March 2022

From the front page of this weekend's WSJ:

Stocks Cap Wild Quarter To Notch Big Gains

Nasdaq turns in its best performance since 2020 as tech sector proves buoyant

BY AKANE OTANI

Markets showed their resilience in the first quarter, despite being rocked by shock waves that few anticipated.

Investors began the year feeling largely upbeat. Inflation appeared to be subsiding, and many bet that would lead the Federal Reserve to switch quickly from raising interest rates to cutting them.

Then economic data started coming in hot. Stocks and bond prices slid, hit by worries that the Fed would likely have to keep rates higher for longer.

The biggest shock of the quarter came in March, when Silicon Valley Bank and Signature Bank collapsed. Bank stocks tumbled. Credit Suisse Group AG came to the brink of failure, forcing rival bank UBS Group AG to arrange a hasty takeover. The biggest U.S. banks scrambled to shore up First Republic Bank to stop growing panic from taking down more lenders.

In the face of significant uncertainty, markets proved to be more buoyant than many investors thought possible.

The S&P 500 rose 7% in the first quarter, while the Dow Jones Industrial Average added 0.4%. The Nasdaq Composite soared. The technology-heavy index jumped 17%, outperforming the Dow industrials by the widest margin since 2001. Overall, it was Nasdaq's best quarter since the second quarter of 2020.

Meanwhile, bond prices climbed. The yield on the 10year U.S. Treasury note, which influences everything from mortgage rates to student loans, fell to 3.491% from 3.826% at the end of 2022. That marks its biggest quarterly decline since 2020. ...

A widely anticipated recession has failed to materialize, at least so far. The labor market has remained robust, even with a pickup in layoffs in the technology sector in recent months. And inflation, while still high, has continued to ease. Data showed consumer prices rose 6% from a year earlier in February, the smallest annual gain since September 2021. ...

Recent projections show Fed officials expect the federal-funds rate to rise to at least 5.1% from its current range of 4.75% to 5%. That suggests the Fed could push through one more quarter-point interest-rate increase and then hold rates at that level for the remainder of the year.

Yet Wall Street has once again grown more confident that the Fed will begin cutting rates as soon as the second half. Derivatives markets show traders expect the federal-funds rate to peak at around 4.9% in May, then fall to about 4.4% by the end of the year, according to FactSet. ...

Heightened expectations for rate cuts have driven investors into many of the stocks that were among the worst hit in last year's market selloff. ...

Bitcoin also jumped. The cryptocurrency traded above $28,000 on Friday, up around 71% for the quarter.

Meanwhile, many of last year's biggest winners have lagged behind. Energy stocks, which soared in 2022, fell in the first quarter. So did crude oil prices. ...

From March 30th's Global Investment Strategy:

Second Quarter 2023 Strategy Outlook: 1998 Or 2008?

I. Macroeconomic Outlook

Yet Another Banking Crisis?

Warren Buffet once colorfully said, "Only when the tide goes out do you learn who has been swimming naked."

The tide finally went out in March. The collapse of Silicon Valley Bank and Signature Bank, followed by the forced marriage between UBS and Credit Suisse, brought back memories of 2008.

The global economy is probably not on the verge of another financial crisis. Banks are much better capitalized than they were in 2008, the quality of loan books is stronger, and there exists a wider suite of tools for mitigating panic.

In 2008, there was little clarity on what a mortgage was worth. Investors just assumed the worst. This triggered a vicious cycle where falling MBS prices made banks less willing to extend credit, leading to a weaker economy and even lower MBS prices.

This time around, the prospect of a weaker economy is leading to higher Treasury bond and MBS prices, which is helping banks that hold these long-dated securities. In this sense, what is happening today looks more like a self-limiting cycle than a self-perpetuating one.

Still, a credit squeeze is probable. Unlike residential mortgages, commercial real estate is under pressure. Given the glut in office space, that pressure will continue to mount.

To make matters worse, a recent study estimated that banks were sitting on $1.75 trillion in unrealized losses on their securities and loans as of the end of 2022.

Footloose Depositors

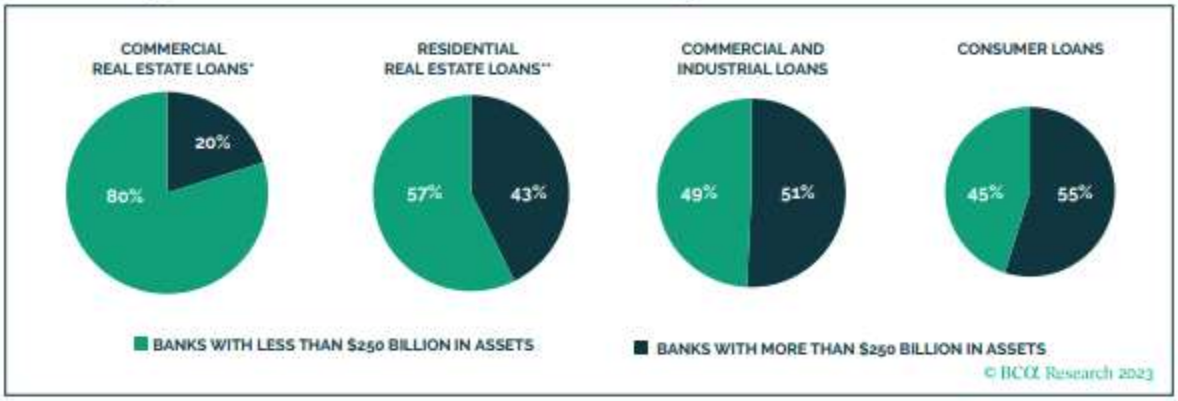
In the normal course of operations, the stickiness of deposit rates provides banks with a built-in buffer: Higher rates lower the present value of banks' assets, but they also raise the franchise value of their deposit base. However, this buffer can only exist if savers are willing to keep their deposits in low-yielding accounts. If they start pulling money out of a bank, the bank will have no choice (if it is lucky) to fund itself at market rates.

This is a particularly big problem for smaller banks. Before the 2008 Global Financial Crisis, the loan-to-deposit ratio was consistently lower for smaller banks than larger banks. Today, the opposite is true (Chart 3).

Close to half of US deposits reside in banks with less than $250 billion in assets. The vast majority of these smaller banks are not subject to the same stringent capital and liquidity requirements that the larger systemically important financial institutions (SIFIs) are subject to.

CHART 5

Economically, Small Banks Tend To Punch Above Their Weight



* INCLUDES COMMERCIAL, MULTI-FAMILY RESIDENTIAL, CONSTRUCTION & LAND DEVELOPMENT, AND FARMLAND REAL ESTATE LOANS.
** INCLUDES SINGLE-FAMILY REAL ESTATE LOANS.
NOTE: DATA AS OF Q4 2022. INCLUDES ALL FDIC-INSURED INSTITUTIONS (COMMERCIAL BANKS AND SAVINGS INSTITUTIONS).
SOURCE: BCA CALCULATIONS BASED ON FEDERAL DEPOSIT INSURANCE CORPORATION (FDIC) DATA.

Ironically, the uneven playing field in regulatory oversight has itself become a source of systemic risk, as it has invited deposit flows from smaller banks to larger, better-capitalized ones. In the absence of a concrete guarantee on all bank deposits, money will continue to migrate to the largest banks.

Bank lending standards, which reliably lead credit growth, were tightening even before the latest turmoil. The need for smaller banks to preserve liquidity in the face of deposit flight, rising funding costs, and increased regulatory scrutiny will only exacerbate this trend.

