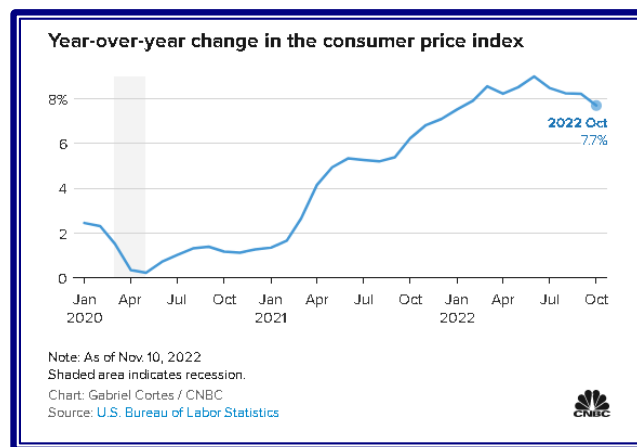


IN VIEW: The Economic Landscape

Consumer prices rose less than anticipated in October as medical care services, used vehicle, and apparel prices declined. The data supports the case for peaking inflation as the overall trend appears to be moderating. Easing supply disruptions, inventory builds and restrictive Fed policy all support lower inflationary trends.

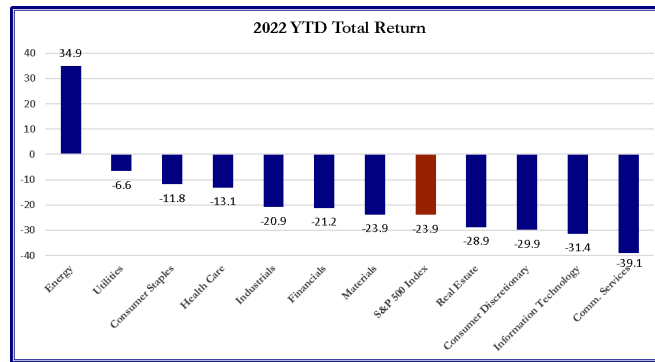


Stocks rose sharply on the latest CPI report, after digesting the latest Federal Reserve comments the prior week. The Fed is still contending with services inflation as rising goods prices subside. The strong jobs market allows the Fed room to pause and assess conditions, before potentially raising its terminal rate again towards a level above 5%. Supersized rate hikes of 75 bps are unlikely to continue for much longer, as we expect the Fed to begin to reduce the pace of its restrictive policy stance by year-end.

CLOSE-UP: Equity Investment Overview

Market Performance & Earnings:

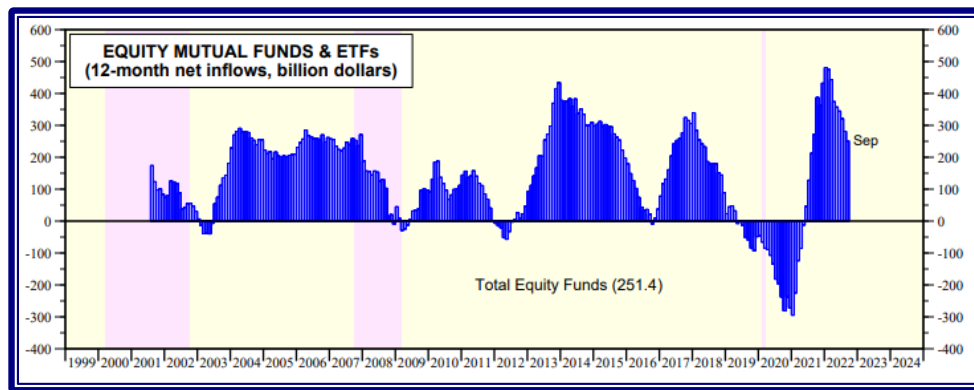
Stocks traded down -23.9% year-to-date, including the most recent leg down in September, a historically weak month. This came on the backs of the 5th Fed interest rate hike of the year, leaving investors with little confidence that inflation was under control and two more rate hikes were possible for the remainder of the year. Energy was the market leader by a significantly wide margin and the only sector to produce positive returns. Outside of Energy, Northrop Grumman, Archer Daniels, and Merck were the top performing stocks. Philips Electronics, Intel, Applied Materials, Comcast and Disney were the laggards as Information Technology and Communication Services traded off over -31.4% and -39.1% for the year respectively.



Source: Bloomberg and Altman Investment Management, LLC

As expected, equity fund flows lost steam throughout the year, particularly in mutual funds where levels sunk below -\$200 billion in net outflows on a rolling 12-month basis. Separately, equity exchange traded funds continue to experience a downward trend but remain around \$493 billion in net inflows. Over the past 6 years, equity ETFs have been the preferred investment for equity inflows over higher fee mutuals funds.

