“Bring out your dead”

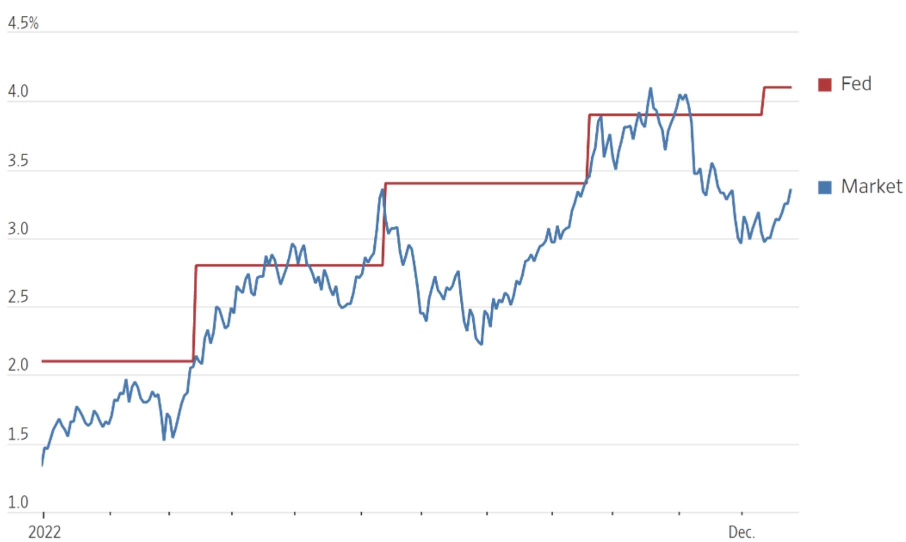
Monty Python [1]

Is it over yet? After the worst equity market performance since the end of the 2008-2009 Financial Crisis, and only the second negative performance year in the last 10 years, we completely agree with the sentiment of this question. Certainly, following a year of a negative 18% return in the S&P 500 and a similar return in “safer” assets such as bonds, the worst must be over, right?

In last year’s Outlook Report “Life is one darn thing after another” we cautioned readers that “in a year that the Fed is more prone to “raise” than to “bailout”, market selloffs may be more tolerated by the Fed, and could therefore prove to be more frequent and deeper, prior to becoming a buying opportunity.” So, is this the buying opportunity? In our opinion, no, not quite yet.

With every rate increase, every Fed forward guidance and every hawkish Fed statement, the market still makes a valiant effort to rebound, essentially saying “I’m not dead yet. I’m feeling better.” (see “Monty Python’s Search for the Holy Grail”). This can be seen in the market’s continued Panglossian take on expected Fed rate increases. As the nearby chart shows, every time the market starts pricing an eventual reduction of short-term rates (the Fed Funds rate by year-end 2024), the Fed communicates a higher rate instead, bludgeoning asset prices once again, just like the dead body collectors of Monty Python.

Fed-funds rate forecast for year-end 2024



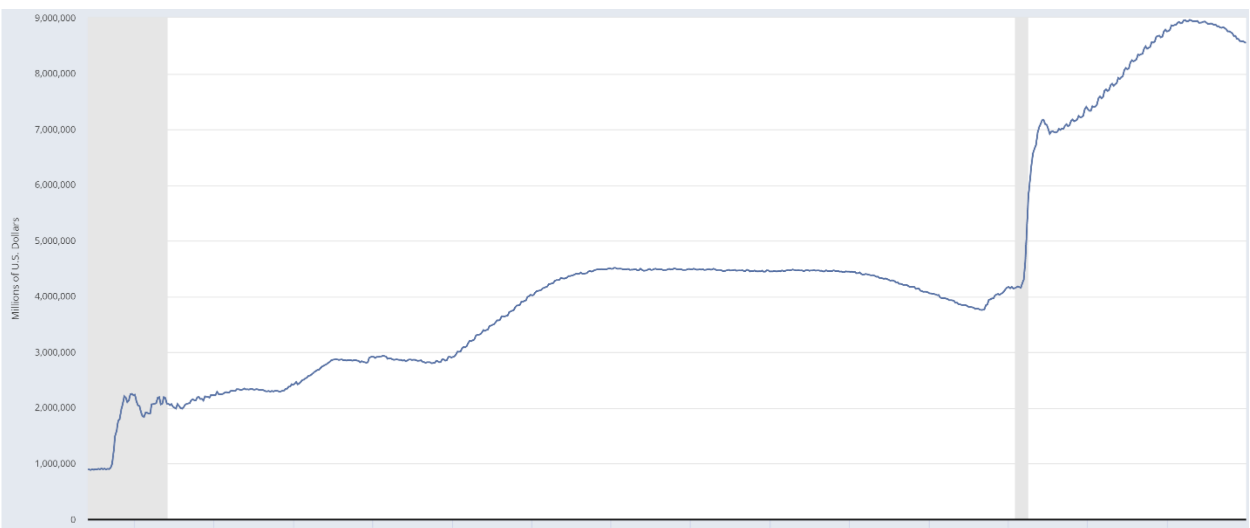
Notes: Market forecast is based on overnight index swaps. Fed forecast reflects median forecast of Fed officials at meetings with economic projections.
Sources: Chatham Financial (Market); Federal Reserve (Fed)