Considering that smaller US banks account for about half of C&I lending and more than half of commercial and residential mortgage lending, a further tightening in credit conditions will weigh on growth (**Chart 5**).

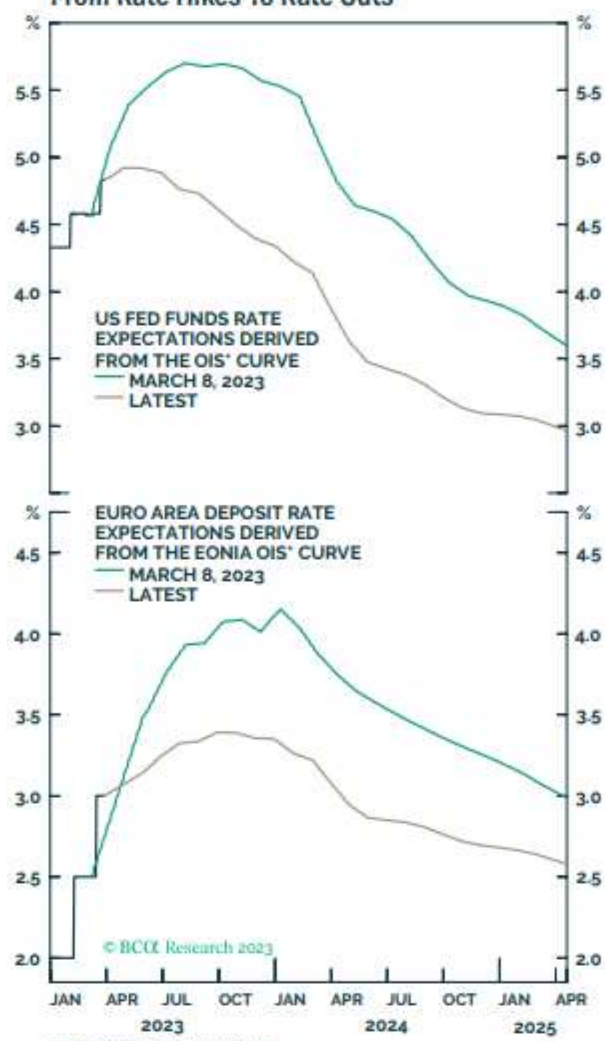
Lower Rates Are a Mitigating Force If that were all there was to the story, it would be easy to conclude that, all things equal, recent banking strains will expedite the onset of the next recession. All things are not equal, however. As **Chart 6** shows, interest rate expectations have plummeted over the past month. Lower rates will cushion the blow to growth.

It is possible that lower bond yields will fully offset the hit to aggregate demand from a further tightening in bank lending standards.

If that were to occur, stocks would benefit (or at least not suffer as much). This is simply because the discount rate would end up being lower in a scenario where growth slowed because banks became more conservative compared to a scenario where growth slowed because the Fed had to raise rates to over 6%.

CHART 6

From Rate Hikes To Rate Cuts



* OVERNIGHT INDEX SWAPS.

It is even possible that lower interest rates will end up more than offsetting the drag on growth from tighter bank lending standards.

The end result could resemble what transpired in 1998. In the autumn of that year, the Fed cut rates by 75 basis points in response to the collapse of Long-Term Capital Management. After bottoming on October 8, the S&P 500 proceeded to rise by 68% over the subsequent 17 months.

2% Inflation Without Recession: Mission Impossible?

Granted, the US economy was in good shape in 1998. Productivity was soaring, while inflation was well contained.

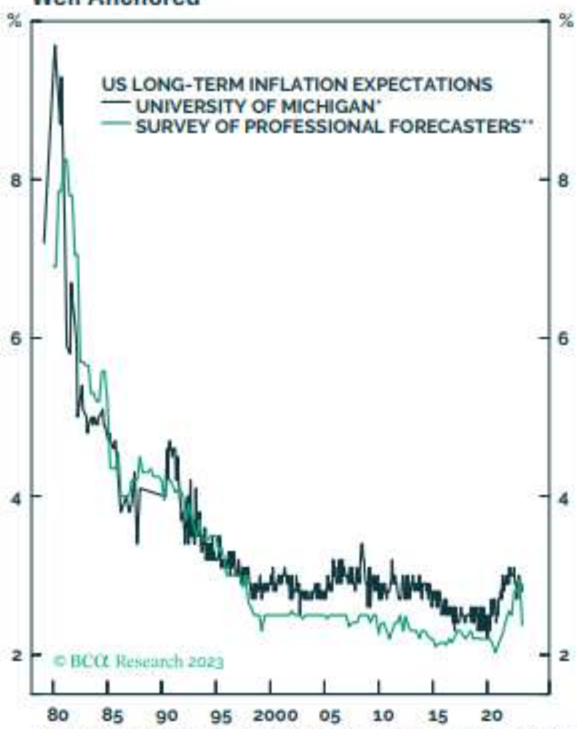
Thus, for equity prices to rise over the remainder of 2023, as they did in 1999, not only would economic growth need to remain resilient, but inflation would need to fall against a backdrop of continued low unemployment.

How likely is that? Our guess is that most observers would say "not very likely." Perhaps ... the odds of a benign disinflation where growth temporarily stays resilient and inflation falls anyway are not as low as widely believed.

... When there is a lot of slack in the labor market, a decrease in the unemployment rate will do little to lift wages or prices since there will still be many people keen to find work. Only when labor market slack is fully absorbed can inflation take off. ...

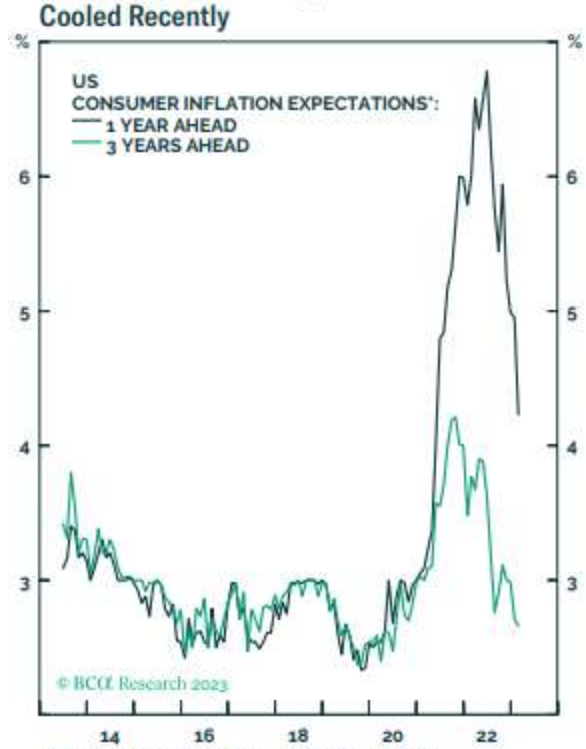
Early on in the pandemic, the combination of fiscal stimulus and monetary easing raised demand while the withdrawal of workers from the labor force and supply-chain disruptions lowered supply. Nevertheless, because

CHART 12
Long-Term Inflation Expectations Remain Well Anchored



* MEDIAN INFLATION EXPECTATIONS OVER THE NEXT 5-TO-10 YEARS. SOURCE: UNIVERSITY OF MICHIGAN, SURVEY OF CONSUMERS.
** MEDIAN CPI INFLATION RATE FORECAST 10 YEARS AHEAD. SOURCE: FEDERAL RESERVE BANK OF PHILADELPHIA.

CHART 13
Short-Term Inflation Expectations Have Cooled Recently



* SOURCE: FEDERAL RESERVE BANK OF NEW YORK.

there was still sufficient slack in the labor market, inflation barely rose. ...

