Equity Intelligence Report

April 2023

GAMMA INVESTMENT CONSULTING

Gamma Global Macro Model Highlights

- **The Gamma US Economic Model continues to predict the economy sliding into recession in the second half of 2023.** The forecast of a mild-to-moderate recession assumes that interest rates will peak in the first quarter and then gradually decline beginning late in the year. The big question is how the recent banking crisis will affect Federal Reserve policy and, by implication, money growth. Money growth is already at its weakest since 1932. Further contraction would threaten to turn a mild-to-moderate recession into something much more severe.

- **The S&P 500 and Nasdaq Models remained neutral (in cash) for April**. Despite the Silicon Valley Bank collapse, the S&P 500 and Nasdaq rallied 3.5% and 6.6%, respectively, courtesy of a $366 billion infusion of cash by the Fed to shore up the banking system. Our Composite Liquidity Indicator remains near its lowest level since 1980, however, which along with persistent overvaluation will continue to weigh on equity price.

- **Consumer Staples replaced Energy as the sector with the highest expected return for April.** With the economy expected to slow significantly in the second half of 2023, Consumer Staples are benefitting from their role as a defensive holding. At the other extreme are Consumer Discretionary and Financials both with negative expected returns.

- **AES Corporation (AES) and Las Vegas Sands Corp. (LVS) were removed from our "hold long" list for April. Centene Corp. (CNC) was added as a new long.** Holdings of individual names remain relatively light due to the negative expected return forecasts for the S&P 500 and Nasdaq.

I. It's All Fun and Games Until Someone Loses a Bank

Markets have been on a roller coaster ride for the past six weeks starting with the unusually strong employment and consumer spending data for January and February. Those numbers triggered a panicked reaction by the markets that inflation was still way too high. Markets immediately priced in at least three more rate hikes in 2023 including a 50 bps Fed increase in March.

Three weeks later, multiple cracks appeared in the banking system courtesy of the Fed's most extreme tightening in 40 years. In rapid succession, Silicon Valley Bank and Signature Bank failed, First Republic Bank was bailed out with $30 billion in deposits from several money-center banks, and Credit Suisse was bought by UBS aided by a $54 billion bailout package from the Swiss National Bank. Interestingly, after all this we are left almost exactly in the same position that we had forecasted in December's Macro Intelligence Report.

To get some perspective on where we go from here, let's look at why Silicon Valley Bank (SVB) and numerous other regional banks were (are) so vulnerable to the Fed's rate hikes. The run on SVB was triggered by depositor concerns over losses the bank had suffered due to rising interest rates. Which raises the question: where did these losses come from?

As we've noted in previous Reports, narrow money supply soared 80% between March 2020 and December 2021 as a consequence of the government's response to the pandemic. All that money had to go somewhere. Banks like Silicon Valley Bank were flooded with deposits as venture capitalists poured money into startups, creating new clients for the bank. SVB deposits rose 3x from $62 bln at the end of 2019 to $189 bln at the end of 2021. In response to the flood of cash, SVB bought billions of dollars' worth of U.S. Treasuries and over

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$80 bln in mortgage-backed securities (MBS) with an average duration of about 10 years and a yield of 1.56%. These would normally be considered safe assets because the default risk is virtually zero if they are held to maturity.

If SVB bought, for example, 5-year Treasury notes at a price of $1,000 with a 2% coupon, the bank would have received a semi-annual payment of $10 per $1,000 for five years. At the end of five years, the bank would have gotten back its $1,000 principal. What SVB did not take into account (or hedge) was the 4.50 percent increase in interest rates since the end of 2021.

Potential problems arise if the bank has to sell the notes before they mature. If interest rates rise, the price of existing notes has to fall (remember that price and yield move inversely) in order for the old notes to have a yield that is competitive with the new, higher-yielding notes. This does not necessarily mean that the bank actually loses money on those notes. If the bank holds the notes until maturity, they will pay off exactly as the bank expected when they purchased them.

Banks are allowed to declare that the notes they buy are going to be "held-to-maturity," which means they do not have to mark them to market prices (i.e., value them at their prevailing liquidation value) and can go on reporting them as being worth their face value on their balance sheet and for the purposes of regulatory capital.

The rules don't let banks entirely hide these mark-to-market losses. In their financial statements banks are required to explain the difference between the market value of their note holdings and the value listed on their balance sheet.

Moreover, if a bank ever sells any of the notes that it has declared as "held-to-maturity," all of the rest of its holdings get disqualified from this treatment. That means they all have to be marked to the market value, potentially triggering a huge accounting loss. To avoid doing this, banks also hold notes that are labeled as "available for sale" as a cushion. These can be sold without disqualifying other notes from being treated as held-to-maturity, but they must be marked to market.

Even the unrealized losses on those available-for-sale notes do not hurt a bank's net income. They get tracked under a balance sheet line item called "accumulated other comprehensive income." It's only when a note is actually sold at a loss that it hits the bank's income statement. Thus, none of this was a problem as long as SVB maintained their deposits, since these securities would eventually pay out more than they cost.

Several days before it collapsed, SVB disclosed it had sold $21 bln of their "available for sale" securities at a $1.8 billion after-tax loss and would, on the (dubious) advice of their investment bank, seek to raise $2.25 billion in new capital by selling common and preferred stock. That effectively waved a red flag in front of a bull. The price of the bank's shares plummeted by 60 percent. Investors and customers quickly realized that SVB had $17 billion of unrealized losses. Spooked customers began pulling deposits, attempting to withdraw as much as $42 billion in a single day. The rest is history.

The FDIC responded by extending its $250,000 limit on insured deposits to effectively cover all the deposits at the now defunct SVB and Signature banks. The action was intended to quell fears of a more widespread run on banks, especially at many regional banks that were (are) potentially in the same situation as SVB. Problem solved.

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Or is it? SVB failed because it faced a liquidity squeeze. The bank could only satisfy withdrawals (short term liabilities) by liquidating long-term assets. The resulting losses ate through the bank's capital, making it insolvent. Silicon Valley Bank was (is) not alone in sitting on a mountain of unrealized losses, however. The Federal Deposit Insurance Corporation (FDIC) revealed in February that across the U.S. banking system, unrealized losses on available-for-sale and held-to-maturity securities totaled $620 billion as of December 31 (Chart 1). A year earlier, before the Fed began hiking rates, unrealized losses were just $8 billion.

