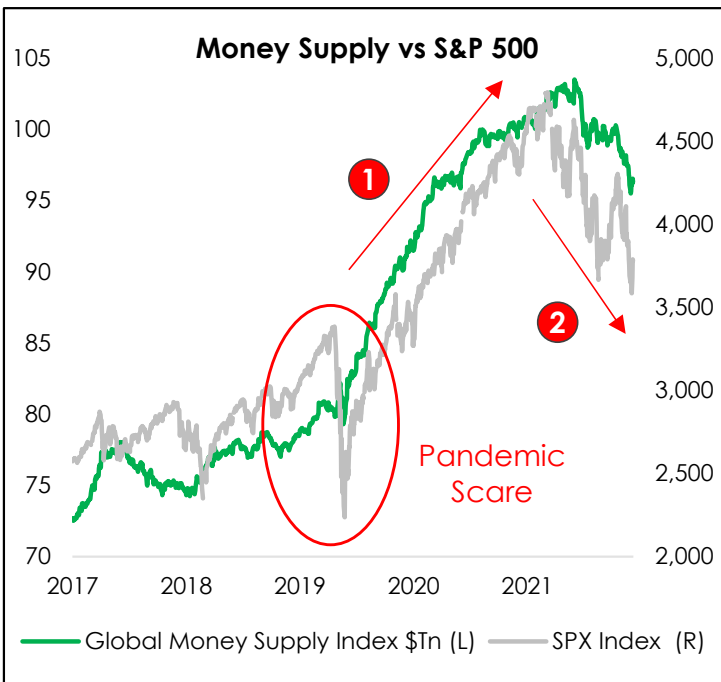


# “Money Makes the World Go Round”

## McLean Research – September 2022 Update

**We are in a bear market. This is a great time to prepare for better times in the future. Remember, this too shall pass, although it may take longer than we like!**

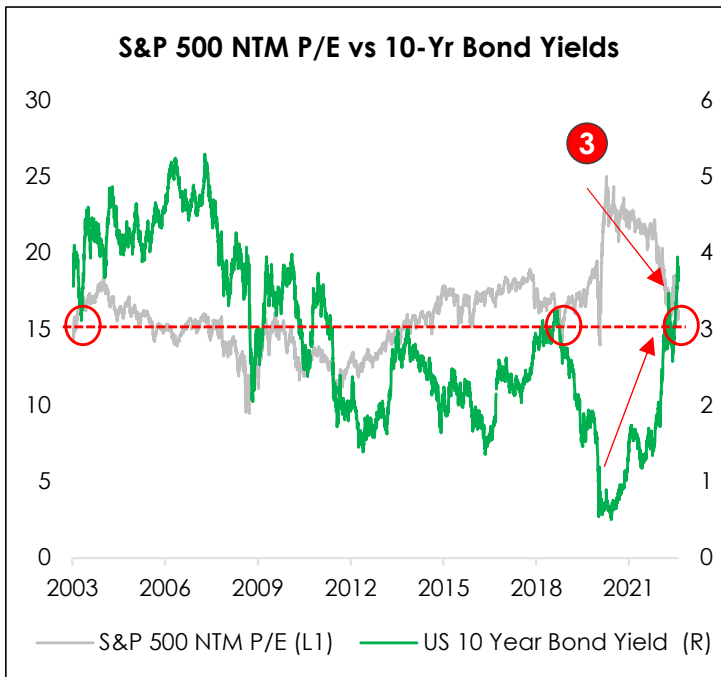
Chart 1



Source: Bloomberg

- 1 Money supply increased at an unprecedented rate in response to COVID-19. The global money supply grew about 25%, fueling ~50% gains in the S&P 500 over the same time (Chart 1). Then came inflation.
- 2 In response to the highest inflation in decades, the Federal Reserve hiked interest rates and moved from QE to QT, **decreasing the money supply at the fastest pace since 1938**. The market has followed the path of money supply with Sep '22 seeing the worst decline for the S&P 500 since Mar '20 (Chart 1).
- 3 The resulting rapid climb in yields has led to an equally fast decline in valuation multiples (Chart 2).

