



FUND DIRECT ADVISORS

Quarter 2 - 2023 Market Review

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Second Quarter Summary

- The first half of 2023 ended on a positive note as markets remained resilient despite continued Fed tightening, calls for an imminent recession, a regional banking crisis, the debt ceiling debate, and more.
- GDP growth remains near trend (pg. 3); however, we believe there are some storm clouds on the horizon. While the likelihood of a mild recession has increased, the current strength of the job market (pg. 12) leads us to believe that any potential recession would be short and shallow.
- As inflation continues to trend downward, we believe that the Federal Reserve is at or near the end of the current rate hike cycle (pg. 11) . After a “skip” in June, the market is anticipating the Fed will resume rate hikes at the July FOMC meeting. The June 2023 meeting was the first FOMC meeting since this rate-hike cycle began in March 2022 without an increase in policy rates.
- P/E multiples have moved higher from the end of Q3-2022, and we continue to view stocks as “fairly valued” at the index level (pg. 7). Investor sentiment, which is a contrarian indicator (pg. 9), flipped from bearish to bullish in June. We also observed that stock volatility, as measures by the VIX Index, became more subdued as the quarter ended. This shift caused the Investor Sentiment gauge to move backwards by two notches (pg. 8).

Latest Assessment of Key Economic Indicators



No Change in Position

Economy

This quarter, we held the Economy gauge in Neutral to reflect that GDP growth remains near trend but there are some storm clouds on the horizon. June marked the eighth consecutive month of declining manufacturing activity in the US. Given the likelihood of tighter lending standards from banks, the odds of a mild recession have increased. However, given the strength of the jobs market any potential recession, in our opinion, would be short and shallow.

Key Takeaways

GDP

The final read of Q1 GDP came in at 2%, revised higher from 1.3%. The Atlanta Fed's GDPNow is currently forecasting growth of 1.9% for Q2.

Labor Market

The unemployment rate of 3.7% is near the lowest level in decades and job openings are plentiful, although they are off their peak of March of 2022.

Inflation

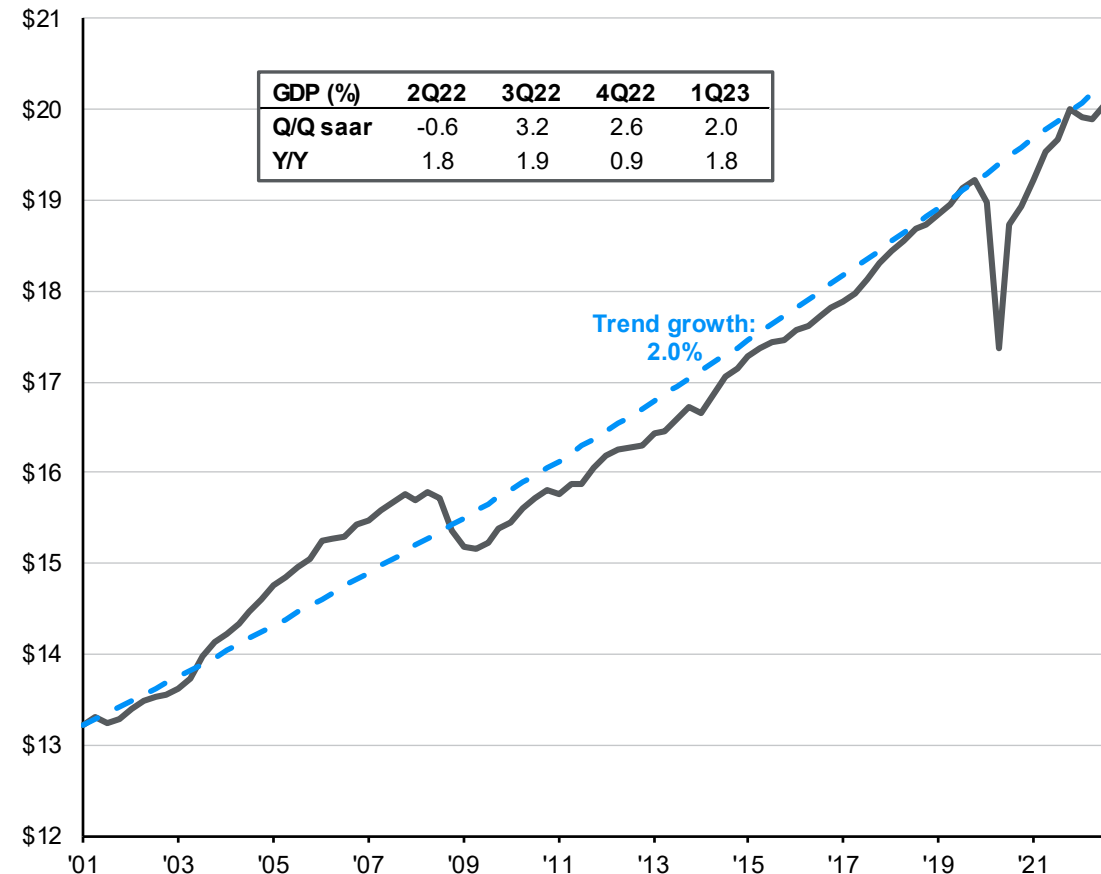
Headline CPI and PPI for May came in at 4.0% and 1.1% respectively. The Fed's preferred measure of inflation, Core PCE, remains above the target of 2%.

