Market Review September 2022

S&P Earnings Growth Rate is Slowing Down!

According to data firm FactSet, third quarter earnings growth rate for the S&P500 is expected to be 2.9% which would make it the lowest earnings growth rate reported by the S&P500 index since third quarter of 2020. On 30th June 2022 analysts had estimated the earnings growth rate for Q3 to be 9.8%. Ten sectors are expected to report lower earnings (compared to the previous estimates provided on June 30) due to downward revisions to EPS estimates. The continuing negative trends in corporate earnings don't bode well for the US and the world economy. As shown in the table below, the average decline in EPS during recessions is circa -29.5% peak to trough and circa -18.7% if we take out the dot com crisis and Global Financial Crisis.

Peak Month	Trough Month	Months of Contraction	Quarters of EPS Decline	EPS Change
August 1957	April 1958	8	4	-17.0%
April 1960	February 1961	10	7	-11.7%
December 1969	November 1970	11	5	-12.9%
November 1973	March 1975	16	4	-14.8%
January 1980	July 1980	6	4	-4.6%
July 1981	November 1982	16	4	-19.1%
July 1990	March 1991	8	10	-36.7%
March 2001	November 2001	8	5	-54.0%
December 2007	June 2009	18	7	-91.9%
February 2020	April 2020	2	4	-32.5%
Average Contraction Duration (months)		**10.3**		
Average EPS Decline (peak to trough)				**-29.5%**
Average EPS Decline (excluding tech bubble-2001 & financial crisis-2007)				**-18.7%**

Data Source: FactSet, National Bureau of Economic Research (NBER), D.A. Davidson
Peak Month is last month of economic growth before contraction, with Trough Month defining the bottom of the contraction (as per the NBER)
EPS Change uses S&P 500 reported EPS, trailing four quarters, updated quarterly

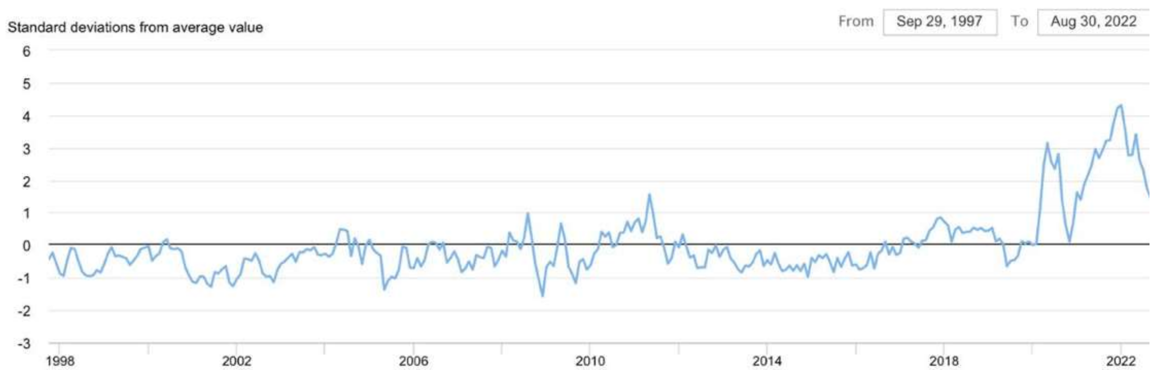
The declining EPS estimates have also had negative impact on valuation levels as well whereby the forward 12-month P/E ratio for the S&P 500 is currently 15.4x which is below the 5-year average P/E ratio of 18.6x and also below the 10-year average P/E ratio of 17.1x.

Global Supply Chain Supply Index Is Showing Signs Of A Decline

The Global Supply Chain Pressure Index (GSCPI) recorded a decline as of August 2022 continuing a four-month streak of easing trends with delivery times decreasing across all countries in the sample as a declining trend in the UK made a major contribution to the overall index.

It is pertinent to note that during 2020, increasing port congestion associated with covid-19 related lockdown measures resulted in the GSCPI surging and this trend was aggravated by the blockage of the Suez Canal in March 2021. By late 2021 and early 2022, the index was on the decline, but geopolitical events (including the War in Ukraine) created additional disruptions, particularly in the energy and agricultural sectors. In light of this backdrop, the recent declines reflect a positive trend that could help ease inflation concerns for the world economy in the short to medium term.

