GAUGE SHIFTS LOWER AS MULTIPLE CATEGORIES GET DOWNGRADED

We’ve moved **U.S. Dollar** and **Technical Picture** to Unfavorable in light of recent developments. On the whole, the Gauge remains negative given restrictive **Monetary Policy**, sticky/structural **Inflation**, elevated market **Valuation**, and a decline of **U.S. Fiscal Health** amid rising interest costs and elevated spending.

**U.S. Dollar**: A strong dollar should mitigate U.S. inflation, but the current geopolitical environment makes a further flight to quality a risk for American exporters and emerging market economies. The greenback has risen nearly 7% off its July lows even though a mature Fed tightening cycle is typically associated with a weaker dollar.

**Technical Picture**: It would be hard to call the technical picture “favorable” with just 41% of S&P 500 firms’ share prices above their 200-day moving average. Small-caps and Banks are struggling, while the global backdrop is bifurcated at best.

On the positive side, the U.S. economy remains buoyant despite gas prices, a resumption of student loan payments, and other challenges to the consumer. In that regard, the employment picture remains key. Despite a decline in trailing earnings and profit margins, companies have, thus far, been loath to let employees go. Last week’s claims for unemployment insurance remain barely above 200,000. The ability of organized labor to earn wages and benefit concessions may suggest a structural change in the labor market.

From here, third quarter **Corporate Earnings** – and importantly, company guidance – will be critical given the recent rise in long-term interest rates. The decline in profit margins has stopped for the time being, and income on cash due to higher rates is helping to offset other areas of weakness.

This table shows the 16 factors we continually monitor to understand the current market environment for U.S. stocks. When there are 8 factors in each group, that is a neutral market environment. We are downgrading two categories to Unfavorable, putting the Gauge at **-8, Unfavorable** (this value being the sum of +4 and -12) amid a strong dollar, global and domestic political turmoil, worsening U.S. fiscal health, and structural inflation pressure.

**Strategas, a Baird Company’s, Market Gauge is meant to be a snapshot of a moment in time, and not a predictive tool. See page two for more on our 16 building blocks, and what we look for to label each one “Favorable” or “Unfavorable.”**
HOW DO WE CATEGORIZE EACH COMPONENT OF MARKET HEALTH?

Administration: Are White House and Congressional priorities market-friendly? How do they view taxes, regulation, trade, etc.?
Commodity Prices: Do commodity prices (e.g., gold, copper, oil) reflect economic growth or contraction?
Corporate Earnings: Are the earnings of U.S. companies growing or falling? Are profit margins expanding or contracting?
Demographics: Is the demographic trend (population growth, average citizen age, worker-to-retiree ratio) positive or negative?
Economic Growth: What is the recent trend in GDP growth? Are leading indicators rising or falling?
Fiscal Health: Is the budget deficit growing or shrinking? Is federal spending commensurate with long-run economic growth?
Fiscal Policy: Are the major policy initiatives from the White House and Congress pro-growth and market-friendly?
Global Trade: Are current attitudes pro-globalization and free trade or pro-nationalism and protectionism?
Inflation: Is there price stability around the Fed’s target? What are the drivers of inflation? How are consumer expectations?
Liquidity: How are measures of money stock growth? What do real rates, credit spreads, and broader financial conditions look like?
Monetary Policy: Are interest rates accommodative or restrictive? Are other central bank programs market-friendly?
Sentiment: Are investors broadly optimistic (a negative) or pessimistic (a positive) about the market?
Technical Picture: What is current price action telling us? What do market breadth, trend, and momentum look like?
U.S. Dollar: Is the dollar strengthening or weakening versus other world currencies? What are the factors causing the move?
Valuation: Do stocks look expensive or cheap vs. historical averages given the current environment?
War vs. Peace: What do the world’s geopolitical tensions look like? Are they inhibiting global economic growth?

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