RAYMOND JAMES

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Sector Analysis - January 2023

CONSUMER DISCRETIONARY • CONSUMER STAPLES • ENERGY • FINANCIALS • HEALTHCARE
INDUSTRIALS • INFORMATION TECHNOLOGY • MATERIALS • REAL ESTATE • TELECOMMUNICATION • UTILITIES

General Summary

Hope springs eternal, especially at the start of a new year. To be sure, we do expect stocks to be climbing out of this bear market by year-end 2023. But the bottoming process and recovery may be elongated, as investor concerns shift from high inflation toward economic damage- with Fed tightening (which remains ongoing) acting with a lag on the economy. There have been signs of progress technically over the past several months, indicating that trends may be attempting to turn. But ultimately the market remains in a downtrend (below its 200-day moving average) and underlying leadership still skews defensive overall. We anticipate increasing our risk-on exposure within sector allocations over the coming year, but do not feel the need to rush into changes at the current time. We maintain an Overweight to Health Care as our favored defensive area, along with Energy due to solid fundamentals (particularly relative to the broad market), and Financials (which is near a relative strength breakout, led by the lower-beta Insurance subsector).

S&P 500 Sector	Weighting S&P 500	Weighting Recommend	Sector Thoughts	Favored Subsectors
Health Care	15.8%	Overweight	Favored "defensive" area for current volatile backdrop, given reasonable valuation and positive relative strength trends.	Providers, Biotech, Pharma
Financials	11.7%	Overweight	Macro concerns and inverted yield curve are headwinds, but banks are well-capitalized and valuation is cheap.	Insurance
Energy	5.2%	Overweight	Strong fundamentals and free cash flow generation continue to drive positive relative strength trends.	Integrateds
Technology	25.7%	Equal Weight	Weakening earnings outlook, along with uninspiring relative strength trends, keep us cautious for now.	Comm. Equipment & Semi Equipment
Consumer Discretionary	9.8%	Equal Weight	Relative earnings trends have improved, supporting better relative performance with valuation at reasonable levels. However, sustainable upside may take time and we stick with an equal-weight for now.	Specialty Retail, Consumer Durables
Industrials	8.7%	Equal Weight	The negative influence of declining ISM new orders (in a weakening economic backdrop) on performance historically, keep us at equal-weight.	Aerospace & Defense, Machinery
Communication Services	7.3%	Equal Weight	Justifiably "unloved" by investors given weak fundamental and technical trends, but valuation is also cheap.	Advertising
Materials	2.7%	Equal Weight	Fundamental trends remain unattractive, and the US dollar may due for a bounce in the short-term (after pulling back to long-term support).	
Real Estate	2.7%	Equal Weight	A lot of negative news has been priced in already, but earnings estimates are in decline and relative strength trends weak.	
Consumer Staples	7.2%	Underweight	Benefitting from their low beta, more defensive status in the current volatility. But relative valuation is now very elevated.	Beverages & Packaged Foods
Utilities	3.2%	Underweight	While the low beta and US-centric business may provide support in volatile periods, relative P/E is now at a new 20+ year-high. We are more interested in other areas at this stage of the bear market.	Electric

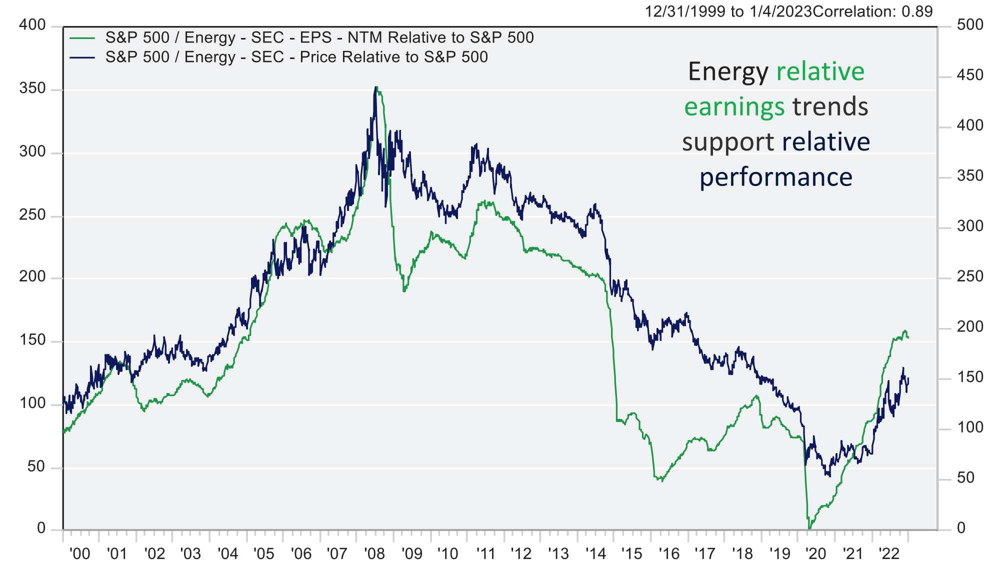
Source: FactSet, Gibbs Capital Management

