Lane Asset Management

Stock Market in Focus

August 1, 2022

www.LaneAssetManagement.com

Edward.Lane@LaneAssetManagement.com

Edward Lane, ASA, CFP®

Stockbridge, MA

Lane Asset Management
Stock Market in Focus

Stock Market in Focus (SMiF) presents my view of equity market conditions and factors that I believe may indicate direction in coming weeks. For the most part, these factors are based on what's called "technical analysis," or TA. Other factors, collectively referred to as "fundamental analysis," or FA, include various economic, political and geopolitical conditions that impact investment markets. Those factors inform my view of the market but trading decisions are based entirely on technical analysis.

Technical analysis is basically the study of price movement and trading volume of stocks, funds or indexes sliced and diced into different indicators that can be suggestive of future price direction. The more these indicators agree with one another, the more reliable the trend interpretation, though there is no guarantee of outcome. TA is essentially an analysis of investor behavior seen through market action which is presumed to indicate, if past is prologue, the direction investors believe a given investment is headed.

The FA factors affecting markets in 2022 are a unique combination and number of headwinds, at least as far as I can remember for the last 50 years. They include the wide-ranging effects of COVID, changing monetary policy by the U.S. Federal Reserve (and other central banks) to fight inflation, the invasion of Ukraine by Russia, climate change, potential recession, Washington politics, currency translation (i.e., relative U.S. dollar strength), a "fiscal cliff" (a reduction if federal spending) and geopolitical tension with China and in the Middle East, to name some of the more familiar factors. Owing to the uniqueness of these factors, traditional means of forecasting market direction are made all the more difficult.

Lane Asset Management
Stock Market in Focus
A Summary

In the charts shown on the pages that follow, I will present a cautiously optimistic outlook for the stock market based on technical characteristics.

Today, the most important issue driving investor expectations is the direction of inflation and its impact on corporate profits. To understand the direction of inflation, a good place to start is understanding where inflation has been coming from.

Since the inflationary peak of nearly 15% in 1980, the inflation rate, measured by the year-over-year increase in the CPI, exceeded 5% only twice, briefly in 1990 and 2008, before spiking to its current level of 9.1% starting in the second quarter of 2021.

Inflation can have two causes: too much demand for the goods and services available and too few goods and services to meet the demand. It is fair to recognize that fiscal stimulus (government spending) was a significant early cause of demand-driven inflation when the $2.3 trillion Cares Act was passed in March 2020 by President Trump with an additional $484 billion in April 2020 followed a year later by President Biden's passage of the $1.9 trillion American Rescue Plan.

However successful these programs were in relieving hardship for millions of Americans, their size and implementation clearly led to a sharp rise in demand and, with it, demand-driven inflation. While household savings had been rising since the Great Recession (2009), savings skyrocketed in 2020 and again in 2021. This led to a spending spree that raised corporate profits to their greatest annual percentage increase since at least back to 1948. The stock market followed suit with three annual back-to-back gains in 2019-2021, increasing the S&P 500 index by an unprecedented 100% over the three-year period.

But fiscal stimulus was only the beginning as COVID-induced manufacturing and supply chain shocks quickly exacerbated inflation from the supply perspective. Russia's invasion of Ukraine on February 24th made matters worse, especially for food and energy. And that's where the problem gets worse since the tools being used by the Federal Reserve to fight inflation can do nothing about either of these two causes.

(cont.)

Lane Asset Management
Stock Market in Focus

A Summary

With the personal savings now below pre-COVID stimulus levels, unless a solution to supply shocks and/or absent resolution of the Ukraine invasion can be found, it seems the chances are that the Fed may need to raise short term rates high enough to cause a severe recession (something economist and former Treasury secretary Larry Summers has predicted). There's now some evidence that the economy is, in fact, slowing with corporate profits declining along with consumer and business confidence. The situation is similar in China and even more so in Europe. Time will tell whether a recession will occur, as many expect, and whether this will bring down inflation without an improvement in supply constraints.

Technical analysis not only tells us where the stock market has been but provides an indication on where investors believe it is going, at least for the immediate future, based on how they see those headwinds in the aggregate.

As shown in the following pages, the broad consensus, as expressed through technical analysis, presents an improving outlook ("green shoots") following six solid months of downward pressure. Whether the rebound is because investors felt that the market was oversold in June, whether they think the "worst is behind us," or whether they look to the historical pattern of market recoveries and want to get ahead of the game, is uncertain. On the other hand, the nascent recovery could indicate no more than a technical "relief" rally, a technical phenomenon that will be short-lived.

Whatever the reality turns out to be, I believe it is not too early to begin increasing equity market exposure focused on those companies and sectors that have the strongest balance sheets, cash flows, and relative performance. I would also be prepared for an event that upsets investor expectations since the risk of further supply side disruptions or investor disappointment remains high.