While it did take a while, the Fed eventually responded to higher inflation by raising interest rates. This helped to cool the economy in the second half of 2022. ... this cooling largely manifested itself in the form of lower inflation rather than rising unemployment. ...

A Detour on the Road to Disinflation

What came next was a bit of a surprise. Rather than continuing to fall, inflation started to rise early this year. ...

The Atlanta Fed's GDPNow model estimates that real GDP grew by 3.2% in Q1. Private final domestic demand increased by 4.1%. While these numbers probably overstate what actually transpired, they do suggest that the economy reaccelerated at the start of the year.

It is probable, though not inevitable, that aggregate demand will start to fall off again over the coming months as payroll growth slows, and the lagged effects of tighter monetary policy and stricter bank lending standards work their way through the economy. That should help lower inflation.

Unlike in the 1970s, long-term inflation expectations are well anchored (**Chart 12**). While short-term inflation expectations did rise in the midst of the pandemic, they have declined quite noticeably in recent months (**Chart 13**). ...

The Three Components of Inflation

Chair Powell has stressed the utility of breaking the inflation basket into three components: 1) goods; 2) shelter; and 3) services excluding shelter.

The good news is that disinflation is probable in all three categories.

Relative to their pre-pandemic trend, goods prices are still 8% above services prices. Unless services inflation explodes higher, goods inflation will remain contained as relative goods prices continue to sink.

The best leading indicator for shelter inflation is rents on newly leased properties. According to Zillow and Apartment List, they have barely risen in recent months (**Chart 15**). A simple regression of new rental prices on shelter inflation suggests that the latter will fall sharply over the remainder of the year.

Services inflation ex shelter is largely governed by the trend in wages. The growth in average hourly earnings has cooled from over 7% to around 5% of late (**Chart 17**). While that is still too high, most leading indicators suggest that wage growth will continue to fall.

Arguably the best leading indicator for wage growth is the quits rate. Unlike say, job openings, which are difficult to measure accurately, the fraction of workers quitting their jobs every month is a robust measure of how confident people feel about their ability to find new work. ... the quits rate has retraced about

CHART 15
Rents On Newly Listed Properties Are No Longer Rising Quickly

* SOURCE: ZILLOW.
** SOURCE: APARTMENT LIST.
NOTE: SERIES SHOWN SEASONALLY ADJUSTED.

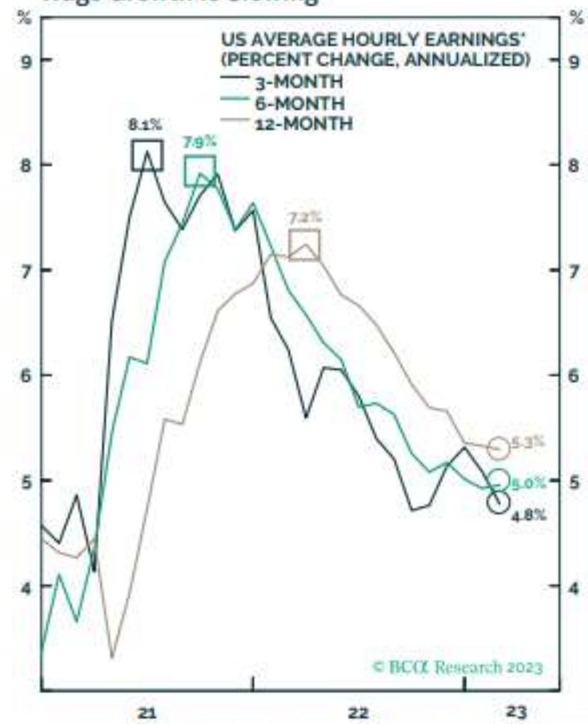
two-thirds of its pandemic surge, suggesting that workers no longer have as much bargaining power as they once did. Business surveys of planned compensation growth tell a similar story.

Could aggregate demand retreat ... over the next few months, at which point any further decline in demand will usher in a recession? That is certainly possible if ongoing bank stresses trigger a full-blown crisis. Absent that, however, our best bet is that the US economy will only succumb to a recession at some point in 2024.

Job openings are coming down, but they are still quite elevated across most industries. For the foreseeable future, most workers who lose their jobs will not have too much difficulty in finding new ones.

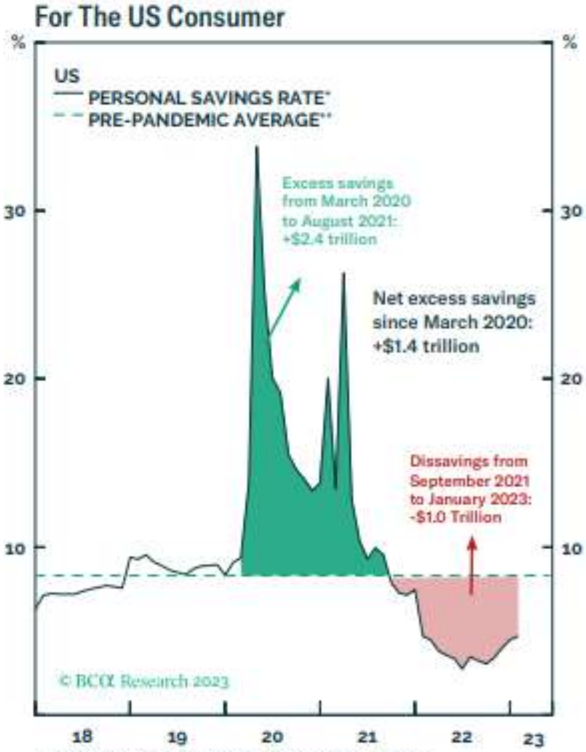
Households are still sitting on about $1.4 trillion in pandemic savings (**Chart 20**). While the bulk of those savings are held by middle-to-higher income households, these are also the households that contribute the most to spending. Despite saving more of their income than other groups, the top 20% of US income-earners accounts for 39% of all consumer spending

CHART 17
Wage Growth Is Slowing



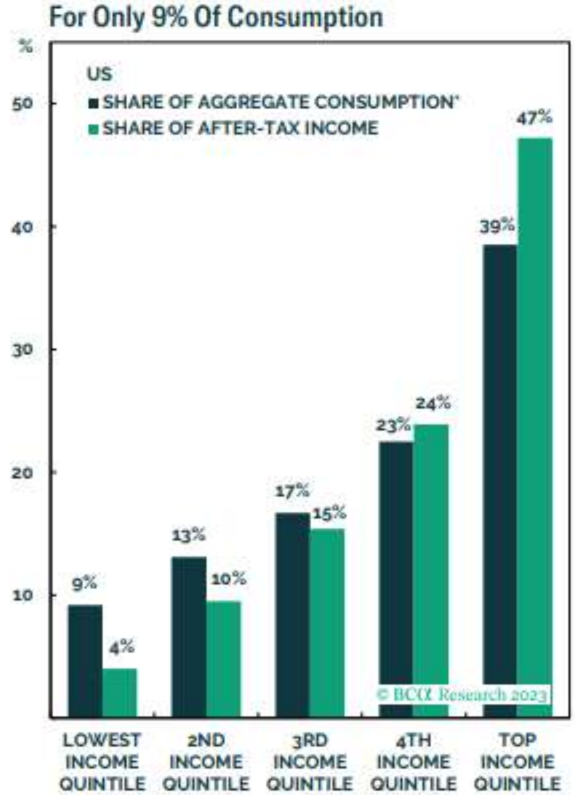
* PRODUCTION AND NONSUPERVISORY EMPLOYEES IN ALL PRIVATE INDUSTRIES.
NOTE: ADJUSTED FOR CHANGING COMPOSITION OF EMPLOYMENT IN MAJOR INDUSTRIES. THE OVERALL MONTHLY RATE OF CHANGE IN EARNINGS IS CALCULATED AS A WEIGHTED-AVERAGE OF INDUSTRY-LEVEL EARNINGS. THE INDUSTRY WEIGHTS ARE CALCULATED USING PRIOR MONTH'S TOTAL HOURS WORKED.

