Sevens Report Alpha Webinar – The Positive and Negative Path for Markets in 2023

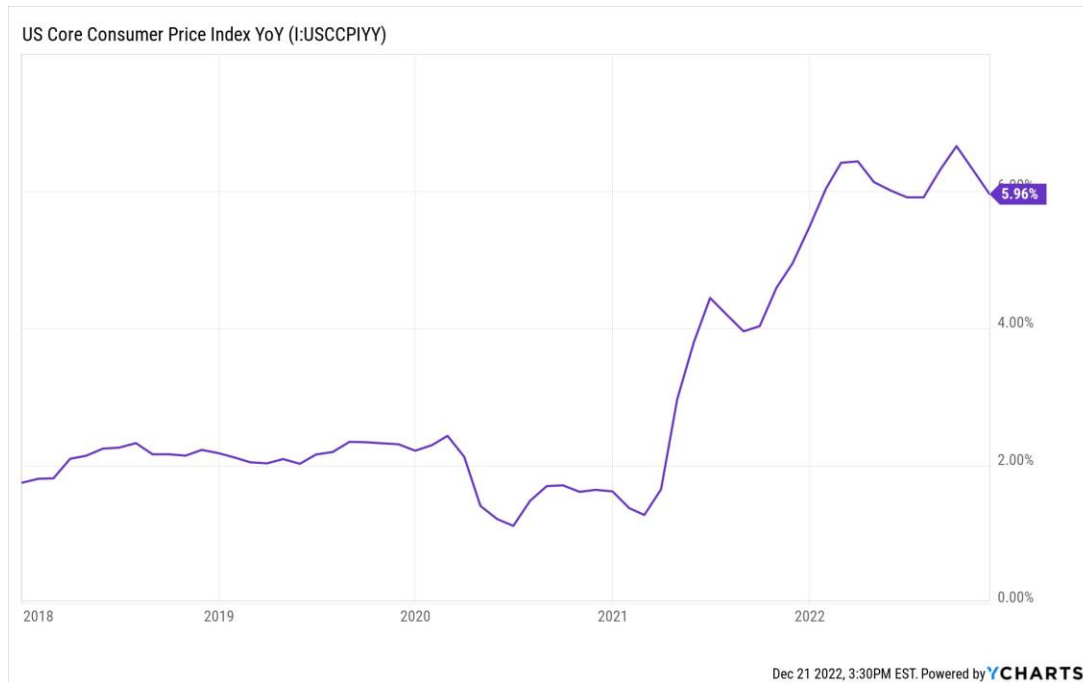## January 5th, 2023

Tom Essaye, President Sevens Report Research

Key Variables for Stocks and Bonds in 2023

- Inflation
- Unemployment
- Corporate Earnings
- Bond Yields
- Fed Policy
- Chinese Economic Activity
- Geopolitics

Inflation

US Core Consumer Price Index YoY (I:USCCPIYY)

5.96%

- Key Index: Core CPI
  - "Good" level: < 4.0%
  - "Ok" level: < 5.0%
  - "Bad" level: > 5.0%
  - Timeline: 1st half of 2023.