[1] *Note: For those needing a refresher: https://www.youtube.com/watch?v=GU0d8kpybVg*

It is only when the market admits defeat to higher terminal rates that we foresee hope for a lasting market turnaround. For this to occur, the Fed must get comfortable with the inflation outlook, which although somewhat improved for commodities and housing, is still a concern for services (which comprise the majority of the US economy and is driven by a continued strength in labor demand). In our opinion, the key "known unknow" for 2023 is not whether an expected recession is mild or severe, but whether inflation can be put back in the genie. A deeper and more fundamental issue for the US, and for that matter, the global economy, is whether a permanent inflation level is actually secretly desired and wished for, as the only means of government debt loads to become sustainable relative to the size of their respective economies. The challenge there of course, is managing the expected massive increase in interest payments, as government debt is refinanced at the new level of rates.

The one way that a central bank can control the refinancing costs of its government, is to deploy a bit of, what we recently labeled the "mullet" strategy (named after the classic men's haircut: "business in the front, party in the bank"). Under this strategy, the Fed maintains a hawkish stance on rates (i.e. short term rates), but manipulates the long end of the curve through asset purchases, striving for an upper acceptable limit on longer term rates. The Bank of England did this to counter the Liz Truss premiership debacle. If we are right, and the Fed essentially controls the entire yield curve for the foreseeable future, just like the Bank of Japan has done for decades, then, any spike in long term rates ought to be viewed as a buying opportunity.

US Federal Reserve Total Assets



Source: https://fred.stlouisfed.org/series/WALCL

Turning to market sectors, in last year's report we noted that "… considering the downward pressure on fixed income assets as rates rise, once again it will be hard for investors to ignore risk-based assets such as equities. We do believe though, that the market's rotation out of the go-go growth stocks will continue, and that companies entering 2022 with more reasonable valuations are likely to outperform."

Within the market's negative return, the market rotation out of the "go-go growth stocks" really punished some of the top performing tech names of 2021, namely "The FANGs" and other tech darlings, whereas "value" sectors such as Energy, Utilities, Healthcare and Consumer Staples, posted anywhere from solid positive returns to only mildly negative. For this year, we urge patience when deploying capital, and continue to favor "value over growth" and more generally "yields over equities".

We appreciate your support, and always welcome your comments and feedback.

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The Year in Review in a Few Charts

Total Return By Asset Class	1 Year
Dollar Index	5.5%
Oil	1.7%
Gold	-1.2%
High Yield	-10.5%
S&P 500	***-15.2%***
60/40 Stock/Bonds	-15.3%
Barclays Agg. Bond Index	-15.4%
International (MSCI) Index	-16.4%

Source: YCharts, Sixty Guilders Management, LLC

Accelerating inflation pushed commodity prices up, financial assets down, and a flight to liquidity boosted the dollar.

