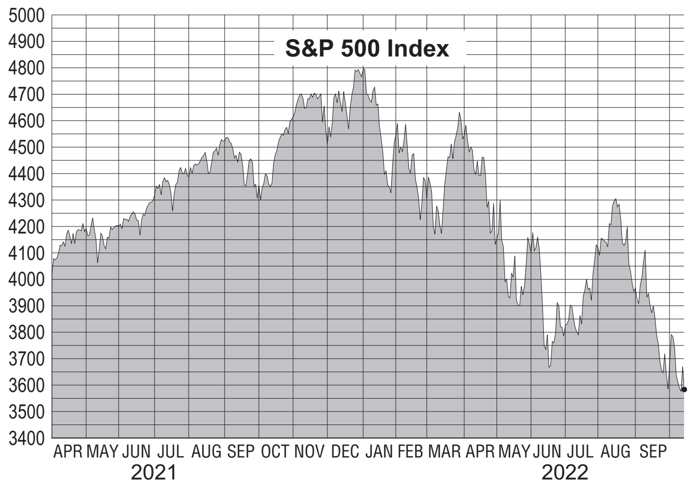
INVESTECH® RESEARCH

Vol22 Iss10 OCTOBER 21, 2022



4 Weeks Ending October 14, 2022

	High	Low	Last
Federal Funds	3.08%	2.33%	3.08%
30yr T-Bonds	3.99%	3.50%	3.99%
Gold (London PM)	$1721.10	$1623.30	$1649.30

	High	Low	Last	200D M.A.
DJIA	31019.68	28725.51	29634.83	32898.56
DJUA	1024.62	838.99	847.11	982.85
NASDAQ	11535.02	10321.39	10321.39	12618.90
S&P 500	3899.89	3577.03	3583.07	4161.33

S&P 500 P/E Current: 18.6 95 yr Avg: 17.6

Technical and Monetary Investment Analysis

Housing – Will the Hard Landing turn into a Crash?

August 20, 2021 – InvesTech Research

"There is strong compelling evidence that the housing market is in a bubble – a potentially bigger and more dangerous one in terms of prices and sentiment than the 2005 Housing Bubble."

Ironically, in 2005, very few believed us when we introduced our *Housing Bellwether Barometer* and *Forbes* brought it to the forefront as a disturbing warning of a dangerous bubble in the housing market. The aftermath of that devastating washout and resulting Financial Crisis is now history. Likewise, our warning [above] over a year ago about the overvaluation extremes and developing danger flags in housing was treated by some with a high degree of skepticism. That is starting to change…

On Second Thought, Maybe Housing Was in a Bubble After All *– Bloomberg, 9/22/22*

The evidence inside this issue is compelling. In fact, *so compelling* that it would be difficult to argue that the U.S. housing market isn't heading for a hard landing. The only question we have now is whether the headline in our April issue six months ago was too mild in describing what lies ahead.


INVESTECH® RESEARCH

Vol22 Iss04 APRIL 15, 2022

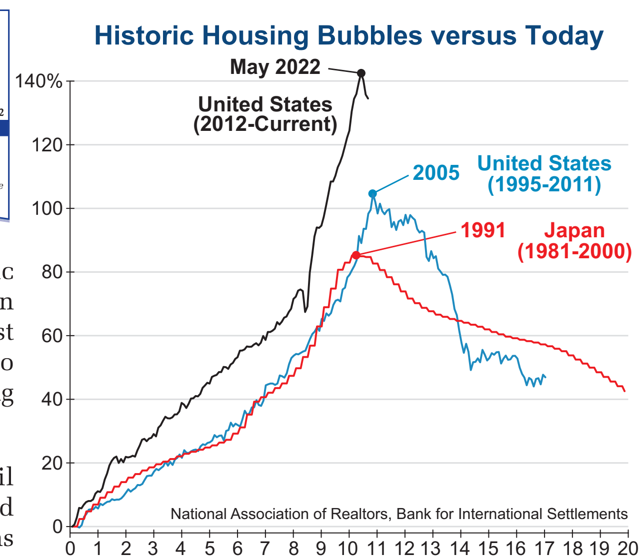
Technical and Monetary Investment Analysis

Housing: Heading for a Hard Landing!

"The continuing shortages of housing inventory are driving the price gains. There is no evidence of bubbles popping." – Chief Economist, National Association of Realtors

The evidence that is unfolding might be called the confluence of a perfect storm! First, to put today's extraordinary post-pandemic runup in housing prices into historical perspective, we have taken the percentage increase in Median Family Home prices over the past 10+ years and overlaid them on the parabolic price gain leading up to the peak of the 2005 U.S. Housing Bubble, as well as Japan's Housing Bubble which peaked in 1991.

And if you think that comparison appears worrisome, then wait until you see the other "perfect storm" clouds inside this issue that would have even the most resolute bulls worried about the stock market, as well as the U.S. economy…



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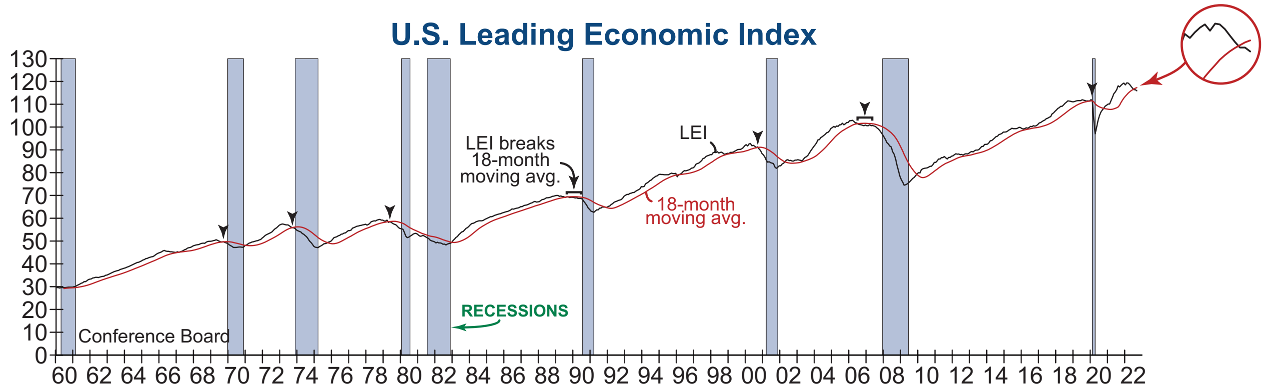
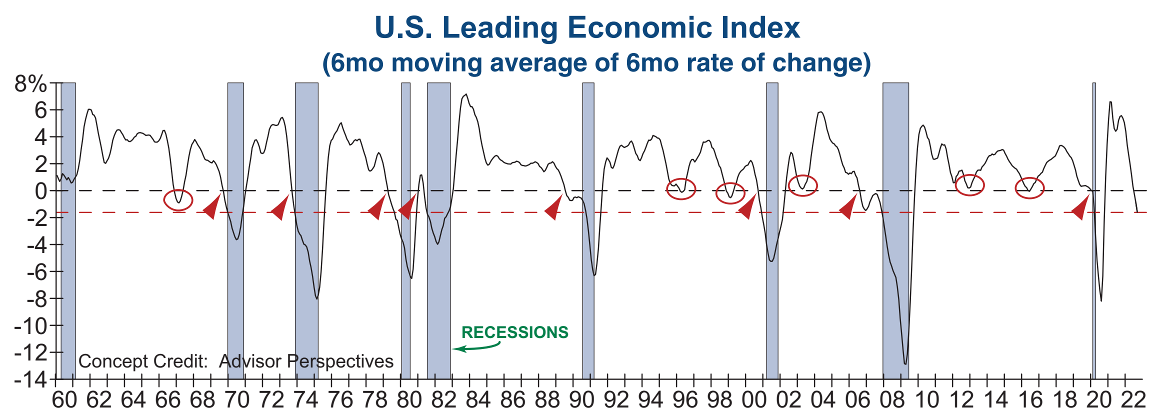
Economic Outlook – *The Recession Debate is over!*