Unemployment

US Unemployment Rate (I:USUR)
3.70%
Dec 20 2022, 11:26AM EST. Powered by YCHARTS
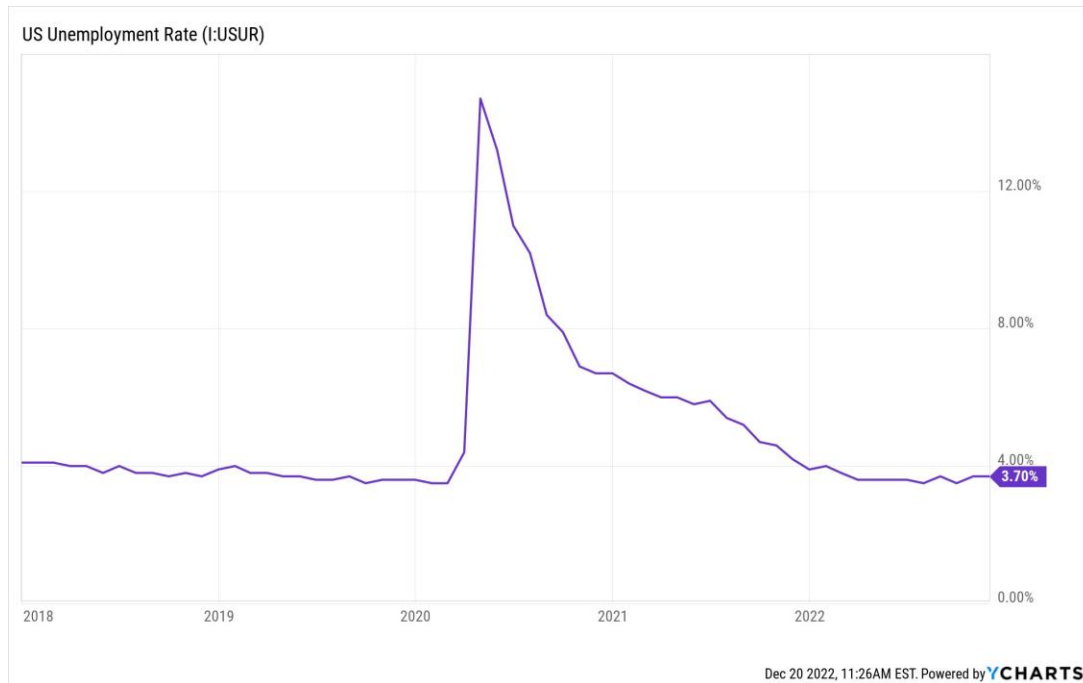
- Key Indicator: U-3 Unemployment Rate
  - "Good" level: > 4.5%
  - "Ok" level: 4.0% - 4.5%
  - "Bad" level: < 4.0%
  - Timeframe: 1st half of 2023.

Corporate Earnings

S&P 500 Expected 2023 EPS

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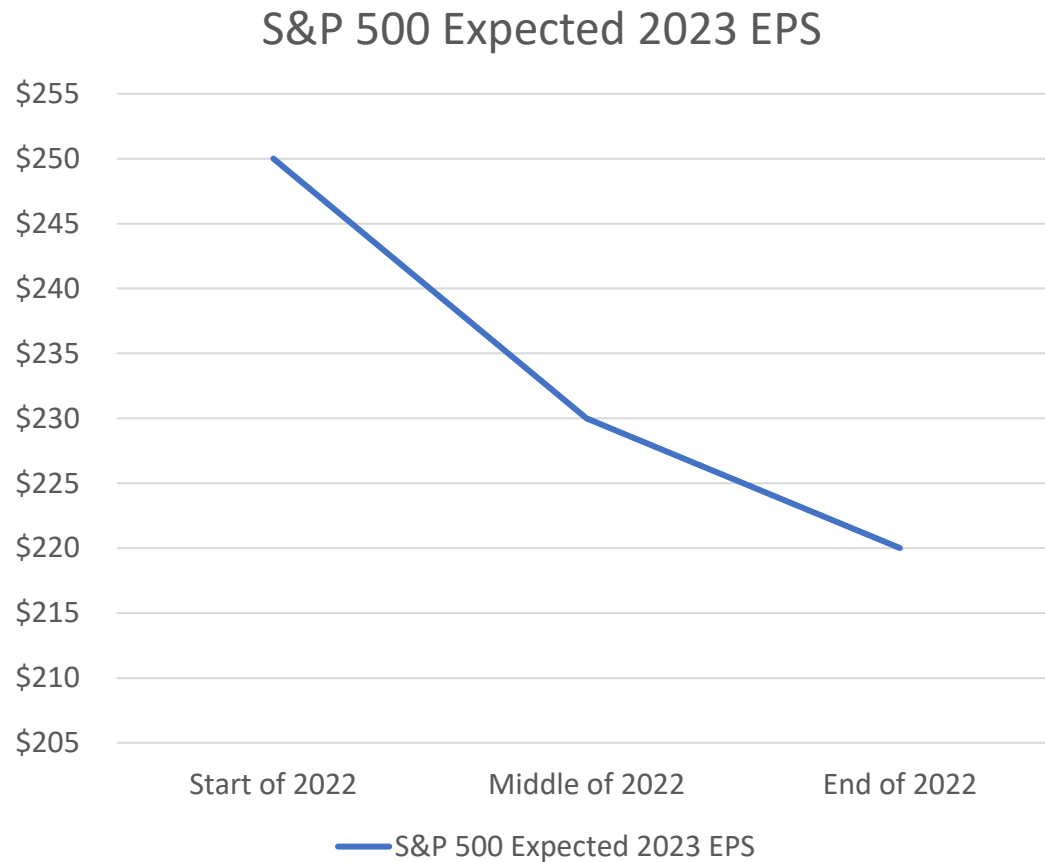
- Key Indicator: Consensus 2023 S&P 500 EPS
  - "Good" level: ≥ 225
  - "Ok" level: 220
  - "Bad" level: < 220
  - Timeframe: Q4 2022 Earnings Season (January/February)