Latest Assessment of Key Economic Indicators



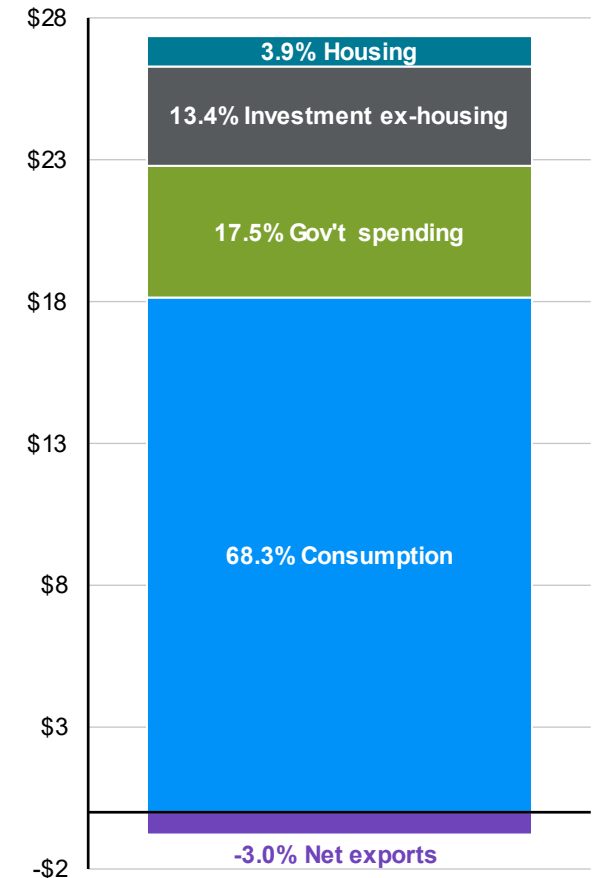
Real GDP

Trillions of chained (2012) dollars, seasonally adjusted at annual rates



Components of GDP

1Q23 nominal GDP, USD trillions



Latest Assessment of Key Economic Indicators



No Change in Position

Monetary Policy

This quarter, we held the Monetary Policy gauge in Slow Reverse to reflect that the Federal Reserve "skipped" raising rates at the June FOMC meeting. While Fed policy is still a headwind for risk assets, we believe that the Federal Reserve is nearing the end of the current rate hike cycle.

Key Takeaways

Rate Hikes

The Fed "skipped" a rate hike at the June FOMC meeting and signaled that additional rate hikes may be appropriate.

Fed Fund Futures

Fed Fund Futures currently imply a final rate hike in July and rate cuts beginning in May of next year.

Balance Sheet

The Fed's Balance Sheet has returned to levels observed prior to the regional bank issues experienced in March. Borrowing by banks through the Fed's Discount Window has declined after spiking in March.

Latest Assessment of Key Economic Indicators

Monetary Policy

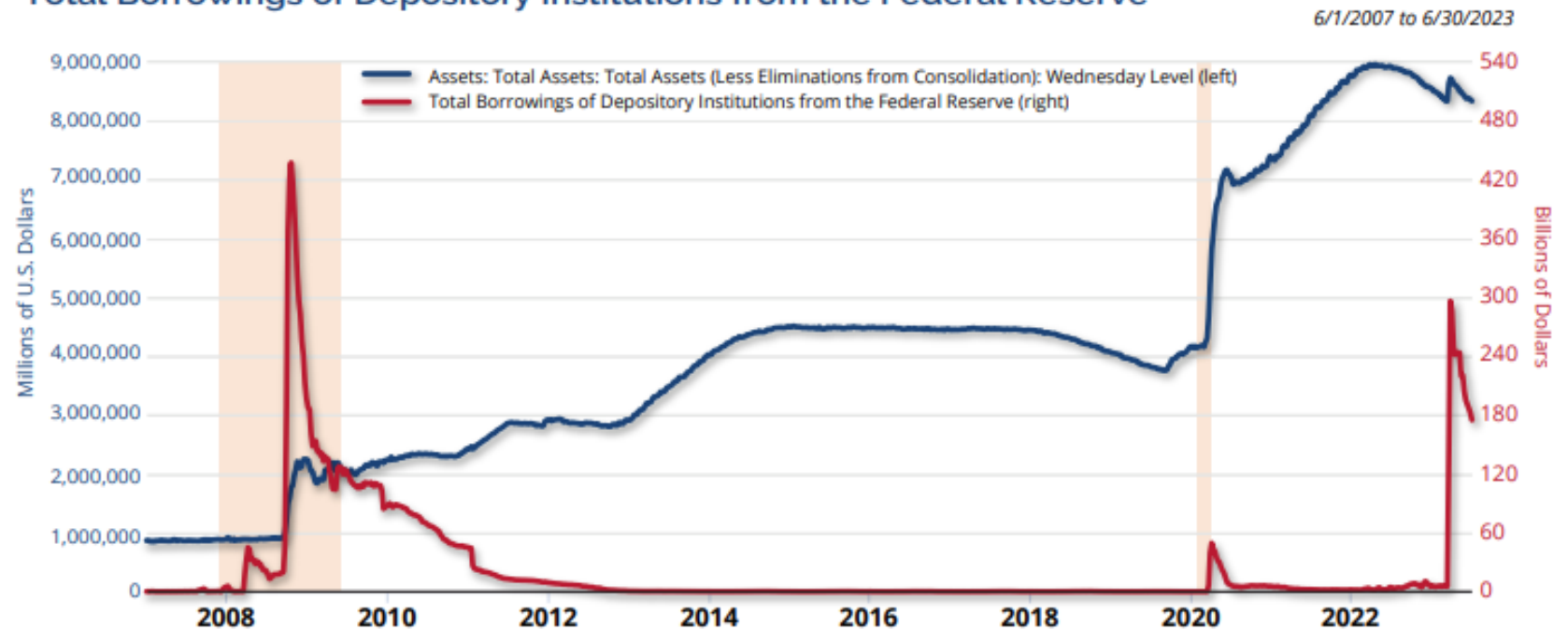


No Change in Position

The Fed's Balance Sheet

After some regional banks scrambled for liquidity in March, the Fed's Balance Sheet has begun to shrink again.

Total Borrowings of Depository Institutions from the Federal Reserve



Source: www.stlouisfed.com

Latest Assessment of Key Economic Indicators



Valuations

This quarter, we held the Valuations gauge in Neutral to reflect that P/E multiples remain in “fair value” range.

No Change in Position

Key Takeaways

P/E Multiples

After reaching undervalued levels at the end of Q3 2022, stocks have staged a rally and remain in “fair value” range.

Earnings

In Q1 S&P 500 companies posted a 6.4% increase in operating earnings compared to a year ago. Analysts are forecasting better earnings growth in the second half of this year.