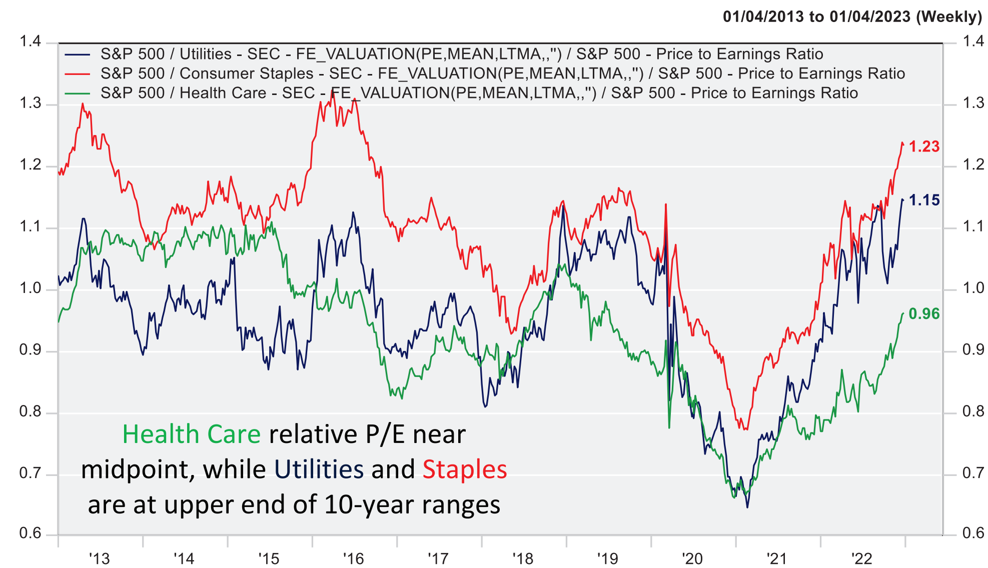
Sector Recommendations

At some point, Energy will consolidate its now two-year span of outperformance. However, we **maintain our Overweight Energy recommendation for now with fundamental and technical trends still solid**. Oil prices have pulled back to the $70s and earnings will moderate from the enormous 156% growth of 2022, but Energy companies are still generating significant free cash flow which is being used in shareholder-friendly ways (i.e. large dividends). Energy also trades at a market-low P/E and EV/EBITDA multiples of 8.5x and 5x respectively, along with a 12.5% FCF Yield (over twice as high as the next closest sector).

Health Care remains our favored "defensive" sector in the current volatile market backdrop due to reasonable valuations. Health Care trades at a 16.9x P/E multiple (in line with its 10-year average), while other "defensive" areas such as Utilities and Consumer Staples trade at the upper-end of their 10-year P/E ranges. Relative strength trends (which recently broke out to new highs) support our positive stance.

We stick with an Overweight recommendation to Financials and continue to highlight market leadership from the P/C insurance subsector given its low beta and hard market pricing. While a slowing global economy and deeply inverted yield curve are headwinds to the sector, the banks are well-capitalized and valuation is relatively attractive. The Financials trade at a 13.6x P/E (second lowest of all sectors) and P/Book ratio in line with its 5-year average. Moreover, relative performance has been solid since August with relative strength now on the verge of attempting a breakout. Market rotation from Growth to Value is likely providing some support to Financials relative performance, given it is the largest weighting (~20%) within Value.