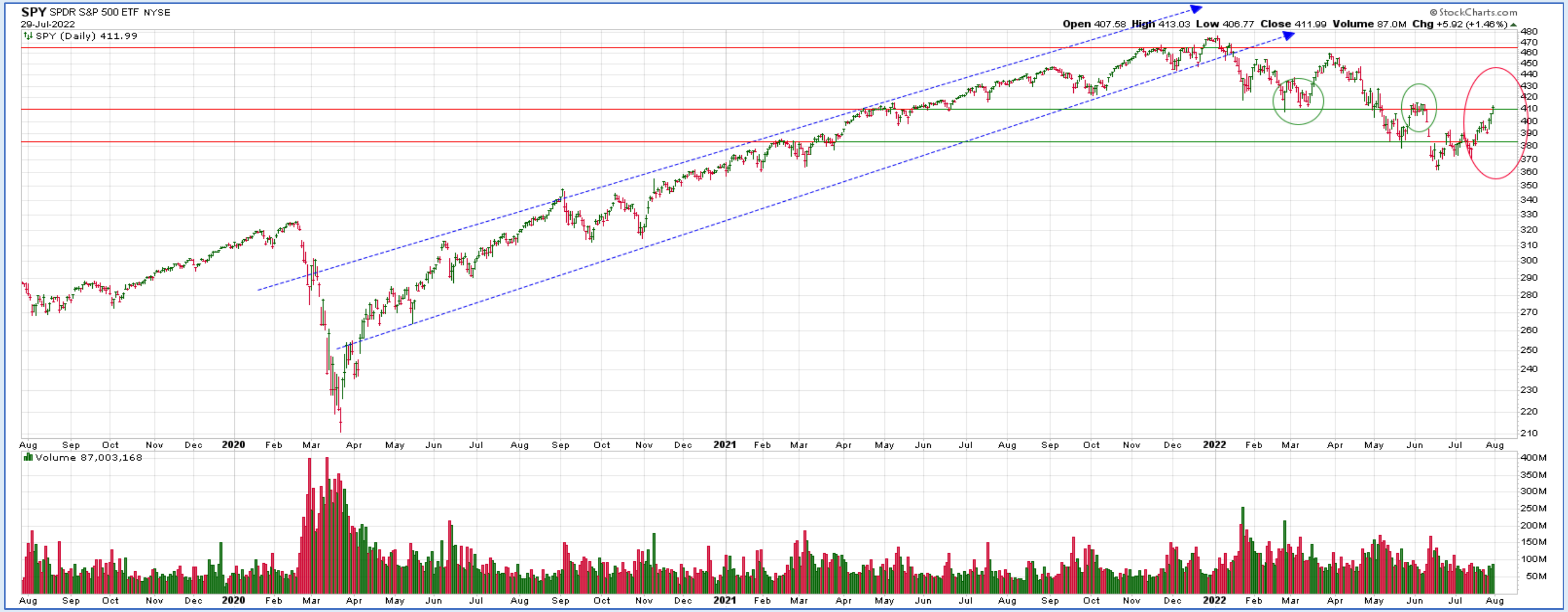
Questions about the above and the analyses that follow are welcome.

Stock Market in Focus

This chart shows the daily movement of the S&P 500 (SPY) for the last 3 years along with several TA factors that are noteworthy:

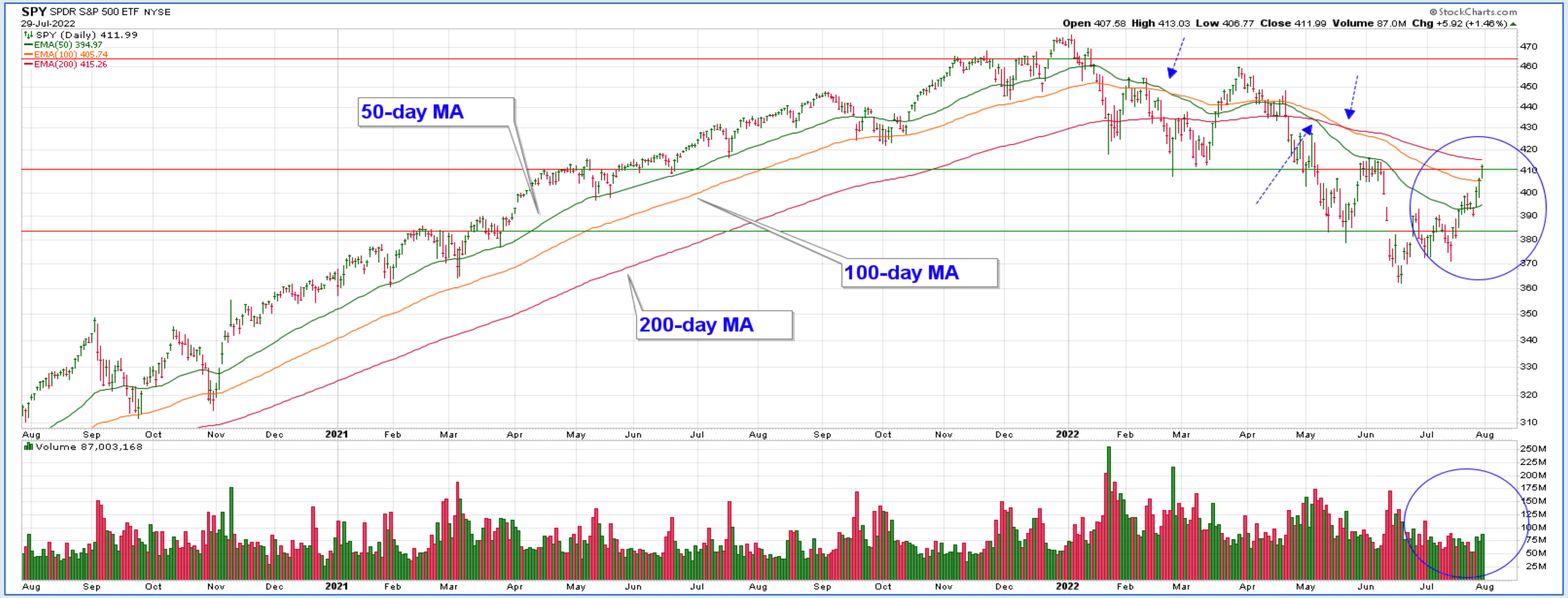
- First, note that price stayed within a channel bounded by the dotted blue lines starting with the recovery from the COVID market correction all the way until the beginning of 2020. Departure from this channel was a warning sign of a potential market correction. The volatility and brief recovery through April belied the severity of the correction to come.