In our view, the debate about whether the U.S. economy is in a recession, or going into a recession, is over. The Leading Economic Index (LEI) from the Conference Board is comprised of 10 different leading macroeconomic indicators – from housing to manufacturing to the yield spreads and so on. After peaking in February, the LEI has fallen in 6 of the past 7 months, and has now crossed below its 18-month moving average as shown in the upper graph below. In addition, the "rate of change" (lower part of the graph) has fallen to a contractionary level.





Question: **When in the past 60 years has the LEI sent this severe of a warning signal, and the economy hasn't ended up in a recession?**

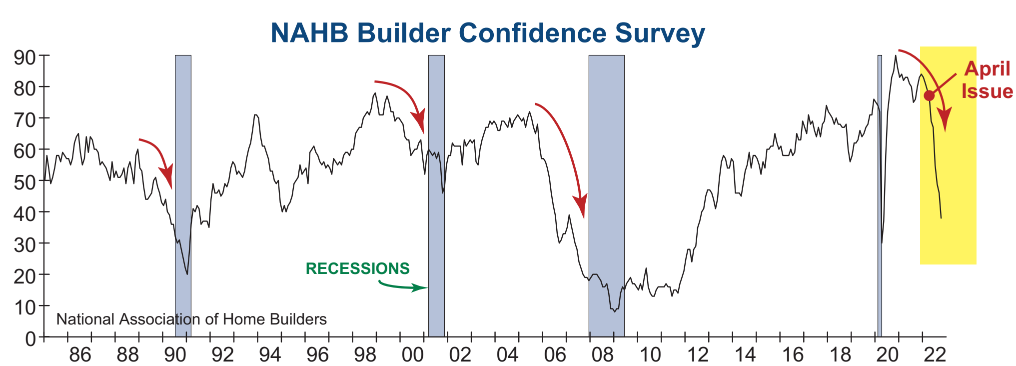
Answer: **Never!**

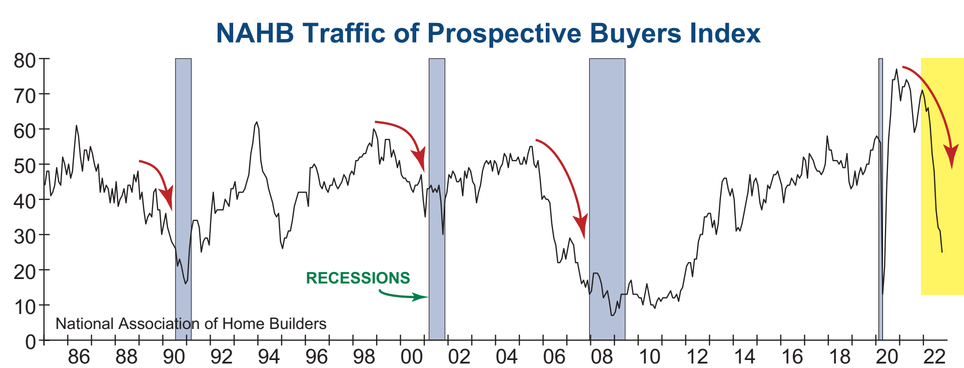
Housing – now confirming a Hard Landing (…or worse)

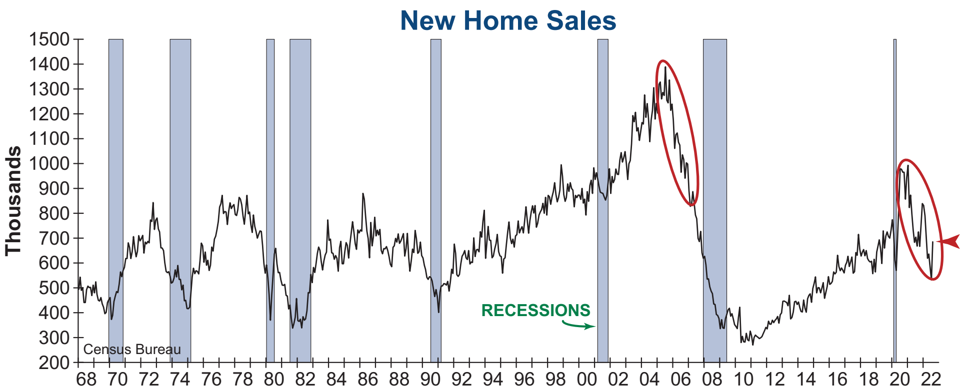
One of the most critical segments of the U.S. economy is housing (17% of GDP), as it can cushion –or instead intensify– a potential economic downturn. In our April housing issue we warned of an imminent hard landing, and specifically said to watch the National Association of Home Builders (NAHB) surveys for confirmation.