These losses, when subtracted from regulatory capital, effectively reduce the capital cushion for many banks, including some of the largest money-center banks, by as much as 80%. That dramatically reduces the cushion that these banks have against operating losses or bank runs. Plus, even though many banks are sitting on safe (from a return-of-principal perspective) "held-to-maturity" assets, many of these assets are being funded at a net loss. Because of the current inverted yield curve, many banks' marginal cost of funds, the Fed Funds rate (currently at 4.75 percent), is higher than the return on some of their assets. These losses potentially eat even further into banks' capital making them even more vulnerable to economic and liquidity shocks.

Add to that one more potential problem. U.S. banks currently have about $22 trillion in deposits. The FDIC fund available for backstopping deposits is less than $130 billion – less than 0.6% of all deposits.

Even at those banks with the highest proportion of FDIC-insured accounts, only about 42% of deposits are covered. The prospect of extending FDIC coverage to all deposits means the FDIC has nowhere near the funds it needs to cover potential depositor losses. In normal times, the chance of a wholesale run on banks would be very small. At the moment, however, banks are sitting on record large unrealized losses. And that doesn't take into account that delinquencies and defaults on loans may begin to increase.

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Bank loan delinquencies and defaults are still near record lows largely because of the Covid stimulus and near record low unemployment. The Gamma Economic Model continues to predict the beginning of a moderate

CHART 2

Charge-Off Rate - All Loans and Leases

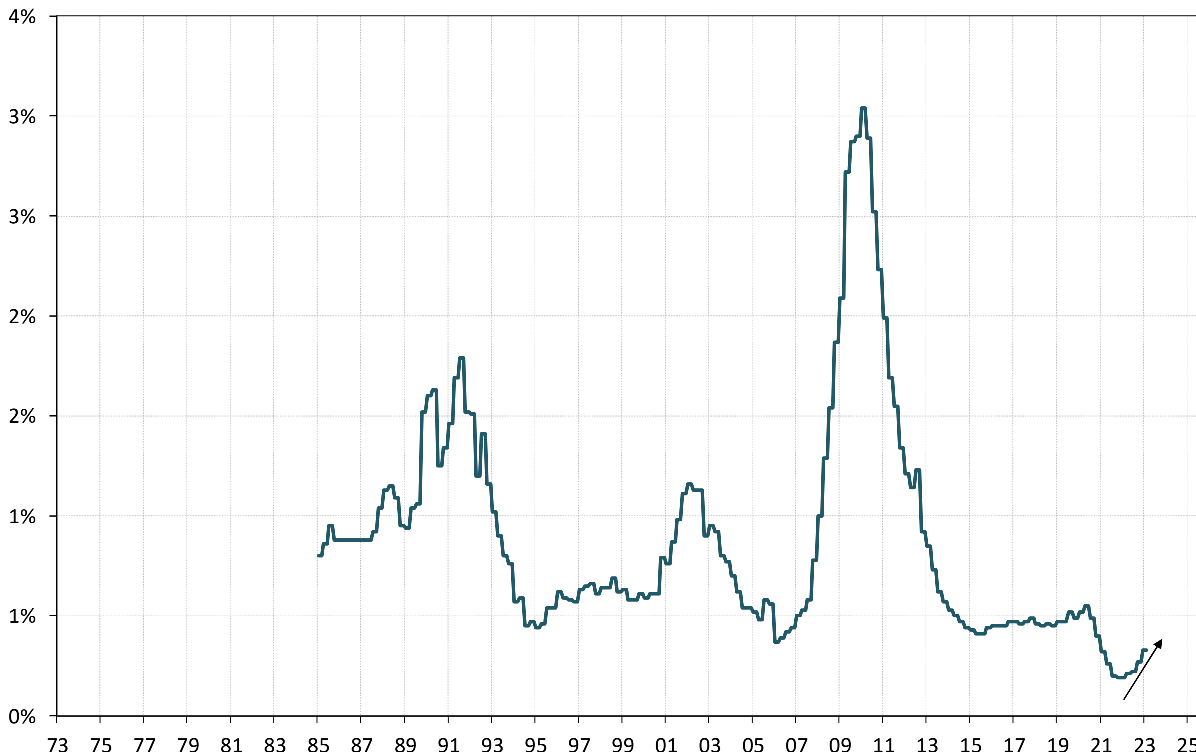

CHART 3

Banks Reporting Tighter Lending Standards (Net Change)

