Ridgetop Wealth Management
2023 Market Outlook

Through a Rearview Mirror
From an investment perspective, 2022 was just plain ugly. The S&P posted its biggest decline since 2008. It was one of the top five worst annual performances for a 60/40 portfolio since 1926, and for the first time ever on record both stocks and bonds fell by more than 10%. We saw the highest inflation and most aggressive tightening cycle in 40 years, while simultaneously long-term Treasurys declined 29.3%. Unlike horrible years prior (1929, 1987, 2000, and 2008 for instance), there was no one defining moment which caused an immediate stock market crash in 2022.[1] Instead what we experienced was a disheartening series of selloffs followed by failed rallies. Lovely.

Now…Lets Please Move On
2023 could very well present one of the best buying opportunities we have seen in a decade. The economic, earnings, and Fed cycle we lived through last year are now further along in their descent. Several cycles including the stock market are in the later innings and should transition to being much friendlier in 2023.

At some point in 2023 as the economic data is nearing its worst, the stock market is likely to rebound, and likely to rebound sharply. When the economic data is at its worst, the stock market will be anticipating the economic recovery. The market tends to lead the economy out of a recession. Markets like 2022 and 2023 require great patience and discipline. It's an emotional roller coaster and bear market rallies can be very enticing. That is why it is crucial to remain objective.

The Objective Indicators
While gut feelings and emotions are valuable tools in much of life, they are not when it comes to investing. When it comes to investing it pays to rely on objective market and economic indicators. Here is what the indicators are currently telling us:

- The Leading Economic Index (LEI) – fell again in November, twice the decline expected by economists. Monthly declines of this magnitude last occurred during the panic of Covid in 2020 and during the 2008 Financial crisis. The LEI has now fallen for nine consecutive months.[2] This leads us to believe that a recession is to be expected in the first half of 2023 (if we are not already in one.)
- The Yield Curve – like the troubled LEI, we have been talking about yield curve inversion for sometime now. The spread between the 10-year and 2-year Treasury have become the most inverted since the early 1980s.[3] While lead times very, inverted yield curves have reliably preceded economic recessions.
- Coppock Guide – (stay with me here) is a long term stock market momentum gauge developed in the 1960s. This technical indicator is calculated by adding the market's 14-month rate of change to its 11-month change and then determining the sum's 10-month weighted moving average. The indicator's current message says that long term momentum has not been this bad since 2009. The Coppock, along with the fact that S&P 500's 50-day moving average is below its

[1] Ned Davis Research
[2] The Conference Board
[3] Ned Davis Research

200-day smoothing (often called a “death cross”) points to continued risk in the market.[4] Caution should be warranted until these indicators turn.

Sector Leadership

Sector leadership is another notable fly in the ointment. The fourth quarter of 2022 brought us a several weeklong stock market rally. While this is good on the surface, it is troubling what sectors led the charge. During the rally the SHUT index (staples, health care, utilities, and telecom**)** outperformed the broader markets.[5] If we were soon moving into a new bull market the SHUT would historically underperform, whereas higher beta growth companies in the technology and consumer discretionary sectors would outperform.

Depressed Yet?

Well, all in all that is not a bad thing when it comes to the market. Market consensus is currently pretty pessimistic as well. Though we have not had the opportunity to use the phrase in years, “bull markets climb a wall of worry.” The more pessimistic investors get, the closer and closer we are likely getting to a rally.

Bottom Line

In the absence of confirmation from economic and market based indicators we are cautious. Several indicators are sending a strong warning of a recession. A recession would likely mean a break of the lows in the first half of 2023 followed by a sharp rebound. If we avoid a recession the first half of 2023 could be strong with less volatility. Unfortunately our indictors are pointing towards the first scenario at this time. All said, while not over, we are in the later innings of this frustrating market and need to remain nimble and ready to act/buy when the time comes. We are getting closer.

Happy New Year everyone. We will continue to keep you updated. Please call or let us know if you need anything or would like to discuss further.

Sincerely,

Brian Pollak, CRPC
Private Wealth Advisor

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[4] Ned Davis Research
[5] Ned Davis Research

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