CHART 20
Excess Savings Provide Some Insulation For The US Consumer



* SHOWN AS A PERCENT OF DISPOSABLE INCOME.
** AVERAGE SAVINGS RATE FROM THE BEGINNING OF 2018 UNTIL THE START OF THE PANDEMIC.
NOTE: THE CALCULATION OF EXCESS SAVINGS ASSUMES A PRE-PANDEMIC BASELINE WITH 4% DISPOSABLE INCOME GROWTH AND 8.3% SAVINGS RATE.

CHART 21
The Bottom 20% Of Income Earners Account For Only 9% Of Consumption



* ANNUAL AGGREGATE EXPENDITURES.
SOURCE: BUREAU OF LABOR STATISTICS (BLS), CONSUMER EXPENDITURE SURVEY. DATA AS OF 2021.

(**Chart 21**).

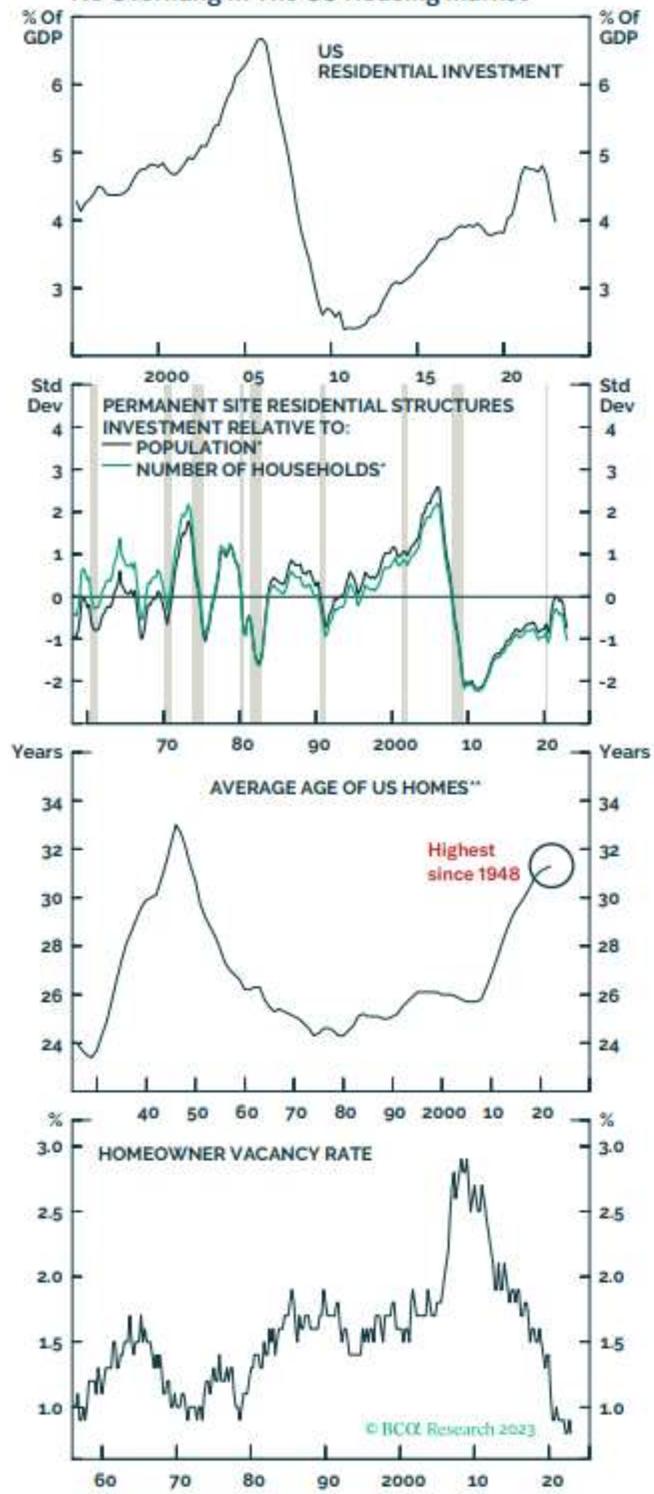
The inventory-to-sales ratio among retailers has risen over the past year. However, it is still well below pre-pandemic levels, implying little need for retailers to cut back on orders.

On the investment front, while corporate spending plans have cooled, there is a limit to how much capital expenditures can decline. In real terms, core capital goods orders are more than 20% below where they were in 2000. Manufacturing capacity has barely grown in two decades.

Likewise, with residential investment dropping to only 4% of GDP in Q4 2022, there is a limit to how much further homebuilding can decline (**Chart 24**). The average age of US homes has risen to 31 years, the highest since 1948. The homeowner vacancy rate remains near a record low of 0.8%. The inventory of homes for sale has risen, but is still 19% below pre-pandemic levels.

CHART 24

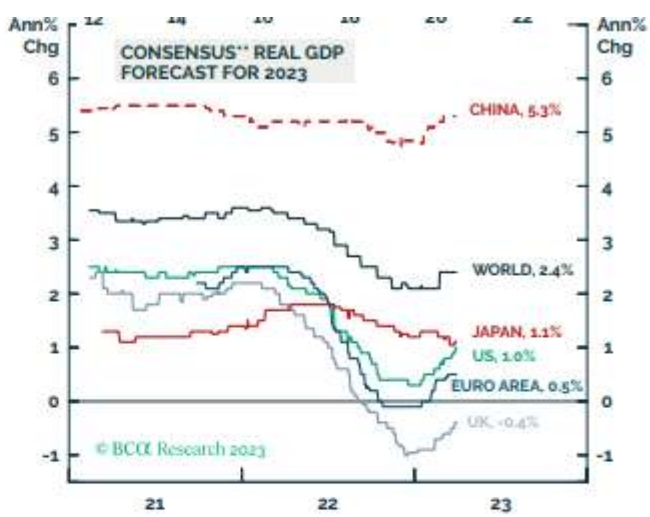
No Overhang In The US Housing Market



* SHOWN STANDARDIZED.
** CURRENT-COST AVERAGE AGE OF PRIVATE RESIDENTIAL FIXED ASSETS. SOURCE: BUREAU OF ECONOMIC ANALYSIS (BEA).
NOTE: SHADED AREAS DENOTE NBER-DESIGNATED RECESSIONS.

Global Growth Firming: Europe Turns the Corner

As in the US, growth abroad accelerated at the start of the year. Purchasing managers' indices have rebounded, confidence has risen, and consensus growth forecasts (** SOURCE: BLOOMBERG FINANCE L.P) have perked up.

