

September 25, 2023

The 2023 Rally Falters

The 2023 stock-market rally is officially in trouble; at the very least, it has stalled. The S&P 500 closed on Friday 9/15/23 in the 4,450 range, which is about where it was trading at the beginning of July. Throwaway summers are nothing new for the stock market; the June-September period is historically the market's worst four-month stretch. However, this past summer was supposed to be different, with stocks expected to extend their rally on slowing inflation and the end of the Fed's rate-hiking cycle.

Some extraneous factors have gotten in the way of the market's progress. Inflation is stubbornly persistent, particularly for the last two or so points on the way to the Fed's 2% target range. Energy prices are resurgent, adding to inflationary pressure and representing one more challenge (commuting costs) in getting employees back to the office. Government shutdown looms yet again as the two parties wrangle over limits on government spending.

Energy Prices Rise

Oil prices have once again confounded the experts and risen sharply in the second half of 2023, at a time when many investors expected prices to cool due to the suppressive effects of global rate hikes. As of 9/18/23, West Texas Intermediate (WTI), the U.S. benchmark, was trading above \$91.50; and Brent crude, the global standard, was at \$94.75. Prices are at their highest levels since 2022 and are up over 25% just from June (the Brent average for June 2023 was \$75). The Energy Information Agency (EIA) within the U.S. Department of Energy forecast that energy prices could continue to rise into 2024.

Industry watchers point to two key drivers of the oil price surge; a third may also be lurking. OPEC cut production targets earlier in 2023. Frequently, OPEC cuts lack

teeth, with member nations routinely exceeding their target ranges. But the two largest non-U.S. oil producers, Saudi Arabia and Russia, are not only matching their targets, they have extended them at least until year-end 2023.

The second and related factor is worsening oil supply. The EIA in mid-September warned that oil markets were in a short-supply situation and that the deficit was likely to worsen in the fourth quarter. In the U.S., inventories at the Cushing Oil Hub in Cushing, Oklahoma, continued to deplete more rapidly than at other locations. Situated at the pipeline crossroads of the U.S., Cushing has historically represented a major storage and logistics hub for domestic oil production and refining.

Cushing's market importance has diminished in recent decades as the U.S. has shifted to an oil exporter with major assets on the West Coast, and the site now holds less than 10% of U.S. oil inventories. Still, Cushing continues to loom large in oil market psychology. Since June 2023, crude stocks at Cushing are down more than 40% and are currently well below the seasonal average. Elsewhere in the U.S., crude inventories have declined though less sharply.

The rise in demand amid lower inventories might be worse if not for the sluggish economy in China, still seeking to recover after prolonged COVID lock-downs. That nation is now seeking to restart its economy with fiscal and other stimulus. Early in September, China cut the reserve ratio for banks, the second time it has done so in 2023, in a move to improve liquidity in the financial system. China has also reduced foreign currency reserves in a bid to lift the yuan and boosted defense spending as part of a broader plan to stimulate domestic activity.

(continued on next page)

ECONOMIC & MARKET COMMENTARY (CONT.)

The Consumer Continues to Spend

The U.S. consumer is not happy about oil prices and gasoline prices in particular. Many employers treated the recent Labor Day holiday as the unofficial “back to office” line of demarcation. Commuting is increasing, in other words, at the worst possible time for gasoline prices. Even if they are grumbling, consumers are still filling their tanks and spending overall.

In mid-September, the U.S. Census Bureau reported that U.S. retail and food service sales were up 0.6% for August 2023 on a month-over-month basis, and up 2.5% year-over-year. That follows a (downwardly revised) 0.5% monthly gain for July. Total sales excluding gasoline was up 0.2% in August, consistent with the rising price of gasoline at the pump absorbing a higher share of the consumer dollar.

On a month-over-month basis, consumer spending grew at electronics & appliance stores (up 0.7%), food & beverage stores (up 0.4%), and clothing & accessories stores (up 0.9%). On a year-over-year basis, growth was strong at restaurants (up 8.5%) and for online or non-store sales (up 7.2%).