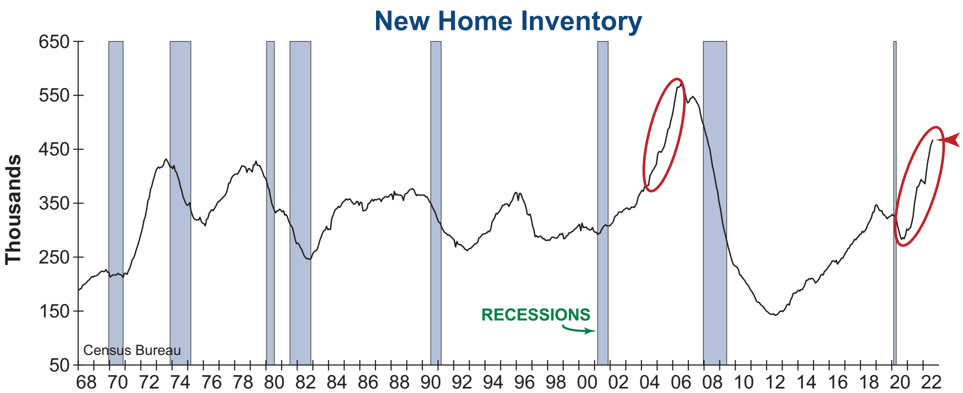
Since then, we have seen a record 10th consecutive decline in Builder Confidence – fueled by the persistent downturn in Traffic of Prospective Buyers. The size and rate of this decline confirms that confidence in the U.S. housing market is on a crumbling foundation very similar to what followed the peak in the 2005 Housing Bubble.

This is compelling evidence that the housing market is heading for a hard landing. And perhaps the major question is whether the landing gear will be torn off… and the landing will turn into something worse.









Meanwhile, other housing data is also mimicking the rapid unwinding that played out after the 2005 Housing Bubble peak. Over the past year, New Home Sales have fallen as homebuyer demand falters and cancellations are on the rise. Although builders have responded by cutting prices, their inventories continue to pile up (bottom graph). With a record number of units (new homes and multifamily dwellings) currently under construction, some builders have gotten desperate enough to unload their homes in bulk to institutional investors… for a hefty discount:

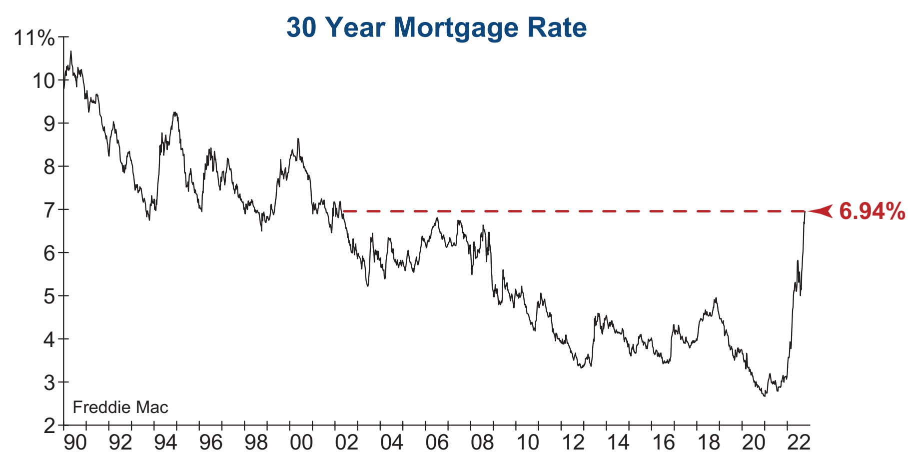
> **Institutional investors 'buying in bulk' as homebuying cools**
>
> *Yahoo! Finance – 10/12/22*

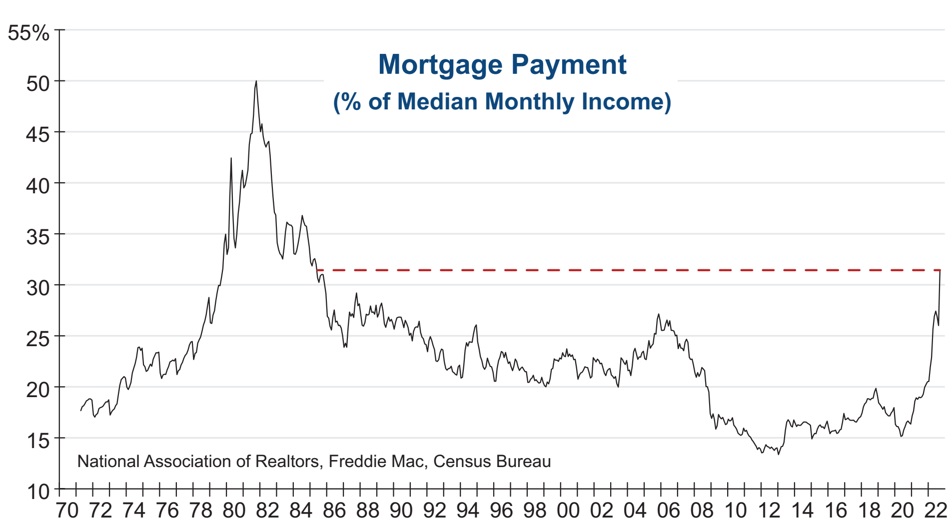
Something tells us this isn't going to end well…

Housing Affordability was already bad …and it just got a lot worse!

The steep runup in housing prices over the past decade has made affordability a major obstacle for new home buyers. However, the dramatic upturn in mortgage rates from sub-3% levels during the pandemic to nearly 7% today is like taking a wrecking ball to the housing market.

This 20-year high in long-term mortgage rates is dramatically impacting affordability to a degree not seen in many decades. →