- Second, note the horizontal lines which indicate areas of support and resistance (S/R lines) to price. The more times price reacts to a S/R line, the more meaningful it is. Here we see resistance at about $465, both support and resistance at about $410 and support around $380. We have now returned to a critical S/R point around $410. Note the price behavior in the green circles where the $410 level provided support in March and resistance in early June. If SPY can move above $410 in the coming days without falling back through, it would be a positive technical sign for the market.



This chart is the same as on the preceding page except that the period shown is 2 years rather than 3 to provide more clarity. Several factors are worth noting:

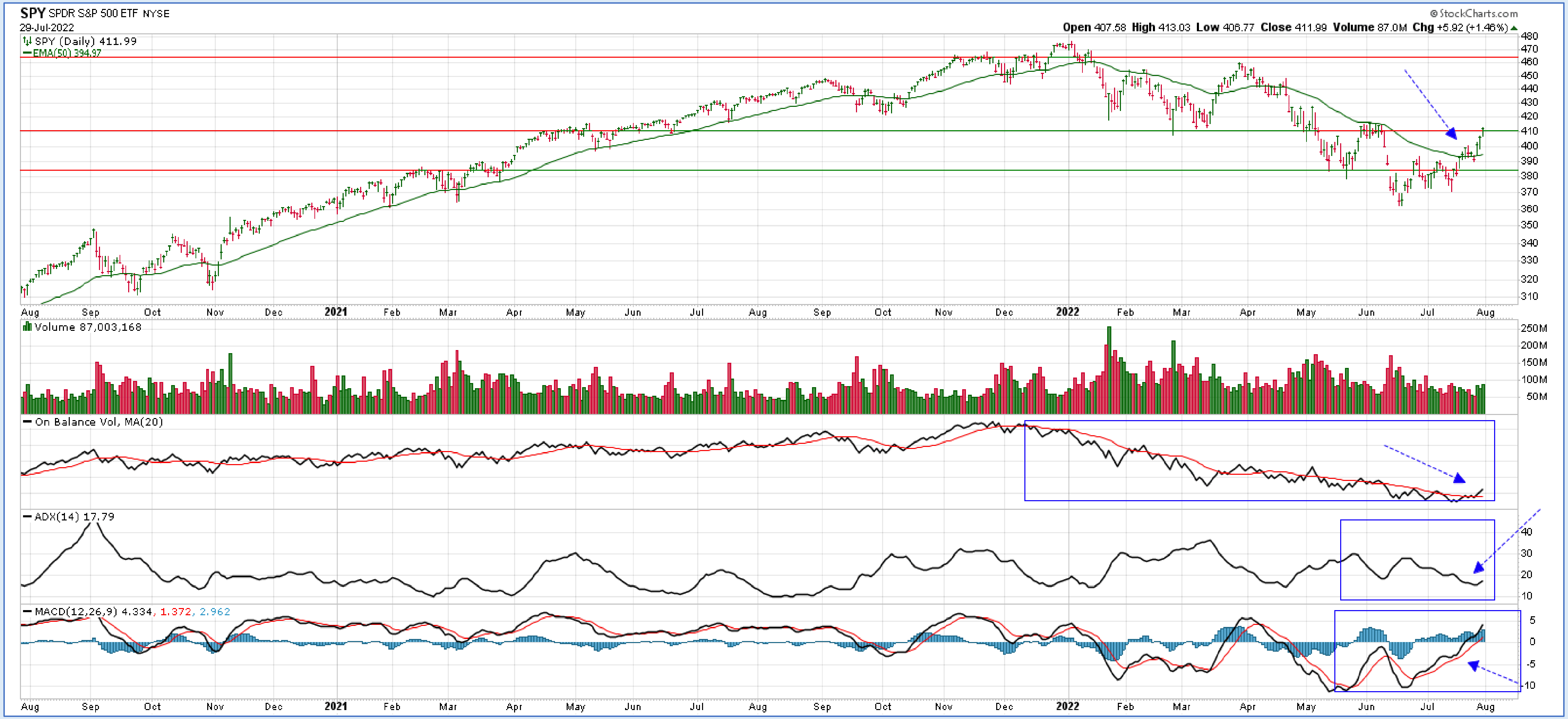
- Tracking the price of SPY are 3 moving averages (MAs): 50, 100, and 200 days. Moving averages are useful in determining trend and price support. As the price of SPY falls through the MAs and as the faster MAs cross over the slower MAs from above (at the blue arrows), this is an increasingly bad signal showing downward momentum. As the faster MAs are beginning to turn up, it will be an especially positive sign if they begin to cross over slower MAs from below.
- The 200-day MA is particularly important to TA analysts as it is seen to be a major support. When price falls below as it did this year, a rarity, it's considered a sign of significant price weakness. If price is able to come above the 200-day MA from below (as it has now done for the 50-day and 100-day MAs), it would be a positive signal to technical analysts.
- Trading volume shown at the bottom of the chart indicates a level of investor commitment. SPY's volume was 25% above its 10-day average on July 29th, a positive signal.