Declining Trends in Equity Investment Persist



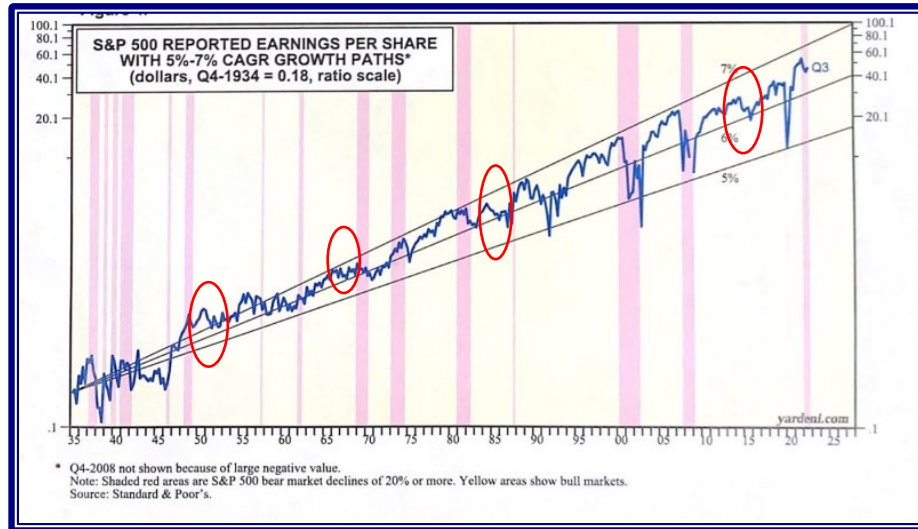
Source: Yardeni Research

On a monthly basis, equity fund inflows began the year strong raking in nearly \$60 billion in March alone - only to fall into negative territory throughout the summer months. The surge in M2 supply, that began in 2020, tells us that there is plenty of money on the sidelines once investors feel as though inflation is getting under control.

That being said, equity clients at Bank of America have been net buyers the past five weeks as of mid-October, suggesting the market is bottoming. During the year, their clients funneled \$8.7 billion into stocks and equity exchange traded funds. Technology and Communication Services were the main sector beneficiaries. New investment targeted value ETFs over growth - favoring attractive relative fundamentals, high quality, dividend paying equity vehicles.

Corporate revenues generally fall in conjunction with contracting profit margins as a result of an economic recession, as it is typical to see costs of goods rise at a pace faster than unit sales during this time. This of course is not good news for stocks. In fact, almost every bear market since the 1930s has been the product of simultaneous economic and earning recessions. Yardeni research takes a deeper dive to determine that there have been several periods of declining earnings during the early 50s, the mid 60s, 80s and 2010s that were not accompanied by recessions.

*Not Every Decline in Earnings is
Accompanied by a Recession*



Source: Yardeni Research

We are inclined to anticipate a soft landing, based upon the trajectory of forecasted forward earnings. We are seeing revenues continue to rise boosted by inflation against narrowing margins. Revenues are growing in tandem with GDP, but given that economic growth is anticipated to slow from here, earnings could in fact weaken from higher input costs. In this scenario profit margins will likely weigh on overall earnings, but revenues could hold up enough to allow for a soft landing as opposed to an all-out recession. However, at this point in the cycle it is still too early to tell.

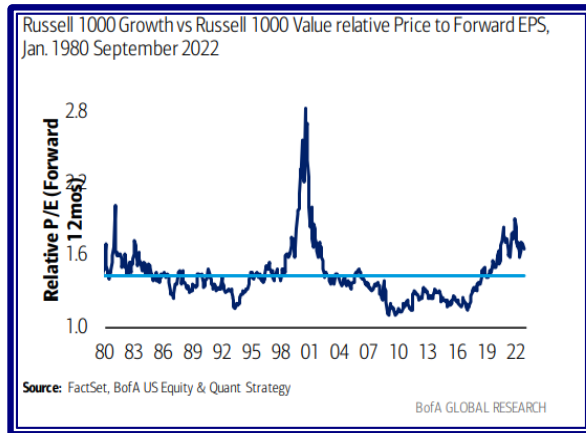
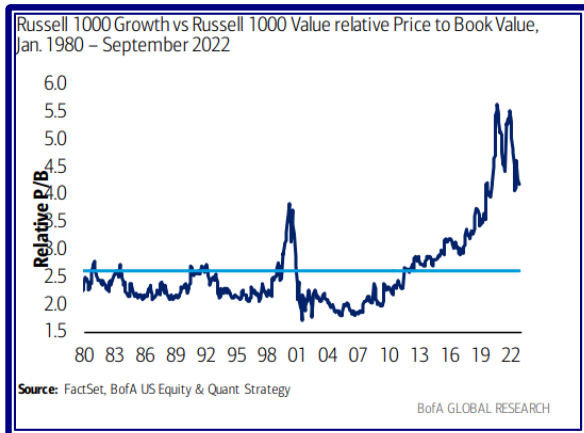
Stock Spotlight and Strategy:

U.S. stocks have transitioned into the late phase of the business cycle exhibiting signs of a tight labor market, rising inventories, higher interest rates, and declining profit margins. Inflation expectations will be key to market performance. Global commodity and agriculture prices may be peaking, shifting focus towards the surging services sector.