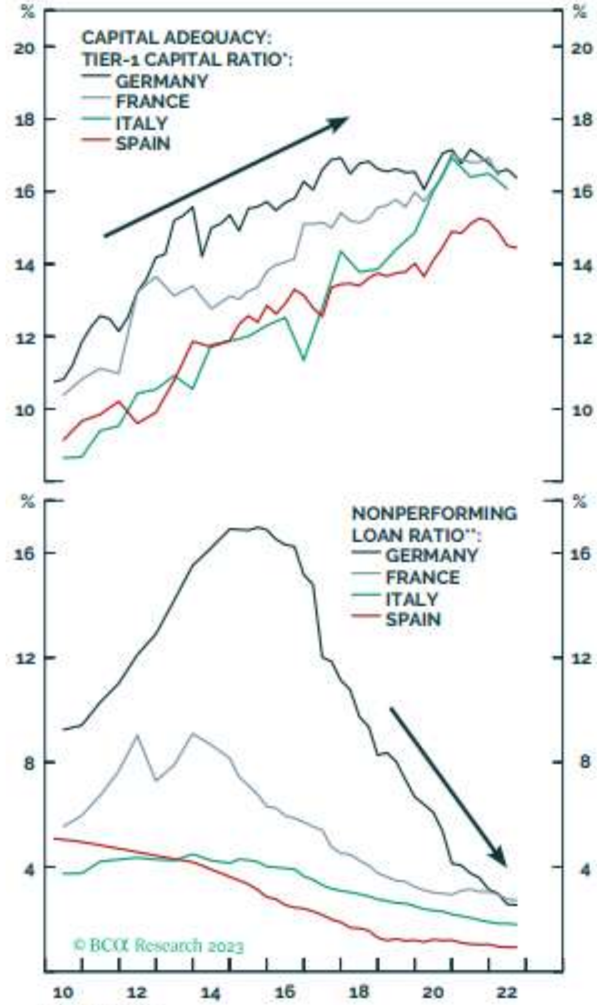


In Europe, falling natural gas prices have dampened fears of an imminent recession. While the warm winter has undoubtedly helped to keep energy costs down, this is not the only factor at work. ... natural gas futures have declined out to end-2025. All the investment in new LNG terminals and gas pipelines has created a newfound sense of optimism that Europe has finally freed itself from its unhealthy dependence on Russian gas.

Fiscal policy has also helped. European governments have either doled out or plan to dole out €750 billion (4.3% of GDP) in support for the private sector to mitigate the energy crunch.

As in the US, tighter bank lending standards and slowing credit demand will weigh on European growth. Fortunately, most European banks are well capitalized, and hence are unlikely to face the sort of existential threats they faced a decade ago (**Chart 29**). While European bank CDS spreads have widened in recent weeks, they are still below where they were last autumn.

CHART 29
...But Healthy Bank Balance Sheets Will Buffer The Blow



* SOURCE: IMF.
** SOURCE: IMF AND EUROPEAN CENTRAL BANK (ECB).

Structurally, the imbalances that paved the way for the euro crisis have abated. As Chart 31 illustrates, unit labor costs in the peripheral economies have now largely converged with Germany. Notably, the Italian BTP-German bund spread has barely widened in recent weeks (Chart 32).

China: From Reopening Boom to Housing Bust?

China continues to benefit from reopening. Mobility measures are recovering while the PMIs have soared.

There is little doubt that the post-Covid reopening boom will fade. However, BCA's Chief EM strategist, Arthur Budaghyan, believes that the government will take steps to limit the downside risks to the economy. He expects the credit and fiscal spending impulse to move broadly sideways this year, consistent with trend-like growth.

Housing is the biggest wildcard facing the Chinese economy. Over a multi-year horizon, it is difficult to be bullish on the Chinese housing sector. Chinese homes are among the most expensive in the world. Just like Japan in the early 1990s, the working-age population is set to shrink, which will sap the demand for housing.

Nevertheless, over a 12-month horizon, China's housing sector could surprise on the upside for two reasons: First, the government is providing developers with financing to allow them to complete a large pipeline of

TABLE 1
Unemployment Was Flattish For Almost Two Years Prior To Recent US Recessions

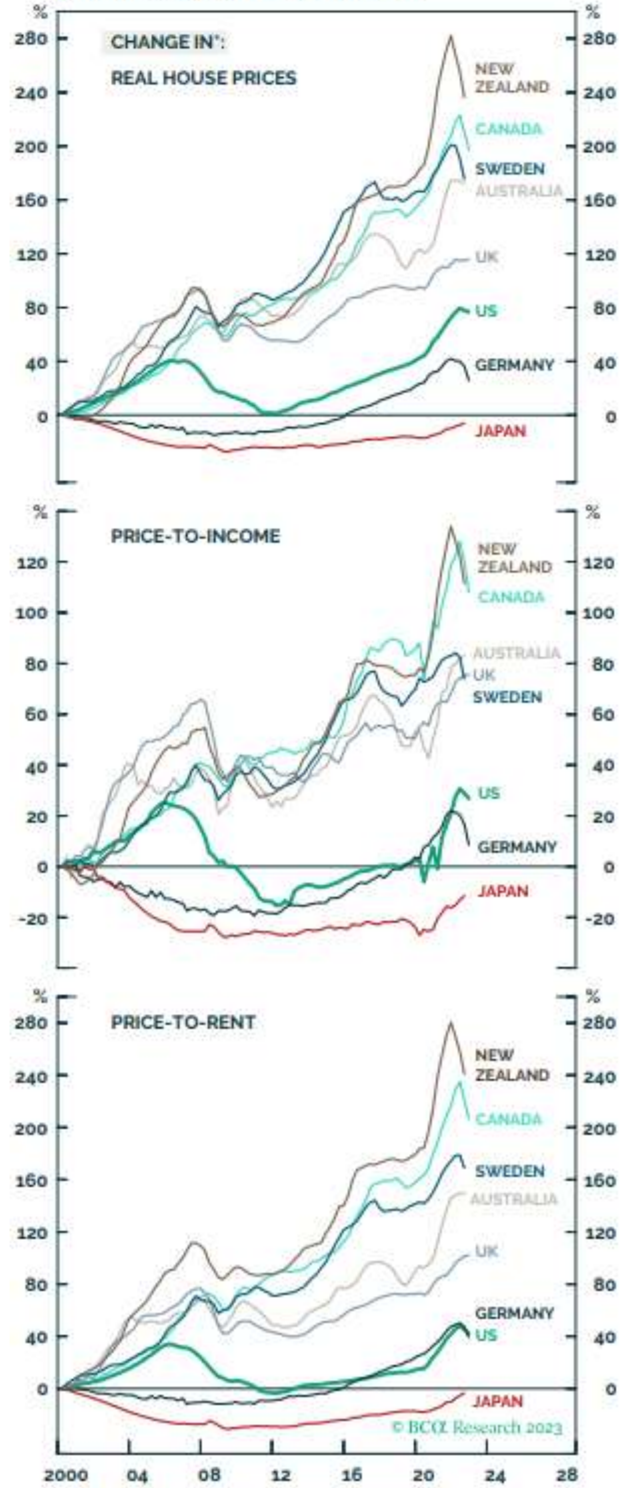
US UNEMPLOYMENT RATE PRIOR TO RECESSIONS				
	MINIMUM (%)	MAXIMUM (%)	DIFFERENCE (%)	DURATION (MONTHS)
APR 1978 TO DEC 1979	5.6%	6.2%	0.6%	21
SEP 1988 TO JUN 1990	5.0%	5.4%	0.4%	22
MAR 1999 TO JAN 2001	3.8%	4.3%	0.5%	23
JAN 2006 TO NOV 2007	4.4%	4.8%	0.4%	23
MAY 2018 TO FEB 2020	3.5%	4.0%	0.5%	22
SINCE MARCH 2022	3.4%	3.7%	0.3%	12

projects. This will support construction activity.