Latest Assessment of Key Economic Indicators

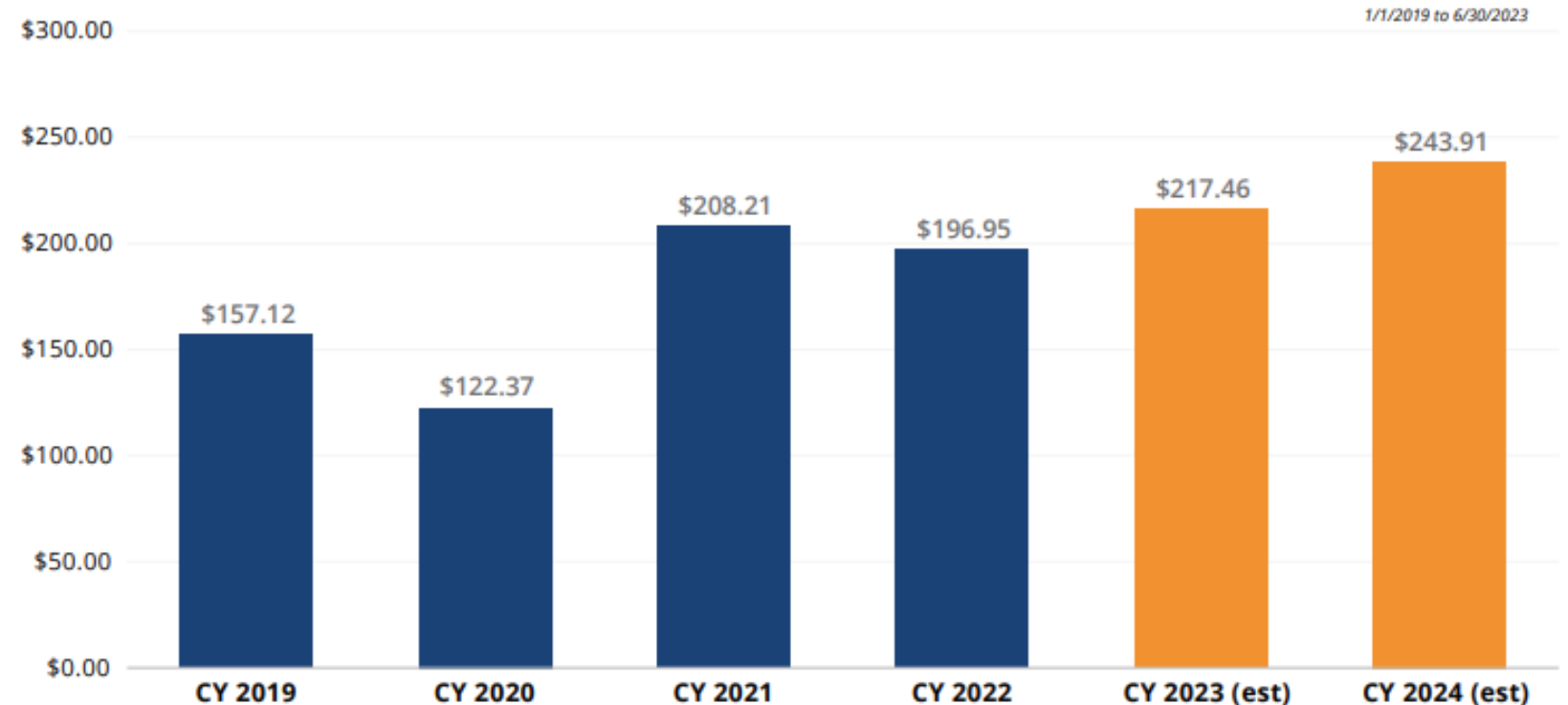
Valuations



No Change in Position

S&P 500 Calendar Year Operating EPS Actuals & Estimates

In 2022 S&P 500 operating EPS declined by 5%, albeit from a record level in 2021. For 2023 and 2024 the consensus of Wall Street analysts are for earnings growth of 10%-12% each year, although we acknowledge the possibility of revisions to those estimates.



Latest Assessment of Key Economic Indicators



Moved Two Notches
to the Left

Investor Sentiment

This quarter, we moved the Investor Sentiment gauge from Slow Forward to Slow Reverse to reflect that investor sentiment flipped from bearish to bullish in June. We also observed that stock volatility, as measured by the VIX Index, became more subdued as the quarter ended.

Key Takeaways

AAll Survey

After a resolution to the Debt Ceiling debate, stability in the regional bank sector, and further stock market gains; investor sentiment became Bullish in June.

VIX Index

After briefly reaching 30 in mid March the VIX Index retreated to a new 52 wk low of 12.73 in June, signaling complacency amongst investors.

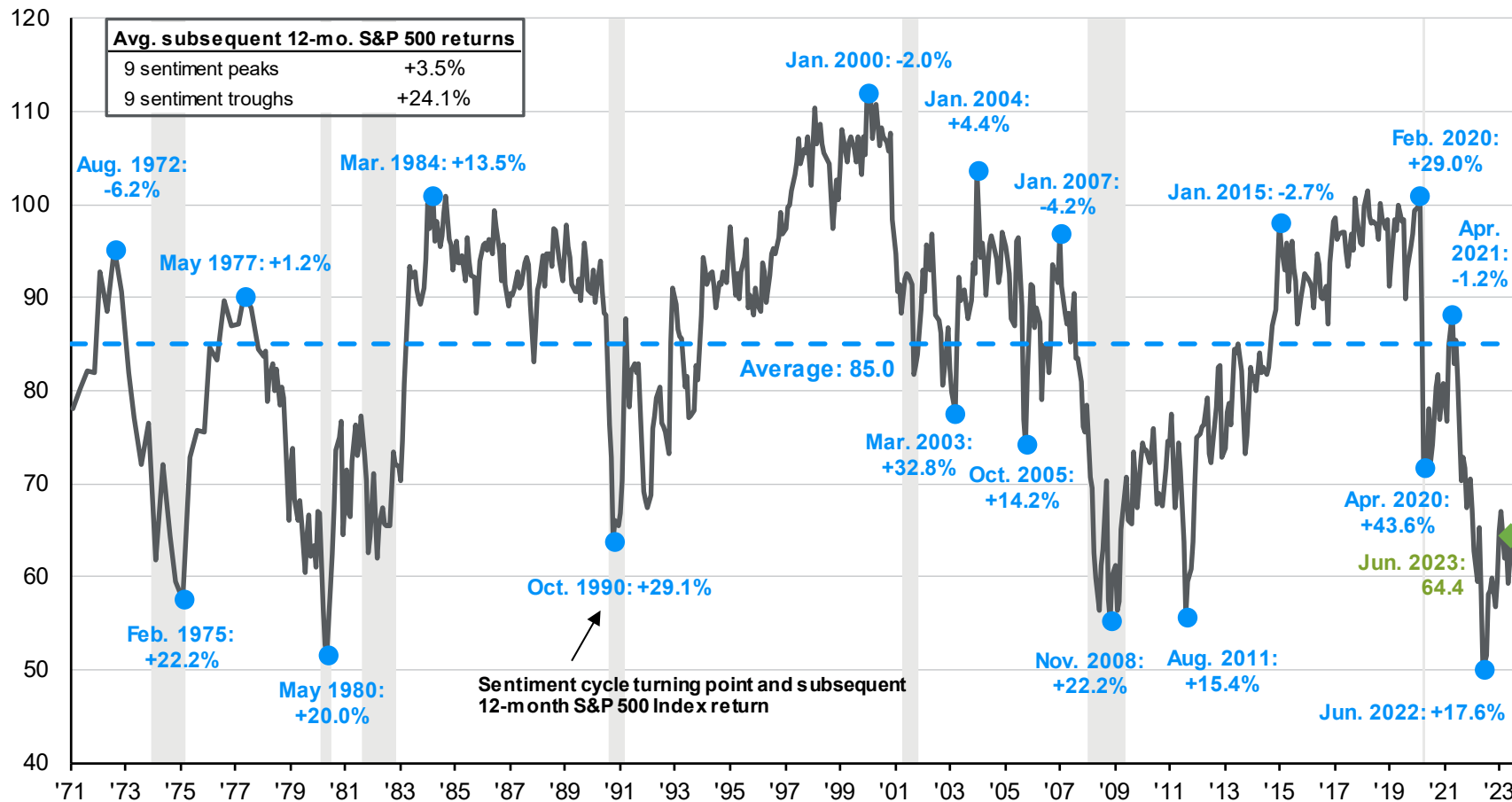
Latest Assessment of Key Economic Indicators

