WEEK AHEAD Nov 21-25, 2022

MARKET COMMENTARY by Sowell Management

SOWELL MANAGEMENT

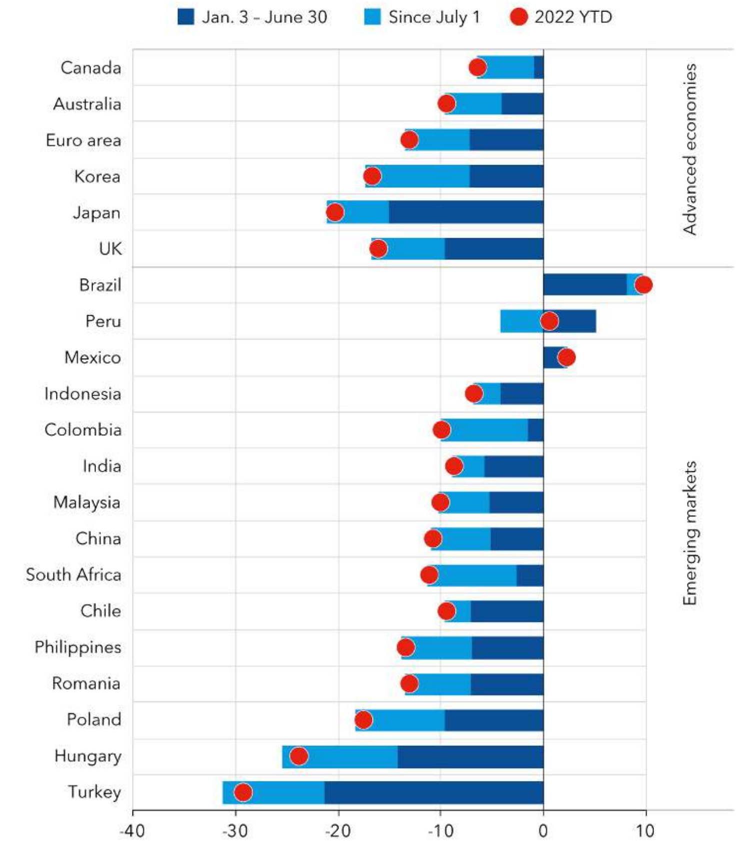
[TACTICAL] Last week's core leading economic and manufacturing reports posted weaker-than-expected results, heightening fundamental concerns of a recession. A mixed blessing likely to strengthen market expectations, the Fed will temper its rhetoric and interest rate policy. Sowell's tactical signal remains in neutral territory as a series of big tech layoffs were announced; still too soon to be a trend.

Equity markets remained relatively flat this past week, with NASDAQ shedding the most gains after rallying in the previous week. U.S. home sales in October fell for the ninth month in a row as this year's sharp rise in mortgage rates continued to weigh on the real estate market.

Dollar surge

For many countries, the weakening of their currencies relative to the US dollar has made the inflation fight harder.

(exchange rates vis-à-vis US dollar, percent change)



Source: Haver Analytics and IMF staff calculations.
Note: As of October 4, 2022.

IMF

The Fed Dilemma

The Federal Reserve's tightening policy to fight inflation in the U.S. has had consequences that stretch past American borders. In fact, the sharp rise in interest rates has led to a substantial capital influx into dollars at the expense of other currencies, sending the USD index to the highest level in over two decades. This has happened before. As the world's reserve currency, marked changes in the USD convenience yield impact every economy and tend to have dire effects on emerging markets in particular.

While now largely forgotten, a surging U.S. dollar in 1985 forced the then-G-5 industrialized nations to intervene in the currency market and weaken the dollar substantially. Similarly, in 1997 with the Asian Currency Crisis, and in 1998 with the Russian Debt Default (and associated collapse of the hedge fund Long-Term Capital Management), a surging dollar caused a great deal of upset in the global economy that forced the Fed either to delay raising rates or cut them in '98 in the wake of systemic financial risks.

What we are seeing today is that the Chinese Yuan Renminbi and the Taiwanese Dollar have slipped to 2019 lows. The Euro is hovering around parity after 20 years, and the Japanese Yen trades at a 24-year low against the greenback, which prompted the Bank of Japan to intervene to support its currency for the first time since 1998.

But why is a strong dollar a problem?

· First, a strong dollar feeds into inflation pressures abroad. Because the prices of commodities such as oil, metals, and corn are quoted in USD, a stronger dollar means that essential raw materials get more expensive, consequently driving other products' prices up. Furthermore, because the U.S. is the second-largest exporter globally, all imports from the United States become more expensive.

· Second, a strong dollar negatively affects those who have borrowed in USD but whose receipts are in other currencies. This is especially problematic for emerging economies that rely heavily on external borrowing and whose debt, on average, is more than 80% denominated in foreign currency.

· Third, a strong dollar can affect foreign Central Banks' policies for the worst. As seen recently with the ECB in the wake of a depreciating euro, foreign Central Banks often react to a strong dollar by increasing rates, even when the underlying economy is not ready to absorb abrupt hikes in borrowing costs. These decisions can lead to a rapid decrease in economic output and potentially drive a recession.