Second, after hunkering down for three years, Chinese households are sitting on a huge amount of pandemic savings. Historically, the Chinese public has tended to invest its excess savings in the housing market. Perhaps as a harbinger of things to come, both home prices and new home sales have rebounded over the past two months.

CHART 39

Developed Economies With The Most Severe Imbalances Will Be Hardest Hit



* SERIES REBASED TO Q1 2000 = 0%. SOURCE OECD.
NOTE: 2022 VALUES FOR AUSTRALIA ARE ESTIMATES BASED ON DATA FROM THE DALLAS FED'S INTERNATIONAL HOUSE PRICE DATABASE.

Darker Outlook Beyond 2023

While we expect the global economy to outperform expectations in 2023, the picture is likely to darken in 2024.

In the US, households will have run down most of their pandemic savings by the middle of next year, leading to lower spending. Job openings will have likely fallen back to pre-pandemic levels. Feeling more nervous about their job prospects, workers will cut back on consumption. Tighter bank lending standards will increasingly weigh on credit growth.

US home prices, which have already fallen by 7.4% in real terms from their peak based on the Case-Shiller index, will continue to slide, producing an ever-larger negative wealth effect. A rising share of new homeowners will be saddled with higher-rate mortgages, resulting in lower discretionary spending.

The Fed will start cutting interest rates in 2024, but given the lags in monetary policy, this will not be enough to preclude a mild recession.

Each one of the last five recessions has been preceded by a period lasting 21-to-23 months where the unemployment rate has moved sideways after falling below its equilibrium level (**Table 1**). The US unemployment rate has been moving sideways since March 2022. This suggests that the next recession could begin in the first half of next year.

If the US falls into recession in 2024, this will likely drag down growth in the rest of the world. While the extent of the downturn will vary across countries, those with the most severe imbalances will be the hardest hit. In that regard, we would highlight Canada, Australia, New Zealand, and Sweden as potential casualties, given their overvalued real estate markets (**Chart 39**).

II. Financial Markets

A. Global Asset Allocation

Neutral Allocation to Stocks and Bonds

Going into this week's stock market rally, sentiment was very dour. Bears exceeded bulls by 28 percentage points in last week's AAII survey, a gap that only improved to 23 points as of this Wednesday. On average, bulls have outnumbered bears by 7 points in the 36-year history of the AAII survey.

According to Bank of America's Global Fund Manager Survey, fund managers were two standard deviations overweight bonds and two standard deviations underweight stocks in March (**Chart 40**).

Against this gloomy backdrop, it did not take much good news to trigger a relief rally. It is possible the rally will continue into the summer months. However, with the S&P 500 now back above 4,000, we think it makes sense to take some chips off the table.

Stocks do best when economies have plenty of room to grow. Considering that unemployment is very low across the major economies, that is not the case today (**Chart 41**). If a recession begins next year in the major developed economies, as we expect, stocks will fall from current levels.

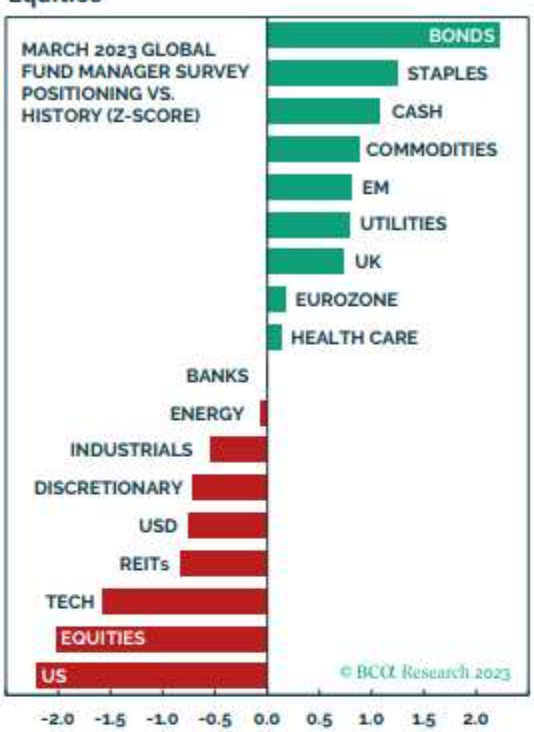
With that in mind, we are shifting our 3-month equity allocation from overweight to neutral (by lifting our cash recommendation from underweight to neutral). We remain neutral on both bonds and stocks over a 12-month horizon but expect to upgrade the former and further downgrade the latter in the second half of this year.

B. Equities Earnings

Estimates Should Temporarily Stabilize

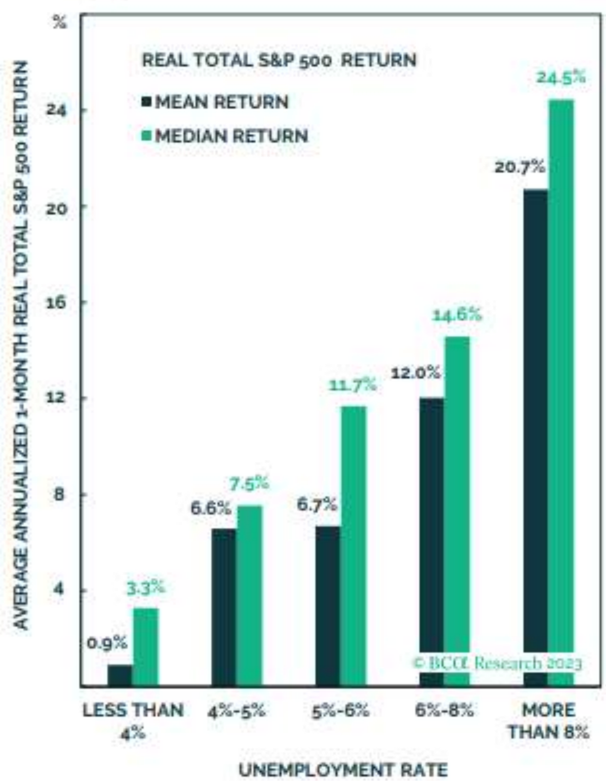
One reason we are not inclined to turn outright bearish on stocks yet, despite expecting a recession in 2024, is

CHART 40
Institutional Investors Are Underweight Equities



SOURCE: BOFA GLOBAL FUND MANAGER SURVEY.

CHART 41
Equity Returns Are Low When Unemployment Is Low



because we see scope for earnings to stabilize, at least temporarily.

Analysts typically revise up earnings estimates when economic growth surprises on the upside (**Chart 42**). The recent jump in both the US and global economic surprise indices into positive territory is encouraging in that regard.

