

Market Commentary
Q3 2023 Recap:

Inflation: The disinflationary trend mostly continued in Q3, although rising oil prices (+\$20/barrel over 3 months) pushed headline inflation higher as the quarter progressed. The y/y change in Headline CPI rose 70bp between June and August to +3.7% currently, while Headline PCE rose 30bp over the same period and stands at +3.5%. Core (ex food and energy) inflation continues to moderate but remains higher, with Core CPI now at +4.3% y/y while Core PCE stands at +3.9%. Of note, consumers' inflation expectations remain well anchored despite rising energy costs, with the U of M survey reporting 1y forward expectations of 3.2% while 5-10y expectations have fallen to 2.8%.

Monetary Policy: The Fed raised overnight interest rates by 25bp at its July meeting, to a range of 5.25% to 5.5%, and then did not change rates at the September meeting. The updated Summary of Economic Projections (SEP) implies one additional 25bp rate hike is still to come before year-end, but futures markets are currently pricing only a 50/50 chance of such an outcome. Sandwiched in between Q3's two FOMC meetings was the Jackson Hole Economic Symposium, where Jerome Powell's keynote speech once again made clear that the FOMC intends to keep its policy rate restrictive for some time to come, as summarized by the "higher for longer" narrative.

Economy: Q3 data was mixed. PMIs from S&P Global and ISM continue to show weakness or outright contraction in manufacturing, as do many regional Fed surveys. Consumer sentiment indicators from the Conference Board and the U. of Michigan have recently moved lower, a reversal of the upward trend from the spring and early summer. Housing markets continue to be plagued by availability and affordability challenges driven by high mortgage rates, hindering activity. Finally, the labor market is slowly normalizing, with wage gains slowing and the number of open jobs falling. Despite these cross-currents, consensus estimates among Wall Street economists for Q3 GDP Growth stand at +3.0% q/q annualized, while the Atlanta Fed's real-time "GDPNow" estimate stands at a whopping +4.9%.

Bond Market: Rates moved significantly higher in the belly and long end of the curve in Q3, as excess refi supply of US Treasuries was met with weaker demand from key domestic and foreign buyers. Mortgage rates followed suit, and now sit well above 7% nationally for traditional 30-year fixed rate loans. Credit spreads were stable to slightly better in the quarter, pushing most of the price declines in Treasuries through to munis and corporates.

Stock Market: Equities rallied to YTD highs in July before succumbing to rates-driven pressure on P/E multiples in August and especially September. Energy stocks posted solid gains driven by rising oil prices, but otherwise the selling was broad-based across market caps, sectors, and geographies.


Albion's "Four Pillars":

***Economy & Earnings** - The US economy has shown resilience so far in 2023, and Wall Street analysts expect full-year corporate earnings to be roughly flat y/y. Albion's base case expectation is that the US economy will enter recession in late 2023 / early 2024, putting downside pressure on earnings.

***Valuation** - The S&P 500's forward P/E of 18x is above the long run average, so valuation could be a headwind to future returns. More predictive metrics like CAPE, Tobin's Q, and the Buffett Indicator (Eq Mkt Cap / GDP) suggest that compound annual returns over the next decade are likely to be in the mid single digits.

***Interest Rates** - Rates rose dramatically in 2022 due to a sharp pivot in monetary policy, and have drifted even higher in 2023 as the Fed remains firmly committed to fighting inflation. Futures markets now imply a roughly 50/50 chance of one additional 25bp rate hike before year-end, followed by a pause.

***Inflation** - After reaching 40yr highs in spring of 2022, inflation has moderated somewhat over the past 18 months. Goods inflation has fallen due to softening demand and excess inventory, while services inflation remains elevated, in part due to shelter costs which are somewhat lagged.

Q3 2023 Market Recap

Market Data

Equity Indices	Close	Index Total Returns (%)				
		MTD	QTD	YTD	1 Year	3y Cum.
S&P 500	4,288	-4.8%	-3.3%	13.1%	19.8%	34.8%
Dow Jones Indus. Avg.	33,508	-3.4%	-2.1%	2.7%	17.1%	29.7%
NASDAQ	13,219	-5.8%	-3.9%	27.1%	24.2%	22.0%
S&P Midcap 400	2,502	-5.3%	-4.2%	4.3%	14.7%	41.6%
Russell 2000 (Small Cap)	1,785	-5.9%	-5.1%	2.5%	8.3%	23.3%
MSCI EAFE (Int'l Dev Mkt Eq)	2,031	-3.4%	-4.0%	7.6%	26.8%	19.2%
MSCI EM (Emerging Mkt Eq)	953	-2.6%	-2.8%	2.2%	12.5%	-2.8%
MSCI World	2,853	-4.3%	-3.5%	11.1%	20.8%	26.7%
S&P Global 1200	3,141	-4.3%	-3.7%	10.9%	21.3%	28.4%