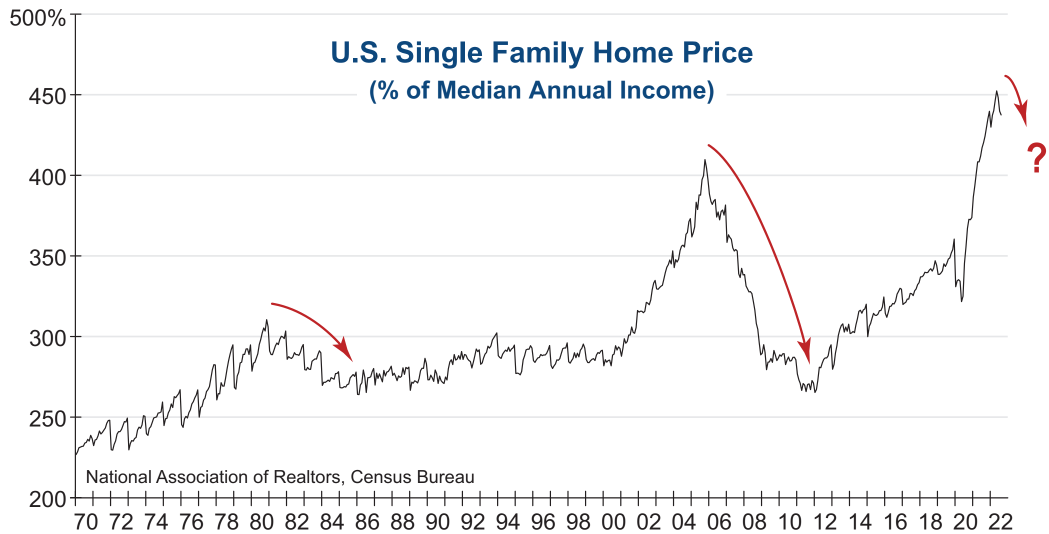




Evidence of this is clearly visible in the median Mortgage Payment as a percentage of Monthly Income which has surged to its highest level in nearly 40 years. As shown at left, the median homeowner's mortgage payment now eats up more than 30% of their income. This degree of payment unaffordability far surpasses the peak reached during the 2005 Housing Bubble and is only exceeded by the period of record high interest rates during the early 1980s.

Throughout history, housing prices have closely tracked both long-term inflation and income. That, in essence, is the measure of affordability – whether new home buyers can scrape together the initial down payment and also afford their monthly mortgage. When the disparity between prices and income (i.e., affordability) gets extreme, there is almost inevitably a normalization.

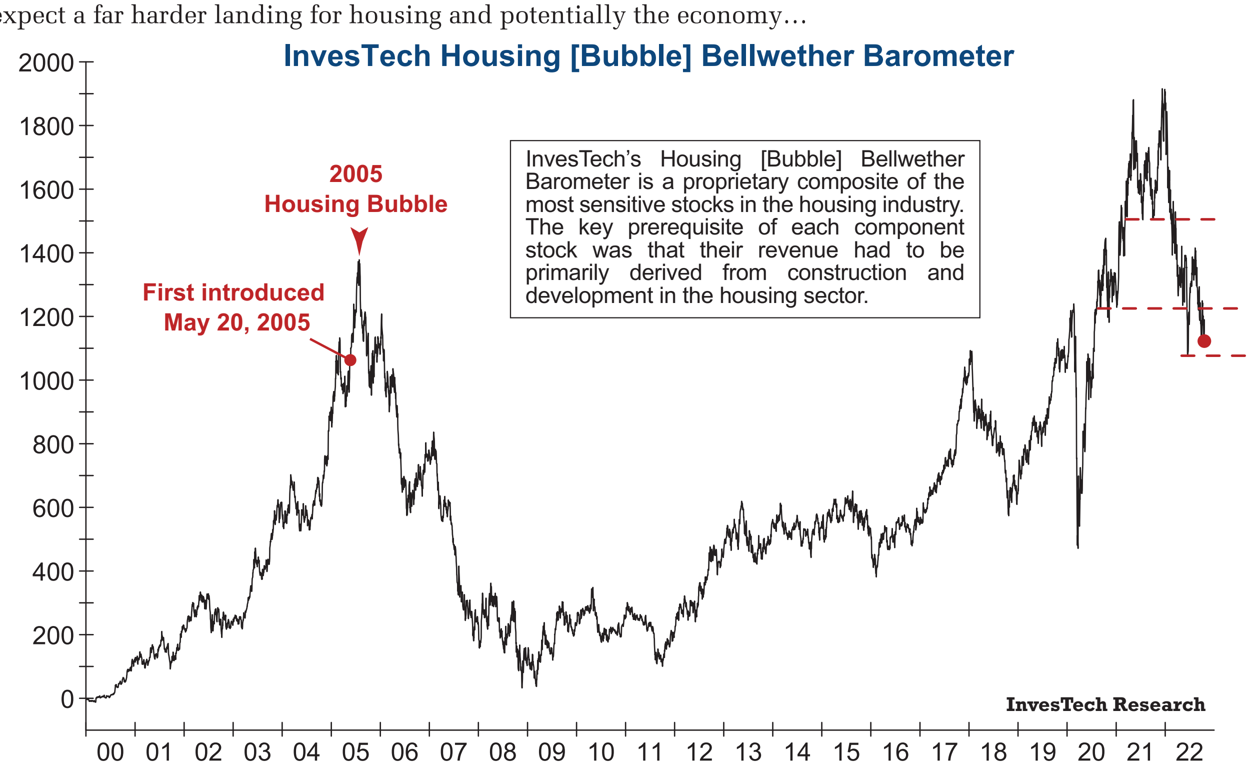
That was the case in the early 1980s, for those who might remember that lengthy housing recession. It was far more dramatic when the last housing bubble peaked in 2005 and required seven years to fully "adjust." With prices now at an even greater extreme relative to income, one can only guess how today's affordability crisis will resolve.



In our view, the housing market is the Achilles heel of today's U.S. economy and the probable recession ahead. How these excesses unwind will be a determining factor in both the depth and duration of the upcoming recession as it starts to unfold.

The most valuable tool in monitoring this risk will be our Housing [Bubble] Bellwether Barometer (below). This proprietary indicator is comprised of the most sensitive and leading stocks related to the housing market – including home builders, lenders, and title companies. First introduced in early 2005, it reliably warned of the peak in home prices later that year. And most importantly, its swift and persistent decline confirmed that the unwinding would be painful well ahead of the 2008 Financial Crisis.

The message today is eerily similar to that warning in 2005. Today, after rallying sharply from the June low, this Housing Bellwether Barometer is close to breaking a critical support level. If it breaks sharply lower in the weeks or months ahead, then expect a far harder landing for housing and potentially the economy…



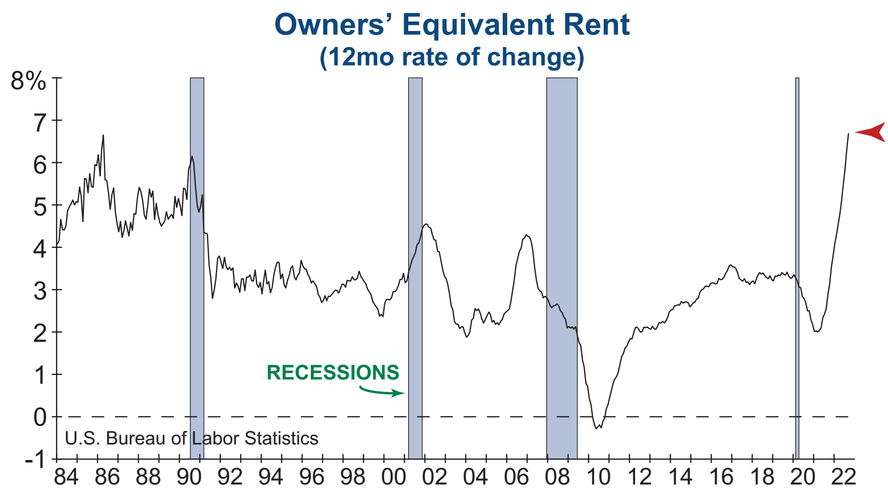
Will the Fed Pivot? (...don't hold your breath)