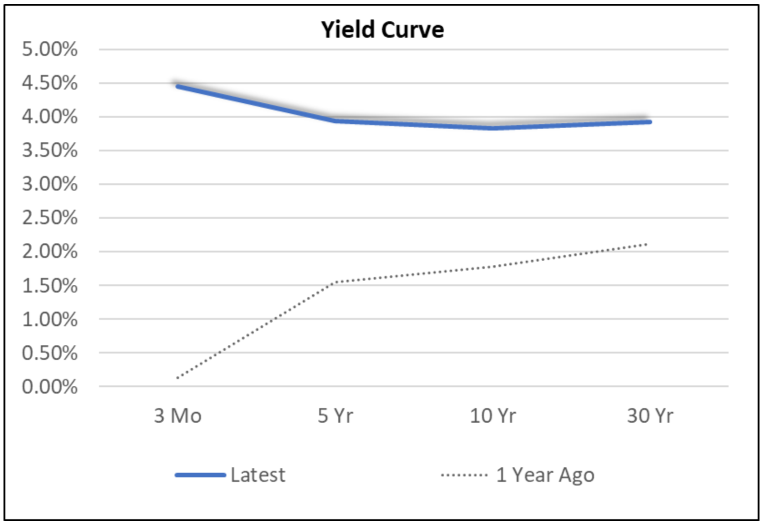
S&P 500 Historical Performance by Industry Sector

2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
FINL 28.8%	COND 43.1%	REAL 30.2%	COND 10.1%	ENRS 27.4%	INFT 38.8%	HLTH 6.5%	INFT 50.3%	INFT 43.9%	MATR 82.9%	ENRS 36.1%
COND 23.9%	HLTH 41.5%	UTIL 29.0%	HLTH 6.9%	TELS 23.5%	MATR 23.8%	UTIL 4.1%	TELS 32.7%	COND 33.3%	FINL 84.5%	UTIL 2.1%
REAL 19.7%	INDU 40.7%	HLTH 25.3%	CONS 6.6%	FINL 22.8%	COND 23.0%	COND 0.8%	FINL 32.1%	TELS 23.6%	ENRS 48.5%	HLTH 0.2%
TELS 18.3%	FINL 35.6%	INFT 20.1%	INFT 5.9%	INDU 18.9%	FINL 22.2%	INFT -0.3%	S&P 31.5%	MATR 20.7%	HLTH 40.8%	CONS -2.9%
HLTH 17.9%	S&P 32.4%	CONS 16.0%	REAL 4.7%	MATR 16.7%	HLTH 22.1%	REAL -2.2%	INDU 29.4%	S&P 18.4%	INFT 28.7%	INDU -7.8%
S&P 16.0%	INFT 28.4%	FINL 15.2%	TELS 3.4%	UTIL 16.3%	S&P 21.8%	S&P -4.4%	REAL 29.0%	HLTH 13.5%	REAL 34.4%	MATR -11.1%
INDU 15.4%	CONS 26.1%	S&P 13.7%	S&P 1.4%	INFT 13.9%	INDU 21.0%	CONS -8.4%	COND 27.9%	INDU 11.1%	CONS 31.9%	S&P -18.2
MATR 15.0%	MATR 25.6%	INDU 9.8%	FINL -1.5%	S&P 12.0%	CONS 13.5%	TELS -12.5%	CONS 27.6%	CONS 10.8%	S&P 30.0%	FINL -15.8%
INFT 14.8%	ENRS 25.1%	COND 9.7%	INDU -2.5%	COND 6.0%	UTIL 12.1%	FINL -13.0%	UTIL 26.4%	UTIL 0.5%	COND 25.0%	REAL -23.9%
CONS 10.8%	UTIL 13.2%	MATR 6.9%	UTIL -4.8%	CONS 5.4%	REAL 10.9%	INDU -13.3%	MATR 24.6%	FINL -1.7%	UTIL 19.2%	INFT -25.2%
ENRS 4.6%	TELS 11.5%	TELS 3.0%	MATR -8.4%	REAL 3.4%	ENRS -1.0%	MATR -14.7%	HLTH 20.8%	REAL -2.2%	INDU 18.9%	COND -31.7
UTIL 1.3%	REAL 1.6%	ENRS -7.8%	ENRS -21.1%	HLTH -2.7%	TELS -1.3%	ENRS -18.1%	ENRS 11.8%	ENRS -33.7%	TELS 15.2%	TELS -37.4