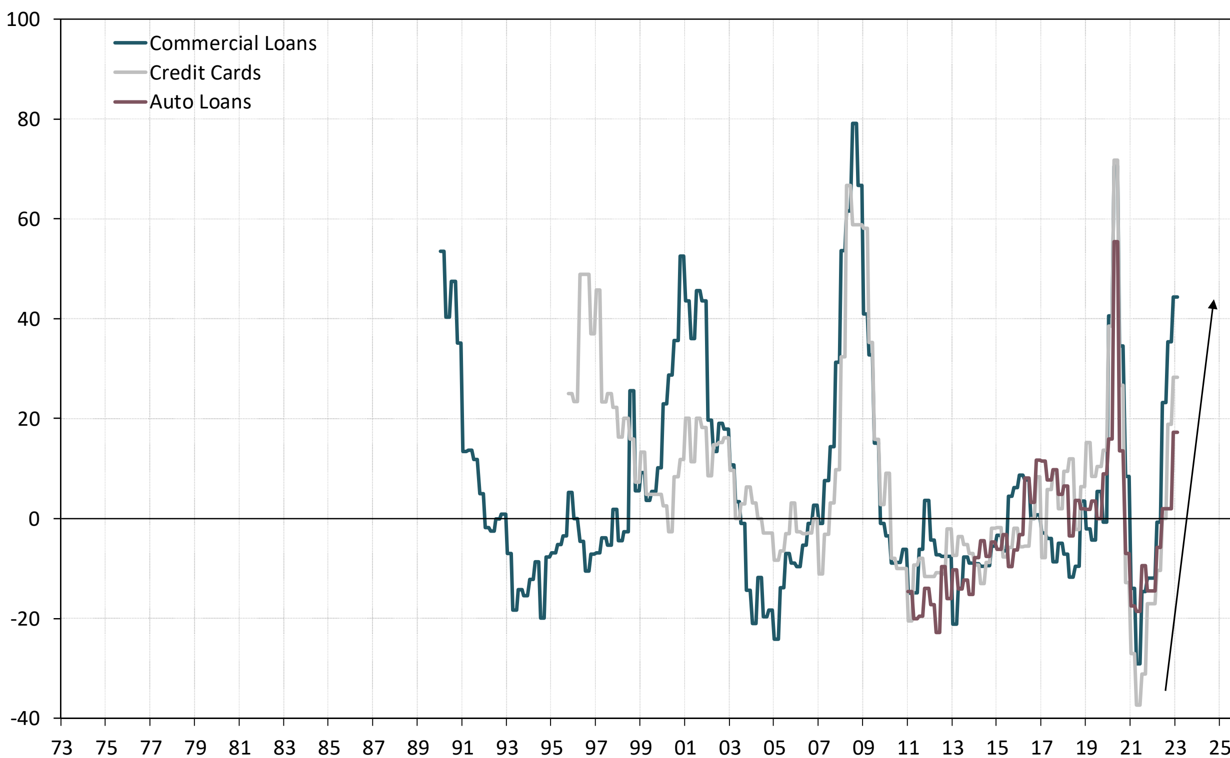

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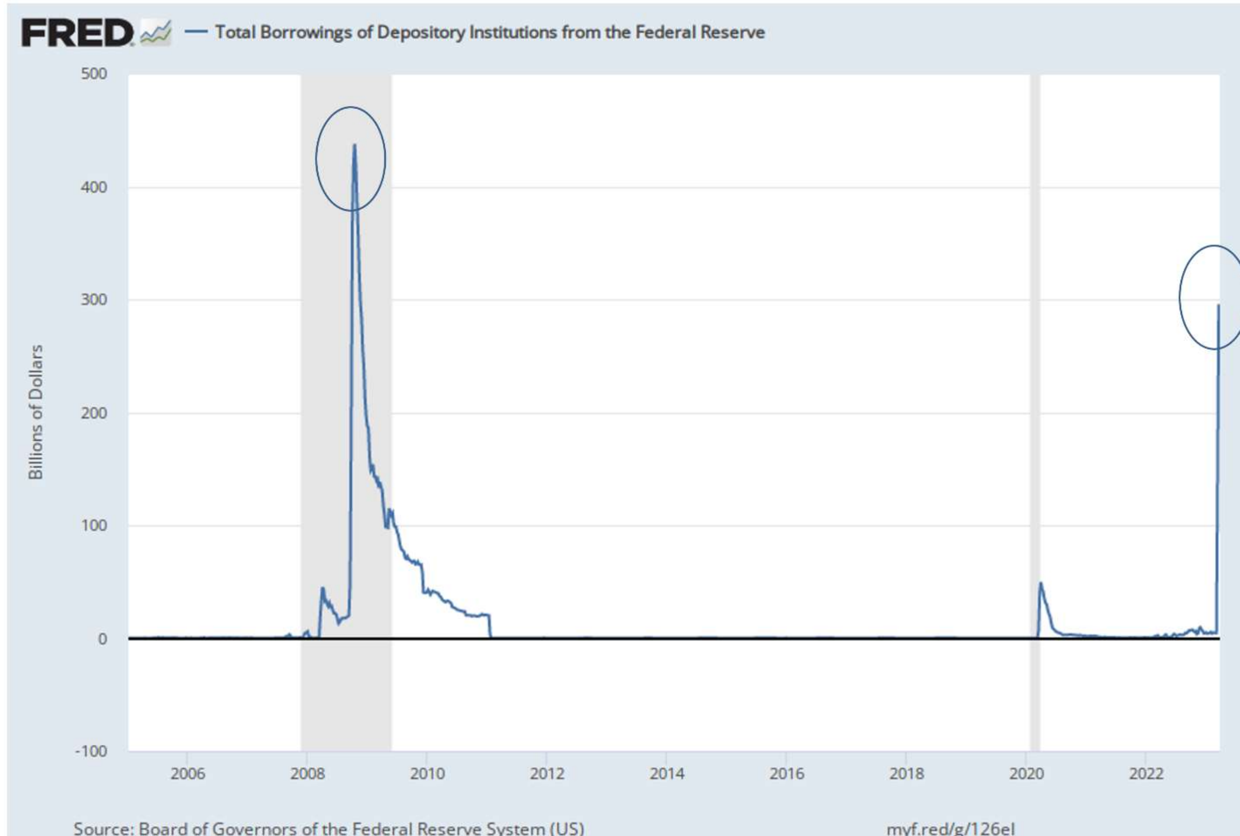
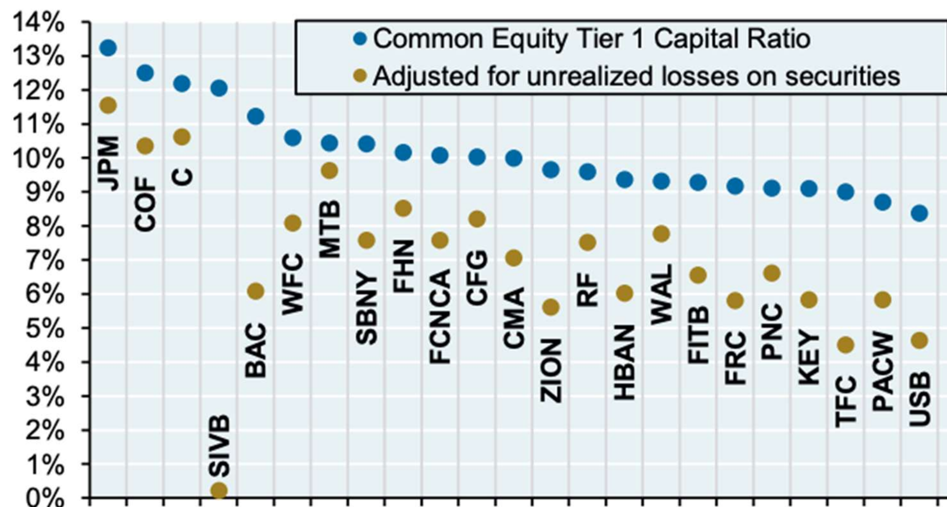
CHART 4



recession later this year. As the economy slows, expect nonperforming loans to have an increased impact on bank earnings. Charge-off rates on loans have risen steadily since the beginning of 2022 (Chart 2) albeit from very low levels. Banks have also been aggressively increasing their lending standards across the board (Chart 3). Credit quality has historically continued to deteriorate through a recession until economic growth has begun to recover. Unless interest rates begin to decline and the yield curve steepens (short term rates fall more than long term rates), banks may be faced with a triple whammy of 1) large unrealized losses on their investment portfolios that 2) are being funded at a loss at the same time that 3) delinquencies and defaults are increasing.

Concern that SVB's problems could spread more widely has receded in recent days based on the performance of bank stocks. **This is despite a surge in emergency borrowing from the Federal Reserve's discount window to its highest level since the 2008 financial crisis (Chart 4)**. That

CHART 4a



Source: "As Investors Look Past Banking Crisis, One Regional Bank Signals More Bad News," by Christine Short, Investing.com

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doesn't mean that the problems have gone away. The regulatory authorities and the Federal Reserve are still faced with:

1) Some banks whose capital is perilously close to being impaired (Chart 4a),
2) Banks that are fundamentally sound but could face liquidity issues if unrealized losses on their investment portfolios are realized,
3) Banks that are fundamentally sound now but could be adversely impacted by an increase in nonperforming loans,
4) All while trying to bring inflation back to its 2% long-term target without triggering a major recession.

