Wellington Shields

CAUTION STILL ADVISED

Stocks continued to fall in the third quarter with September, true to form, once again proving to be the most difficult month of the year. For the quarter, the S&P 500 fell 5.3%, the Dow Jones Industrial Average lost 6.7%, and the NASDAQ dropped 4.1%. The NASDAQ 100 (QQQ), populated with mega-cap growth companies, broke below the key technical level market watchers were eyeing, the June 2022 lows, and may be signaling another leg downward.

The two primary issues facing investors remain the central bank's efforts to arrest inflation and a deterioration of the corporate earnings outlook. These come as the FOMC remains committed to taking the benchmark interest rate to at least 4.25%, and perhaps higher. With the Conference Board's leading Economic Index now in contraction for six consecutive months, shipping rates and orders in free fall, commodity prices well off the high and many now at pre-COVID levels, investors are becoming increasingly concerned about both faltering growth and the Fed hiking too aggressively into a recessionary economy. The most recent Chicago PMI, a bellwether for economic activity, came in at 45.7, firmly in contraction and far below economists' estimates.

On the positive news front, the Atlanta Fed, in a surprise move, upgraded the outlook for the third quarter for the U.S. economy, sharply revising real GDP growth estimates from 0.5% to 2.4%. The main driver for the revision was the strong uptick in personal consumption expenditures. Clearly, the consumer has exhibited some firepower, but it remains to be seen whether this is temporary. With weakening leading economic indicators and a deeply inverted Treasury yield curve, we should remain skeptical.

The Federal Reserve has made it quite clear that fighting inflation is its number one priority and, we think a Fed "pivot" towards easier money is premature. The jobs market remains strong, with initial claims for unemployment at record lows, and hiring consistently above 300,000 per month. As long as jobs remain widely available, it is unlikely the Fed will ease its policy stance on interest rates.

With the twin headwinds of further tightening and earnings estimates falling, it is too early to declare the end of the bear market. We believe, however, we are getting closer to that end rather than the beginning. While high-quality growth companies should remain long-term holdings, our position continues to be that a higher-than-average cash level and allocations to short-term investments is a sound tactical strategy in the current environment.

October 2022

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