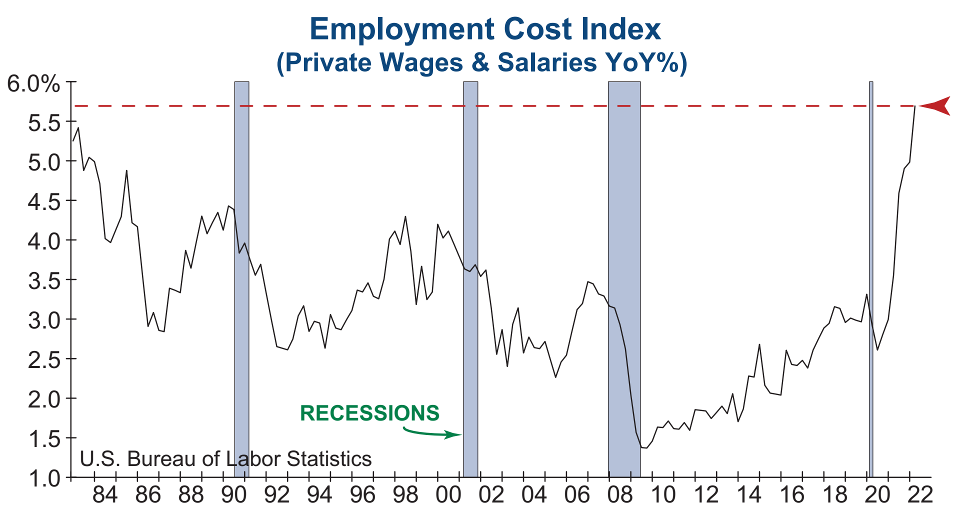
The widely debated question –both on and off Wall Street– is when will the Fed pivot and stop raising interest rates, or even reverse policy and start easing. These hopeful expectations are based on the past 4 years surrounding the Covid pandemic. Unfortunately, for those anticipating Jerome Powell's Fed to ride in on a white horse and save the day (once again), that wait could be painfully long.

Here are 3 compelling reasons why...

First, the biggest component making up the Consumer Price Index (CPI) is Owners' Equivalent Rent (OER), which is determined by asking homeowners what they believe their home would rent for. This is the Bureau of Labor Statistics' estimate of housing costs and makes up a whopping 24% of the CPI today!

This important inflation contributor now stands at an all-time high, and it is showing no sign of slowing down. While OER will begin to level off in the months ahead if home prices start plummeting, the Fed is unlikely to proactively reverse policy until this inflation data noticeably rolls over.



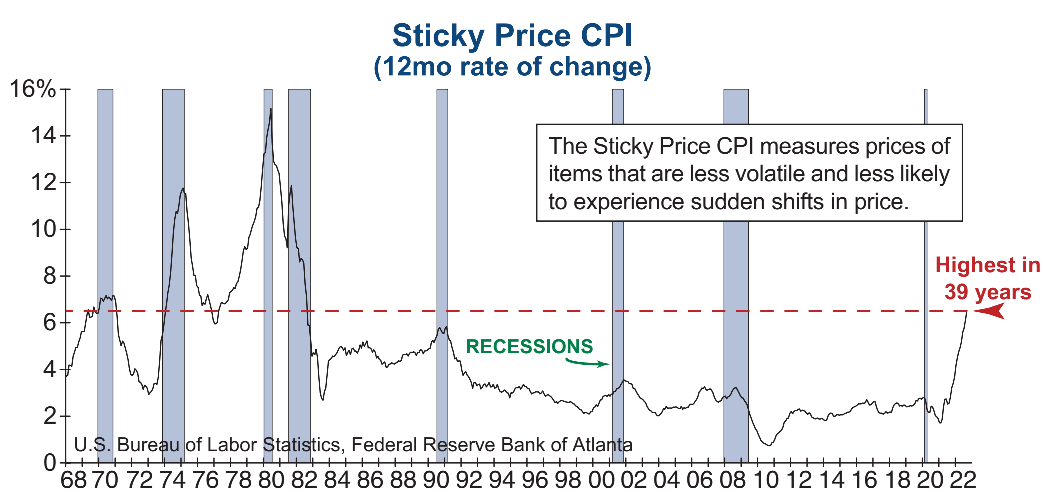


The second reason lies in one of the most stubborn inflation contributors of the past – wages. Another BLS statistic tracks private wages and salaries in its Employment Cost Index. Not only is it also at an all-time high, but this has been by far the strongest acceleration in its history.

This is NOT a good omen for Fed policy reversal!

And lastly, another reason the Fed may hold firmer for significantly longer than most think, lies in one of their own inflation measurement tools from the Atlanta Federal Reserve dubbed the Sticky Price CPI. It measures prices of items that are less volatile or transient. In other words, once prices of these "stickier" items start rising, they don't reverse easily.

