First Trust Portfolios Canada
Monday Morning OUTLOOK

Brian S. Wesbury – *Chief Economist*
Robert Stein, CFA – *Dept. Chief Economist*
Strider Elass – *Senior Economist*
Andrew Opdyke, CFA – *Economist*
Bryce Gill - *Economist*

416-865-8065 • www.firsttrust.ca

September 26, 2022

More Trouble Ahead

We had been bullish on stocks all the way back to March 2009, when mark-to market accounting was fixed and the Financial Panic started to recede. At that time the S&P 500 traded as low as 677. What a time to buy!

After that we remained bullish. We didn't recommend selling in spite of a wide range of fears that spooked many others, including the Great Recession lasting through 2010, a double-dip recession, a second wave of home foreclosures, an implosion in commercial real estate, the passage of Obamacare, a Greek debt default, a potential breakup of the Eurozone, the Fiscal Cliff, Brexit, or the election of President Trump. While others bailed out way too early on the bull, we kept riding.

We rode it so long that some called us "perma-bulls." But as we looked at low interest rates and healthy profits, we didn't see any other choice.

Then in June we announced we were bullish no more. In particular, we said "we don't expect the S&P 500 to hit a new all-time high, above the old high of 4,797, anytime soon." Instead, until one of our two scenarios plays out – a recession or the realization the Fed has pulled off a soft-landing – US equities are likely to be in a trading range with potential bear market rallies that come and go."

We still expect the *much* more likely scenario is that a recession will arrive sometime in 2023 (possibly early 2024) and that stocks will remain in a bear market until the recession hits. Why a recession? Because the Federal Reserve will have to get tight enough to reduce inflation toward its target and a monetary policy that's tight enough to control inflation is going to send the economy into a recession.

Back in June we said that stocks could easily rally from then-current levels, when the S&P 500 was at 3675, but that such a rally wouldn't last. After that the S&P rallied up to a closing high of 4305 in mid-August before dropping to 3693 at Friday's close. Don't be surprised by other bear-market rallies, which will also fade.

As always, we used our Capitalized Profits Model to assess fair value for the stock market. The model starts with the government's measure of economy-wide corporate profits and uses the yield on the 10-year Treasury Note to discount those profits.

The yield on the 10-year Treasury Note finished last week right around 3.70%, which, when plugged into our model, suggests fair value for the S&P 500 is about 3600. That would be a 2.5% decline versus the Friday close.

But long-term yields may go higher from here. With a 4.00% yield on the 10-year Treasury, the model says fair value on the S&P is about 3325, which would be a 10% drop versus Friday's close. And even if long-term yields don't go higher from here, approaching and entering a recession is highly likely to eventually cut corporate profits. Either way, there are reasons to expect we haven't seen the bottom yet for stocks.

A couple of things to keep in mind. If you're a very long-term investor who doesn't want to time the market, none of this discussion matters much. Just maintain your normal allocation to stocks and don't be shy about continuing to buy stocks at your normal intervals. That way you'll be buying at low stock prices, too, and stocks should be worth substantially more when you're spending down assets in the far away future.

However, those investors willing to take some risk on timing the market should consider that the future year or so probably includes better entry points for broad stock indexes than today's levels.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
9-27 / 7:30 am	Durable Goods – Aug	-0.3%	**+0.4%**		+0.0%
7:30 am	Durable Goods (Ex-Trans) – Aug	+0.2%	**+0.1%**		+0.2%
9:00 am	New Home Sales – Aug	0.500 Mil	**0.495 Mil**		0.511 Mil
9-29 / 7:30 am	Initial Claims – Sep 24	215K	**215K**		213K
7:30 am	Q2 GDP Final Report	-0.6%	**-0.5%**		-0.6%
7:30 am	Q2 GDP Chain Price Index	8.9%	**8.9%**		8.9%
9-30 / 7:30 am	Personal Income – Aug	+0.3%	**+0.3%**		+0.2%
7:30 am	Personal Spending – Aug	+0.2%	**+0.2%**		+0.1%
8:45 am	Chicago PMI – Sep	51.8	**51.3**		52.2
9:00 am	U. Mich Consumer Sentiment - Sep	59.5	**59.5**		59.2

Consensus forecasts come from Bloomberg. This report was prepared by First Trust Advisors L. P., and reflects the current opinion of the authors. It is based upon sources and data believed to be accurate and reliable. Opinions and forward looking statements expressed are subject to change without notice. This information does not constitute a solicitation or an offer to buy or sell any security. Such statements are generally identifiable by the terminology used, such as "plan", "anticipate", "intend", "expect", "estimate", or other similar wording. These forward-looking statements are subject to known and unknown risks and uncertainties and other factors that are beyond the control of the Funds, FT Portfolios Canada Co. and its affiliates, and First Trust Advisors L.P. and which may cause actual results, levels of activity and achievements to differ materially from those expressed or implied by such statements. Such factors include, but are not limited to: general economic, market and business conditions; fluctuations in securities prices, fluctuation in interest rates and foreign currency exchange rates; and actions by governmental authorities. Future events and their effects on a fund may not be those anticipated by us. Actual results may differ materially from the results anticipated in these forward-looking statements. We do not undertake, and specifically disclaim, any obligation to update or revise any forward-looking information, whether as a result of new information, future developments or otherwise. This information does not constitute a solicitation or an offer to buy or sell any security.