Investor Sentiment



Moved Two Notches to the Left

Consumer Sentiment Index and subsequent 12-month S&P 500 returns



Latest Assessment of Key Economic Indicators



No Change in Position

Interest Rates

This quarter, we held the Interest Rates gauge in the Slow Reverse position to reflect that both the level of interest rates and shape of the yield curve remain a slight headwind for risk assets.

Key Takeaways

Change in Yields

Short term interest rates have moved higher since March. At the same time, long-term interest rates have returned to the levels they were at during the beginning of the year.

Yield Curve

The spread between the 3m and 10yr Treasuries remains inverted. This signal has preceded prior recessions, although it does not indicate the depth or duration of a potential recession.

Interest Rate Volatility

Interest rate volatility, as measured by the MOVE Index, reached levels not seen since October of 2008 in March but retreated in June.

Latest Assessment of Key Economic Indicators

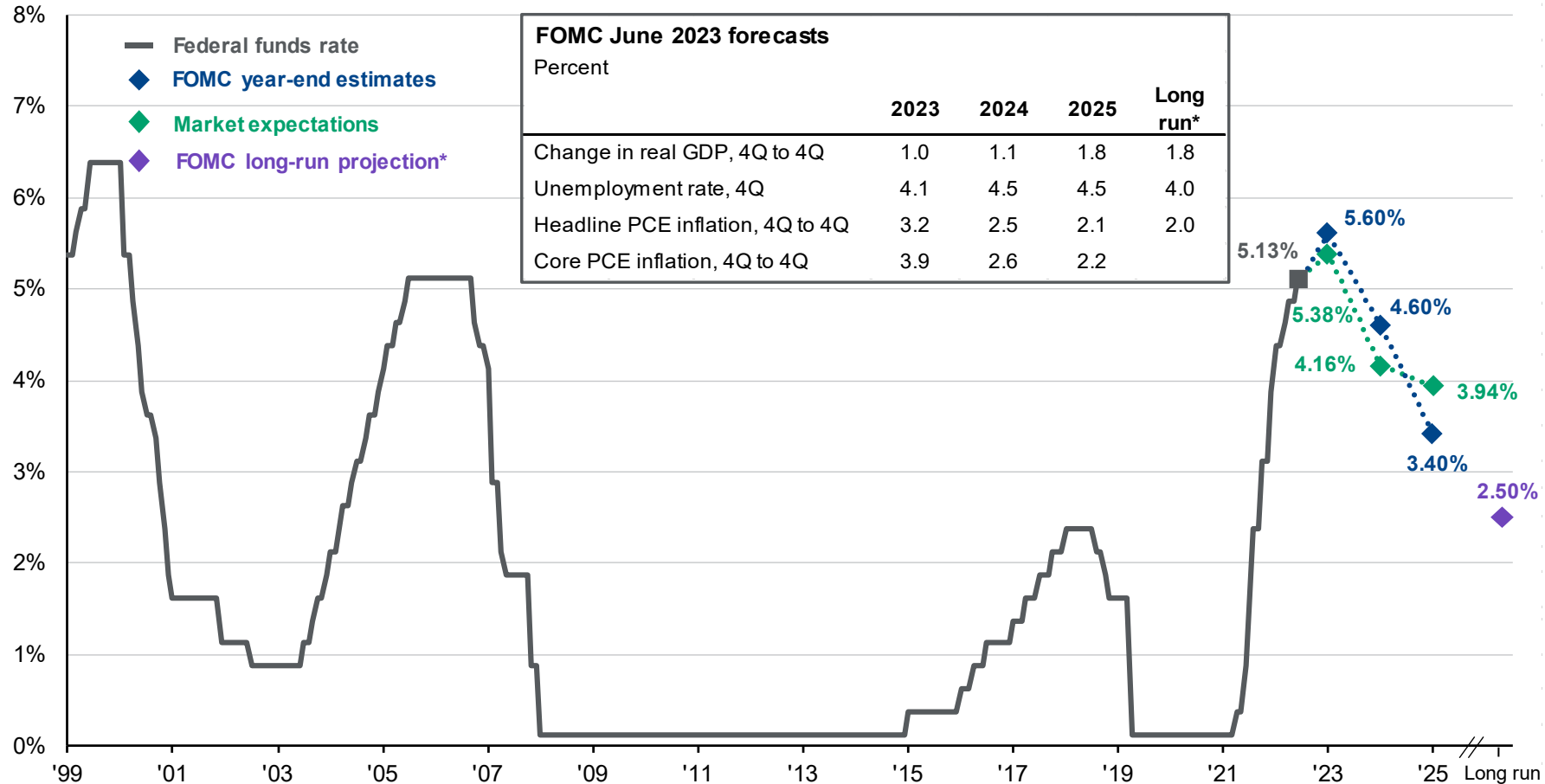
Interest Rates



No Change in Position

Federal funds rate expectations

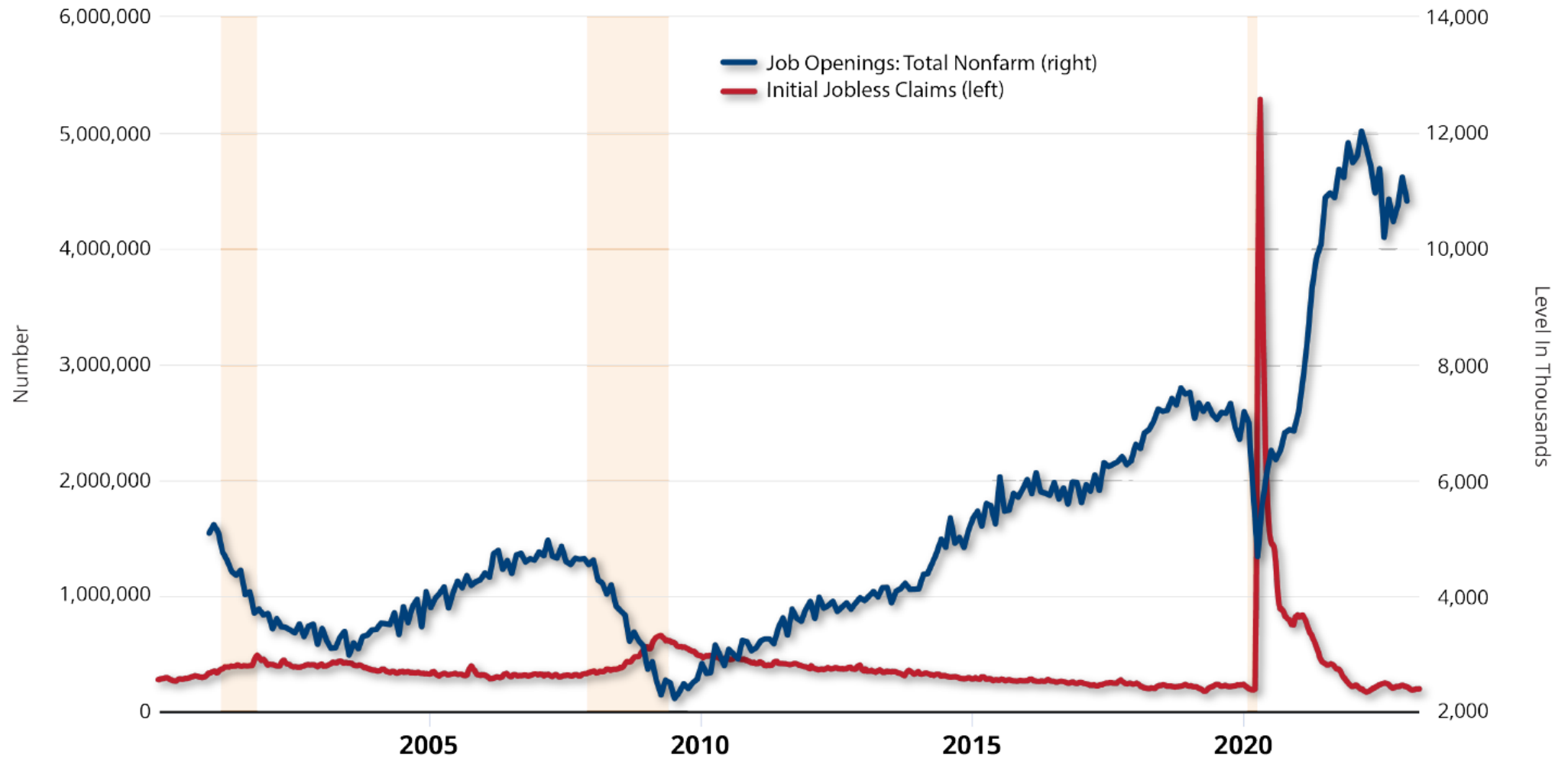
FOMC and market expectations for the federal funds rate