Bond Yields

10 Year Treasury Rate (I:10YTCMR)

3.79%
3.60%
2.40%
1.20%
0.00%

2019   2020   2021   2022   2023

Jan 04 2023, 1:02PM EST. Powered by YCHARTS
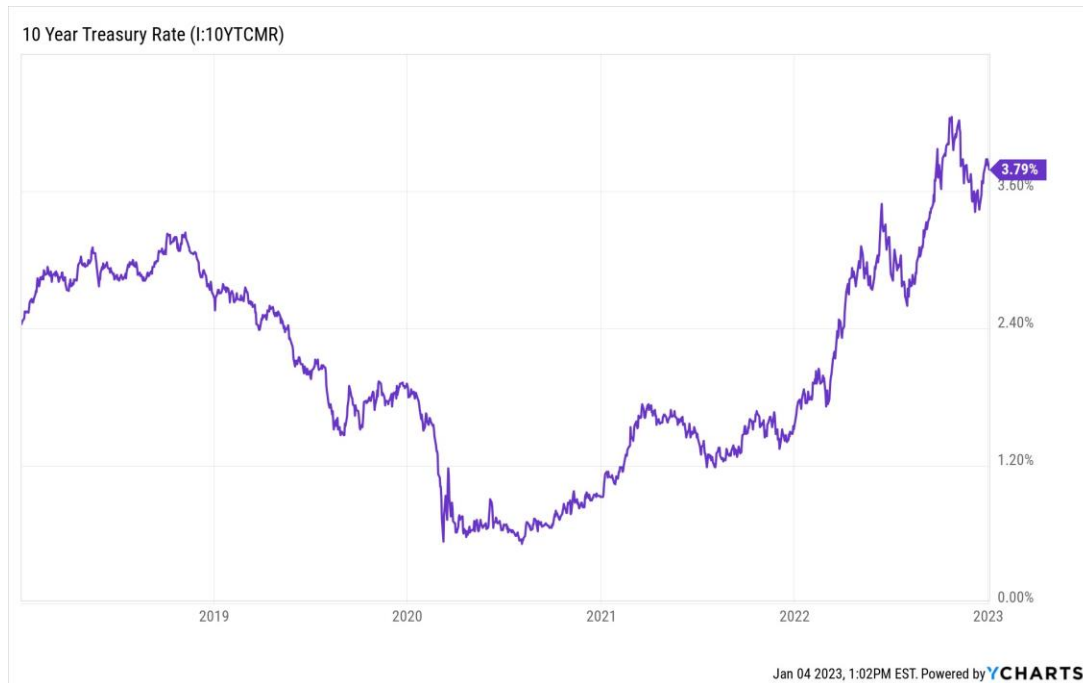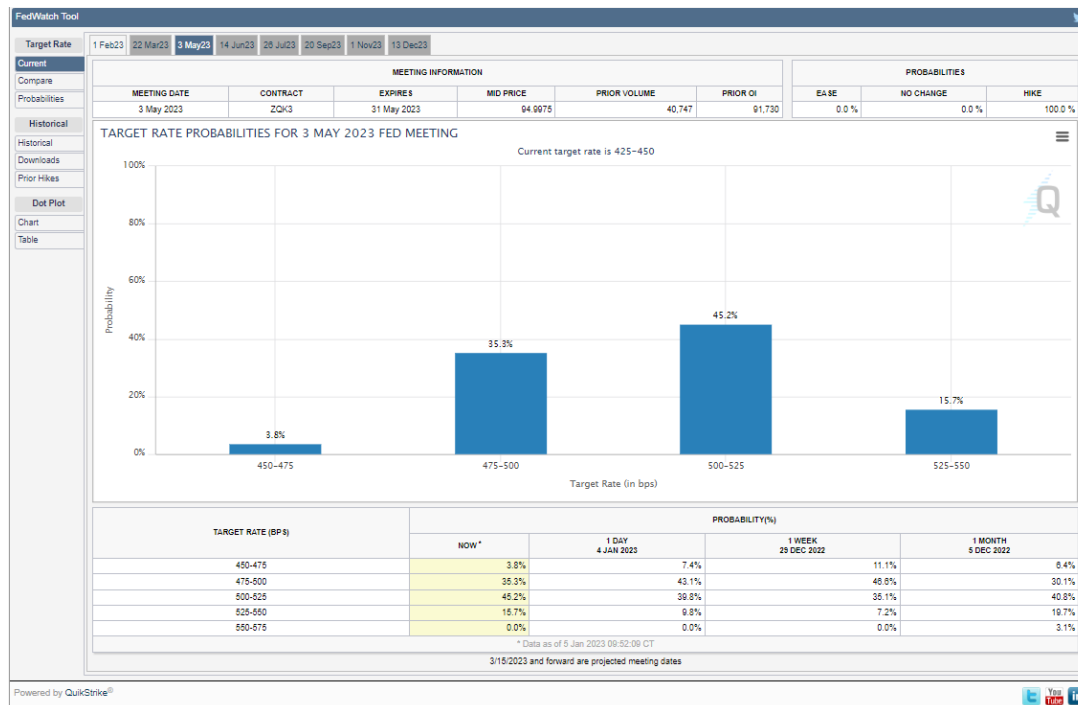