The Federal Reserve is walking through a minefield of its own making. Its primary long-term goal is to return the inflation rate to its 2% target rate. The problem is how to reach that goal without triggering additional bank insolvencies or bank runs while also maintaining its inflation-fighting credibility. Ignoring the inflation rate is not an option. That that would risk an even more severe crisis down the road. The short-term solution to the bank problem (i.e., supporting banks through additional liquidity), however, is diametrically opposed to the Fed's inflation mandate. **It is quite possibly that there is no path forward that doesn't lead to a severe recession, additional bank failures, or a resurgence of inflation.** Keep in mind that there is no "master plan" the Fed is following. The Fed is making this up as it goes along. We'll discuss the Fed's options and their implication for financial markets below.

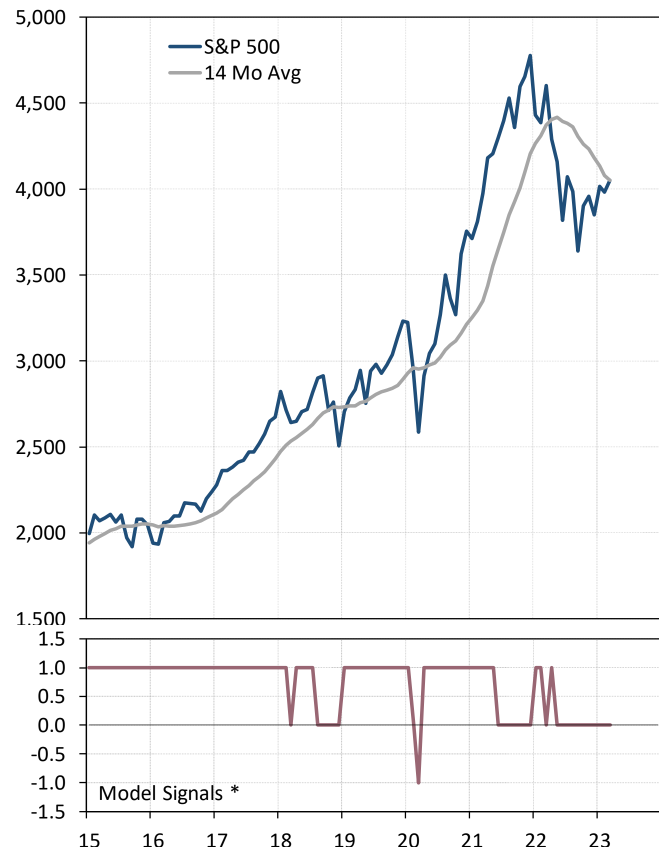
II. Equity Index Outlook

Despite the worst financial crisis since 2008, stocks actually ended higher in March. The S&P 500 rose 3.5% while the Nasdaq jumped 6.6%. Markets continue to be wedded to the idea that the "Greenspan put" of Fed easing aggressively into a financial crisis will always bail them out. So far, they've been right. As emergency Fed lending soared last month to nearly $300 bln (Chart 4), markets promptly took that as an "all clear" sign and drove stock prices higher. Even bank shares which were down -19% for the month still managed to rally 5% off their lows. Despite all this the underlying fundamentals for stocks actually worsened during the month. As a result, the Gamma Equity Models for the S&P 500 and Nasdaq remained neutral (in cash) for April (Chart 5).

CHART 5

Country	Instrument	1 Mo Fcst	Position	Trade	Updated
USA	S&P 500	0.00%	Neutral	Hold	3/31/23

USA: S&P 500 Model Forecast



Negative Factors

- <u>Short-term interest rates continue to rise</u>. While markets focused on the billions in emergency liquidity that the Fed injected last month, they also conveniently forgot that the Fed raised rates by an additional 25 basis points to a 4.75-5% range at its March meeting. The Fed has now hiked rates nine times since February 2022. **The 4.75% increase is the largest 13-month rise since 1981 (when interest rates started at 11%, not 0.25%) (Chart 5a).** The CME Fedwatch Tool also shows odds favoring another 25 basis point increase in May. The steady rise in rates is further inverting

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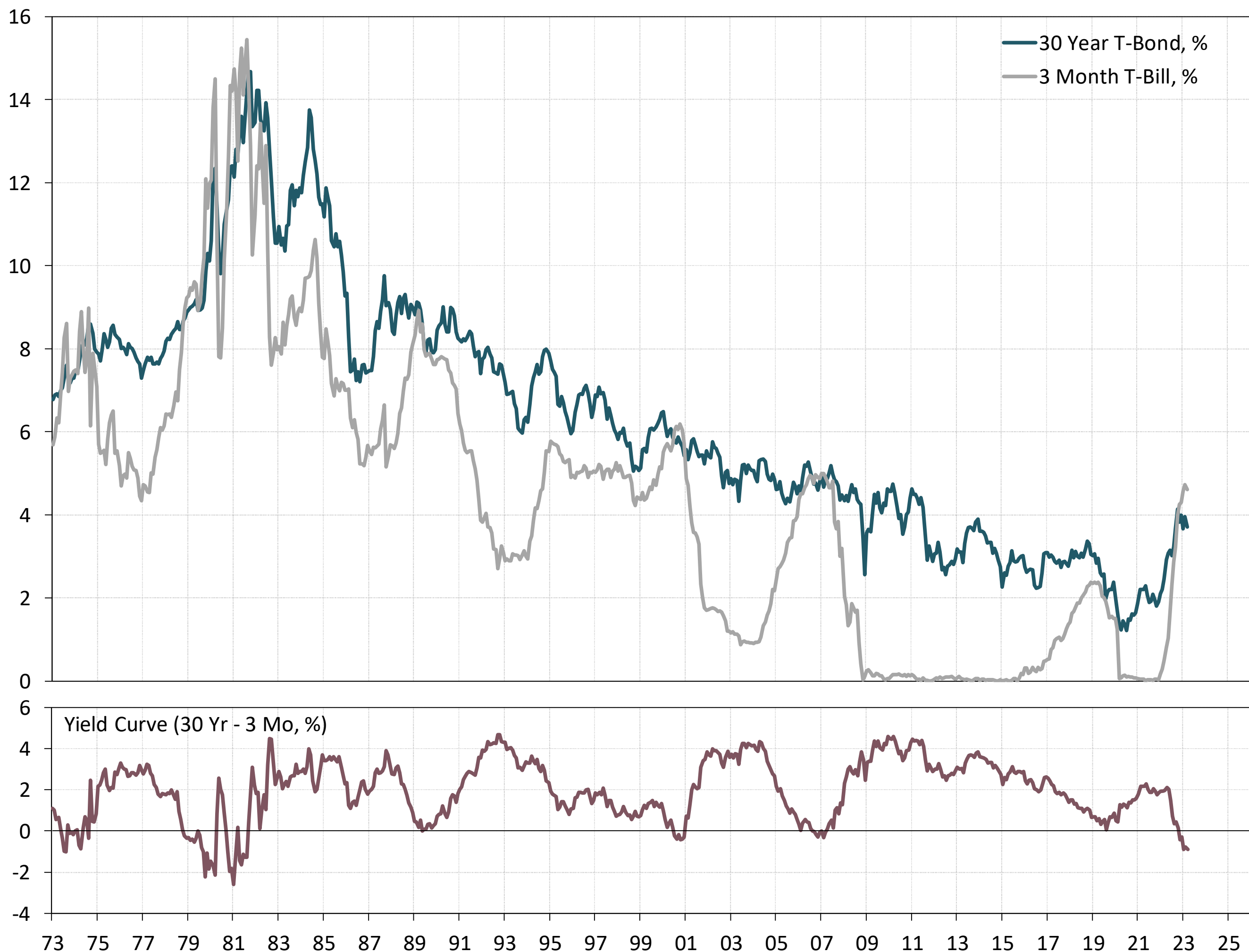
CHART 5a