Labor Market Still Robust

Initial Jobless Claims vs Non-farm Job Openings

1/1/2002 to 3/31/2023



S&P 500 Index at Inflection Points

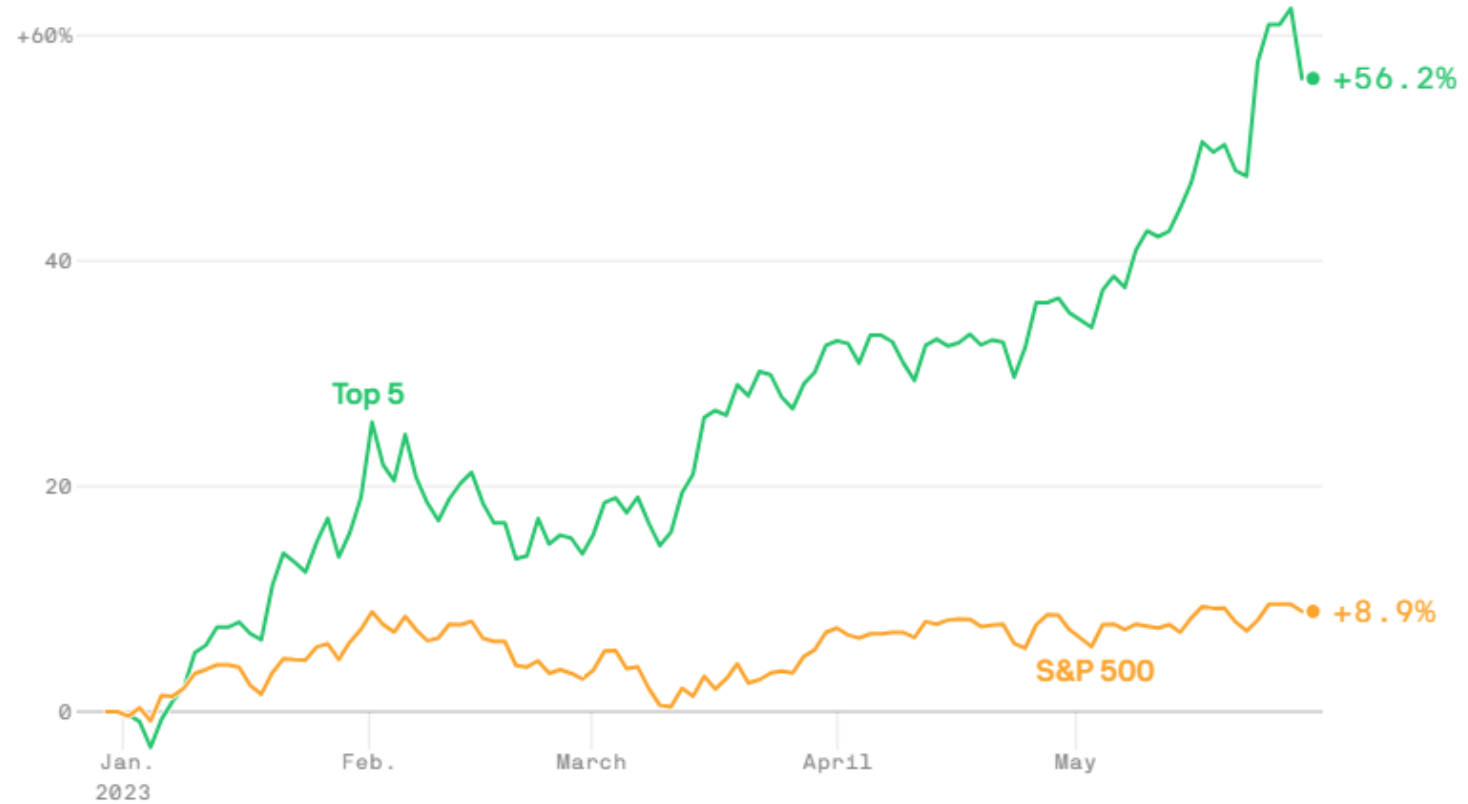
S&P 500 Price Index



S&P 500 Index Analysis