Inflation data remains stubborn and, because of energy costs, has lately ticked higher. The all-items CPI for August was up 0.6% month-over-month, in line with consensus though up sharply from 0.2% for July. The year-over-year change of 3.7% was a tick higher than consensus and up from 3.2% in July.

Consumers cannot “back out” energy prices, particularly when they are filling their gas tanks. Nonetheless, core CPI (excluding food and fuel) was up 0.3% month-over-month and 4.3% year-over-year. The annual number was in line with consensus but represented a nice improvement from 4.7% for July.

The PPI, which captures prices further up the pipeline, had been coming down faster than the CPI; with energy prices rising, it now risks rising faster than CPI. For August, all-items PPI jumped to 0.7% month-over-month and 1.6% year-over-year, from 0.4% and 0.8%, respectively, from July. Ex food and energy, the annual PPI change of 2.2% for August was better than 2.4% price growth in July.

If energy prices remain elevated, that could put more pressure on consumer spending, particularly for durable goods. The housing market, which is trying to climb out of a hole dug by high mortgage rates and high home prices, would also be further strained by higher gasoline and heating oil prices.

The Federal Reserve Bank of Atlanta’s GDPNow “statcaster” is forecasting third-quarter 2023 GDP growth of 4.9%. If realized, that would represent the strongest GDP growth for any quarter in 2023. Argus President John Eade recently increased the Argus GDP forecast for 2023 to 2.3%, from 2.2% at mid-year and from less than 2% at the beginning of 2023. The consumer remains an import-

ant driver of this growth, despite all the challenges in the economy.

Positive Earnings Growth on the Way

A key driver on the stock market’s generally solid performance from 2016 through 2021 was the sharp rise in S&P 500 earnings from continuing operations. Beginning in 2022, that earnings growth began to slow on a quarterly basis. And in 4Q22, S&P 500 earnings from continuing operations turned negative on a year-over-year basis.

Earnings remained negative on a year-over-year basis in 1Q23 and in 2Q23. Compared with 4Q22, however, the 2023 first and second quarters had “better” metrics. The number of companies exceeding EPS expectations for 1Q23 and 2Q23 was higher than the five-year average of 75%. And the magnitude of the earnings beat against pre-reporting estimates, at about 6%-7%, was higher than the five-year average.

Based on pre-reporting expectations for S&P 500 earnings, the third quarter of 2023 is on track for year-over-year earnings growth for the first time since 3Q22. The forecast heading into this earnings season is for not much growth; on a year-over-year basis, growth is expected to be in the low-single-digit percentage range. In any quarter, three-quarter of companies beat EPS expectations; and the average beat against expectations is 6%. Thus, if the pre-reporting expectation is for 0%-1% EPS growth, actual EPS growth should be in the 4%-5% range, statistically speaking.

Conclusion

As noted, summer is not a great time for stocks regardless of the economic and geopolitical environment. Since 1980, the S&P 500 has averaged 10% annual capital appreciation for all years. That works out to roughly 0.8%-0.9% appreciation per month; but gains are not dispersed so neatly. Since 1980, total capital appreciation in the June-September period has averaged a tepid 1.1% in total. Summers have been a bit better since 2010, averaging a 2.7% gain for the four-month span.

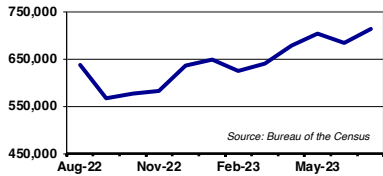
If expectations are met, the S&P 500 in October and November 2023 will record its first positive earnings season since 3Q22 exactly one year earlier. In terms of stock performance, those are already better-than-average months for the S&P 500, with average monthly gains since 1980 of 1.2% for October and 1.9% for November.