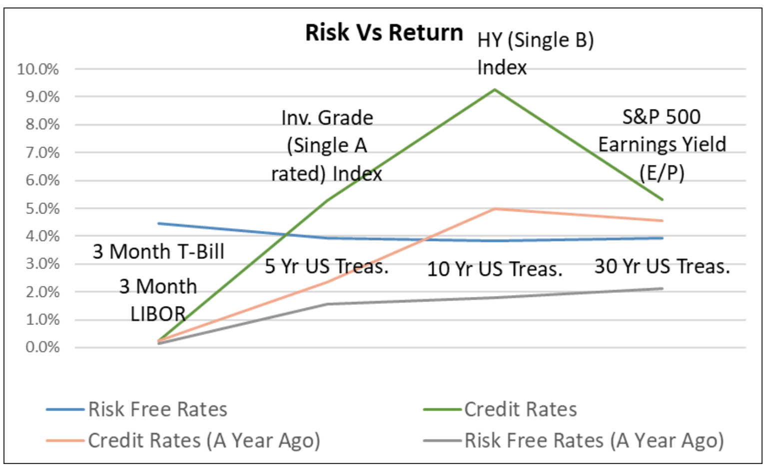
The market selloff pushed most sectors lower, with the notable exception of Energy, which continued its strong performance from 2021.

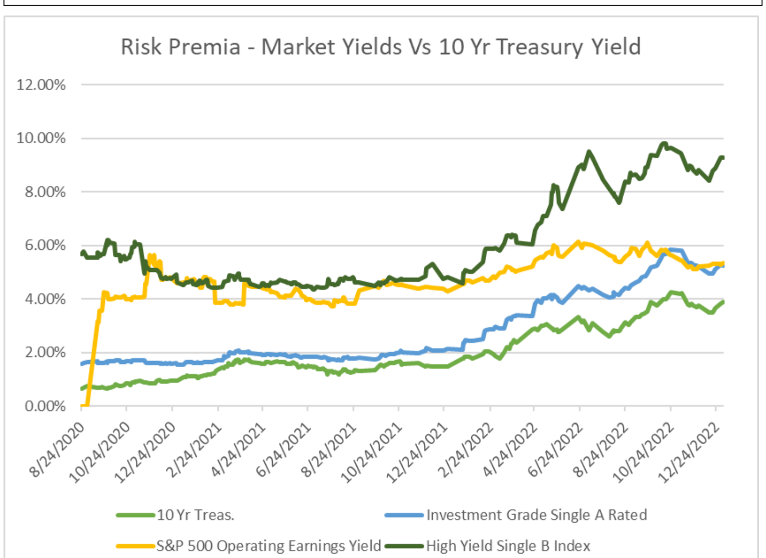
Abbr.	Sector Index
COND	S&P 500 Consumer Discretionary Index
CONS	S&P 500 Consumer Staples Index
ENRS	S&P 500 Energy Index
FINL	S&P 500 Financials Index
HLTH	S&P 500 Health Care Index
INDU	S&P 500 Industrials Index
INFT	S&P 500 Information Technology Index
MATR	S&P 500 Materials Index
REAL	S&P 500 Real Estate Index
TELS	S&P 500 Communication Services Index
UTIL	S&P 500 Utilities Index
S&P	S&P 500 Index

Source: https://novelinvestor.com/sector-performance/, YCharts, Sixty Guilders Management, LLC



The Fed's renewed hawkish strategy has not only pushed up short term rates, but long term as well. Nonetheless, the long end of the curve has come back down from higher levels witnessed in the fall of 2022.





As the yield curve has shifted up (higher market rates), risk premia have increased for risk assets, proportionally to their risk level. If anything, equities have help up better than other risk assets, in relative terms.

Source: YCharts, Sixty Guilders Management, LLC

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Asset Classes, Credit Markets, Rates & Currencies

		Latest		1 Year Ago
Economy				
Economic Growth (Real GDP)	↑	3.2%	↑	2.3%
Inflation (Ex. Food & Energy)	→	6.0%	↓	5.5%
Nominal GDP	↑	9.2%	↑	7.8%
Unemployment Rate	↓	3.7%	↑	3.9%
Money & Commodities				
Gold ($/Troy ounce)	↑	1,801	↑	1,823
Oil (WTI Crude, $/barre)	↓	79.45	↓	78.11
TIPS (breakeven rate)	↑	2.3%	↓	0.0%
Rates				
3 Month T-Bill	↑	4.45%	↓	0.13%
5 Yr US Treas.	↑	3.94%	↓	1.55%
10 Yr US Treas.	↑	3.83%	↓	1.78%
30 Yr US Treas.	↑	3.92%	→	2.12%
Credit Markets				
3 Month LIBOR	↓	0.2%	↓	0.2%
Inv. Grade (Single A rated) Index	↑	5.3%	↓	2.4%
HY (Single B) Index	↑	9.3%	↓	5.0%
Equity Market				
S&P 500	↓	3,819	↑	4,581
Price/Book	↓	3.8x	↑	4.4x
P/E	→	18.8x	↑	21.9x
Earnings Yield (E/P)	→	5.3%	↓	4.6%
Volatility (VIX)	↓	24%	↓	25%
International Snapshot				
MSCI	→	1,955	↑	2,338
Dollar/Yen	↑	132.8	↑	115.6
EUR/Dollar	↓	1.06	↓	1.14
10 Japanese Bond Yield	↑	0.50%	↓	0.00%