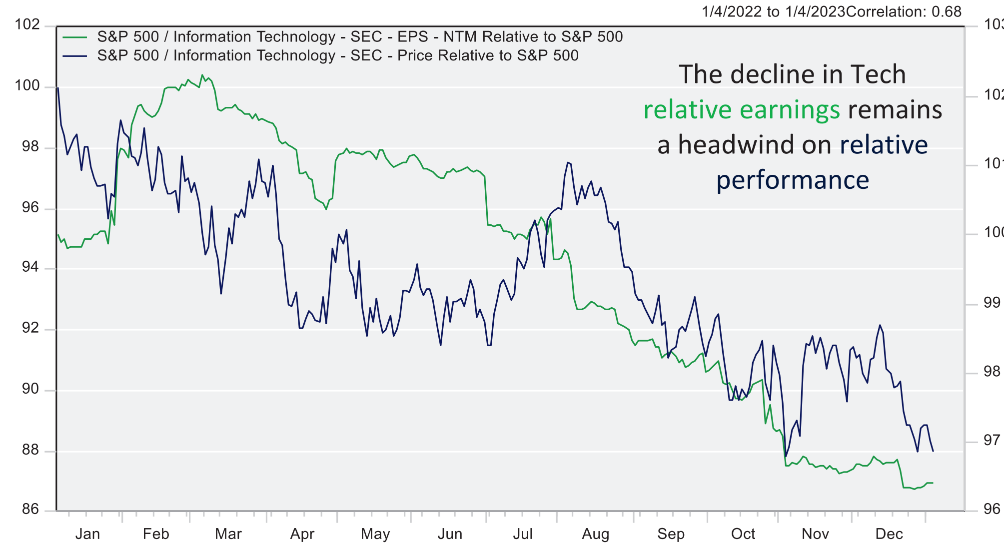




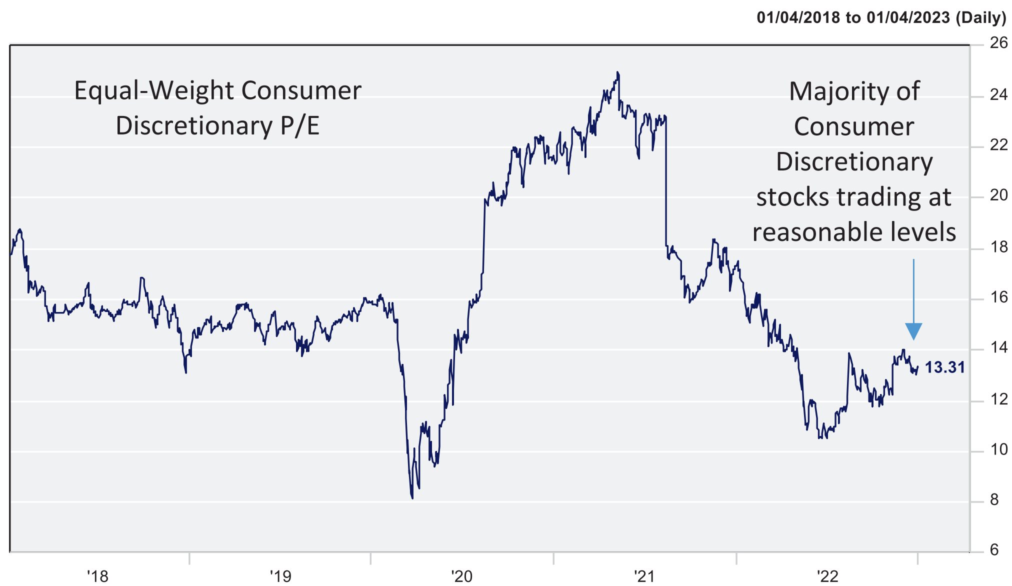
Source: FactSet, Gibbs Capital Management

Sector Recommendations

Technology performance remains weak- the index is in a downtrend with relative strength near lows. While valuation has become more reasonable within the sector (following a ~30% decline over the past year), P/E multiples are still relatively high and earnings estimates are getting revised downward at a quicker pace than the S&P 500. This **weak relative earnings trend, in conjunction with uninspiring relative performance, keeps us at Equal-Weight on Technology** for now.



Despite high inflation eating into consumer disposable income levels and increasing concerns on profit margins and earnings potential over the next year, relative performance for the average Consumer Discretionary stock has been improving over the past several months. This is encouraging, and is likely a function of valuations reaching very low levels in 2022 accompanied by relative earnings trends showing some improvement in recent months**. While we do believe that Consumer Discretionary presents long-term opportunity on the other side of this bear market, we also believe that sustainable upside for equities may take time- and stick with our Equal-Weight recommendation on Consumer Discretionary for now**.



Communication Services have pulled in over 40% from their highs with **earnings weakness acting as the major headwind**. This remains an issue (with relative earnings still weak), **however valuation is also cheap**. The sector trades at a 16x P/E, which is in line with 2018 trade war and 2020 Covid shutdown lows. While valuation is often not a great timing indicator, it does increase long-term potential. We are reluctant to make changes to our stance at this point- and **maintain our Equal Weight recommendation on Communication Services**.

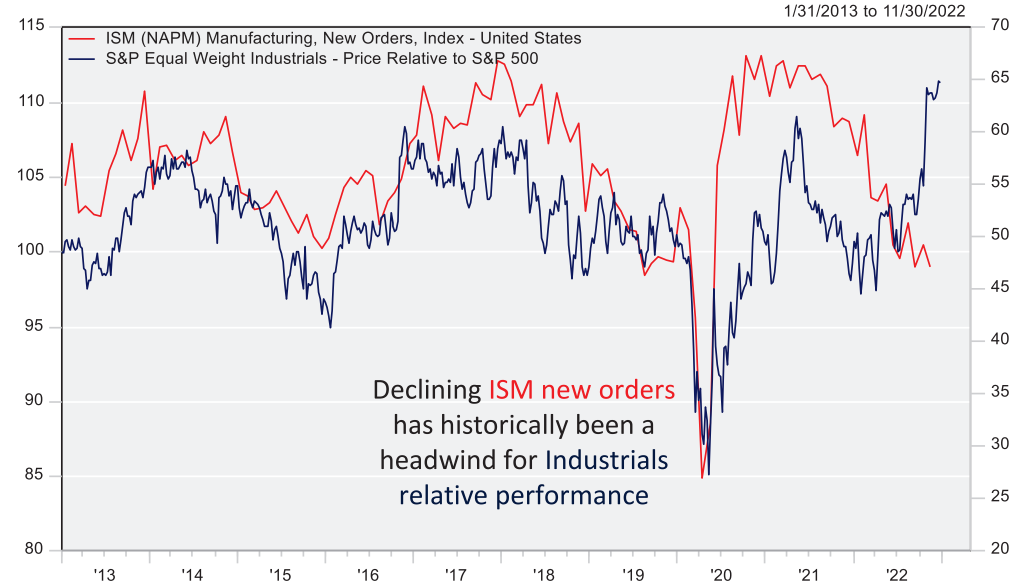
Source: FactSet, Gibbs Capital Management