The potential for a rally in stocks is viable - however it likely will not escape volatility. Stocks appear to be pricing in slower growth with the possibility of a mild recession. Historically, Consumer Discretionary and Technology stocks lag during this phase of the cycle which supports our underweight in these areas.

Growth valuations remain at historically high levels as compared to value. The widening gap makes growth stocks vulnerable in a volatile equity market. As a result, we maintain our low multiple, high quality, dividend-paying bias, and believe it remains too early to shift our focus into the “growthier” segments of the equity market.

Valuation Gap Between Growth and Value Stocks Remains High



Consumer Discretionary Overview

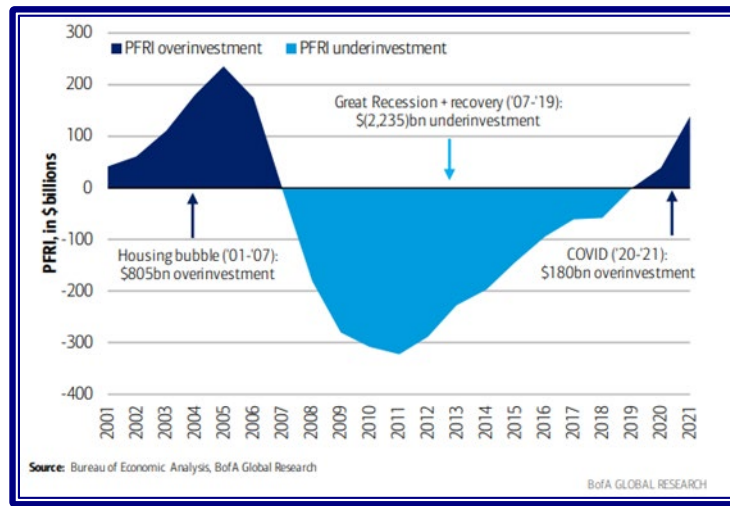
Consumer Discretionary stocks had a tough year pressured by inflation and rising yields. We maintain our underweight in this sector, as higher cost loans and rising credit card rates impact borrowing. Rising rent, gasoline prices, and healthcare costs are also compressing consumer budgets. Retail sales reflected this pressure in September as sales shifted towards services with declines in areas such as auto, furniture, and building materials and sporting goods. A bright spot was sales in clothing, restaurant receipts, and online retailers. The 0.6% rise in Personal Consumption Expenditures for the same month was attributable in large part to spending on services. Sentiment improved some in October, as inflation expectations rolled over for the same month. While we do believe inflation may have peaked, the Fed still has the support of a strong labor market to maintain restrictive policy - and they reiterated their intention to do so at the latest Fed meeting. A sustained decline in yields is necessary to support consumer spending on discretionary items - and until then, we believe an underweight is warranted in the sector.

The Rise in Bond Yields Points to Additional Underperformance
(Yield line is inverted)



Within the Consumer Discretionary space, that currently trades at a 48% premium to the benchmark S&P 500 index stock, selection is key. We find value in the home improvement industry. At a TTM multiple of 13x, LOW's trades at a 49% discount to the Consumer Discretionary sector as a whole and appears to be oversold, absent any housing crisis on the horizon. Pent-up demand is evident in the Bureau of Economic Analysis's private fixed residential investment (PFRI) figures, as summarized by Bank of America research. The data suggests that \$1.25 trillion in underinvestment has built up over the past two decades, and can work to support growth and offset waning sentiment should a hard landing be realized.

Accumulated Underinvestment Over the Last 2 Decades



Banking Overview

Inflationary pressures and quantitative tightening are accelerating the credit cycle for banks. Higher interest rates are supporting loan growth during a time when deposit growth is slowing. This squeezes liquidity, forcing banks to fund loan growth by raising deposit costs and borrowing from the banking system. Loan growth needs to continue to trend higher in order to support net interest margins into 2023. Capital is also getting squeezed due to regulatory requirements.

Large Cap Banks

Total Loans and Leases Growth



Total Y/Y % Deposit Growth



According to Betsy Graseck at Morgan Stanley, tangible common equity ratios are at a level below that of the last four recessions. She has reined in her net interest margins on rising deposit betas, stopped buybacks through 2Q 2023, pushed the investment bank rebound to end of 2023, and is accounting for higher provisions.