Chart 2



Source: Bloomberg

The good news is inflation appears to be moderating as indicated by several factors:

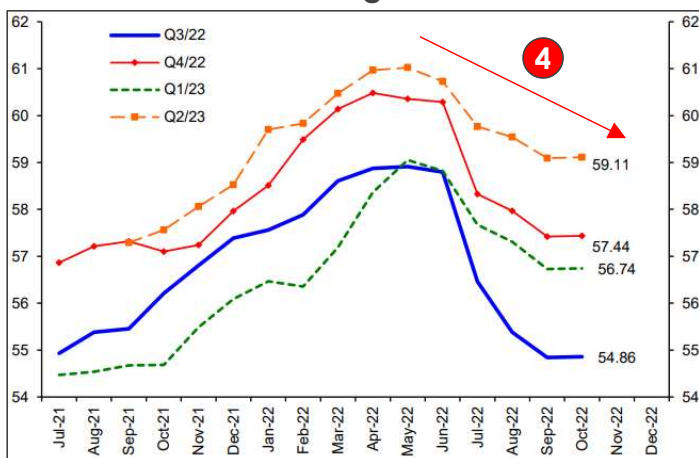
- I. NY Fed Global Supply Chain Pressure Index has declined significantly from an all-time high of 4.3 in Dec '21 to 1.1 in Sep '22. Container costs are almost back to pre-COVID levels.
- II. CRB commodity price index is down 12.7% from the high in May '22.
- III. New and existing home sales are -33.9% and -27.8% from their highs reached in Aug '20 and Jan '21.
- IV. Global food prices have started to roll over, declining 13.6% since Mar '22.

**Employment growth** has been very strong and is the last key element that **needs to moderate before inflation can decline significantly** and a potential Fed pivot can occur.

# “Money Makes the World Go Round”

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Chart 3 – S&P 500 Earnings Estimates



Source: Scotiabank GBM Portfolio Strategy, FactSet

As interest rates continue to rise, the threat of a recession looms and earnings estimates will continue to decline (Chart 3).

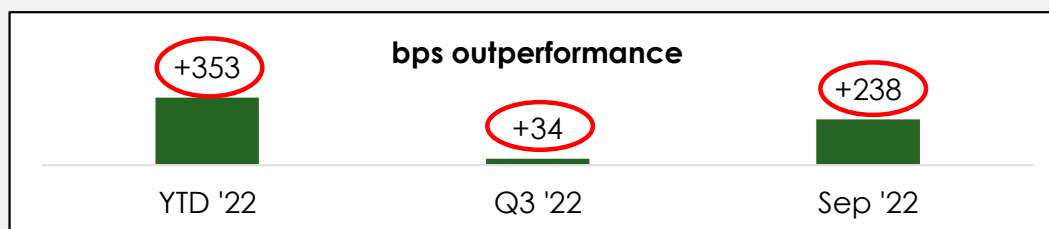
4 Earnings estimates have seen a significant decline since Jun '22. More importantly, we expect S&P 500 earnings to decline 10-20% in the next twelve months.

Current consensus is calling for S&P 500 earnings to be up 8% YoY to \$243 for 2023. Assuming a recession, we see \$190-\$200 as more likely.

### Now What?

- We currently have a 22% cash position in the portfolio, driven by our expectations of a coming recession and an earnings decline.
- As the economy weakens, credit spreads widen significantly, and VIX explodes to the upside, we expect inflation to decline to 3-5% YoY in the next 6-9 months, and from there, we expect the Fed to pause or pivot between Q4 '22 to Q2 '23.
- At that point, we expect to be aggressive buyers of quality compounders, including increasing our new positions in Ulta Beauty and The Home Depot, along with other great compounders currently in the portfolio.

### Portfolio Update vs. Benchmark



Source: Bloomberg, McLean Research  
Benchmark = 65% S&P 500 Index, 35% S&P TSX Index.

### Great Time to Prepare: New Initiation on Adobe

- The negative reaction to the Figma deal has provided an attractive opportunity to invest in a high-quality compounder. We await more information at the Investor Day on Oct 18<sup>th</sup> before initiating a position.
- If you would like a copy of our full initiation report, please be in touch with our team at [team\\_mfo@mcleanresearch.ca](mailto:team_mfo@mcleanresearch.ca).