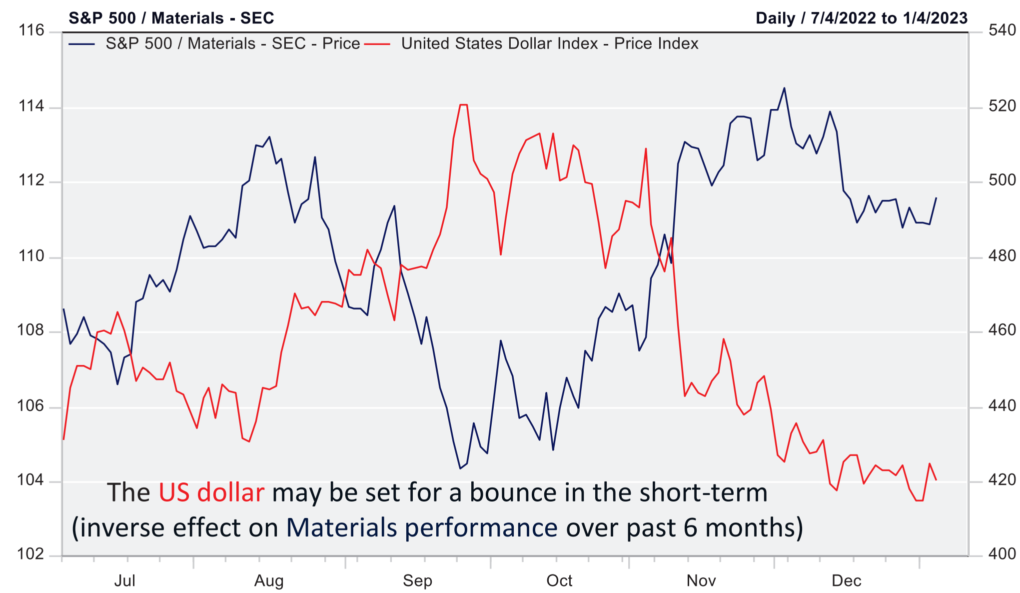
Sector Recommendations

Despite a weakening global economy, the Industrials have shown strong relative performance trends. This strength has been predominantly due to Aerospace & Defense (low beta, elevated geopolitical risk) and Machinery (0.86 beta, exposure to “clean energy” incentives) making up 44% of the sector. While trends in these subsectors remain promising, **the negative influence of declining ISM new orders (in a weakening economic backdrop) on sector relative performance historically, keep us at Equal-Weight on Industrials** for now.

Real Estate has pulled in significantly over the last year (-28%) as sharply higher interest rates weigh on the sector’s fundamental outlook. Valuation has become much more compelling now at a 16.8x P/FFO, which is the lower end of its past 10-year range (though did touch 14x at the Covid shutdown low, as well as a very low 9x in the ’09 credit crisis). We believe **a lot of negative news has been priced in already**, but **we maintain an Equal-Weight recommendation on Real Estate with earnings estimates in decline and relative strength trends weak**.

Materials relative strength has benefitted greatly from the drop in the US dollar since October. **While the US dollar’s sharp ascent may be set to moderate (a positive development for Materials), it is now sitting on long-term technical support and may be due for a short-term bounce**. Additionally, valuation is cheap at a 8.9x EV/EBITDA and 13.9x P/E (both below 10-year averages), but earnings estimate revision trends are weak. We maintain our **Equal-Weight recommendation on Materials**.



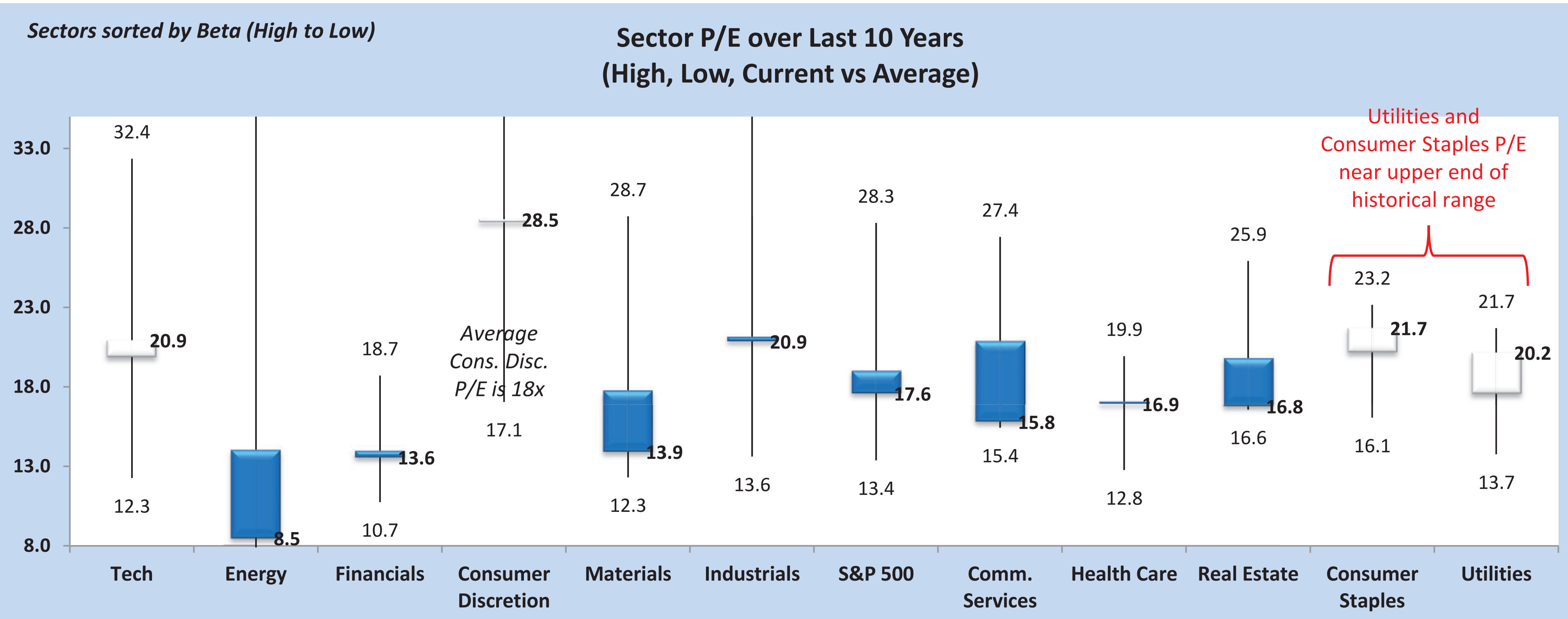


Source: FactSet, Gibbs Capital Management

Sector Recommendations

We **maintain an Underweight recommendation on Utilities**. The sector's P/E of 20.2x is at the upper-end of its historical range and its **relative P/E of 1.15x is a new 20+ year high**. Additionally, Utilities have stalled near technical resistance at the 200-day moving average and relative strength trends have become more sideways over the past six months. While the sector's defensive qualities (low beta) and US-centric business may provide support in volatile market periods, we are **more interested in other areas at this stage of the bear market**.