We anticipate a pause by the Fed within the next 3-5 months, as tighter policies work their way through the system. The potential to avoid a hard landing exists in part to the aggressive interest rate policy underway since the beginning of the year. A slowdown that avoids any sustained period of unemployment growth could reduce credit loss builds and limit downside for banks.

Our overweight in banks is based upon valuations that have likely already priced in a soft to moderately hard landing. At a 10.9x trailing 12-month price to earnings ratio, banks are trading at 53% of the S&P multiple. Over the past three decades, these stocks have traded closer to 81% of the benchmark. Similarly, at 1.18x price to book ratio, banks have traded at 30% of the S&P index as compared to a long-term average of 52%.

Semiconductor Overview

U.S. semiconductor stock performance has been very weak in 2022, falling nearly 40% year-to-date against a backdrop of slowing global economic growth that triggered a cyclical downturn in the semiconductor sales cycle. After lagging behind the broad equity market, we believe the technical conditions are now relatively oversold, and sentiment towards the sub-group is very negative, thus implying that there is a reasonable expectation for a near-term bounce in relative performance.



Much of the cyclical headwinds facing the industry appear to have been fully discounted. However, it is important to recognize that this year's decline in semiconductor shares comes after a period of tremendous outperformance in 2020-2021 that saw chip stocks rise by more than 25% in Q4 of last year alone.

During this time, the industry experienced an unprecedented run of revenue and earnings growth, driven by remote work and learning, and exacerbated by acute supply chain shortages and double ordering by customers. Slowing global economic growth has resulted in inventory gluts across numerous semiconductor end-markets, which has taken considerable time to unwind. The implication is that the industry downturn is near completion and still warrants our current exposure to the sub-group.

Keep in mind that there remains some near term uncertainty to the relative earnings outlook of the group. The U.S. government's recently announced ban on the exports of advanced semiconductors and chip equipment to China adds significant uncertainty. This tipped the risk-reward for these stocks this year and warrants some caution in adding to the subgroup until we see clear evidence a trough has formed in demand.

According to the Semiconductor Industry Association, worldwide semiconductor sales fell 3% on a year-over-year (YoY) basis in September, the last month for which data is available. September marked the first month since January 2020 that the annual growth in sales contracted. Semiconductor demand growth is correlated with global economic momentum, as proxied by the global manufacturing PMI. The latter is likely to soften further in the coming months as the lagged impacts of central bank rate hikes weigh on global economic activity. This will potentially put some downward pressure on semiconductor sales growth in the near term.

We expect further weakness in semiconductor and chip equipment demand to detract from forward earnings momentum. Against this backdrop, it is difficult to envision the chip stocks enjoying a sustained rebound in relative performance into an expected year-end market rally. If history is any proxy, the relative share prices of semiconductor companies tend not to make a defined low in their share prices until their absolute and relative forward earnings growth hit their troughs. Given these developments, we are patient and cautious before building back exposure to these stocks.

IN CONCLUSION:

At current levels, the Standard and Poor's 500 implies a forward price to earnings ratio of 16.6 X and is consistent with a soft-landing scenario. After mid-term elections, the markets tend to perform well and we do not anticipate this quarter being any different. Earnings estimates are inflated when compared to narrowing profit margins on the back of rising labor and input costs. Value stocks should continue to outperform as long as earnings visibility is cloudy and central banks remain hawkish on forward interest rate guidance. As we navigate this later stage of the market cycle, a fully invested diversified portfolio comprised of dividend-paying, quality, low P/E should fare better.

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Any performance reference represents a hypothetical composite compiled from actual equity, fixed income or balanced client portfolios and includes cash. These three composites reflect aggregated returns that address differing objectives. As such, the performance of each composite does not reflect the actual total portfolio returns earned by our clients. The investment performance records are compiled from a capital weighted average of the equity, bond and cash components of a broadly representative group of discretionary accounts that meet certain minimum size thresholds.

No gross performance returns that are referenced that are calculated after brokerage commissions but before investment counsel fees are presented without the comparable net performance figures after both commissions, investment counseling fees and other custodial charges. The net counseling fees are the actual average counseling fee calculated across all the portfolios included in the composite. All performance figures are presented on a time-weighted total return basis and assume all income is reinvested. The investment advisory fees are disclosed in Part II-A of the Investment Form ADV. Some clients may benefit from available discounting in the management fee schedule associated with the overall size of the portfolio. Management fees will reduce overall returns to the client.

The composites were created in 2001 and the inception dates start on August 17th, 2001. The composites include only discretionary fee-paying accounts managed in the strategies, and additional information associated with the composites are available such as: dispersion in individual portfolio results as well as the % of the firms AUM in the strategy. All performance calculations are presented within the GIPS® guidelines of the CFA Institute. The CFA institute does not endorse or promote this organization nor does it warrant the accuracy of the content herein.

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