Source: YCharts, Sixty Guilders Management, LLC

Disclosure Statements

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Appendix

Industry Sectors Valuation

Industry Sector	EV/ LTM EBITDA	EV/ Forward EBITDA	5 Yr Low EV/ EBITDA	5 Yr High EV/ EBITDA	10 Year Bond Yield	Estimated P/E	Estimated Earnings Yield (E/P)	E/P Yield to Bond Yield	Debt/EV	Equity/ EV	Relative Market Capitalization	Relative Price/Book Ratio	Beta
	Valuation								Leverage, Capitalizaiton and Volatility				
Autos	8.0x	6.9x	5.9x	9.2x	3.9%	8.9x	11.2%	2.9x	38%	62%	85%	49%	1.7x
Advertising	13.8x	7.4x	7.2x	12.0x	2.5%	13.0x	7.7%	3.0x	51%	49%	18%	101%	1.7x
Aerospace-Defense	14.0x	12.8x	10.1x	14.6x	2.5%	16.8x	6.0%	2.4x	21%	79%	83%	63%	1.6x
Agriculture	10.8x	9.0x	8.0x	13.1x	2.4%	12.2x	8.2%	3.4x	22%	78%	133%	38%	0.9x
Apparel	13.3x	8.3x	8.4x	13.1x	2.4%	14.1x	7.1%	3.0x	18%	82%	65%	75%	1.5x
Beverages	19.8x	16.6x	13.3x	20.0x	2.1%	22.1x	4.5%	2.2x	15%	85%	170%	218%	0.9x
Internet	19.0x	13.3x	12.5x	19.1x	2.4%	17.7x	5.7%	2.3x	15%	85%	144%	127%	1.1x
Biotechnology	25.5x		15.7x	20.0x	2.4%	27.9x	3.6%	1.5x	6%	94%	151%	184%	1.0x
Chemicals	11.7x	9.2x	8.7x	16.1x	2.4%	13.9x	7.2%	3.0x	21%	79%	117%	65%	1.4x
Coal	4.9x	3.4x	3.8x	6.4x	7.4%	13.3x	7.5%	1.0x	45%	55%	15%	24%	1.4x
Commercial Serv.	15.4x	12.4x	9.4x	16.1x	2.4%	18.3x	5.5%	2.3x	18%	82%	64%	106%	1.2x
Computers-Office Equip	13.1x	9.6x	8.1x	13.2x	2.5%	16.6x	6.0%	2.4x	16%	84%	137%	90%	1.0x
Diversified Finan Serv	15.4x	16.1x	14.7x	20.0x	2.0%	22.0x	4.5%	2.3x	10%	90%	135%	82%	1.0x
Utilities	12.1x	11.2x	9.7x	12.7x	2.5%	17.1x	5.8%	2.4x	45%	55%	116%	40%	0.4x
Electrical Equipment	9.6x		8.8x	16.4x		38.7x	2.6%		9%	91%	114%	392%	1.3x
Electronics	15.2x	13.5x	10.7x	16.7x	2.0%	18.3x	5.5%	2.7x	10%	90%	155%	85%	1.2x
Food	12.5x	11.0x	11.0x	15.3x	2.4%	15.6x	6.4%	2.7x	29%	71%	91%	70%	0.6x
Forest Products-Paper	9.0x	3.4x	4.1x	8.2x	5.8%	11.6x	8.6%	1.5x	45%	55%	7%	27%	1.9x
Healthcare-Services	17.0x	13.2x	13.1x	20.0x	2.3%	19.8x	5.1%	2.2x	18%	82%	116%	82%	0.9x
Holding Companies	9.0x	5.8x	4.8x	15.3x	4.8%	19.3x	5.2%	1.1x	28%	72%	111%	76%	0.9x
Homebuilders	7.2x	4.4x	7.0x	13.2x	2.9%	5.3x	19.0%	6.5x	26%	74%	48%	31%	1.6x