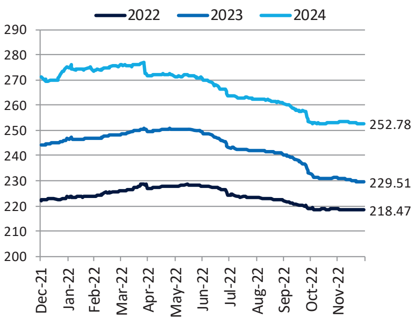
Consumer staples have benefitted from their low beta, more defensive status in this year's volatility. However, like Utilities, **valuation is now very elevated**. The sector's **relative P/E of 1.23x is at the upper-end of its historical range** (20+ year high is ~1.3x). While the sector is likely to hold up better in a potential down-leg for equities, **we find other areas more compelling over the next 12 months**. Remain **Underweight Consumer Staples**.



Source: FactSet, Gibbs Capital Management

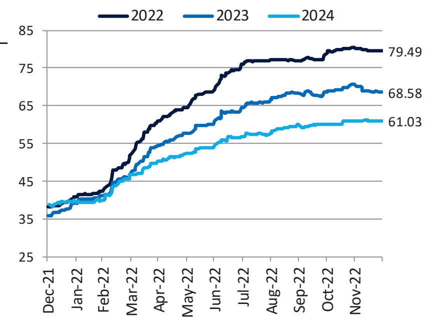
Sector Earnings Estimate Revision Trends

S&P 500



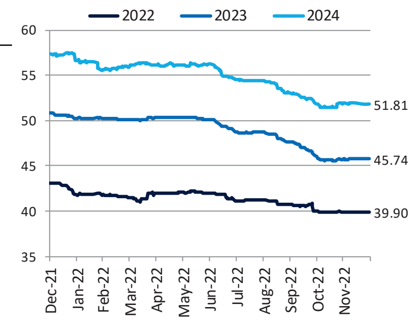
EPS Growth Estimates	
2022	5.7%
2023	5.0%
2024	10.1%

Energy



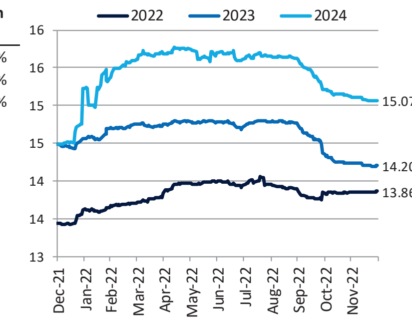
EPS Growth Estimates	
2022	156.6%
2023	-13.7%
2024	-11.0%

Industrials



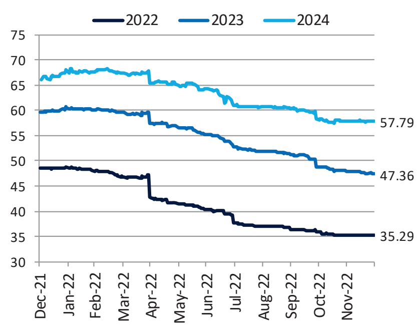
EPS Growth Estimates	
2022	29.6%
2023	14.6%
2024	13.2%

Real Estate



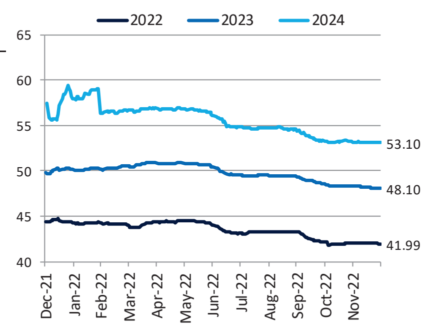
FFO Growth Estimates	
2022	10.8%
2023	2.5%
2024	6.1%

Consumer Discretionary



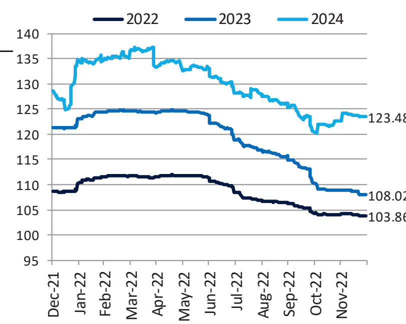
EPS Growth Estimates	
2022	-11.0%
2023	34.1%
2024	22.0%

Financials



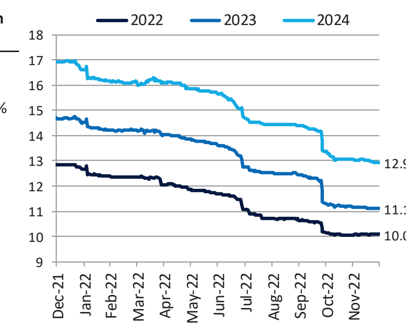
EPS Growth Estimates	
2022	-14.9%
2023	14.6%
2024	10.4%