· Last, a stronger local currency creates headwinds to U.S. exporters, as higher prices lower demand. At the same time, it cuts into the repatriated profits of U.S. multinational corporations, putting corporate earnings at even greater risk in an already weakening U.S. and global economy.

So, even though Americans may temporarily enjoy cheaper vacations abroad, a sustained dollar appreciation will also negatively affect the American economy. The Fed is facing a dilemma. As it fights inflation at home by raising interest rates and tightening credit conditions at the fastest pace in decades, it is also exporting inflation to other nations and making U.S. goods more expensive in overseas export markets. This is one of the consequences of being globalized.

Therefore, in future FOMC meetings, we expect a more cautious Federal Reserve, as Jerome Powell will have to find a tradeoff between continuing the fight against inflation and safeguarding foreign exchange markets and the global economy.

The crypto world is seeing growing fear of contagion after FTX collapse last week, with crypto exchange Gemini and crypto-lender Genesis showing signs of distress. Reports about FTX's faulty management and unethical practices suggest that the company may have been one of the largest Ponzi schemes in history. In the words of the new CEO, John Ray III, who oversaw Enron's bankruptcy in the past: "Never in my career have I seen such a complete failure of corporate controls."

On Saturday, countries at the United Nations COP27 summit stroke a deal to set up a fund that would pay for climate-related damage in countries deemed particularly vulnerable. The agreement represents a major win for poorer countries that have pushed for the move for years and opens up further progress on addressing global warming.

The Week Ahead

In the week of Thanksgiving and Black Friday, we can expect fresh data on U.S. home sales, the latest Manufacturing Purchasing Managers' Index (PMI), and the University of Michigan's Consumer Sentiment Index (MCSI). These reports will give an updated look at the state of the American economy.

On Wednesday, the Federal Reserve will release meeting minutes from the latest FOMC's monetary policy meeting.
Giants like Dell Technologies, HP, and Best Buy are scheduled to release their quarterly results on Monday and Tuesday.

"The period of 1979 to 2019 was epic in U.S./China relations. I call it the epic of Unconscious integration... We (U.S.) were the real one country, two systems, not Hong Kong and China. Unfortunately, that period is over, and now we are in the transition to see what comes next. Can we as two peer rivals foster a relationship that at least preserves a lot of the benefits of that last 40 years but deals with the fact that we are peer rivals, we are going to compete, and we don't share values."

– Thomas Friedman, New York Times Foreign Affairs Columnist,

MON NOVEMBER 21, 2022
Chicago Fed National Activity
Germany PPI
Hong Kong CPI
Agilent, Dell, Toro, Urban Outfitters, and Zoom earnings
TUE NOVEMBER 22, 2022
Redbook
Euro Zone Consumer Confidence
FOMC Members George and Bullard Speaks
Autodesk, Baidu, Best Buy, Dick's Sporting Goods, HP, Jack In the Box, Medtronic, Nordstrom, Signify, and Vmware earnings
WED NOVEMBER 23, 2022
New Home Sales
Manufacturing PMI
Durable Goods Orders
Deere, and National Steel earnings
THU NOVEMBER 24, 2022
Initial jobless claims (weekly)
Continuing jobless claims
Thanksgiving Day - markets closed
FRI NOVEMBER 25, 2022
Markets closed at 1pm ET

SELECT INDICES

	YTD Daily	1 Wk Daily	MTD (Daily)	3 Mo Daily	1 Yr Daily	2 Yr Daily	3 Yr Daily
S&P 500 Index	(15.60)	(0.61)	2.56	(7.02)	(14.36)	7.04	10.09
S&P 500 Growth Index	(25.85)	(1.26)	1.97	(12.93)	(25.66)	1.76	10.82
S&P 500 Value Index	(4.10)	(0.04)	3.08	(1.16)	(1.24)	12.13	7.82
NASDAQ Composite	(28.23)	(1.51)	1.55	(13.83)	(29.75)	(2.11)	10.12
Bloomberg US Agg Bond	(13.69)	0.48	2.40	(5.02)	(13.48)	(7.57)	(2.89)
Bloomberg Long Term US Treasury	(30.03)	1.42	4.10	(11.79)	(28.94)	(18.46)	(8.12)
Basic Materials	(9.52)	(1.60)	7.85	0.04	(6.85)	11.81	13.16
Communication Services	(38.32)	(0.32)	2.61	(16.76)	(40.79)	(13.26)	(3.37)
Consumer Cyclical	(30.25)	(2.70)	(1.06)	(16.06)	(32.77)	(2.83)	10.06
Consumer Defensive	(2.18)	1.32	2.66	(2.45)	3.44	8.83	10.66
Energy	69.73	(1.84)	1.85	15.61	67.04	69.04	23.08
Financial Services	(9.66)	(1.56)	3.49	(1.33)	(10.30)	11.82	7.55
Healthcare	(6.43)	0.72	1.30	0.62	(2.57)	9.16	12.16
Industrials	(6.76)	(0.19)	4.85	(1.39)	(7.02)	8.08	8.18
Real Estate	(24.02)	(1.77)	2.98	(13.83)	(19.46)	3.44	0.35
Technology	(27.54)	(1.43)	2.88	(13.24)	(27.29)	3.23	14.86
Utilities	(1.30)	1.13	3.03	(10.29)	6.20	7.06	5.97

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