Household Products	17.4x	14.3x	13.4x	18.7x	2.1%	22.0x	4.5%	2.2x	13%	87%	130%	129%	0.9x
Iron-Steel	7.2x	2.4x	4.6x	8.4x	3.5%	6.3x	15.8%	4.5x	19%	81%	123%	45%	1.4x
Lodging	34.1x	19.6x	10.4x	20.0x	3.5%	30.9x	3.2%	0.9x	29%	71%	108%	115%	2.0x
Machinery	16.8x	15.0x	10.6x	17.6x	2.1%	19.8x	5.1%	2.4x	13%	87%	114%	91%	1.2x
Metal Fabric.-Hardware	6.7x	13.2x	5.8x	12.9x	3.4%	19.5x	5.1%	1.5x	14%	86%	25%	54%	1.2x
Media	7.9x	9.5x	6.4x	11.4x	3.1%	14.7x	6.8%	2.2x	36%	64%	112%	53%	1.3x
Mining	7.7x	6.8x	6.5x	13.7x	3.4%	15.0x	6.6%	2.0x	17%	83%	23%	57%	1.8x
Oil-Gas_Sector	11.0x	7.5x	5.7x	14.1x	3.0%	11.4x	8.8%	2.9x	36%	64%	63%	32%	2.2x
Packaging-Containers	12.2x	9.5x	9.4x	13.8x	2.5%	14.0x	7.2%	2.9x	30%	70%	118%	105%	1.1x
Pharmaceuticals	15.5x	10.3x	10.3x	17.4x	2.2%	11.4x	8.7%	4.0x	20%	80%	191%	108%	0.7x
Hand-Machine Tools	11.7x	9.8x	8.9x	15.9x	2.0%	14.6x	6.8%	3.4x	13%	87%	38%	47%	1.4x
Real Estate	11.3x	11.0x	8.2x	13.8x	2.2%	17.6x	5.7%	2.6x	34%	66%	66%	46%	1.5x
REITS	22.3x		14.7x	20.0x	2.5%	17.7x	5.6%	2.2x	29%	71%	88%	51%	0.9x
Retail	13.3x	10.5x	8.1x	12.3x	2.4%	15.3x	6.6%	2.7x	20%	80%	99%	108%	1.5x
Software	36.5x		15.8x	20.0x	2.0%	35.8x	2.8%	1.4x	7%	93%	118%	230%	1.1x
Airlines		-30.8x	3.6x	5.6x	2.8%	14.4x	6.9%	2.5x			101%	68%	1.6x
Telecommunications	9.2x	8.0x	5.7x	8.8x	3.4%	18.0x	5.6%	1.6x	39%	61%	72%	70%	0.7x
Transportation	14.1x	11.7x	10.1x	15.1x	2.2%	17.9x	5.6%	2.5x	17%	83%	141%	131%	1.1x
Engineering	13.5x	10.9x	6.7x	18.2x	3.3%	16.5x	6.1%	1.9x	22%	78%	75%	65%	1.3x
Building Materials	11.2x	9.4x	9.1x	13.4x	2.5%	13.6x	7.4%	3.0x	20%	80%	100%	83%	1.1x
Leisure Time	18.2x	13.5x	8.4x	14.6x	3.7%	24.5x	4.1%	1.1x	19%	81%	108%	184%	1.8x
Semiconductors	17.9x	13.3x	9.5x	18.8x	2.1%	17.2x	5.8%	2.7x	6%	94%	170%	134%	1.3x
Sixty Guilders Coverage Index													
Average	14.0x	9.3x	9.0x	14.7x	2.8%	17.3x	6.7%	2.6x	23%	77%	100%	100%	1.3x
Median	13.1x	10.1x	8.7x	14.6x	2.5%	16.7x	6.0%	2.4x	20%	80%	108%	79%	1.3x
Standard Deviation	6.5x	7.5x	3.2x	3.8x	1.1%	6.6x	3.0%	1.2x	11%	11%	44%	67%	0.4x

Notes: 1. EV represent

Source: YCharts, Sixty Guilders Management, LLC