the yield curve and causing money growth to collapse. The increase in banks' short-term borrowing costs will keep downward pressure on bank earnings while also discouraging lending. The rise in short-term rates is also likely to slow economic growth in the second half of the year which could worsen default rates on existing credit lines for both businesses and consumers. Some investors may believe that the end to the Fed tightening in May would mark the end of the bear market. Unfortunately, history doesn't bear this out. **Of the last ten major tightening cycles, stock prices hit their cyclical lows after the Fed started to cut rates. The average maximum drawdown in the S&P 500 after the Fed's first cut was over -25% (Chart 6).** The only exception was the tightening cycle that ended in 1989. Even then, however, stock prices were largely unchanged for seven months. The delay reflects the fact that the Fed usually starts to ease when economic activity is clearly slowing. At that point, however, corporate earnings also tend to drop which puts additional downward pressure on stock prices.

- The yield curve remains inverted. After steepening briefly in February, the 3-30 Treasury yield curve inverted further in March, matching its most extreme level of this cycle (Chart 5a). The 3-30 curve has now been inverted for five months, the longest such stretch since 2000. The 2-10 curve steepened, however, as the yield on 2-year Treasury notes fell sharply on expectations that the Fed tightening will be over by its May meeting. **Both curves still remain indicative of a very restrictive monetary policy.** Short-term funding costs above the yield on long-term assets will put a damper on bank lending. That will further slow money growth that, on both a nominal and inflation-adjusted basis, is already strongly negative. The longer

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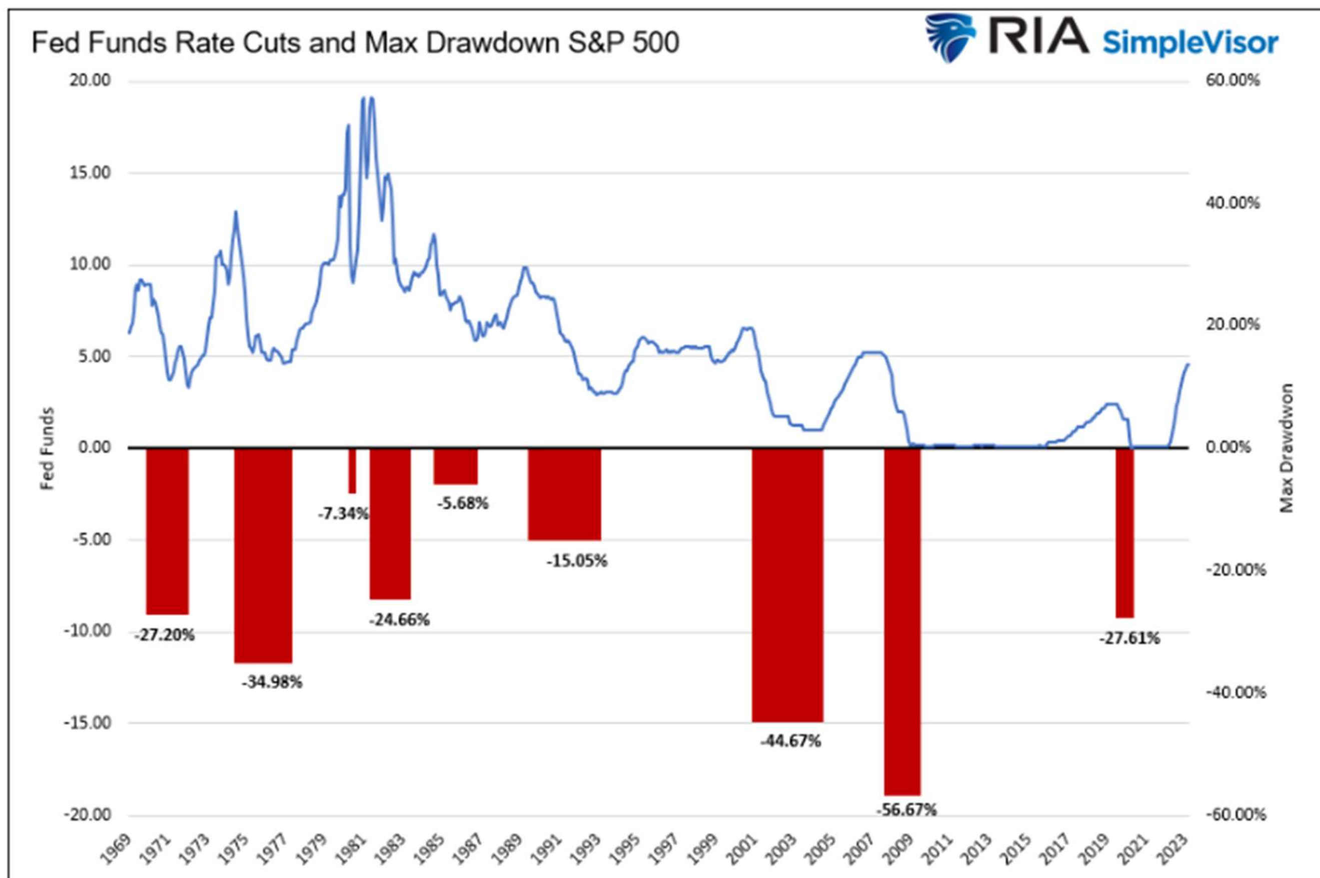
CHART 6



Source: "A Federal Reserve Pivot Is Not Necessarily Bullish," by Michael Lebowitz, Investing.com

and more extreme the inversion, the greater the risk of another major leg down in equity prices. As we noted last month, since 1960 inversions in the 3-30 curve have invariably been followed by much lower stock prices. **The bottom in stock prices has occurred on average 13.5 months after the curve inverts.** Assuming that this cycle plays out similar to others, stock prices are not likely to bottom until mid-to-late 2023.