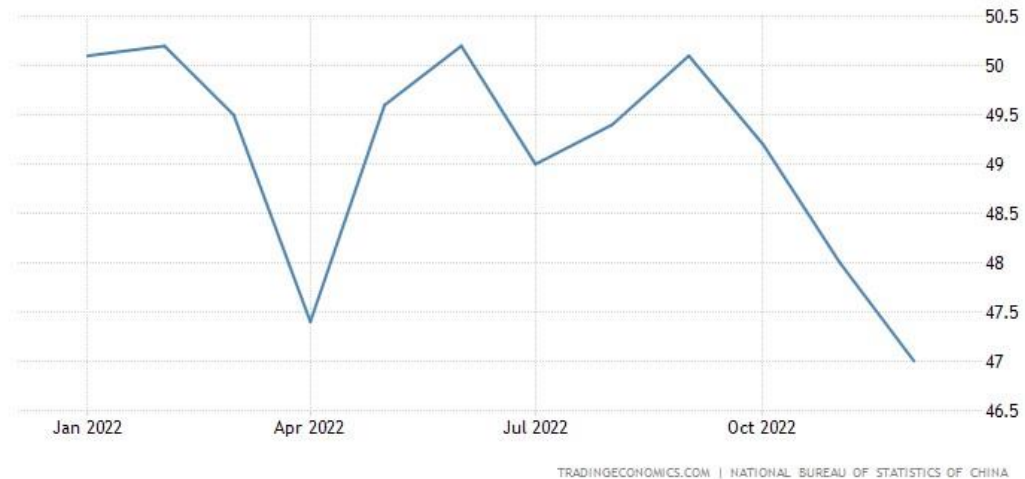- Key Indicator: 10-year Treasury Yield
  - "Good" level: < 3.0%
  - "Ok" level: 3.00% - 3.50%
  - "Bad" level: > 3.50%.
  - Timeframe: Q1 2023.