Will a good or at least positive EPS season be enough to restore bullish momentum in the market? Maybe. But a lot depends on oil prices, the trend in inflation, and whether Washington can avoid a government shutdown.

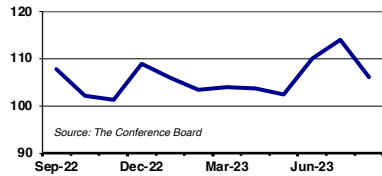
Jim Kelleher, CFA,
Director of Research

ECONOMIC TRADING CALENDAR

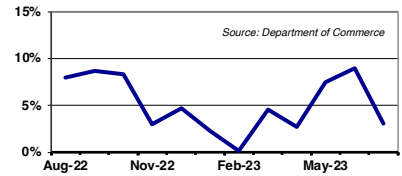
Release: **New Home Sales**
 Date: 9/26/2023
 Month: August
 Previous Report: 714000
 Argus Estimate: 705000
 Street Estimate: 700000



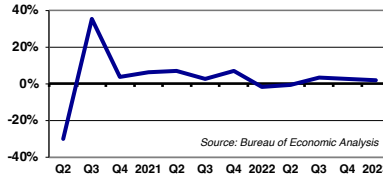
Release: **Consumer Confidence**
 Date: 9/26/2023
 Month: September
 Previous Report: 106.1
 Argus Estimate: 105.0
 Street Estimate: 106.0



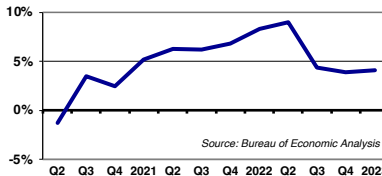
Release: **Durable Goods Orders**
 Date: 9/27/2023
 Month: August
 Previous Report: 3.1%
 Argus Estimate: 2.3%
 Street Estimate: NA



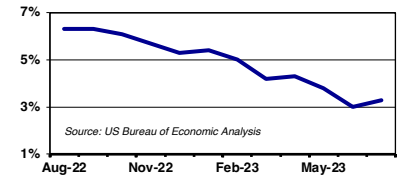
Release: **GDP Annualized QoQ**
 Date: 9/28/2023
 Month: 2Q
 Previous Report: 2.1%
 Argus Estimate: 2.1%
 Street Estimate: 2.2%



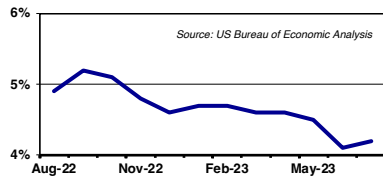
Release: **GDP Price Index**
 Date: 9/28/2023
 Month: 2Q
 Previous Report: 2.0%
 Argus Estimate: 2.0%
 Street Estimate: 2.0%



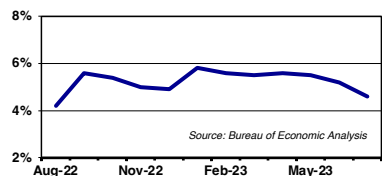
Release: **PCE Deflator**
 Date: 9/29/2023
 Month: August
 Previous Report: 3.3%
 Argus Estimate: 3.4%
 Street Estimate: NA



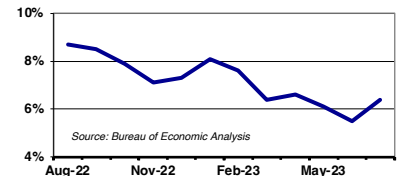
Release: **PCE Core Deflator**
 Date: 9/29/2023
 Month: August
 Previous Report: 4.2%
 Argus Estimate: 4.0%
 Street Estimate: 3.9%



Release: **Personal Income**
 Date: 9/29/2023
 Month: August
 Previous Report: 4.6%
 Argus Estimate: 4.4%
 Street Estimate: NA



Release: **Personal Spending**
 Date: 9/29/2023
 Month: August
 Previous Report: 6.4%
 Argus Estimate: 6.1%
 Street Estimate: NA



Previous Week's Releases and Next Week's Releases on next page.