- Every measure of money growth continues to deteriorate. Real (inflation-adjusted) True Money Supply (TMS) growth fell sharply again last month. Real TMS was down -7.5% yr/yr in March, its sharpest 12-month drop since December 1981 (Chart 7). The alternative narrow money measure, real M1, was down -12.2% yr/yr, the tenth negative month in a row. **Real M2 was down -8.7%, the largest 12-month decline since 1932!** All the measures are indicative of a severe contraction in liquidity which is also likely to worsen. Banks sitting on $620 billion of unrealized losses won't be rushing to add long-term assets that yield less than their funding costs (remember the inverted yield curve?). Slower lending growth then translates into slower money growth at a time when yr/yr money growth is already negative at or near historic lows.
- Composite Liquidity Indicator continues to deteriorate. The Gamma Composite Liquidity Indicator (CLI) remains near its cyclical low despite a slight improvement in March. The Index has swung from a record high in March 2021 to last month's near-record low in the most extreme reversal on record. Weaker money growth was offset by an improvement in the 2-10 yield curve and a slower rate of increase in short- and long-term interest rates. The Index is likely to stabilize around current levels as further expected weakness in money growth is likely to be offset by steadier interest rates as the Fed's tightening winds down.
- Corporate earnings are falling. 12-month trailing earnings for the total US market, S&P 500, and Nasdaq indexes continued to weaken in March (Chart 8). S&P 500 earnings were down -9% from a year earlier.

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CHART 7

Real True Money Supply and M2

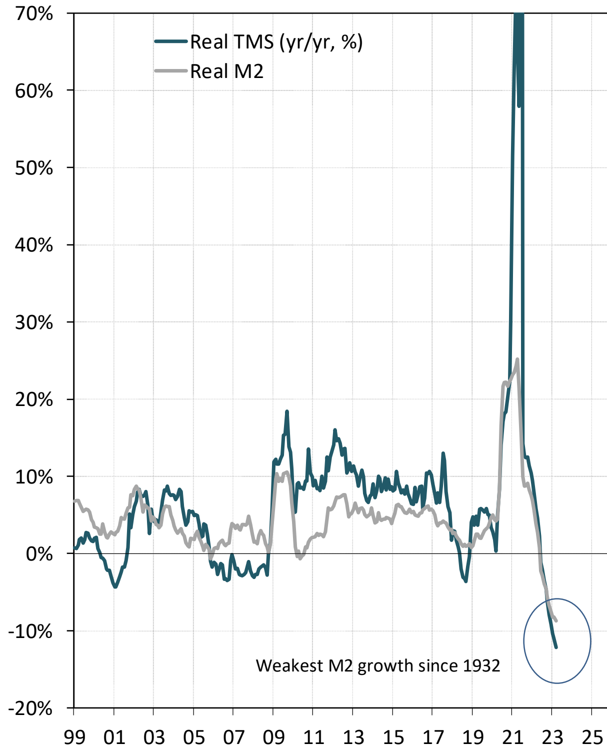
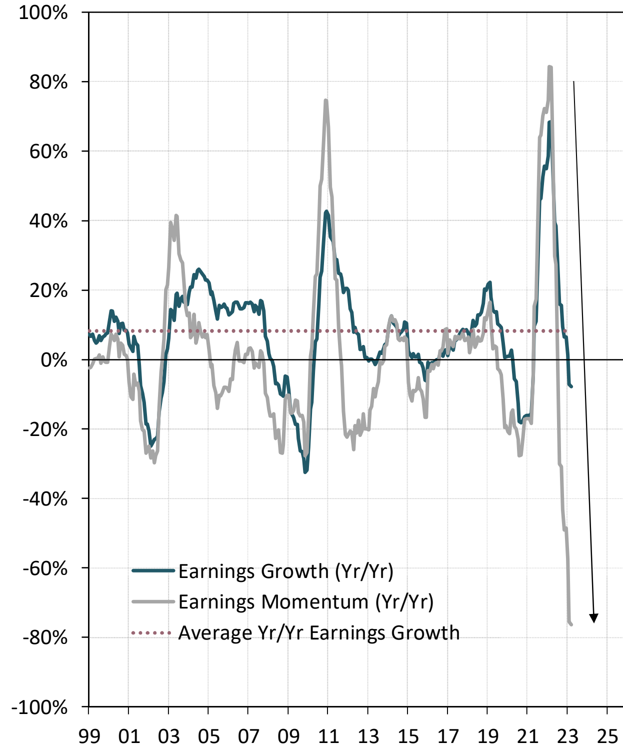


CHART 8

US Total Market Earnings Growth



Nasdaq earnings were down -14%, though 12-month earnings momentum improved marginally for both indexes. Historically, the equity markets have tended to bottom when 12-month earnings momentum turns positive. Current -73% earnings momentum for the S&P 500 is a record low. Nasdaq momentum at -57% is the lowest since after the dot com collapse in 2002. Historically, in those cases where equity indexes dropped over 20% from their peaks, earnings continued to fall for an average of 12 months after their yr/yr growth turned negative. That implies that earnings will remain a drag on equity prices into 2024.

- Equities Remain Overvalued. The single biggest obstacle to a sustained equity rally is the current level of valuation. Despite the S&P 500 being down -14% from its December 2021 peak, valuation continues to run stubbornly high (Table 1). The combination of higher interest rates, higher bond yields, and the decline in corporate earnings has more than offset the effect of lower equity prices on valuation. As a result, the S&P 500 remains 19% (0.9 standard deviations) overvalued according to the Gamma Valuation Model. The Nasdaq remains even more extreme at 33% overvaluation (1.2 standard deviations). We have noted in past Reports that **no recovery from a major bear market low has occurred in the last 60 years when stocks were not at least fairly valued. On average, new bull markets launched when stocks were 25% undervalued.** We believe that the severe liquidity contraction since the end of 2021 will eventually trigger the second major leg down of the current bear market. That correction will bring valuation to levels capable of sustaining a new bull market.