The chart on the next page presents several optimistic indicators (“green shoots”).

- First, while we are anxious about price getting past the resistance at $410, the fact that we have moved convincingly above the 50-day moving average is a hopeful sign.
- The blue box below the volume shows “On Balance Volume” (OBV) along with its 20-day moving average. OBV is an indicator that measures buying and selling pressure. OBV showed there was selling pressure for most of the time after late 2021. While still in a downtrend, some positive buying pressure is beginning to show up.
- The next block contains the “Average Directional Movement” index (ADX) that measures the strength of the trend averaged over 14 days. When the ADX has a negative slope, the strength of the price trend over the preceding 14 days is weak, not a good sign. This has been true since the mid-June recovery began but some positive strength seems to be developing in recent days.
- The bottom block contains the “MACD” momentum indicator which has been showing improvement since the mid-June reversal. While this indicator can change direction quickly, for now, the positive price advancement of the last several days is showing no weakness.

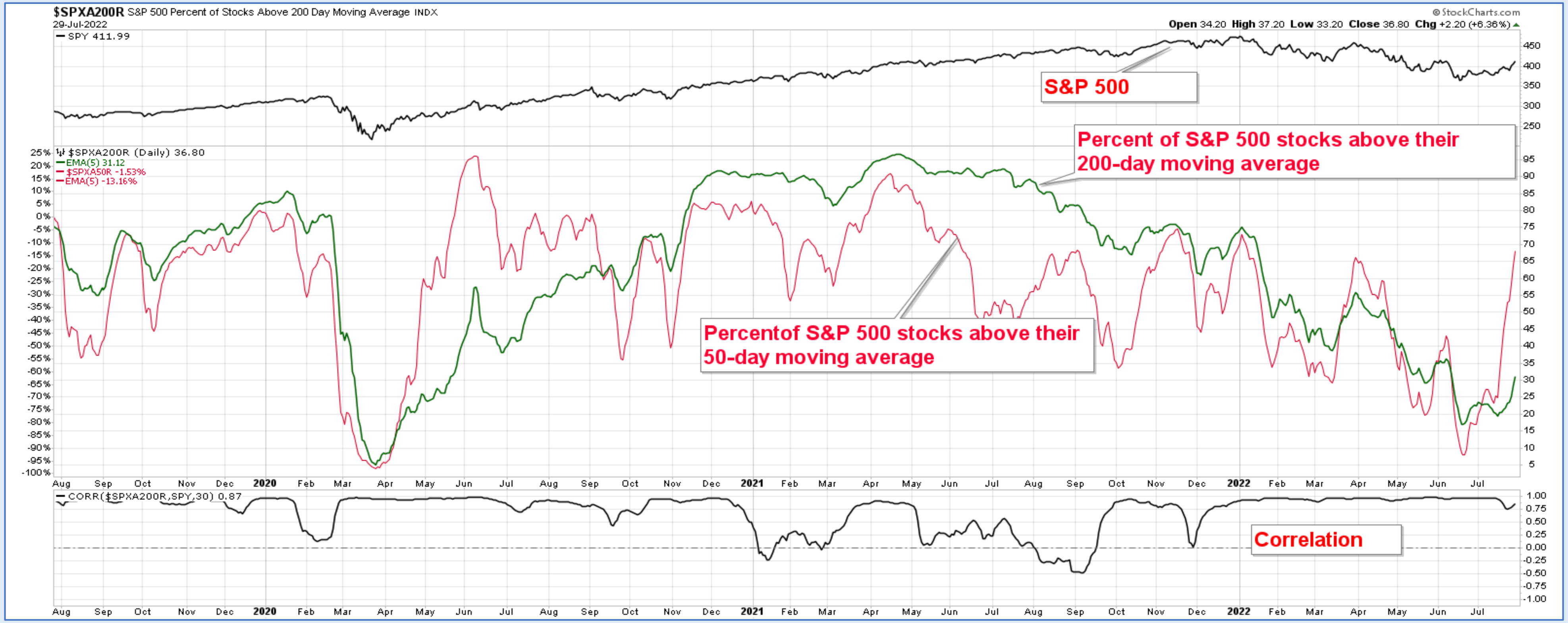
Lane Asset Management
Stock Market in Focus