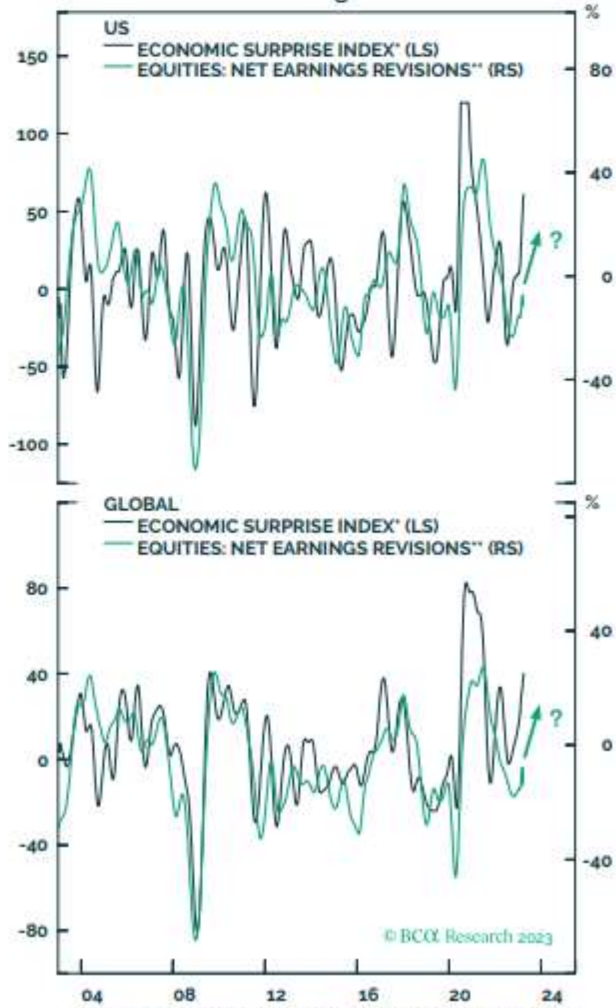
US 12-month forward earnings estimates rose in March for the first time since June 2022. Outside of the banking sector, where rising deposit rates and higher loan loss provisions will dampen earnings, estimates could surprise on the upside in the remainder of the year, before falling again in 2024.

For calendar year 2023, US earnings estimates ex energy have declined by 15.4% since the beginning of last year, or by more than 20% in real terms. For calendar year 2024, ex energy earnings estimates have fallen by 11.1% since July 2022.

Reported earnings have generally tracked the direction of earnings estimates. In Q4 2022, S&P 500 earnings were down 3.2% year-over-year.

It is worth noting that S&P 500 sales still managed to grow by 5.8% in Q4 2022 over the prior year. As a result of the divergence between earnings and sales growth, profit margins have fallen back to where they were in mid-2019.

CHART 42
Positive Economic Growth Surprises Tend To Bode Well For Earnings



* ROLLING 3-MONTH STANDARD DEVIATION OF DATA SURPRISES; US ECONOMIC SURPRISE INDEX TRUNCATED AT 120. SOURCE: CITIGROUP GLOBAL MARKETS INC.
** NET POSITIVE REVISIONS AS A SHARE OF TOTAL REVISIONS. SOURCE: REFINITIV / IBES.
NOTE: SERIES SHOWN SMOOTHED EXCEPT FOR LATEST DATA POINT.

Favor Non-US Equities for Now

Earnings have held up better outside the US over the past two quarters, especially when measured in dollar terms. At least for the remainder of this year, we expect non-US stocks to outperform their US peers. Not only has the cyclical acceleration in growth been stronger outside of the US, but valuations are much more favorable abroad. Non-US equities currently trade at 12.5-times forward earnings, compared to 18.2-times in the US.

A softer dollar should also bolster non-US stocks (**Chart 45**). ...

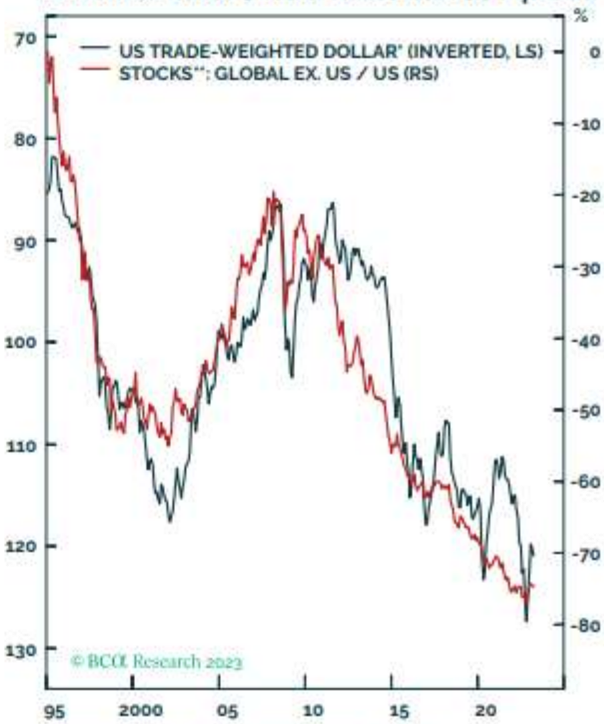
Since peaking in September 2022, the trade-weighted US dollar has depreciated by 6.8%. Despite this retreat, the greenback remains quite expensive, trading 19% above its Purchasing Power Parity (PPP) fair value. As **Chart 52** illustrates, the dollar's deviation from PPP has been a reliable guide to the long-term direction of the currency.

While valuations are an important driver of the dollar over the long run, business-cycle considerations dominate over shorter-term horizons.

In general, the dollar is a countercyclical currency, meaning that it tends to strengthen when global growth is weak and weaken when global growth is strong. This is especially the case when the acceleration in global

CHART 45

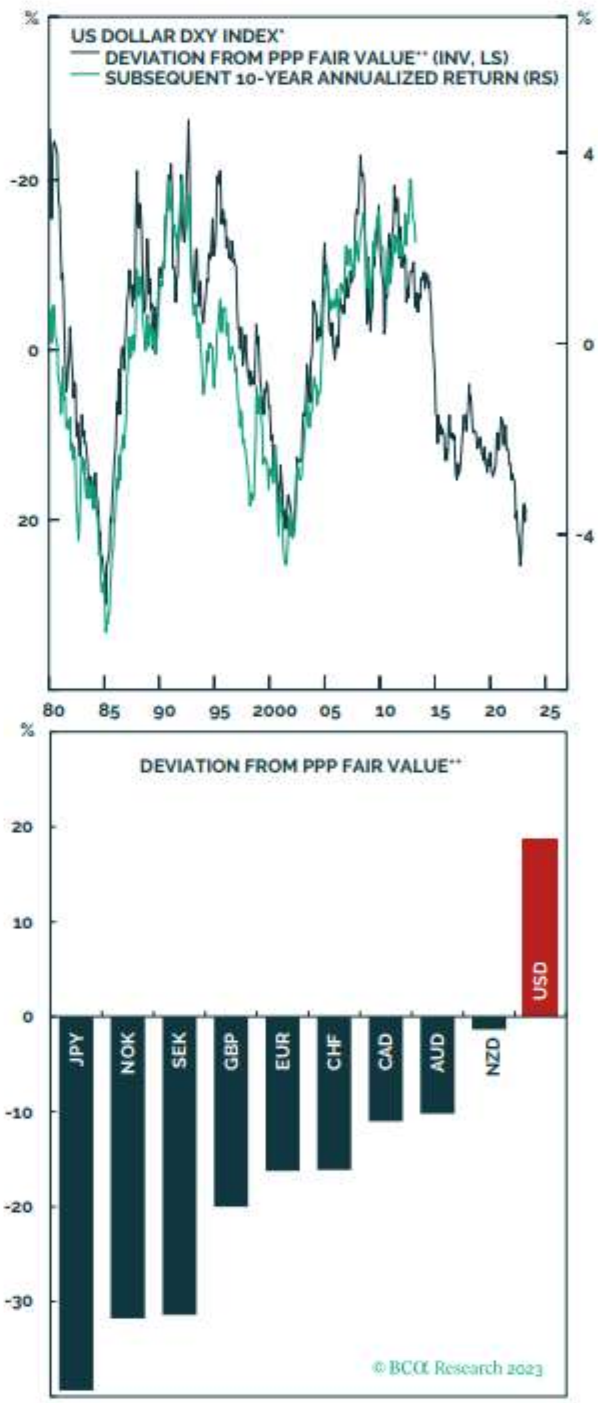
A Weaker Dollar Should Boost Non-US Equities



* BROAD, NOMINAL. SOURCE: FEDERAL RESERVE.
** IN US DOLLARS, REBASED TO JAN. 1995 = 0%.
SOURCE: MSCI INC. (SEE COPYRIGHT DECLARATION).