Neutral Factors

- The Federal Reserve's portfolio. Prior to the collapse of Silicon Valley Bank, the Federal Reserve had shrunk its assets by $626 billion from its May 2022 peak. The reduction in its assets was part of the plan to slow inflation by gradually draining liquidity from the banking system. Sales (or the maturing) of Treasury securities or mortgage-backed securities (MBS) causes money leave the banking system as the issuers of the debt repay the holder (the Fed). The banking crisis has undone almost 60% of this tightening. The Fed's balance sheet expanded by about $366 bln last month largely due to a surge in emergency borrowing at the

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Fed's discount window (Chart 4). The collapse of Silicon Valley Bank and Signature Bank prompted other banks to shore up their liquidity (and borrow some cheap money) in order to avoid a similar fate. Between the collapse of SVB over the March 10 weekend and March 22, domestically chartered banks in the United States lost $213 billion in deposits ($190 bln of it from smaller, non-top 25, banks) as skittish savers rushed to withdraw their money. Money market funds were the big beneficiaries as they gained $286 billion in March. There are signs that the immediate crisis may be receding. But many smaller regional banks are still faced with the withdrawal of billions of dollars of deposits that will likely have to be replaced at higher interest rates. This at a time when their capital positions have become increasingly shaky (Chart 4a). **We do not believe that bank regulators and the Fed will allow the collapse of a large regional bank without full FDIC protection for depositors.** That implies that the Fed's inflation mandate may clash headlong with its interest in preventing additional bank runs. Given the uncertainty over these conflicting demands, we now place the Fed's portfolio decisions into the "neutral" category regarding their impact on equity prices.

TABLE 1

EQUITY INDEX VALUATION

Country	Valuation (σ)	Valuation (%)
United States	+0.94	+19%
S&P 500	+0.88	+19%
Nasdaq	+1.19	+33%
S&P 600 Small Cap	-1.09	-18%
Canada	-1.38	-24%
Brazil	-2.58	-56%
Mexico	-0.84	-12%
Australia	-1.65	-39%
Japan	+0.02	+1%
China	-0.91	-34%
S. Korea	-0.73	-17%
India	-0.94	-17%
Europe	-1.22	-28%
Germany	-1.42	-30%
France	+0.48	+10%
Italy	-1.51	-37%
Switzerland	-0.13	-3%
UK	-0.27	-6%
Russia	-1.72	-67%
S. Africa	-1.66	-28%

Positive Factors

- Seasonals. April is the last strong positive seasonal month before the summer doldrums begin. The S&P 500 has historically risen 1.7% in April, tied with November as the strongest positive month of the year.
- Non-US equity performance. Several non-US markets have significantly outperformed the US market this year. The S&P 500 is up 7.2% year-to-date through March. European stocks over the same period are up 9.4% including a 12.5% gain in Germany and a 13.2% rise in France. Even with this rally, non-US equities are still, on average, 22% undervalued compared to 19% overvalued for the S&P 500 (Table 1). This extreme 41% differential in valuation may help cushion the expected second leg down in US equites as the economy slows later this year.

II. Equity Sector Outlook

For the first time in nine months, the Energy sector is no longer forecasted to have the highest return for April (Table 2). Energy, which had held the top spot due to earnings that dwarfed the other sectors, slipped to second place having been replaced by the defensive Consumer Staples sector. Health Care was third followed by Gold Mining Shares which bounced back strongly on the heels of gold's 9% March rally. Interestingly, seven sectors had positive expected returns for April despite the overall negative view expressed by the S&P 500 and Nasdaq index Models. Not surprisingly, the Financials sector was forecasted to be the worst performer after the banking sector chaos of recent weeks.

TABLE 2

1 Mo Stock Sector Index Forecasts (%)

Sector	Ticker	1 Mo Forecast	Previous Forecast	Change
Consumer Staples	XLP	0.84%	-0.10%	0.94%
Energy	XLE	0.72%	1.06%	-0.34%
Health Care	XLV	0.58%	-0.13%	0.71%
Gold Miners		0.50%	-1.29%	1.79%
Utilities	XLU	0.31%	0.17%	0.14%
Real Estate	XLRE	0.11%	-1.02%	1.13%
Materials	XLB	0.02%	-0.12%	0.14%
Communications Services	XLC	-0.22%	-1.41%	1.20%
Technology	XLK	-0.29%	-1.47%	1.18%
Industrials	XLI	-0.37%	-0.65%	0.29%
Consumer Discretionary	XLY	-1.16%	-2.20%	1.04%
Financials	XLF	-1.16%	-1.14%	-0.02%

Consumer Staples climbed to the top of the list courtesy of a 0.84% expected return for April. The Gamma Economic Model continues to forecast the beginning of a recession by mid-year. The Conference Board's

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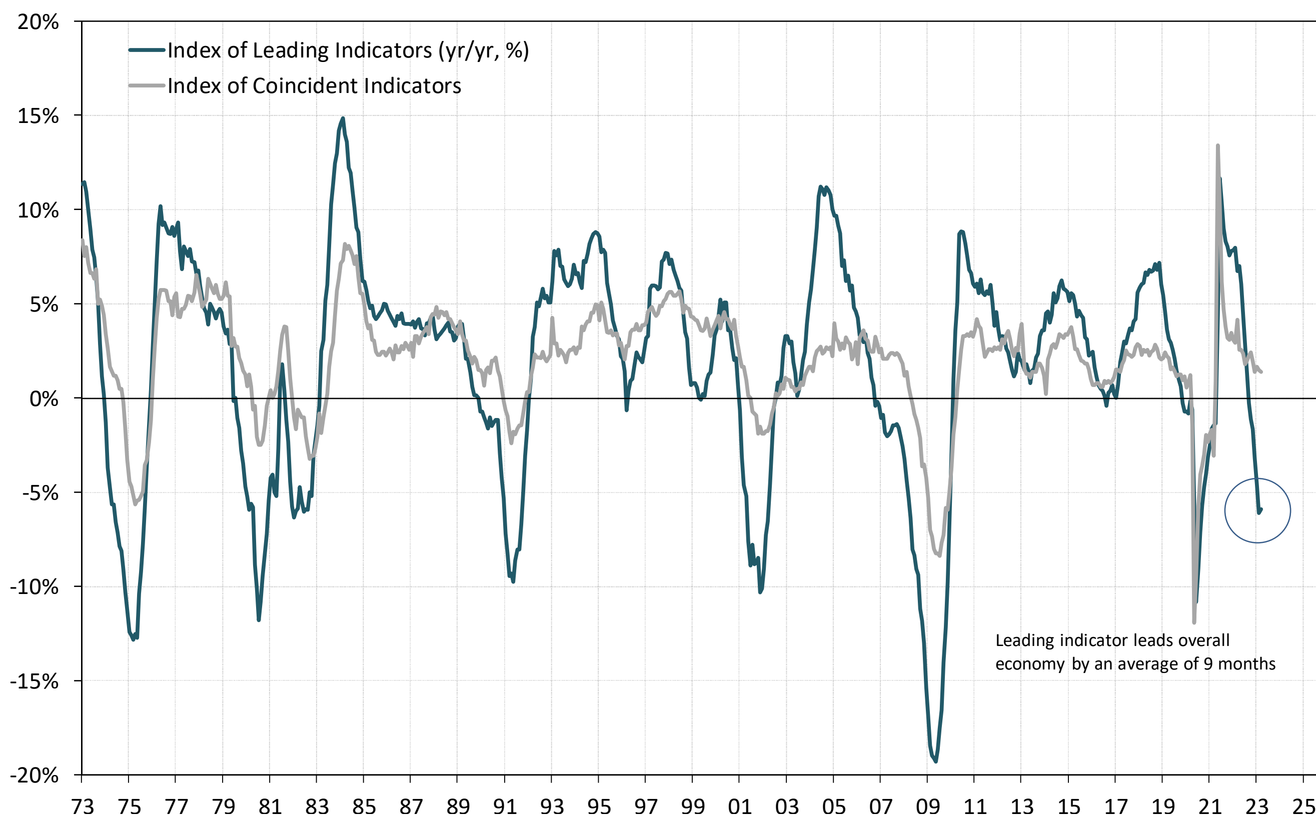
CHART 9