Stock Market in Focus

This chart shows the percentage of S&P 500 stocks above their 50-day and 200-day moving averages. The following points are important:

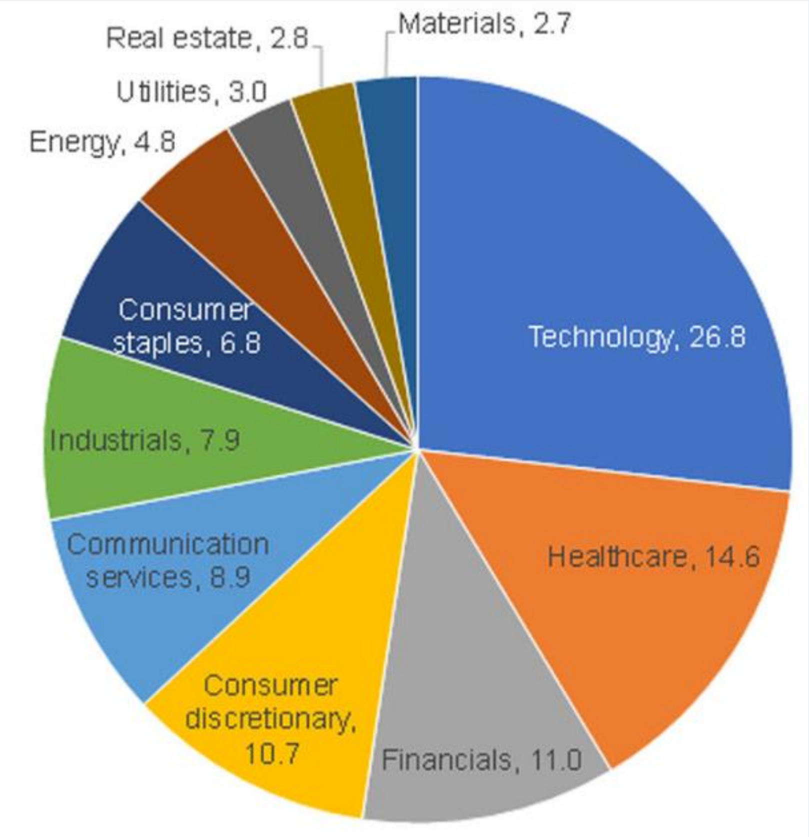
- There is generally a high correlation between the changes in the 200-day percentages and the performance of the S&P 500.
- Such a diversion began in middle 2021 as the percentage of stocks above their 200-day moving average stabilized and then began to fall while the S&P 500 continued to rise. The divergence ended with the market correction that began in early 2022.
- When the percentage of stocks in the S&P 500 below their 200-day moving average falls below 15% as they did 3 times in the last 20 years, most recently in 2020 (not shown), market participants have treated this as an extreme oversold situation and have come back into the market. This may help explain the recovery in prices since mid-June.
- The recent increase in the percentage of stocks above their 50-day moving average coming off a value of less than 10% is a positive sign.