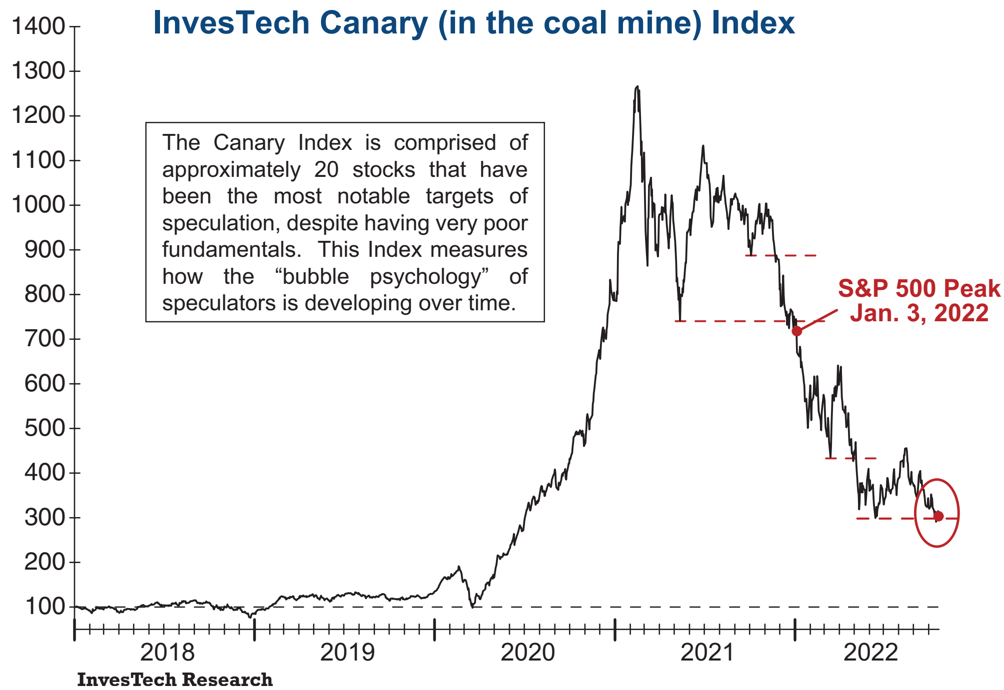
With Sticky Prices now at a 39-year high, one can understand why "transitory" is no longer in the Fed's vocabulary.



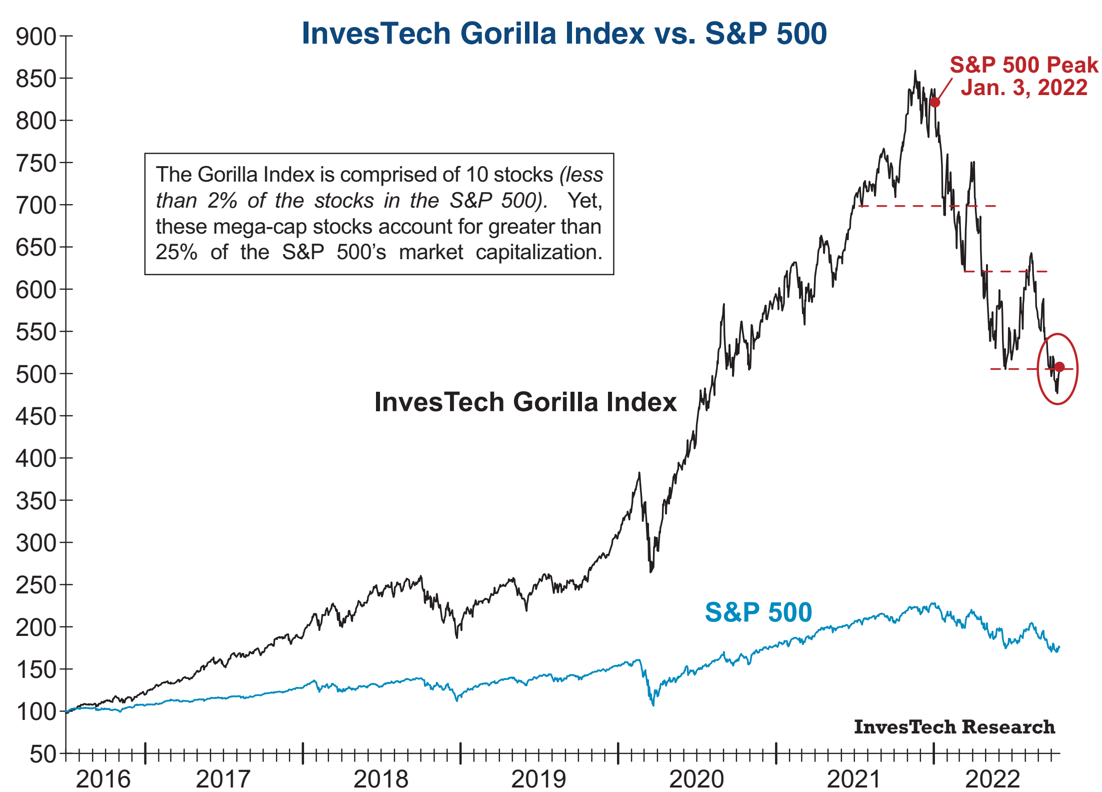
Technical – *Standing on the precipice?*

We first introduced *InvesTech's* Canary (in the coal mine) Index in early 2021 as stock market speculation reached heights not seen since the Tech Bubble. This index was designed to hold stocks that were most representative of the obvious bubble developing in speculative investments – including Snap, Pinterest, DoorDash, Beyond Meat, Virgin Galactic, and others. The concept was similar to the Internet Index that we tracked and utilized during the 1990s Tech Bubble. We knew that when these high-flying favorites peaked and started tumbling, that it would mark an important shift in investor psychology and point to a potential bear market ahead.

Our Canary Index peaked a remarkable 11 months ahead of the S&P 500, and its breakdown last December played a decisive role in our move to a more defensive bear market position. Today, these stocks are down -76% on average. But the most important news is that after a valiant summer rally, this Canary Index of speculative growth stocks is now breaking down again.



Another dynamic of the post-pandemic rally, that we last observed during the Tech Bubble era, was the over-concentration of gains in mega-cap momentum stocks. We called them "Gorillas" at that time, and reintroduced a new *InvesTech* Gorilla Index in the summer of 2020. These 10 stocks (which included the likes of Tesla, Netflix, Apple, Google and Nvidia) represented only 2% of the S&P 500 Index, but were contributing over 27% of the S&P's gains! Our belief was that when our Gorilla Index peaked, the rest of the market would follow – *and it did!*



The important message today is that BOTH of these leading indexes are now testing critical support levels. If these levels are decisively broken, then it could trigger a significant negative impact on investor psychology and usher in more severe losses ahead…

STRATEGY UPDATE

Don't Bet Against Historical Odds

There is a tremendous amount of risk in today's economy, and a lot not to like about the current stock market environment:

- Inflation is hitting 40-year highs.
- The Federal Reserve has already raised interest rates 5 times this year, with another 2 rate hikes expected before year end.
- Inflation pressures on the Federal Reserve remain extraordinarily high. That means Wall Street's widespread hopes of a reversal or pivot in Federal Reserve policy will be met with disappointment.
- Housing is already falling into a recession, as new home buyers are drying up. And the full effect of 7% mortgage rates hasn't yet been felt.
- While the ISM Surveys in manufacturing and services are still positive, they are both falling and could reach contractionary levels by early next year.
- Our *InvesTech* Canary Index and *InvesTech* Gorilla Index are both sending red flag signals that any further break from current levels could trigger a significant increase in investor selling.