ECONOMIC TRADING CALENDAR (CONT.)

Previous Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
19-Sep	Housing Starts	August	1,452 K	1,410 K	1,440 K	NA
21-Sep	Existing Home Sales	August	4.07 Mln.	4.10 Mln.	4.05 Mln.	NA
	Leading Index	August	-0.4%	-0.5%	-0.5%	NA

Next Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
2-Oct	ISM Manufacturing	September	47.6	NA	NA	NA
	ISM New Orders	September	46.8	NA	NA	NA
	Construction Spending	August	5.5%	NA	NA	NA
4-Oct	ISM Services Index	September	54.50	NA	NA	NA
	Factory Orders	August	-0.7	NA	NA	NA
5-Oct	Trade Balance	August	-\$65.0 Bil.	NA	NA	NA
6-Oct	Nonfarm Payrolls	September	187 K	NA	NA	NA
	Unemployment Rate	September	3.8%	NA	NA	NA
	Average Weekly Hours	September	34.4	NA	NA	NA
	Average Hourly Earnings	September	4.3%	NA	NA	NA
	Total Vehicle Sales	September	15.04 Mil.	NA	NA	NA

Argus Research Co. (ARC) is an independent investment research provider whose parent company, Argus Investors' Counsel, Inc. (AIC), is registered with the U.S. Securities and Exchange Commission. Argus Investors' Counsel is a subsidiary of The Argus Research Group, Inc. Neither The Argus Research Group nor any affiliate is a member of the FINRA or the SIPC. Argus Research is not a registered broker dealer and does not have investment banking operations. The Argus trademark, service mark and logo are the intellectual property of The Argus Research Group, Inc. The information contained in this research report is produced and copyrighted by Argus Research Co., and any unauthorized use, duplication, redistribution or disclosure is prohibited by law and can result in prosecution. The content of this report may be derived from Argus research reports, notes, or analyses. The opinions and information contained herein have been obtained or derived from sources believed to be reliable, but Argus makes no representation as to their timeliness, accuracy or completeness or for their fitness for any particular purpose. In addition, this content is not prepared subject to Canadian disclosure requirements. This report is not an offer to sell or a solicitation of an offer to buy any security. The information and material presented in this report are for general information only and do not specifically address individual investment objectives, financial situations or the particular needs of any specific person who may receive this report. Investing in any security or investment strategies discussed may not be suitable for you and it is recommended that you consult an independent investment advisor. Nothing in this report constitutes individual investment, legal or tax advice. Argus may issue or may have issued other reports that are inconsistent with or may reach different conclusions than those represented in this report, and all opinions are reflective of judgments made on the original date of publication. Argus is under no obligation to ensure that other reports are brought to the attention of any recipient of this report. Argus shall accept no liability for any loss arising from the use of this report, nor shall Argus treat all recipients of this report as customers simply by virtue of their receipt of this material. Investments involve risk and an investor may incur either profits or losses. Past performance should not be taken as an indication or guarantee of future performance. Argus has provided independent research since 1934. Argus officers, employees, agents and/or affiliates may have positions in stocks discussed in this report. No Argus officers, employees, agents and/or affiliates may serve as officers or directors of covered companies, or may own more than one percent of a covered company's stock. Argus Investors' Counsel (AIC), a portfolio management business based in Stamford, Connecticut, is a customer of Argus Research Co. (ARC), based in New York. Argus Investors' Counsel pays Argus Research Co. for research used in the management of the AIC core equity strategy and model portfolio and UIT products, and has the same access to Argus Research Co. reports as other customers. However, clients and prospective clients should note that Argus Investors' Counsel and Argus Research Co., as units of The Argus Research Group, have certain employees in common, including those with both research and portfolio management responsibilities, and that Argus Research Co. employees participate in the management and marketing of the AIC core equity strategy and UIT and model portfolio products.