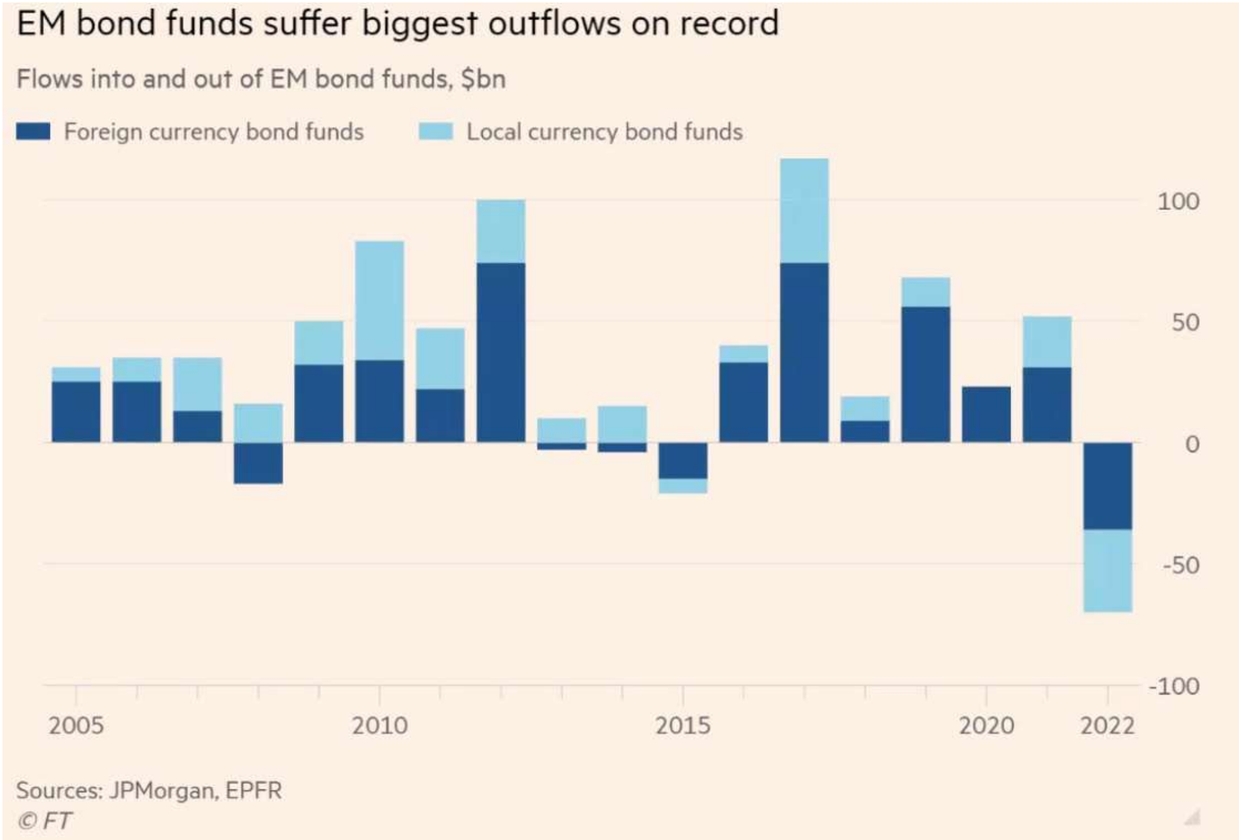
Global Supply Chain Pressure Index (GSCPI)



Source: New York Fed

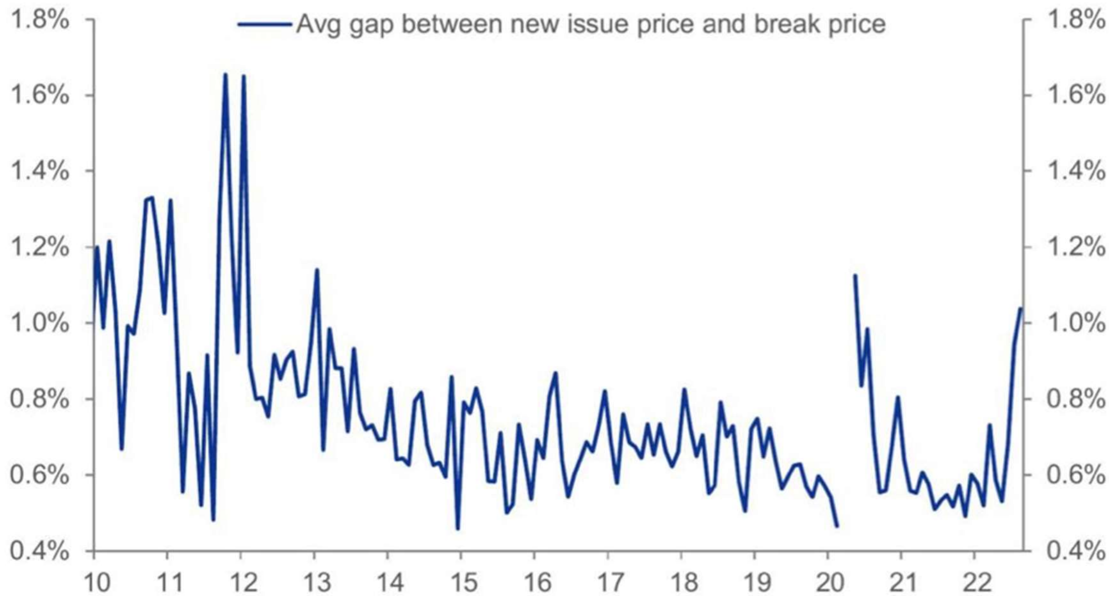
In Signs of Increasingly Difficult Environment for Emerging Markets, Investors Withdraw $70B from Emerging Market Debt Funds