Fed Policy

- Key Indicator: Fed Funds Rate
  - "Good" level: < 5.00%
  - "Ok" level: 5.125%
  - "Bad" level: > 5.125%.
  - Timeframe: By May.

Chinese Economic Activity

- Key Indicator: Chinese Manufacturing PMI
  - "Good" level: > 50.5
  - "Ok" level: 48-50
  - "Bad" level: < 48
  - Timeframe: 1st half of 2023.

Geopolitics

- Key Indicator: Peace Talks
  - "Good" outcome: Peace talks in February.
  - "Ok" outcome: Peace talks by June.
  - "Bad" outcome: Further escalation or no peace talks.
  - Timeframe: 1st half of 2023.

The "Good" Scenario

- Core CPI < 4.0%.
- U-3 Unemployment > 4.5%
- 2023 Consensus S&P 500 EPS ≥ $225
- 10-year Treasury yield < 3.0%
- Fed Funds < 5.00%
- Chinese Manufacturing PMI > 50.5%
- Russia/Ukraine Peace Talks by February

- S&P 500 Target: 4,370.
  - How I get there: An 18.5X multiple times $225 EPS. Plus, another several percentage points as underexposed investors add long positions.
  - Return from current level: 14.7%
- Strategies that should outperform:
  - Small Cap Stocks (IJR/RWL/CALF). 11/29/22.
  - Russia/Ukraine Ceasefire Playbook (EMB/HYEM/EUFN/JETS/FXE). 3/22/22.
  - What Would Outperform If Markets Turn Around (XITK/VCR/USHY/SRLN). 2/23/22.
  - China Growth (KWEB/CXSE). 12/28/21.

The "OK" Scenario

- Core CPI < 5.0%.
- U-3 Unemployment: 4.0% - 4.5%
- 2023 Consensus S&P 500 EPS = $220.
- 10-year Treasury yield 3.0% - 3.5%
- Fed Funds = 5.125%
- Chinese Manufacturing PMI 48-50
- Russia/Ukraine Peace Talks by June

- S&P 500 Target: 3,520.
  - How I get there: 16X multiple times $220 earnings.
  - Return from current level: - 8.0%.
- Strategies that should outperform:
  - MOAT Stocks (MOAT/MOTE/SMOT). 11/2/22.
  - Opportunities in Municipal Bonds (JMST/HYMB/MMIT). 10/18/22.
  - Positioning for Another Rollover (RYU/SPHD/USFR). 9/7/22.
  - Sectors That Outperformed During Recent Recessions (VHT/IHF/VDC/PBJ). 7/12/22.

The "Bad" Scenario

- Core CPI > 5.0%.

- U-3 Unemployment: < 4.0%

- 2023 Consensus S&P 500 EPS < $220.

- 10-year Treasury yield: > 3.5%

- Fed Funds: > 5.125%

- Chinese Manufacturing PMI: <48

- No Russia/Ukraine Peace Talks

- S&P 500 Target: 3,225
  - How I get there: 15X multiple times $215 EPS.
  - Return from current level: -15%.

- Strategies that should outperform:
  - Protection in a Deeper Bear Market. (SH/PSQ/PTLC/SGOV). 10/4/22.
  - Cash Management (MINT/FPNIX).