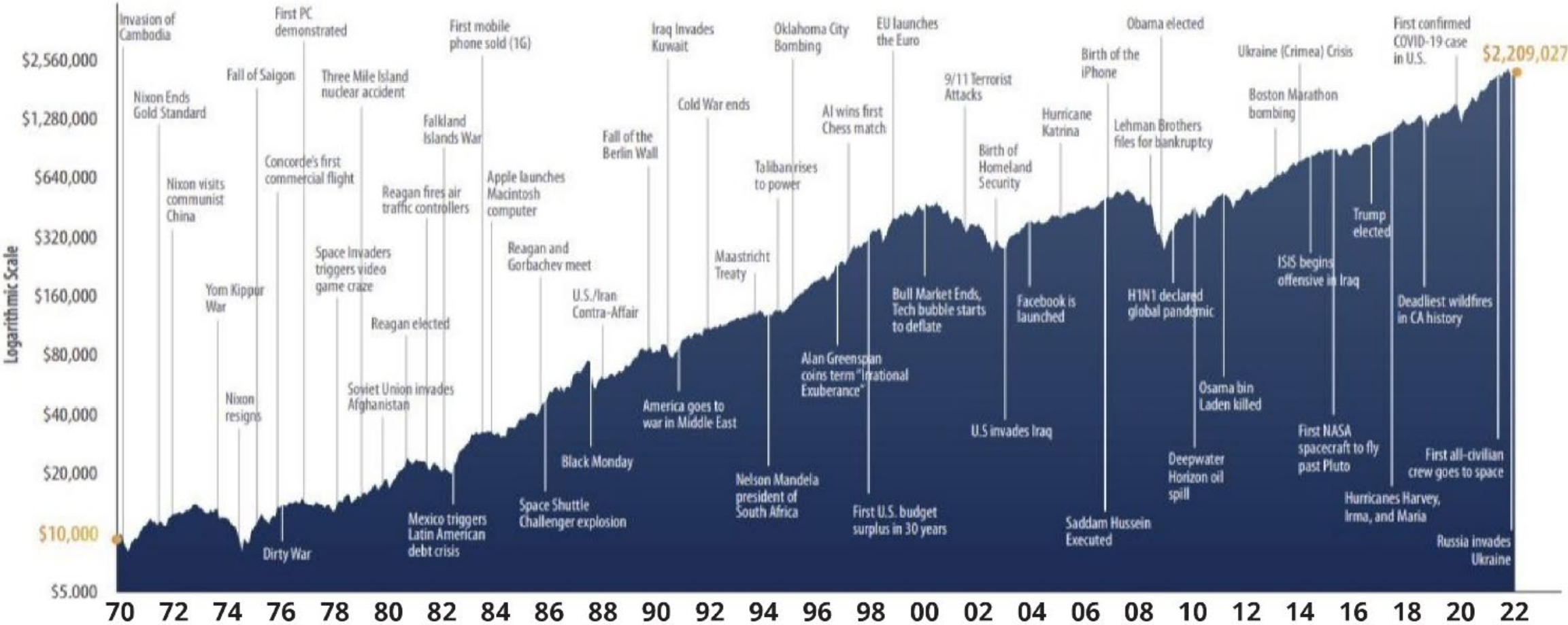
Average return of five largest S&P 500 companies

Year-to-date performance; Daily; Dec. 31, 2022, to May 31, 2023



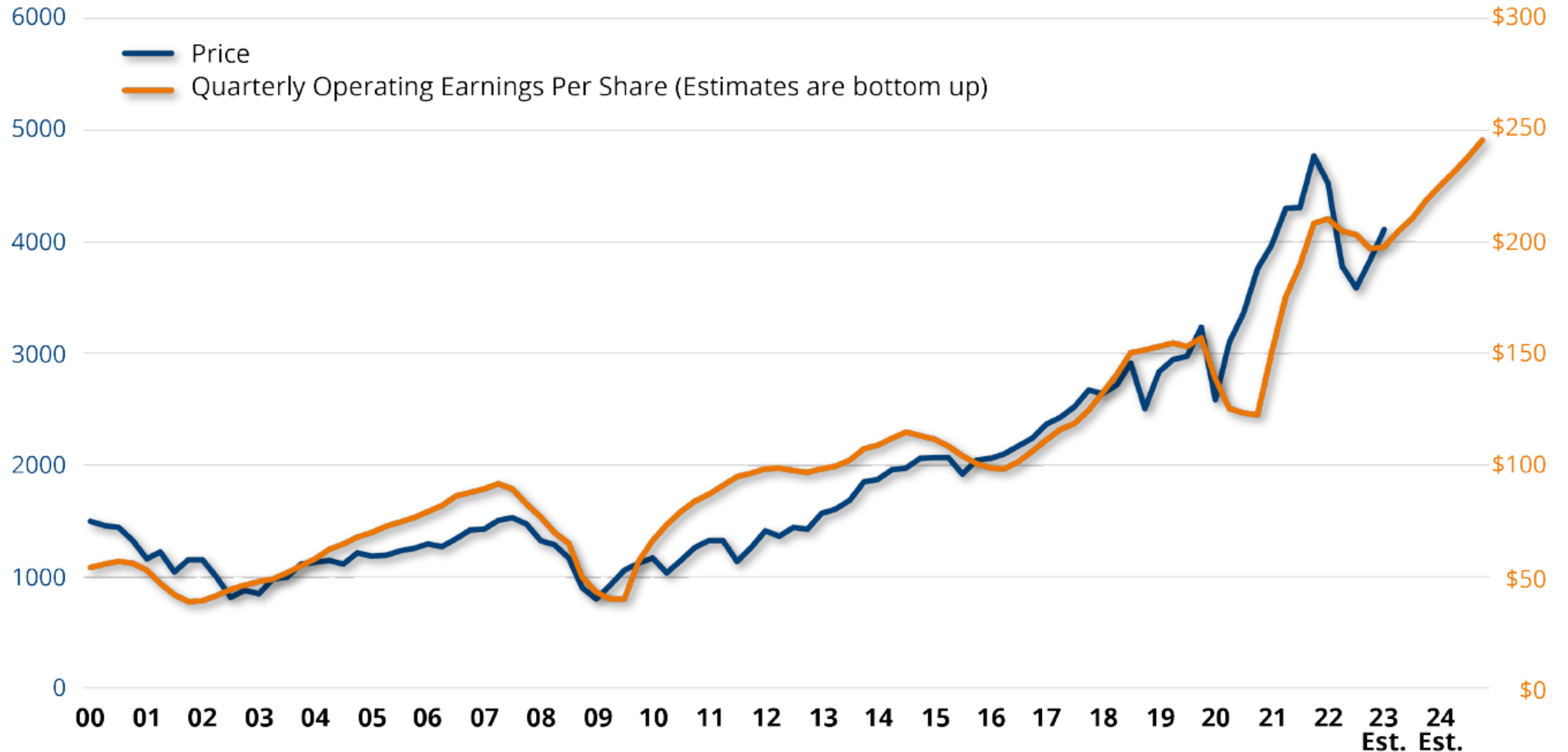
There is Always Something to Worry About