Technology



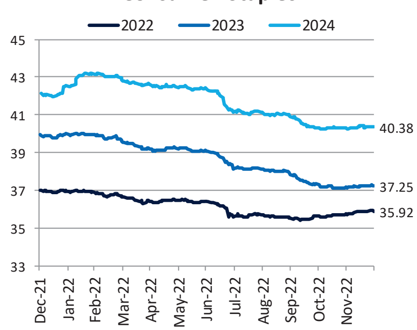
EPS Growth Estimates	
2022	4.4%
2023	4.0%
2024	14.3%

Communication Services



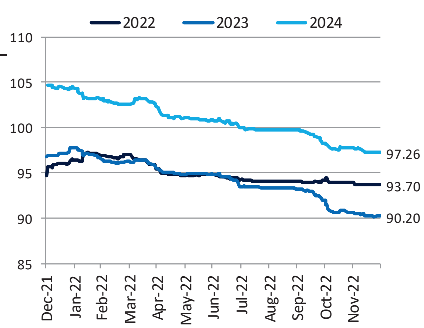
EPS Growth Estimates	
2022	-16.6%
2023	10.1%
2024	16.4%

Consumer Staples



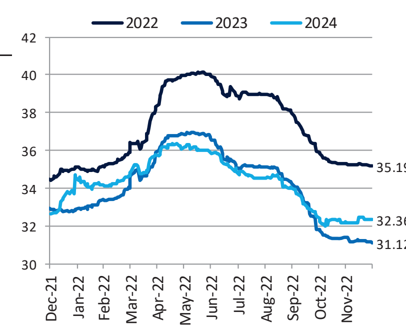
EPS Growth Estimates	
2022	2.5%
2023	3.8%
2024	8.4%

Health Care



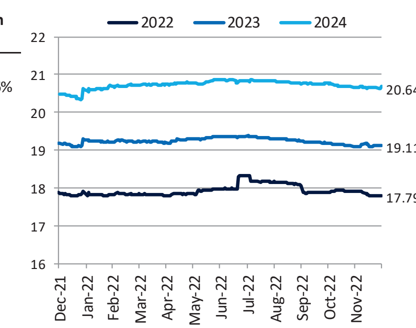
EPS Growth Estimates	
2022	3.9%
2023	-3.7%
2024	7.8%