Investors have withdrawn record $70B from emerging market debt funds during 2022 in a sign that rising interest rates in advanced economies leading to a soaring US dollar are increasing the stress on emerging market economies. For reference, this is the highest level of annual outflows since at least 2005. This capital flight from Emerging Market debt funds underscores how investors' perceptions are changing about the rising risk from emerging markets following increase in interest rates from developed economies which for once are making the typically high yields on Emerging Market debt as less attractive. US Investment Bank JP Morgan has revised their forecast for Emerging Market debt outflows in 2022 from $55B (previously) to $80B now.



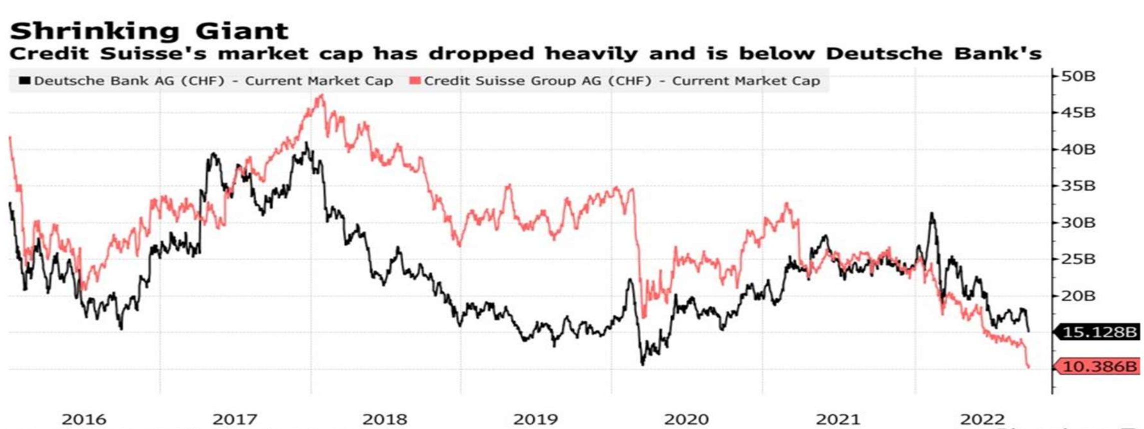
Loan Discounts Are Near Their Highest Levels in 10 Years

Average difference between the primary market price and the first secondary market price as a % of par value for corporate loans has reached their highest level in 10 years. The secondary market has been showing signs of drying up for a while now but the chart below underscores the difficult situation facing the credit markets. Secondary loan discounts are important since they indicate the level of liquidity available for new loans as they indirectly impact the funds committed to new corporate debts. This happens as it becomes difficult for banks to issue new corporate debt if they are unable to distribute existing loans underwritten by them in the secondary market. Given this, the increasing discounts in an already increasing interest rate environment present an ominous sign.



Credit Suisse Issues

Credit Suisse Group's share price has hit record lows after attempts to reassure markets on its financial stability only added to the sense of turmoil surrounding the difficult situation of the Swiss bank. The share price has dropped recently as the bank has lost about 60% of its market value during 2022 and is on track for the biggest ever annual drop in its operating history. Credit Suisse's market capitalization has dropped to around 9.5B Swiss francs, meaning any share sale would be highly dilutive to longtime holders. For reference, the market value was above 30B Swiss francs as recently as March 2021. The graph below reflects the rapid decline in share price.



The cost of insuring the firm’s bonds against default climbed about 15% in the last week of September 2022 reaching levels CDS levels not seen since 2009. The five-year credit default swaps price of about 250 bps is up from about 55 bps at the start of 2022 and is near their highest levels on record. While these levels are still far from distressed and are part of a broad market selloff, they signify deteriorating perceptions of creditworthiness for Credit Suisse in the current deteriorating environment. The Bank management is currently finalizing plans that will likely see sweeping changes to its investment bank and may include cutting thousands of jobs over several years in their continuing efforts to pacify the market and address concerns.