The Average Annual Total Return of the S&P 500 Index for the Period Shown below was 10.88%.



Earnings Drive Stock Prices

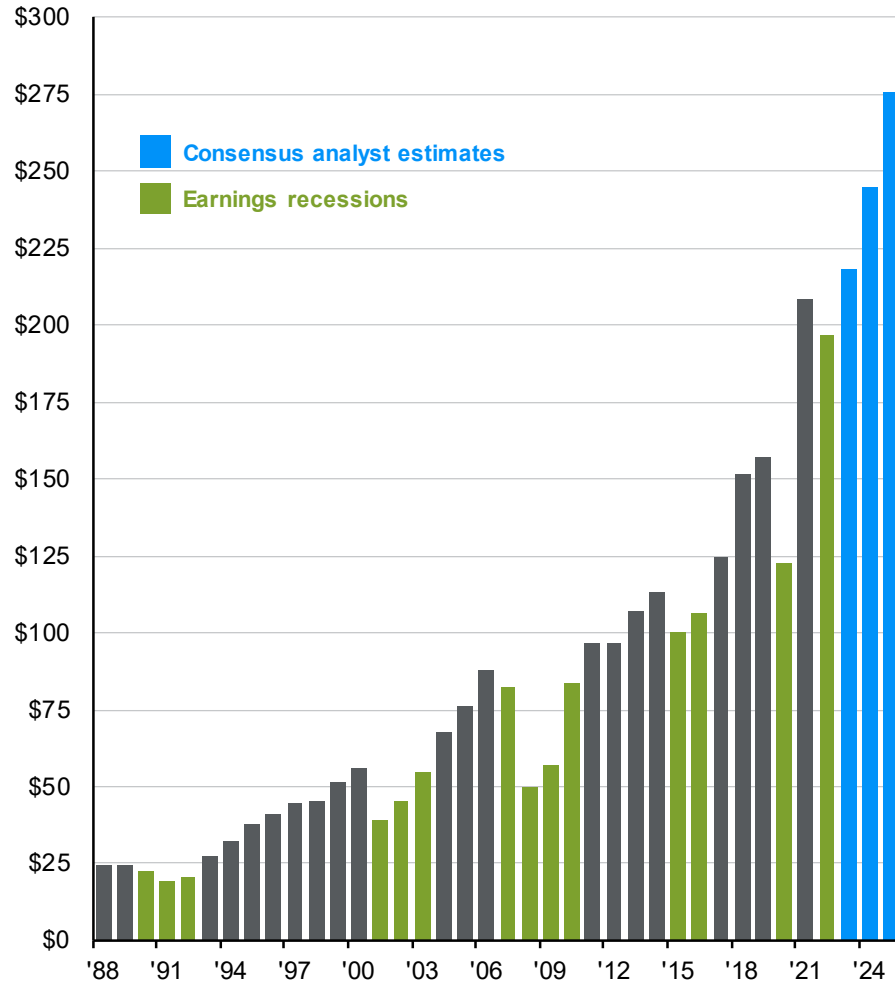
S&P 500 vs. Operating Earnings



Earnings Drive Stock Prices

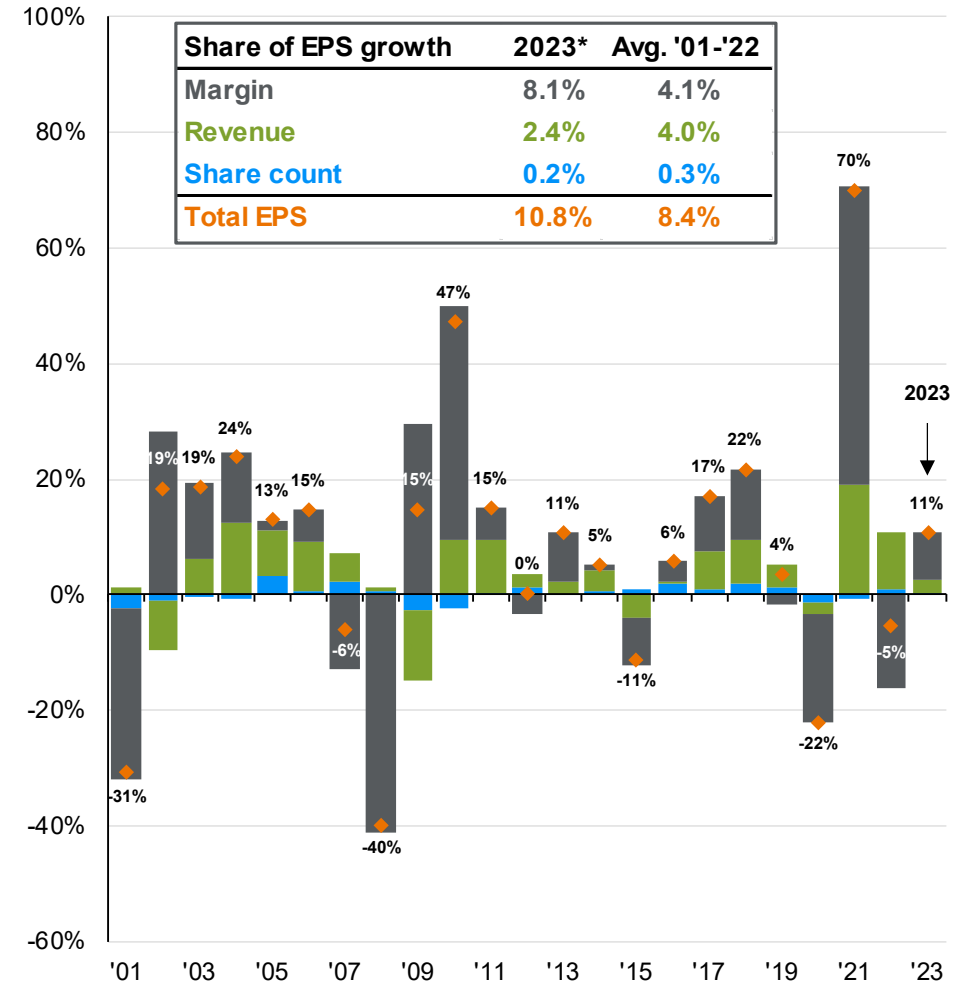
S&P 500 earnings per share

Index annual operating earnings, USD



S&P 500 year-over-year operating EPS growth

Annual growth broken into revenue, changes in profit margin & changes in share count



The Perils of Market Timing

2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	YTD	2008 - 2022	
																Ann.	Vol.
Fixed Income 5.2%	EM Equity 79.0%	REITs 27.9%	REITs 8.3%	REITs 19.7%	Small Cap 38.8%	REITs 28.0%	REITs 2.8%	Small Cap 21.3%	EM Equity 37.8%	Cash 1.8%	Large Cap 31.5%	Small Cap 20.0%	REITs 41.3%	Comdty. 16.1%	Large Cap 16.9%	Large Cap 8.8%	REITs 23.4%
Cash 1.8%	High Yield 59.4%	Small Cap 26.9%	Fixed Income 7.8%	High Yield 19.6%	Large Cap 32.4%	Large Cap 13.7%	Large Cap 1.4%	High Yield 14.3%	DM Equity 25.6%	Fixed Income 0.0%	REITs 28.7%	EM Equity 18.7%	Large Cap 28.7%	Cash 1.5%	DM Equity 12.1%	Small Cap 7.2%	Small Cap 23.2%
Asset Alloc. -25.4%	DM Equity 32.5%	EM Equity 19.2%	High Yield 3.1%	EM Equity 18.6%	DM Equity 23.3%	Fixed Income 6.0%	Fixed Income 0.5%	Large Cap 12.0%	Large Cap 21.8%	REITs -4.0%	Small Cap 25.5%	Large Cap 18.4%	Comdty. 27.1%	High Yield -12.7%	Small Cap 8.1%	REITs 6.6%	EM Equity 23.0%
High Yield -26.9%	REITs 28.0%	Comdty. 16.8%	Large Cap 2.1%	DM Equity 17.9%	Asset Alloc. 14.9%	Asset Alloc. 5.2%	Cash 0.0%	Comdty. 11.8%	Small Cap 14.6%	High Yield -4.1%	DM Equity 22.7%	Asset Alloc. 10.6%	Small Cap 14.8%	Fixed Income -13.0%	Asset Alloc. 7.8%	Asset Alloc. 6.1%	Comdty. 20.2%
Small Cap -33.8%	Small Cap 27.2%	Large Cap 15.1%	Cash 0.1%	Small Cap 16.3%	High Yield 7.3%	Small Cap 4.9%	DM Equity -0.4%	EM Equity 11.6%	Asset Alloc. 14.6%	Large Cap -4.4%	Asset Alloc. 19.5%	DM Equity 8.3%	Asset Alloc. 13.5%	Asset Alloc. -13.9%	High Yield 5.2%	High Yield 5.4%	DM Equity 20.0%