Lane Asset Management

Stock Market in Focus

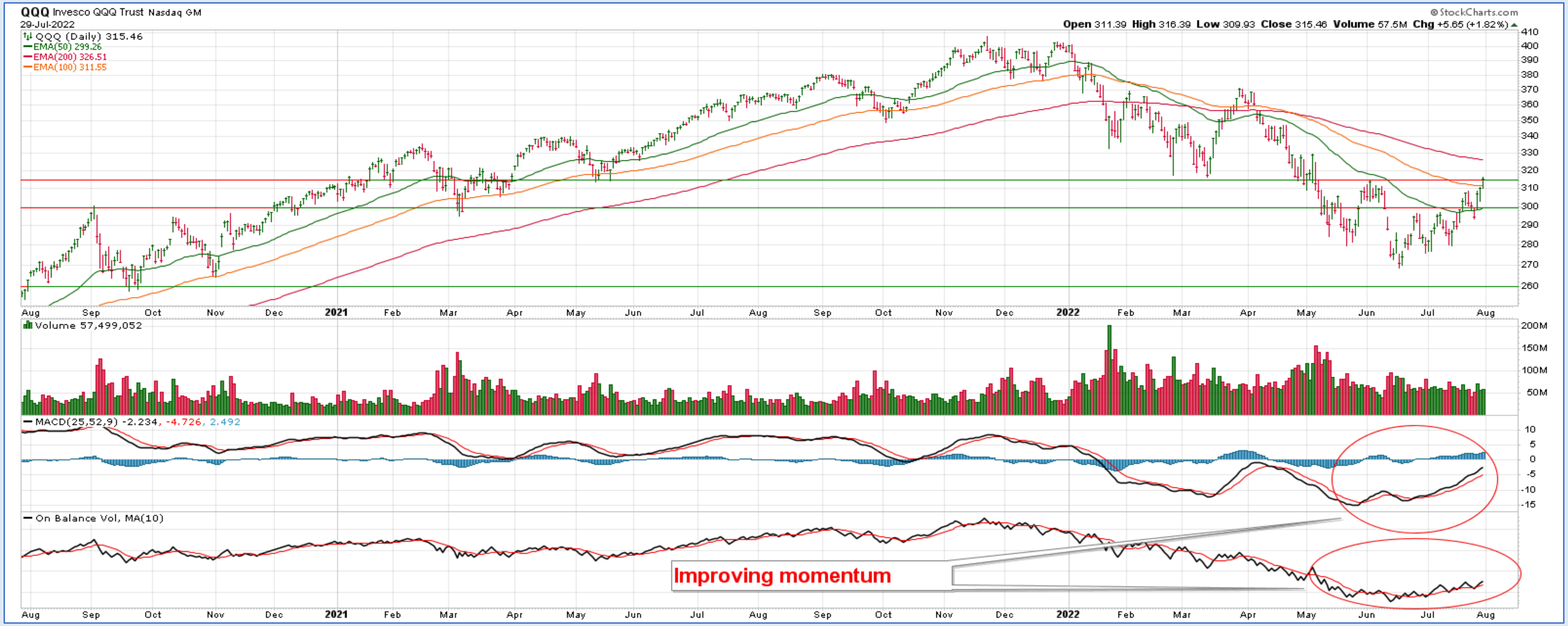
The charts below show the 11 sectors and their weighting that make up the S&P 500, only two of which - energy and utilities - had a positive return for the year (as of July 31st). All sectors have a positive return over the most recent month but four, technology (XLK), consumer discretionary (XLY), industrial sector (XLI) and real estate (XLRE), outperformed the broad S&P 500 index. Within the S&P 500, 10 companies (11 individual stocks since Alphabet (Google) has two classes of stock) make up about 29% of the entire index. Generally, as these companies go, so goes the entire S&P 500, and that has certain been true in recent days.



NAME	1D PERF	5D PERF	1M PERF	3M PERF	6M PERF	YTD PERF	1Y PERF
XLE - Energy Select Sector SPDR Fund	+04.34%	+10.22%	+07.35%	+05.52%	+21.98%	+44.25%	+63.54%
XLY - Consumer Discretionary Select Sector SPDR Fund	+03.88%	+05.22%	+16.70%	+00.20%	-08.22%	-20.05%	-11.00%
XLI - Industrial Select Sector SPDR Fund	+02.06%	+05.74%	+09.84%	+00.97%	-03.33%	-08.91%	-06.28%
XLK - Technology Select Sector SPDR Fund	+01.53%	+05.10%	+11.94%	+02.25%	-08.32%	-16.68%	-05.28%
XLF - Financial Select Sector SPDR Fund	+01.41%	+02.93%	+06.24%	-01.80%	-12.13%	-12.88%	-06.73%
XLB - Materials Select Sector SPDR Fund	+01.34%	+04.09%	+04.90%	-07.48%	-05.11%	-12.85%	-04.74%
XLU - Utilities Select Sector SPDR Fund	+00.86%	+06.51%	+06.62%	+04.61%	+10.42%	+04.83%	+14.54%
XLRE - Real Estate Select Sector SPDR Fund	+00.38%	+04.92%	+08.60%	-04.08%	-03.99%	-13.24%	-01.38%
XLC - Communication Services Select Sector SPDR Fund	+00.05%	+00.68%	+02.62%	-04.32%	-21.66%	-27.07%	-31.23%
XLV - Health Care Select Sector SPDR Fund	-00.33%	+01.98%	+03.01%	+02.05%	+02.22%	-05.33%	+01.76%
XLP - Consumer Staples Select Sector SPDR Fund	-00.77%	+01.76%	+03.27%	-03.34%	-00.38%	-02.23%	+06.99%

While the previous pages focused on the S&P 500, the chart below shows the picture for the technology-heavy NASDAQ 100 index (represented here by the ETF QQQ). Several factors are noteworthy:

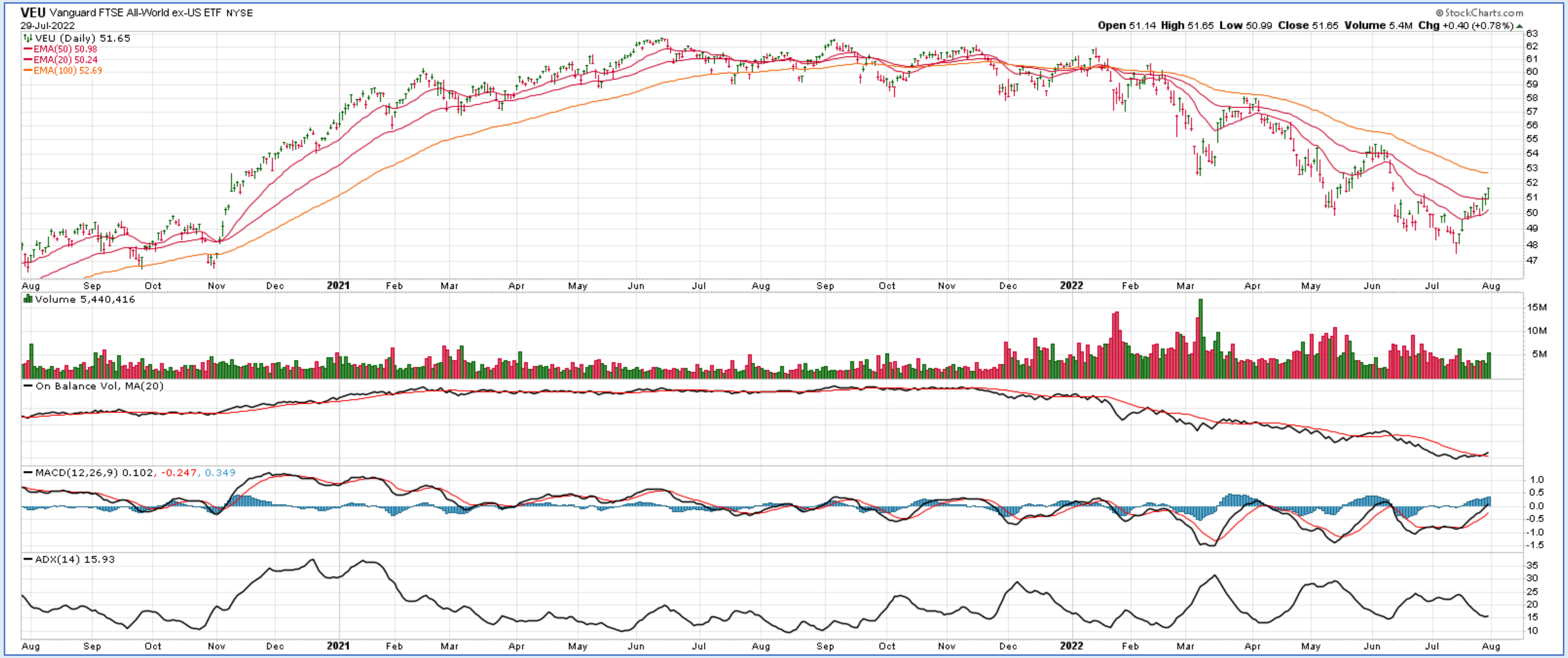
- The chart is similar to the S&P 500 though a bit more positive lately.
- Support and resistance is occurring at about $315 and $300, with $315 currently playing a pivotal role (similar to $410 for the S&P 500).
- At the bottom of the chart, both the MACD and the OBV are showing improving momentum (and stronger than the S&P 500), a very good sign.



Lane Asset Management
Stock Market in Focus

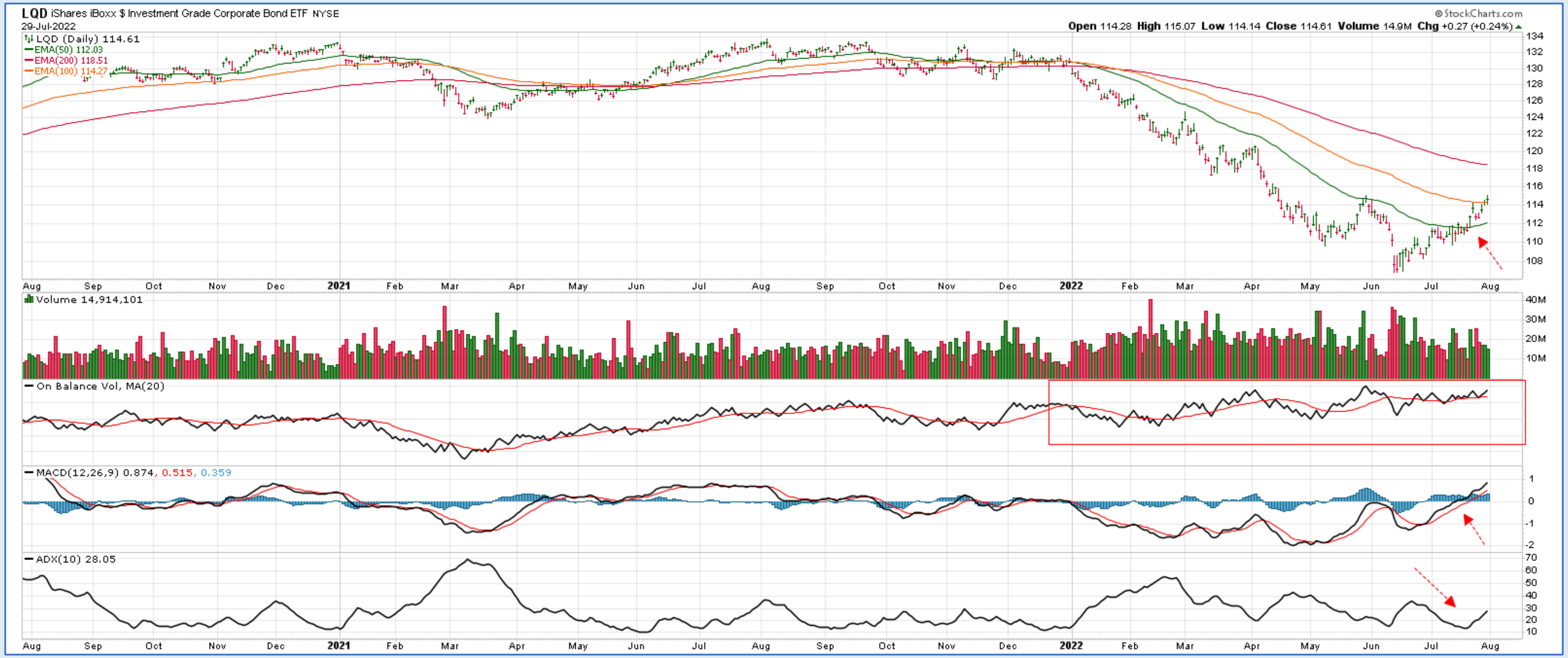
The chart below shows the performance of the Vanguard All-World (ex-US) ETF with the same TA tools as contained in prior charts. The following is noteworthy:

- Developed (mature) markets in Europe comprise about 30% of the fund, followed by emerging markets in Asia (16%), Japan (15%), and developed markets in Asia (11%).
- International stocks underperformed domestic stocks by about 7% in 2020 and an additional 20% in 2021 but have been similar in performance so far in 2022, including the more recent green shoots.



The chart below shows the performance of the Investment Grade Corporate Bond index using the ETF "LQD" as a proxy. The following points are worth noting:

- Performance characteristics and the technical indicators are remarkably similar to the S&P 500. Through this writing on July 31st, the cumulative returns for LQD and SPY are virtually identical.
- The On Balance Volume indicator is the only one of the highlighted indicators in this analysis that significantly differs from the equity analyses shown previously in that the OBV for LQD indicates that there has not been a substantial change in money flows into and out of LQD so far this year.
- The recent positive performance of LQD reflects the decline in 10-year bond yields since mid-June - a surprising result as the Federal Reserve continues to increase the federal funds rate and may suggest investor expectations of more moderate long-term rates despite current monetary policy.



Edward Lane is a CERTIFIED FINANCIAL PLANNER™. Lane Asset Management is a Registered Investment Advisor with the States of MA, NY, CT and NJ. Advisory services are only offered to clients or prospective clients where Lane Asset Management is properly licensed or exempted. No advice may be rendered by Lane Asset Management unless a client service agreement is place.

Investing involves risk including loss of principal. Investing in international and emerging markets may entail additional risks such as currency fluctuation and political instability. Investing in small-cap stocks includes specific risks such as greater volatility and potentially less liquidity. Small-cap stocks may be subject to higher degree of risk than more established companies' securities. The illiquidity of the small-cap market may adversely affect the value of these investments.

Investors should consider the investment objectives, risks, and charges and expenses of mutual funds and exchange-traded funds carefully for a full background on the possibility that a more suitable securities transaction may exist. A prospectus for all funds is available from Lane Asset Management or your financial advisor and should be read carefully before investing.

Note that indexes cannot be invested in directly and their performance may or may not correspond to securities intended to represent these sectors.

Investors should carefully review their financial situation, making sure their cash flow needs for the next 3-5 years are secure with a margin for error. Beyond that, the degree of risk taken in a portfolio should be commensurate with one's overall risk tolerance and financial objectives.

The charts and comments are only the author's view of market activity and aren't recommendations to buy or sell any security. Market sectors and related exchanged-traded and closed-end funds are selected based on his opinion as to their usefulness in providing the viewer a comprehensive summary of market conditions for the featured period.

Chart annotations aren't predictive of any future market action rather they only demonstrate the author's opinion as to a range of possibilities going forward. All material presented herein is believed to be reliable but its accuracy cannot be guaranteed. The information contained herein (including historical prices or values) has been obtained from sources that Lane Asset Management (LAM) considers to be reliable; however, LAM makes no representation as to, or accepts any responsibility or liability for, the accuracy or completeness of the information contained herein or any decision made or action taken by you or any third party in reliance upon the data. Some results are derived using historical estimations from available data. Investment recommendations may change without notice and readers are urged to check with tax advisors before making any investment decisions. Opinions expressed in these reports may change without prior notice. This memorandum is based on information available to the public.

This memorandum is not an offer to buy or sell or a solicitation of an offer to buy or sell the securities mentioned. The investments discussed or recommended in this report may be unsuitable for investors depending on their specific investment objectives and financial position. The price or value of the investments to which this report relates, either directly or indirectly, may fall or rise against the interest of investors. All prices and yields contained in this report are subject to change without notice. This information is intended for illustrative purposes only.

PAST PERFORMANCE DOES NOT GUARANTEE FUTURE RESULTS.