Materials



EPS Growth Estimates	
2022	5.3%
2023	-11.6%
2024	4.0%

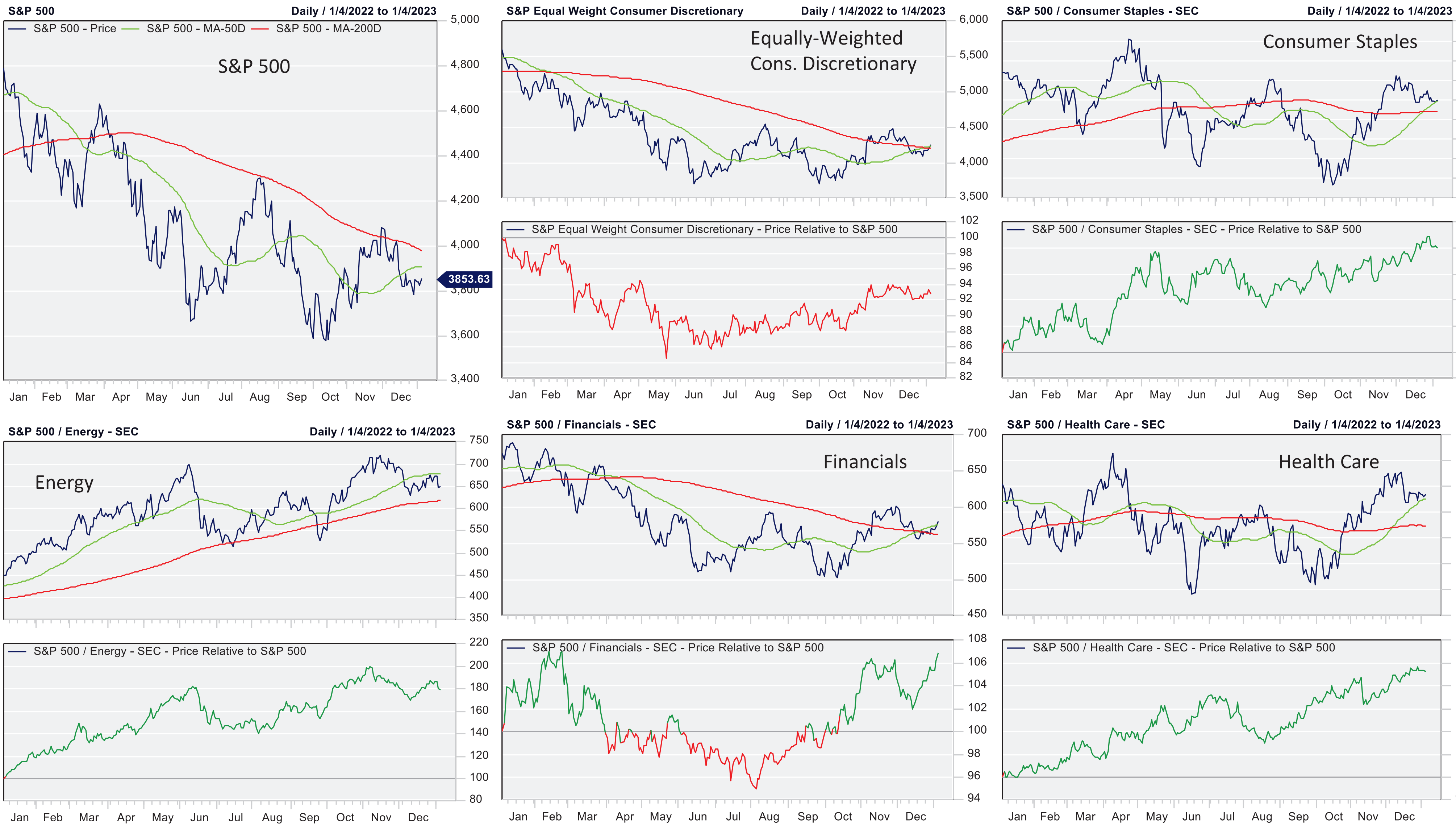
Utilities



EPS Growth Estimates	
2022	1.4%
2023	7.5%
2024	8.2%

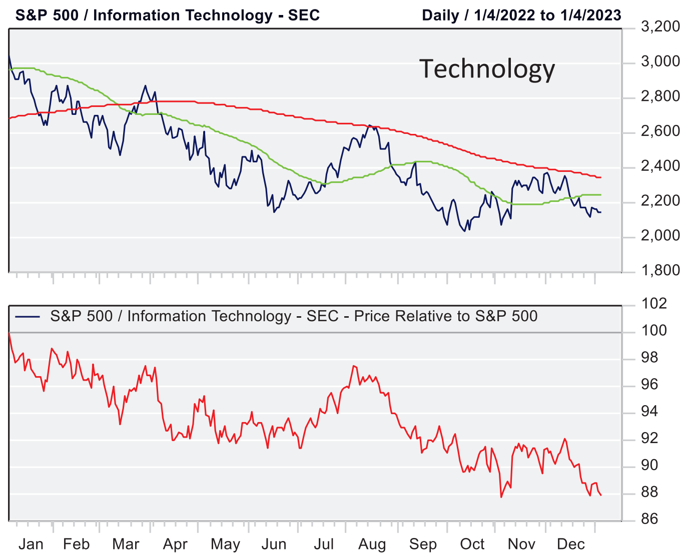
Source: FactSet, Gibbs Capital Management

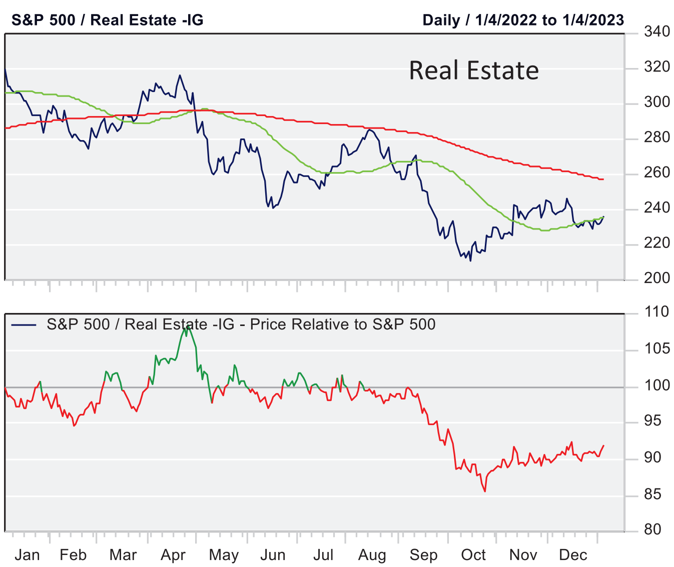
Sector Relative Performance Charts

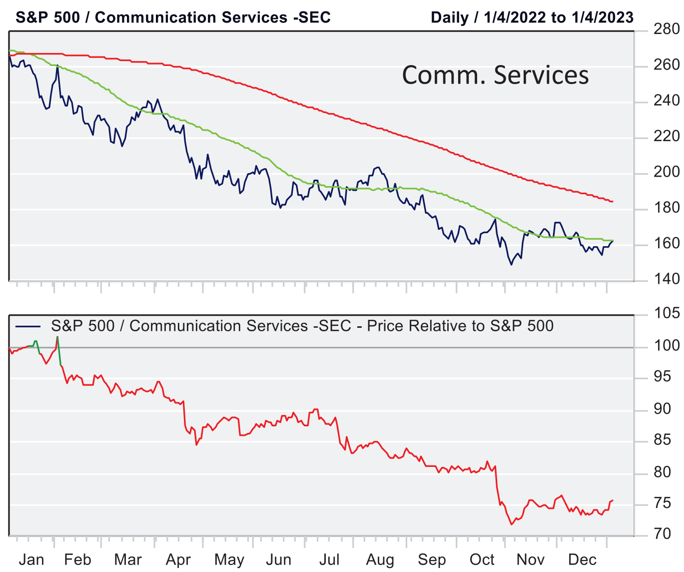


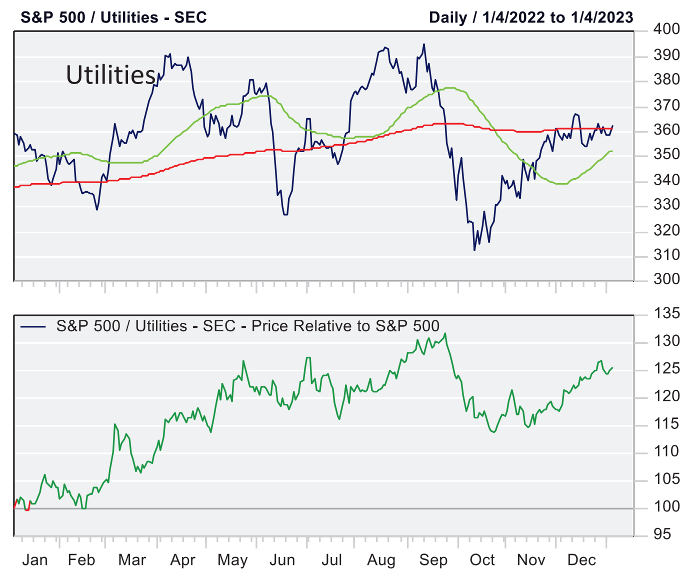
Source: FactSet, Gibbs Capital Management

