



Market Commentary
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English Version

Insigneo Weekly Dispatch

Navigating Uncertain Markets

In an uncertain environment, where the proverbial tide does not lift all boats, careful sector and stock selection are key.

Guidance on investments and the major structural factors behind your clients' portfolios.

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**By Mauricio Viaud**

PM and Senior Investment Strategist
Insigneo

Navigating Uncertain Markets

What a difference a month makes. We started the year on a strong footing, with the S&P 500 up 6.2% in the month of January. However, February was a different story. In the newsletter published on [February 9](#), we cautioned that a near-term pullback in equities would not be unusual, as the market seemed to be telling the Federal Reserve that it did not believe the possibility of seeing rates higher for longer. Investors also appeared to be telling company management teams that the sales and earnings headwinds they were experiencing would most likely be short-lived. We made the case then that equity market expectations needed to adjust to the data. The market has retreated close to 3% from that time, and unfortunately, we believe that further adjustments in expectations might be necessary.

Personal Consumption Expenditures (PCE) data published in February gave indications that inflation may be proving to be more resilient than expected, increasing the probability that the Fed would need to keep interest rates elevated, and decreasing the probability of a “Fed-pivot” in the near term. This began the shake out of speculative investors out of equities, those who had invested in anticipation of the elusive pivot. Believe it or not, this process is healthy for the market, helping remove some of the speculative “froth”. Going forward, inflation expectations and the Fed’s actions required to contain it will be key for equity market performance.

Another important dynamic at play stems from companies’ earnings expectations. Inflation, and the

possibility of slower economic growth, has an impact on earnings growth, which is something management teams expressed in the most recent earnings season. In fact, this past reporting period was the first earnings season where we saw year-on-year declines in earnings since 2020. The current Wall Street consensus is for earnings per share to contract over the next 1 to 2 quarters but are then expected to rebound after that. If interest rates need to stay elevated for longer, or even rise higher than expected, the Street's expectations of an earnings recovery would be pushed further out, possibly sending markets lower.

In an uncertain environment, where the proverbial tide does not lift all boats, careful sector and stock selection are key. Looking for sectors and companies with earnings that are sustainable, diversified, or of greater quality is important. At this point in the market cycle, when overall earnings tend to be on the downswing, sectors in the defensive and cyclical value areas of the market tend to outperform. These include sectors such as Consumer Staples, Energy, Industrials, and Financials. We are seeing these sectors perform better not only on a fundamental analysis basis, but also on important technical analysis attributes such as Price Breadth.

Price Breadth measures the percent of stocks in a particular sector that are trading above their 200-day price moving averages. In essence, it gives a sense of which sectors are seeing their stock prices hold up relatively well and which sectors are trending down. The logical question that comes to mind is "Don't we want to buy stocks when their prices are down?" The answer is absolutely, yes.

However, just because prices in certain sectors are holding up better than the rest of the market, does not mean that stocks in these sectors have not seen their prices go down also. As a matter of fact, the Industrials and Financials sectors are currently trading 13%-15% lower than they were a year ago. What we have to remember is that in a market that has the potential to continue trending downwards, we do not want to hold stocks that are going down faster than the market. **A prudent mix of offense and defense sometimes proves to be the best way to navigate uncertain markets.** That being said, tactical exposure to the aforementioned sectors could be attained through ETFs or for more risk tolerant investors, individual equities.

Within Energy, the Energy Select Sector SPDR ETF (XLE) and the VanEck Oil Services ETF (OIH) are good vehicles to gain diversified exposure to energy production and service companies in the United States. An investor with a higher tolerance for risk could consider Shell PLC (SHEL), BP PLC (BP), and ExxonMobil (XOM). These companies are leading global producers with large earnings and cash flow generation. Additionally, SHEL and BP are also focusing on developing sustainable and green energy assets such as blue hydrogen and LNG. In the oilfield services industry, Haliburton (HAL), Schlumberger (SLB), or Baker Hughes (BKR) could also be considered. These three companies have well diversified revenues streams, as they offer services on a global scale to end customers ranging from larger Super Majors to small Exploration and Production companies.

The Consumer Staples Select Sector SPDR ETF (XLP) provides an effective way to get exposure to

large, diversified companies in this sector with operations across the globe. Companies such as Pepsico (PEP), Mondelez International (MDLZ), or Nestle ADR (NSRGY) have diversified revenue streams across products and geographies.

The iShares Global Industrials ETF (EXI) or the Vanguard Industrials ETF (VIS) both provide diversified exposure to the Industrials sector. With an expense ratio of 0.40%, EXI is costlier than VIS at 0.10%. However, EXI does have its holdings diversified across the United States, Europe, and Asia, while VIS consists predominantly of U.S. holdings. As a result, EXI's holdings generally trade at a slight valuation discount to those in VIS. From an individual equity perspective, risk tolerant investors could consider companies such as Lockheed Martin (LMT), Airbus ADR (EADSY), Siemens ADR (SIEGY), or United Airlines (UAL). Apart from UAL, these companies have diversified business lines in their individual niches and trade at relative valuation discounts when compared to their peers. As an airline, UAL has a less diversified business profile; however, it also trades at a relative discount and is in the midst of repositioning its operations to capitalize on favorable industry dynamics.

The iShares US Financials ETF (IYF) or the Vanguard Financials ETF (VFH) both provide diversified exposure to the Financials sector, although at an expense ratio of 0.10%, VFH is less costly than IYF at 0.40%. From an individual equity perspective, a risk tolerant investor could consider J.P. Morgan Chase (JPM) or Morgan Stanley (MS).

These two companies are leaders in the financial industry, have diversified business lines within that

industry, and trade at attractive historical relative valuations.

It is important to keep in mind that the ETFs and individual equities mentioned here can exhibit high degrees of volatility and are not suitable for every investor. These investments are best considered on a case-by-case basis, based on a particular investor's willingness and ability to tolerate risk. If you need more information or would like to discuss these potential ideas in more detail, please do not hesitate to contact the Insigneo Research Team.



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