In this issue, we revealed why a recession is –in all probability– imminent. While an increasing number of economists and analysts are finally starting to acknowledge this fact, the real risk is that no one knows the depth or duration the path of that recession might take.

As noted previously, the greatest risk to the economy or even the stock market may not lie in Federal Reserve policy, but in housing. Our Housing Bellwether Barometer will likely prove an important guiding factor as this perfect storm of converging forces continues to run it course.

Looking across the valley…
It is important to never underestimate the downside risk in a bear market. And while this bear market may be far from over, there is a light at the end of this dangerous tunnel in simply knowing that bear markets always end.

We successfully navigated the washout of the Tech Bubble that stretched for two and one-half years before hitting bottom in October 2002. And again, during the 2008 Financial Crisis and 18-month bear market, we avoided a major portion of the downside risk with our defensive allocation and high 45-55% cash reserve.

Today, *InvesTech's* Model Fund Portfolio is even more defensively allocated with only a 40% net exposure to stocks. That is more cautious than at any time since the Tech Bubble washout in 2002. And we plan to continue our focus on risk management and maximum defenses as long as dark storm clouds are gathered overhead. A patient and disciplined approach remains imperative as evidence strongly points to new bear market lows ahead. At a time like this, it's valuable to remember that those who successfully navigate through this bear market will eventually be rewarded with a great buying opportunity!

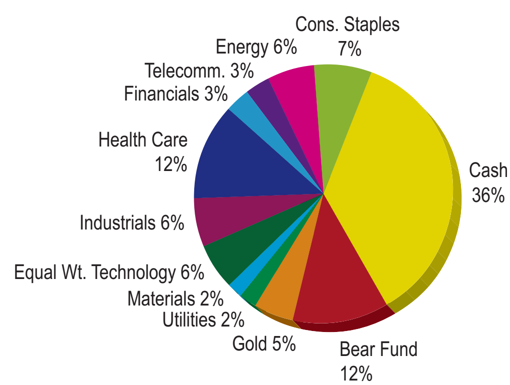
MODEL FUND PORTFOLIO

NEXT ISSUE: November 18, 2022

CHANGES SINCE THE LAST ISSUE: On the September 23 Hotline Update, we advised making the following changes.

- **Reduce the Materials Select Sector SPDR ETF (symbol: XLB) from 4% to 2%.**
- **Reduce the Invesco S&P 500 Equal-Weighted Technology ETF (symbol: RYT) from 8% to 6%.**

The Model Fund Portfolio currently has a net invested allocation of 40% (52% long positions and 12% in an inverse index ETF). The remainder of the Portfolio (36%) is held in short-term Treasurys or a money market fund.



Percent	Fund	Symbol	52-week Hi	52-week Low	Init. Recommended Date	Init. Recommended Price	Recent Price	Alternate Funds
36.0%	T-BILLS/ CASH/ MONEY MARKET	---						Money Market Fund
7.0%	CONS. STAPLES SELECT SECTOR SPDR	XLP	79.46	66.50	7/1/11	23.27	68.26	
6.0%	ENERGY SELECT SECTOR SPDR	XLE	90.31	51.39	7/1/11	52.06	81.28	
3.0%	FIDELITY SELECT TELECOMM PORTFOLIO	FSTCX	58.55	41.03	9/18/20	52.83	42.60	Invesco S&P500 Eq Wt Comm(EWCO)
3.0%	FINANCIAL SELECT SECTOR SPDR	XLF	40.83	30.29	6/8/12	7.23	31.79	
12.0%	HEALTH CARE SELECT SECTOR SPDR	XLV	141.68	118.92	7/1/11	29.77	125.89	
6.0%	INDUSTRIAL SELECT SECTOR SPDR	XLI	105.73	82.84	7/1/11	30.39	86.59	
6.0%	INVESCO S&P 500 EQUAL WEIGHT TECHNOLOGY	RYT	325.99	220.06	9/18/20	203.43	225.90	
2.0%	MATERIALS SELECT SECTOR SPDR	XLB	89.36	67.32	11/20/20	67.03	69.88	
2.0%	UTILITIES SELECT SECTOR SPDR	XLU	77.59	61.52	9/9/22	76.86	63.45	
5.0%	VANECK VECTORS GOLD MINERS	GDX	40.87	21.86	9/29/17	22.00	23.45	
12.0%	DIREXION DAILY S&P 500 BEAR 1X	SPDN	17.88	13.94	1/20/22	14.89	17.37	

PERSONAL PERSPECTIVE

The Truth About Bear Markets
…and the importance of persistent patience

From the moment this bull market peaked in January, Wall Street pundits have downplayed the growing risk and tried to cheerlead stock prices higher…

Day after Bull Market Peak: **JPMorgan Strategists Say Global Stock Market Party Far From Over** – *Bloomberg, January 4, 2022*

And literally every step of the way down –*month by month*– investors have received new encouragement that the bear market lows are at hand, if not behind us…

Jan: **After vicious stock market sell-off, it's time to buy: Goldman Sachs** – *Yahoo! Finance, 1/26/22*

Feb: **We've hit the market bottom, if you're not buying it's a mistake** – *CNBC, 2/28/22*

Mar: **Signs Of Market Bottom Emerge On Wall Street** – *Bloomberg, 3/11/22*

Apr: **Stock market outlook: There's a 90% chance bottom already in for 2022** – *Markets Insider, 4/3/22*

May: **The Stock Market Selling Storm Is Over – Time To Buy** – *Forbes, 5/7/22*

Jun: **S&P 500: Indicator Signals Start Of Potential New Bull Market** – *Investing.com, 6/1/22*

Jul: **S&P 500 triggers signal with perfect track record for calling end of bear markets** – *CNBC, 7/20/22*

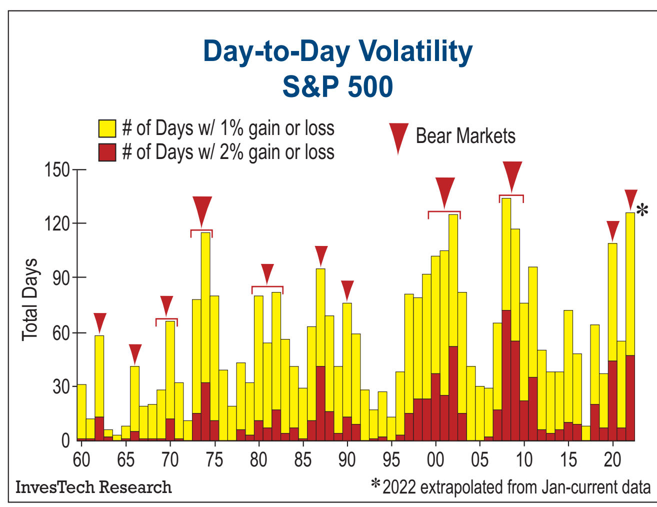
Aug: **Opinion: Evidence for a new bull market in stocks is rapidly piling up** – *MarketWatch, 8/18/22*

