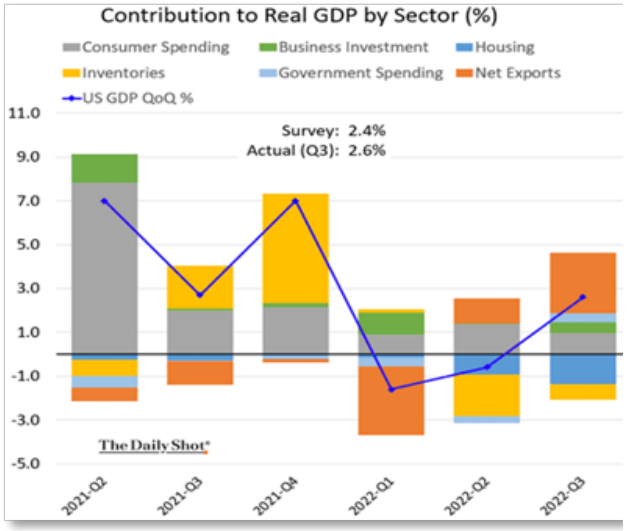
The upper right-hand chart shows that the **IMF projects +1.6% real GDP growth for the United States in 2022, followed by +1.0% real GDP growth for 2023** (which may or may not include a recession of unknown severity and duration — our call at this point includes a modest recession in 2023). The euro area — which is facing monetary tightening, elevated inflation, and proximity to the Ukraine-Russia conflict, among other challenges — is projected by the IMF to generate only real GDP growth of +0.5% in 2023, down from +3.1% in 2022.





The U.S. Economy & Corporate Profits Cont.

The top chart sets forth the pattern of seasonally adjusted annual rate quarter-over-quarter U.S. real GDP growth: +7.0% in 2Q21; +2.6% in 3Q21; +7.0% in 4Q21; -1.6% in 2Q22; -0.6% in 2Q22; and +2.6% in 3Q22. Close observation of this chart shows that the 3Q22 growth rate was augmented by exports, consumer spending, government spending, and business investment, and somewhat reduced by declining inventory investment and residential investment. **Given the ongoing effects of the prevailing restrictive monetary policies, our current estimate for 4Q22 GDP ranges between +1.0-2.0%.**



The bottom chart shows that analysts' consensus estimates of 2023 earnings per share for the S&P 500 companies has declined -6.0% from $250 in March of this year to approximately $235 at present. Against a background of still-elevated inflation, tight monetary policy, housing sector weakness, softening revenue generation in the technology space, and a strong dollar (limiting exports and reducing the value of foreign currency earnings), and feeble economic growth, **we currently estimate a range of $210-225 in earnings per share for S&P 500 companies in 2023.**

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