Fixed Income	Yield	Index Total Returns (%)				
		MTD	QTD	YTD	1 Year	3y Cum.
10y U.S. Treasuries	4.57%	-3.5%	-5.1%	-3.4%	-3.0%	-23.8%
U.S. Bonds (Aggregate)	5.39%	-2.5%	-3.2%	-1.2%	0.3%	-14.9%
Global Bonds	4.22%	-2.9%	-3.6%	-2.2%	2.5%	-19.4%
U.S. Munis	4.32%	-2.9%	-3.9%	-1.4%	2.7%	-6.9%
U.S. Investment Grade Corp	6.04%	-2.7%	-3.1%	0.0%	3.6%	-14.3%
U.S. High Yield Corporates	8.88%	-1.2%	0.5%	5.9%	10.5%	5.7%

US Interest Rates	Levels (%)					
	9/29/23	8/31/23	6/30/23	12/30/22	9/29/22	9/29/20
2y Treasuries	5.04	4.86	4.90	4.43	4.19	0.12
10y Treasuries	4.57	4.11	3.84	3.87	3.79	0.65
30y Treasuries	4.70	4.21	3.86	3.96	3.72	1.41
Fed Funds (Effective Rate)	5.33	5.33	5.08	4.33	3.08	0.09
SOFR (USD)	5.31	5.31	5.09	4.30	2.96	0.07
30y Fixed Mortgage	7.35	7.22	6.70	6.41	6.70	2.90

Commodity Prices	Levels					
	9/29/23	8/31/23	6/30/23	12/30/22	9/29/22	9/29/20
Oil (WTI)	90.79	83.63	70.64	80.26	81.23	39.29
Gasoline	3.82	3.82	3.54	3.20	3.80	2.19
Natural Gas	2.93	2.77	2.80	4.48	6.87	2.56
Gold	1,849	1,940	1,919	1,824	1,661	1,898

Currency Crosses	Levels					
	9/29/23	8/31/23	6/30/23	12/30/22	9/29/22	9/29/20
\$ per €	1.22	1.27	1.27	1.21	1.11	1.29
¥ per €	1.06	1.08	1.09	1.07	0.98	1.17
¥ per \$	149.4	145.5	144.3	131.1	144.5	105.7
\$ per Bitcoin	26,903	26,013	30,391	16,579	19,508	10,757

Macroeconomic Data	Value	Date	Next Rel.	Cons Est
Fed Funds Target (Lower)	5.25%	09/29/23	11/01/23	5.25%
Inflation (Core PCE Deflator)	3.9%	08/31/23	10/27/23	-
Inflation (Headline CPI)	3.7%	08/31/23	10/12/23	3.6%
Unemployment (U-3)	3.8%	08/31/23	10/06/23	3.7%
GDP Growth (Q/Q SAAR)	2.1%	06/30/23	10/26/23	3.0%
ISM Manufacturing PMI	47.6	08/31/23	10/02/23	47.9
Consumer Confidence	103.0	09/29/23	10/31/23	-

Data Sources: - Bloomberg, Factset

Albion's Dashboard of Key Leading Economic Indicators as of 09/29/23

- Initial Jobless Claims (211k 4wk m/a) - Stronger: have moved lower after an early summer peak
- Conference Board LEI (-7.6% y/y) - Weaker: has declined significantly since peaking in Dec 2021
- Residential Building Permits (1,541k) - Stronger: gradual improvement after early 2023 trough
- Corporate Bond Spreads (1.12%) - Steady: stabilized near long run averages after summer rally
- Treasury Yield Curves (77.8% inv) - Steady: curve has remained almost fully inverted throughout 2023
- Consumer Confidence (103.0) - Mixed: dropped in August & September after an early summer rebound
- Real Final Sales (+2.7% y/y) - Stronger: has rebounded after a weak first half of 2022

Legend: ● = All Clear; ● = Caution; ● = Strong Warning

Q3 2023 S&P 500 Total Return by Sector