Sep: **The conditions needed for a stock market bottom are forming as investors get overly bearish, JP Morgan says** – *MSN, 9/26/22*

One must step back over 13 years to find the lessons of a major bear market, and over 40 years to relearn the torturous lessons of an inflationary bear market. Very few bear markets are short, timid, or simply end when blue chip indexes are down -25% or so. In fact, the bigger ones often result in -50% losses in the S&P or DJIA, and can last 18 to 24 months or longer. And every major, painful bear market started out as a minor, painless correction. That is the historical truth about larger bear markets that can turn out to be life-changing events.

Warning Flags are still increasing…

The compelling evidence in this issue is clearly ominous enough to warrant maintaining our high-cash, high-defense allocation for as long as it takes for storm clouds overhead to eventually pass. Yet another thunderstorm has struck with surging volatility in day-to-day market action. Shown at right is a "heat map" of volatility that totals the number of 1% daily moves (yellow bars) and 2% daily moves (red bars) on a yearly basis all the way back to 1960. It doesn't matter if the 1% or 2% move is up or down – *volatility is volatility!*



There are two notable points: **First**, the higher volatility always occurs in the bear markets [RED arrows]. **Second**, the most extreme volatility has accompanied the biggest bear markets, including 2007-09 (-57%), 2000-02 (-49%), and 1973-74 (-48%).

Thus far in 2022, volatility is running at the second highest level of the past 60 years – matched only by 2008. That's not a good omen for those who think the bear market lows are behind us.

Fortunately, we received preemptive confirmation of a probable bear market from several early warning flags prior to last January's final top. A number of these were discussed in my interview last December with *Barron's* titled, *"Preparing for a Bear Market"* (posted on our homepage). Our "less-than-optimistic" outlook for the bull market, interest rates, housing, and other assets at the time could easily have come across as a bit too dire – especially my closing comment that *"Bitcoin could drop 90% in value."*

Yet here we are nine months later with the S&P 500 down -25%, the NASDAQ Index losing -35%, and the FANG stocks off close to -50%. And Bitcoin? Bitcoin was trading above $50,000 the week that I did that interview, and is now at $19,080 – a loss of -62%. So in that regard, one might say we've only been 2/3's right …so far 😉.

James B Stack

STACK FINANCIAL MANAGEMENT

SFM Celebrates 15 Years of Recognition on *Barron's* "Top 100 Independent Advisors" List

Stack Financial Management (SFM) of Whitefish, Montana is pleased to announce that they were recently named to *Barron's* 2022 list of the "Top 100 Independent Advisors" in the United States. This marks SFM's 15th year of recognition by *Barron's*. SFM is the only firm recognized in Montana, and one of only three firms included from the Rocky Mountain region, which includes Montana, Colorado, Wyoming, Idaho, Utah, New Mexico, and Arizona.

> *"We are honored to be recognized by Barron's as one of the Top Independent Advisors in the country. This is truly a team effort, and now more than ever our disciplined risk-managed investment approach coupled with a superior service experience reinforces our long-standing commitment to our clients."*
>
> ***– Zach Jonson, SFM Chief Investment Officer***

The select group of advisors considered for *Barron's* "Top 100" are ranked on an extensive list of over 100 criteria that include assets under management, client satisfaction and retention, quality of the practice, revenue growth, succession planning, and range of staff to name a few. The ranking is responsive to trends and important issues in the industry, and it focuses on the criteria that should matter most to investors.*

About Stack Financial Management
Stack Financial Management is an independent registered investment advisor and wealth management firm based in Whitefish, MT. Founded by James Stack, SFM is most well-known for its "safety-first" investment philosophy and client-first experience. SFM has been helping conservative minded investors preserve and grow their wealth since 1994. The firm is consistently recognized as a leading independent advisor by national publications and manages approximately $1.6 billion in assets.

Stack Financial Management's other rankings and recognition in 2022 include: *

- #1 in the state of Montana for *Barron's* 2022 "Top 1200 Financial Advisors by State"
- #1 in the state of Montana for *Forbes* 2022 "Best-in-State Wealth Advisors"
- *Forbes* 2022 "America's Top 250 Wealth Advisors"

To learn more about Stack Financial Management:

Call (406) 862-8000

OR

Visit www.StackFinancialManagement.com

*For more information regarding these lists, see the *Rankings Methodology and Important Disclosures* on the following page.

IMPORTANT DISCLOSURE INFORMATION: This is a paid insert from Stack Financial Management (SFM). SFM is a registered investment advisor and is a separate company from InvesTech Research.

Rankings Methodology and Important Disclosures

Barron's – On September 16, 2022, Stack Financial Management (SFM) was ranked #60 out of 100 on *Barron's* 2022 list of the "Top 100 Independent Advisors" in the United States. On March 11, 2022, SFM was ranked #1 out of 6 in the state of Montana on *Barron's* 2022 "Top 1200 Financial Advisors by State" list. *Barron's* rankings are based upon data provided by individual advisors and their firms. *Barron's* confirms that data via regulatory databases, crosschecks with securities firms, and conversations with individual advisors. The formula *Barron's* uses to rank advisors is proprietary. It has three major categories of calculations: assets under management, revenue, and quality of practice. *Barron's* also measures the growth of an advisor's practice and their client retention. In addition, they consider a wide range of qualitative factors, including the advisors' experience, their advanced degrees and industry designations, the size, shape, and diversity of their teams, their charitable and philanthropic work, and their compliance records. Investment performance is not a component of the rankings. *Barron's* is a registered trademark of Dow Jones & Company, Inc.

Please visit the following link for more information about Barron's methodology:
https://www.barrons.com/advisor/articles/barrons-methodology-for-ranking-financial-advisors-51615843316

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For more information about "America's Top Wealth Advisors" methodology, visit:
https://www.forbes.com/sites/rjshook/2022/08/24/methodology-americas-top-wealth-advisors-2022/?sh=6a514ba756e8

For more information about "Best-In-State Wealth Advisors" methodology, visit:
https://www.forbes.com/sites/rjshook/2022/04/07/methodology-forbes-best-in-state-wealth-advisors-2022/?sh=5f750ffe7fee

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