Sector Relative Performance Charts









Source: FactSet, Gibbs Capital Management

S&P Industry Group Returns

S&P 500 Industry Group	Beta (3Yr)	1 Month	3 Month	12 Month
Consumer Durables & Apparel	1.14	3.1%	25.2%	-28.6%
Household & Personal Products	0.62	0.9%	16.6%	-10.8%
Utilities	0.78	-0.1%	4.7%	-0.5%
Telecommunications Services	0.60	-0.5%	6.0%	-11.5%
Insurance	0.96	-2.4%	12.4%	8.9%
Capital Goods	0.99	-2.5%	19.4%	-1.2%
Health Care Equipment & Services	0.88	-2.6%	6.9%	-8.4%
Pharmaceuticals Biotechnology & Life	0.66	-2.9%	11.7%	1.5%
Food Beverage & Tobacco	0.67	-3.3%	10.1%	4.7%
Banks	1.21	-4.4%	8.1%	-23.2%
Diversified Financials	1.05	-4.4%	10.8%	-12.8%
Real Estate	0.96	-4.5%	1.3%	-27.5%
Software & Services	1.15	-5.7%	3.2%	-26.9%
Energy	1.10	-5.7%	10.9%	48.7%
Commercial & Professional Services	0.88	-5.9%	4.0%	-8.1%
Transportation	0.98	-5.9%	8.6%	-18.9%
S&P 500	***1.00***	***-6.1%***	***4.0%***	***-20.3%***
Consumer Services	1.04	-6.4%	12.2%	-15.9%
Retailing	0.99	-6.4%	-8.8%	-34.7%
Materials	0.99	-6.9%	10.6%	-13.0%
Food & Staples Retailing	0.63	-7.7%	2.2%	-11.5%
Media & Entertainment	1.06	-8.0%	-4.7%	-43.5%
Semiconductors & Semiconductor Equ	1.41	-9.9%	6.8%	-38.9%
Technology Hardware & Equipment	1.16	-13.3%	-7.9%	-29.7%
Automobiles & Components	1.42	-37.7%	-45.7%	-67.8%

Source: FactSet, Gibbs Capital Management. All charts and data as of 1/4/2023

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The **S&P 500** is an unmanaged index of 500 widely held stocks that is generally considered representative of the U.S. stock market.

The **Dow Jones Industrial Average (DJIA)** is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange (NYSE) and the NASDAQ.

The **NASDAQ Composite** is a stock market index of the common stocks and similar securities listed on the NASDAQ stock market.

The **MSCI World All Cap Index** captures large, mid, small and micro-cap representation across 23 Developed Markets (DM) countries. With 11,732 constituents, the index is comprehensive, covering approximately 99% of the free float-adjusted market capitalization in each country.

The **MSCI EAFE (Europe, Australasia, and Far East)** is a free float-adjusted market capitalization index that is designed to measure developed market equity performance, excluding the United States & Canada. The EAFE consists of the country indices of 21 developed nations.

The **MSCI Emerging Markets Index** is designed to measure equity market performance in 23 emerging market countries. The index's three largest industries are materials, energy, and banks.

The **Russell 2000** index is an index measuring the performance of approximately 2,000 smallest-cap American companies in the Russell 3000 Index, which is made up of 3,000 of the largest U.S. stocks.

The **NYSE Alerian MLP** is the leading gauge of energy infrastructure Master Limited Partnerships (MLPs). The capped, float-adjusted, capitalization-weighted index, whose constituents earn the majority of their cash flow from midstream activities involving energy commodities, is disseminated real-time on a price-return basis (AMZ) and on a total-return basis (AMZX).

The **Barclays Intermediate Government/Credit Bond** index measures the performance of U.S. Dollar denominated U.S. Treasuries, government-related and investment grade U.S. corporate securities that have a remaining maturity of greater than one year and less than ten years.

The **Euro Stoxx 50 Index** is a market capitalization weighted stock index of 50 large, blue-chip European companies operating within Eurozone nations. Components are selected from the Euro STOXX Index which includes large-, mid- and small-cap stocks in the Eurozone.

The **China CSI 300** is a capitalization-weighted stock market index designed to replicate the performance of top 300 stocks traded in the Shanghai and Shenzhen stock exchanges. It had a sub-indexes CSI 100 Index and CSI 200 Index.

The **S&P 500 Futures** is a capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The **DJIA Futures** is a stock market index futures contract traded on the Chicago Mercantile Exchange`s Globex electronic trading platform. Dow Futures is based off the Dow 30 stock index.

The **Nasdaq 100 Futures** is a modified capitalization-weighted index of the 100 largest and most active non-financial domestic and international companies listed on the NASDAQ.

Europe: DAX (Deutscher Aktienindex (German stock index)) is a blue chip stock market index consisting of the 30 major German companies trading on the Frankfurt Stock Exchange.

Asia: Nikkei is short for Japan's Nikkei 225 Stock Average, the leading and most-respected index of Japanese stocks. It is a price-weighted index composed of Japan's top 225 blue-chip companies traded on the Tokyo Stock Exchange.

Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance. Individual investor's results will vary. Past performance does not guarantee future results. Future investment performance cannot be guaranteed, investment yields will fluctuate with market conditions.

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