CHART 52

The US Dollar Remains Overvalued



* SOURCE: ICE FUTURES US.
** BCA PURCHASING POWER PARITY MODEL BASED ON ADJUSTED CPI. PLEASE REFER TO THE FOREIGN EXCHANGE STRATEGY JANUARY 20, 2023 SPECIAL REPORT TITLED "CURRENCY VALUATION AND LONG-TERM RETURNS: PART 1," FOR FURTHER DETAILS.

growth is more pronounced outside of the US, as has been true recently based on the movement in relative PMIs.

As with most currencies, interest-rate differentials are an important driver of the dollar. Real 2-year rate differentials have narrowed against the dollar since last October, which accounts for much of the dollar's weakness (**Chart 54**).

We do not have a strong view on how interest-rate differentials will evolve over the coming months. However, if the US experiences a mild recession in 2024, rate differentials will probably narrow further, given that the Fed has more scope to cut rates than other central banks.

In our base case of moderate growth this year and slower growth in 2024, the US dollar is likely to weaken. On both sides of that base case view, however, the dollar could strengthen.

On the one extreme, if US growth slows sharply because a full-blown financial crisis erupts, capital will flow into safe-haven US Treasuries, leading to a stronger dollar. This is precisely what happened in 2008.

On the other extreme, if growth fails to slow at all and the US experiences a second wave of inflation, then the Fed will have to hike rates, rather than cut them as the market expects. This would also cause the dollar to appreciate. ...

E. Commodities

Near-Term Upside for Oil ... but Pain Awaits in 2024

Consistent with our view that global growth will surprise positively over the remainder of 2023 but then begin to surprise negatively in 2024, we see near-term upside for commodity prices this year, with a more somber outlook unfolding next year.

The good news for commodities is that tight supply conditions will limit the extent of price declines during the next recession. Globally, capital spending per barrel of oil produced is down two-thirds from its peak (**Chart 55**). Most oil companies continue to prioritize returning cash to shareholders over new investment. ...

Over a multi-year horizon .... The transport sector currently accounts for about 60% of global petroleum demand. According to one poll, 40% of US households expect to buy an electric vehicle over the next five years, up from 15% in 2018. The shift towards electric vehicles will steadily erode the demand for oil.

Downgrading Gold

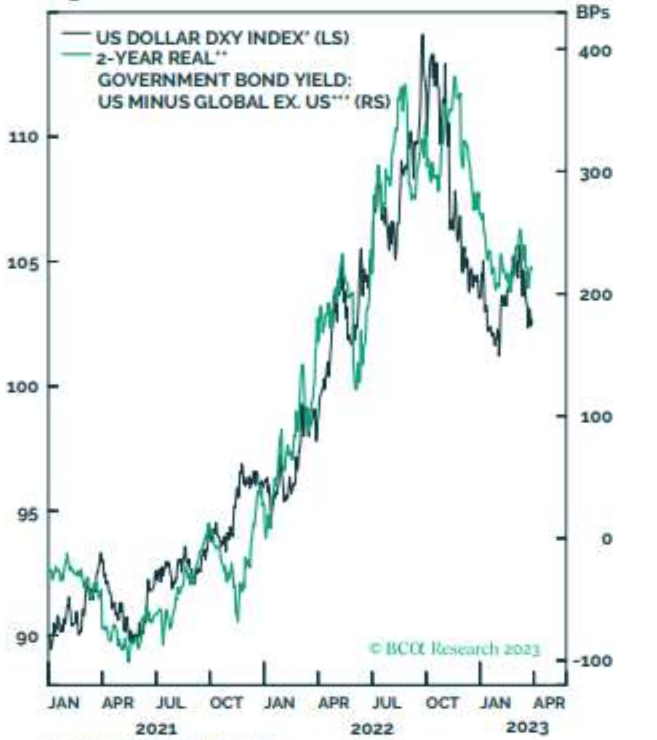
Gold prices have risen by 20% since November 3. High inflation, growing geopolitical risks, and most recently, fears over another banking crisis, have all buoyed gold prices.

Despite the latest rally, neither investor sentiment nor speculative positioning towards gold appear particularly stretched. The volume of gold held in all ETFs has declined by 12% since last April, a sign of restrained retail demand.

All that said, gold prices typically move in tandem with TIPS yields. That relationship broke down starting in late 2021, as gold prices remained resilient despite soaring real yields.

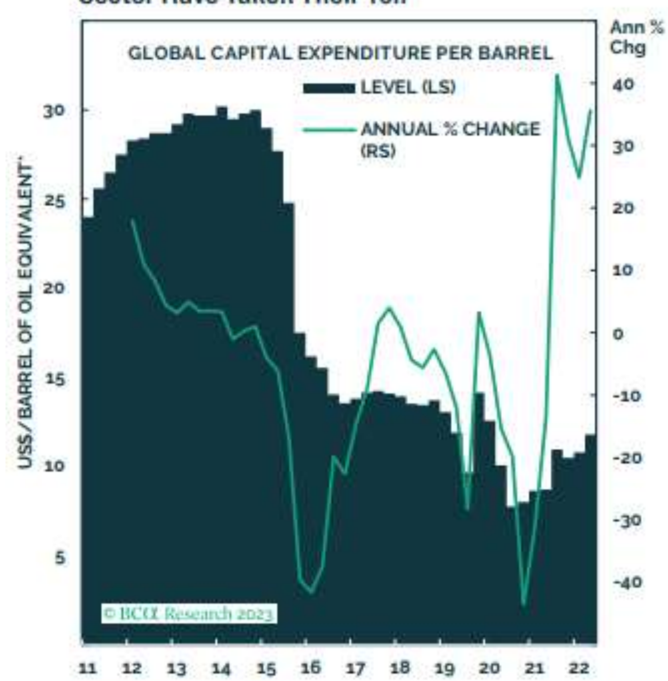
A reassertion of this relationship could see gold prices fall to about $1,200/oz from today's price of $1,980/oz. That is enough for us to recommend downgrading gold to underweight from neutral.

CHART 54
Real Interest-Rate Differentials Have Moved Against The Dollar Since October



* SOURCE: ICE FUTURES US.
** DEFLATED BY CPI SWAPS AND CORE CPI FOR CANADA AND SWITZERLAND.
*** WEIGHTED AVERAGE OF THE US DOLLAR DXY INDEX CONSTITUENTS.

CHART 55
Eight Years Of Underinvestment In The Energy Sector Have Taken Their Toll



* IN 2015 US DOLLARS.
SOURCE: US EIA.
NOTE: BASED ON PUBLIC FINANCIAL STATEMENTS FROM GLOBAL OIL AND NATURAL GAS COMPANIES. THE VALUE FOR Q4 2015 HAS BEEN INTERPOLATED.

Positions

PACW - Lots of Insider Buying in March among Regional Banks, but only one also met our Valuation criteria, with a PEG of 0.4. PACW had 10 insiders buying on 3/9&10 @ 15.07-22.16. We added 1% positions for 5 clients on the 15th @ 11.07 to this IVE System pick.

Insider Buying:

Trade Date↑	No. Part	Participants	Net Sell (Shares)	Net Buy (Shares)
03/10/2023	5	Eggemeyer John, Blake Christop...		36,808
03/09/2023	5	Taylor Paul, Black William, Mudi...		42,050