Comdty. -35.6%	Large Cap 26.5%	High Yield 14.8%	Asset Alloc. -0.7%	Large Cap 16.0%	REITs 2.9%	Cash 0.0%	Asset Alloc. -2.0%	REITs 8.6%	High Yield 10.4%	Asset Alloc. -5.8%	EM Equity 18.9%	Fixed Income 7.5%	DM Equity 11.8%	DM Equity -14.0%	EM Equity 5.1%	Fixed Income 2.7%	Large Cap 17.7%
Large Cap -37.0%	Asset Alloc. 25.0%	Asset Alloc. 13.3%	Small Cap -4.2%	Asset Alloc. 12.2%	Cash 0.0%	High Yield 0.0%	High Yield -2.7%	Asset Alloc. 8.3%	REITs 8.7%	Small Cap -11.0%	High Yield 12.6%	High Yield 7.0%	High Yield 1.0%	Large Cap -18.1%	REITs 3.0%	DM Equity 2.3%	High Yield 13.0%
REITs -37.7%	Comdty. 18.9%	DM Equity 8.2%	DM Equity -11.7%	Fixed Income 4.2%	Fixed Income -2.0%	EM Equity -1.8%	Small Cap -4.4%	Fixed Income 2.6%	Fixed Income 3.5%	Comdty. -11.2%	Fixed Income 8.7%	Cash 0.5%	Cash 0.0%	EM Equity -19.7%	Cash 2.3%	EM Equity 1.0%	Asset Alloc. 12.4%
DM Equity -43.1%	Fixed Income 5.9%	Fixed Income 6.5%	Comdty. -13.3%	Cash 0.1%	EM Equity -2.3%	DM Equity -4.5%	EM Equity -14.6%	DM Equity 1.5%	Comdty. 1.7%	DM Equity -13.4%	Comdty. 7.7%	Comdty. -3.1%	Fixed Income -1.5%	Small Cap -20.4%	Fixed Income 2.1%	Cash 0.6%	Fixed Income 4.2%
EM Equity -53.2%	Cash 0.1%	Cash 0.1%	EM Equity -18.2%	Comdty. -1.1%	Comdty. -9.5%	Comdty. -17.0%	Comdty. -24.7%	Cash 0.3%	Cash 0.8%	EM Equity -14.2%	Cash 2.2%	REITs -5.1%	EM Equity -2.2%	REITs -24.9%	Comdty. -7.8%	Comdty. -2.6%	Cash 0.4%

The logo for Fund Direct Advisors features a stylized triangle on the left composed of three stacked sections: a small black triangle at the top, a medium green triangle in the middle, and a large black triangle at the bottom. A horizontal green arrow extends from the right side of the middle green section. To the right of the triangle, the words "FUND DIRECT" are stacked above "ADVISORS" in a large, black, serif font.

FUND DIRECT ADVISORS

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