

Despite a flurry of destabilizing blows to investor confidence, most major market averages rose in March. Tech stocks led the way with the NASDAQ-100 Index posting a 9.54% gain.¹ The S&P 500 Index rose 3.67% while the Dow Jones Industrial Average added 2.08%.¹ The weak spot in this overall positive picture were small cap stocks. The Russell 2000 Index was significantly weaker than the other market averages and fell -4.78%.¹ While the failures of Silicon Valley Bank in California and UBS's purchase of ailing Credit Suisse shook the markets early in March, investors were heartened later in the month by the U.S. Commerce Department's report that the personal consumption expenditures price index rose less than expected in February. This new data suggested to some analysts that the combination of the Federal Reserve's (Fed's) injection of liquidity to the system due to the banking crisis and a slowing economy might mean that the Fed could pause or even reverse its tightening program in the near future.

With respect to the investment team's four pillar process, equity valuations remained above their historical mean, both in absolute terms and relative to inflation. Monetary policy remained negative and yet, despite the banking crisis, interest rates declined and credit spreads remained stable and within historical norms. Investor sentiment remained pessimistic in March, which is positive from a contrary point of view. The big change in the team's four pillar process during the month was the improvement in the team's volume and breadth momentum models.

As the result of this improvement in momentum, the team raised market exposure in March. The team would raise exposure further if interest rates continued to decline, investor sentiment remained pessimistic and if the team's volume and breadth momentum models continued to improve. The team would lower exposure if interest rates rose, credit spreads widened, investor sentiment became overly optimistic and if the team's volume and breadth momentum models once again deteriorated.

Our assessment of the four pillars of our investment process is as follows:

Valuation: The S&P 500 median price-earnings ratio (using trailing 12-month earnings) at 24.2x is well below its 2021 high of 34.0x but still above its 59.1-year median of 17.6x.³ From a longer-term perspective, it would seem that equity valuations are still too high.

Monetary factors and credit conditions: The Fed hiked interest rates by 25 basis points (bps) at the March meeting. Nonetheless, interest rates declined following the rate hike, which is a positive development. The 10-year U.S. Treasury Note yield dropped from 4.01% at the start of March to 3.48% by the end of the month.² Also, despite the concern over the banking system, credit spreads remained near their 23.2-year average³ suggesting that the banking crisis has not spilled over into the general economy.

Sentiment: Both the NDR Crowd Sentiment Poll and the NDR Daily Trading Sentiment Composite data showed that investors remained quite pessimistic in March despite the market's strength. This is a positive sign from a contrary point of view.⁴

Momentum: Both the volume and breadth intermediate-term momentum models improved in March.³ Further improvement in these models would signal a possible continuation of the market's recent strength.

¹ Source: Bloomberg. March 31, 2023

² Source: U.S. Department of Treasury. March 31, 2023

³ Source: Ned Davis Research. March 31, 2023

⁴ Source: Ned Davis Research. March 27, 2023

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