Hamilton-Bates
Market Update

November 23, 2022

The Market has Rallied as Expected in Last Update

Is it Too Much Too Soon?

P.O. BOX 98 Mertztown, PA 19539 877.768.4247 www.hbir.com

Stocks have rallied over the past few weeks, ignoring some bad news, and once again is challenging key levels on the major averages. The DJIA and S&P 500 are more than 10% above their mid-October lows. The market is showing strength as corporate buy-backs couple with seasonal trends to buoy prices. Bond yields have also backed off their highs, also relieving some pressure on stocks.

The Fed, the Economy, and Interest Rates
The Fed is expected to hike rates again at its December meeting, after hiking 75bp in November. This time the hike is expected to be 'just' 50bp and taking the Federal Funds rate to 4.25%. More importantly, the Fed could possibly signal a move to smaller hikes in the future, and even a 'pause' to wait and see how the hikes in 2022 affect the economy. Interest rate hikes take time to have an economic effect, with a lag time of up to a year. So far the economy remains strong, and jobs robust—but some fear a slowing in 2023 as these hikes start to hit.

What has Really Happened This Year
Inflation, rates hikes, and now fears of recession have all been said to be causes for the financial market's volatility this year, both for stocks and bonds. Almost under the radar-bonds are having their worst year in over 200. In our opinion what is happening this year is largely a reflection of the rapid move up in interest rates.

Since the wake of the financial crisis of 2008, the Fed cut rates to ZERO and left them there for over a decade. A move which in hindsight and in history is likely to prove very misguided. **Interest rates play a part in the valuation process of all assets, lower rates equal higher prices for stocks, bonds, real estate etc...especially real estate.** Zero rates created the 'everything bubble' of the late 2010's, pushing many asset prices to nose-bleed levels.

The inflation shock of 2020 as the economy shut down crippling supply, while fiscal stimulus fueled demand—set the stage for the inflation plaguing the world today. Now the Fed is hiking rates to tame it. **This rise in rates is simply causing assets that had been priced for much lower rates to revalue**. That has been the driver for 2022 downside in stocks, bonds, and real estate.

Stock Market Outlook and Investment Strategy
The stock market came into October very oversold, down near its low, with investor sentiment very bearish (naturally) given the troubles in both stocks and bonds in 2022. This decline priced in a good deal of bad news, as we noted in the last Update. The decline of 30% into the October low was consistent with the typical market declines for an economy in recession.

With so much bad news priced in, there was little more that bad news could do to push stocks down, and that is what we have seen. Stocks even ignored an errant missile strike that threatened to escalate the Ukraine conflict further. Seasonal strength, coupled with the return of corporate buy-backs, along with short-covering as stocks failed to fall further this month—have pushed stocks up to DJIA 34000 and 4000 on the S&P 500. These are key levels. If the S&P can move above 4000 and stay there, the window of opportunity can last for the bulls.

We could see strength persist into Q1 of 2023. Fears of recession are real, as the inversion of the yield curve tells us. However, if the recession holds off until the middle of 2023 or later, the window for stocks to stage a surprising rally is open. We remain opportunistic, buying value in the fixed income area, and in select areas of the stock market. We are nibbling more than aggressive buying, and we are inclined to hold positions. It is too early to declare a new bull market, but we are inclined to hold positions and let this rally run its course. It could run further than most expect given hugely negative investor

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Market Charts S&P 500 Testing Key Level

S&P 500
The S&P has rallied over 10% from its October lows, and is now challenging its long-term moving average (red line). This line was challenged in August but that attempt failed. We believe this time will be successful but it may take a little time to get through it. A move above 4000 would set the stage for another 5-7% into early 2023.