Measures of Economic Activity



Index of Leading Economic Indicators (LEI) has dropped 11 months in a row and was down -5.9% yr/yr last month. Historically, when the LEI yr/yr change has turned negative, the overall economy has slipped into recession on average 9 months later (Chart 9). The yr/yr change in the LEI turned negative seven months ago which strongly suggests that the economy will slow rapidly by mid-year.

The prospect of a downturn has pushed Consumer Staples to the top of the list. Consumer Staples stocks have historically been "defensive" investments that tend to outperform when the economy weakens since the items that these companies sell are purchased regardless of whether the economy is booming or contracting. The sector's earnings are holding up (-2% yr/yr) and earnings momentum, while negative, is higher than any sector other than Utilities (Table 3).

TABLE 3

Earnings Growth (12-Month Trailing)

Sector	Yr/Yr % Change	Yr/Yr Moment
Energy	+123%	-1112%
Industrials	+4%	-50%
Materials	+2%	-147%
Real Estate	+2%	-54%
Utilities	+1%	-18%
Health Care	-2%	-51%
Consumer Staples	-2%	-23%
Technology	-13%	-58%
Communication Services	-18%	-72%
Consumer Discretionary	-30%	-102%
Financials	-34%	-122%
Gold Mining Shares	-35%	-27%
USA (Total Market)	-8%	-76%
USA (S&P 500)	-9%	-73%
USA (Nasdaq Composite)	-14%	-57%

Energy slipped to the second spot but still sported an expected return of 0.72%. This sector is supported by the strongest earnings growth of all the sectors with a 123% yr/yr gain. Earnings growth momentum is slowing rapidly, however, which contributed to the sector's downgrade compared to previous months. The sector is also suffering from downward pressure on energy prices. Natural gas prices are down to $2 from over $10 last August. Crude oil prices have fallen from $125/barrel to as low as $65 in March.

In contrast to Consumer Staples, Consumer Discretionary tends to underperform in a downturn which is why that sector is second-to-last on this month's list (only above battered Financials). Discretionary items such as vacations and luxury goods tend to be the first thing to be jettisoned when unemployment rises. Sector earnings

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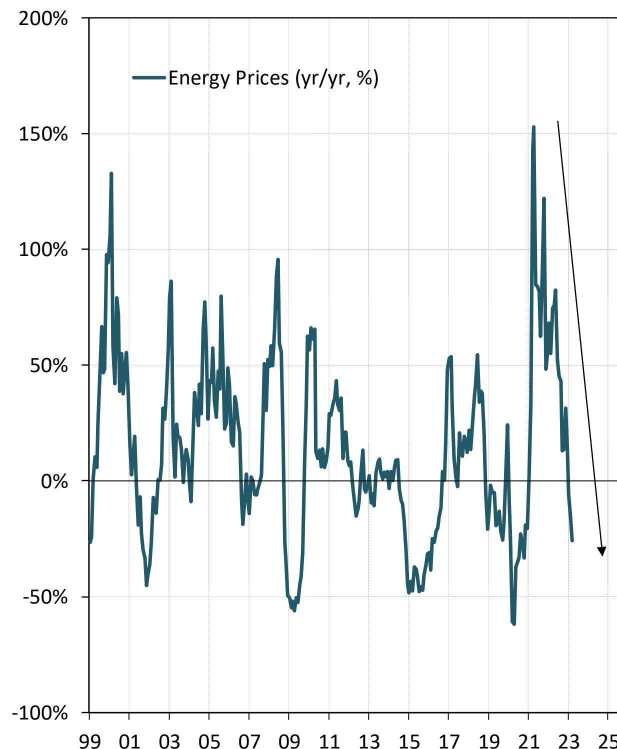
are already down -30% from a year ago and are not likely to rebound anytime soon if economic activity slows. The sector is projected to be down -1.2% in April, tied with Financials which, for obvious reasons, are languishing at the bottom.

Financials are at the bottom of the heap with an expected loss of -1.2% next month. Earnings are down -34% yr/yr, and earnings momentum is in a -122% freefall. Banks, in particular, are likely to continue to grossly underperform given the capital, funding, and credit quality issues discussed above.

CHART 10

GSCI Commodity Index



III. Stock Recommendations and Review

The Gamma Company Model starts April with ten names on our "hold long" list of companies (Table 4). AES (AES) and Las Vegas Sands (LVS) were removed this month as their expected returns for April dropped below the average expected return for all the stocks in the S&P 500.

Only one new name is being added this month: Centene Corp. (CNC). CNC has a well above-average forecasted expected return (+1.86%), positive factor momentum, and is part of the Healthcare sector which has a positive expected return for April.

In general, we do not like being long ANY stocks at the moment given the negative forecasts from the S&P 500 and Nasdaq Models. The stocks on our recommended list, however, are likely to have the best chance of outperforming the overall market according to our Models.

TABLE 4

GAMMA COMPANY MODEL - Recommended List Performance — As of: Mar 31, 2023

Company	Ticker	Entry Price	Closing Price 3.31.23	% Change	Trade Date	S&P 500 % Change	Excess Return
Centene	CNC	$63.21	$63.21	0.0%	3.31.23	0.0%	0.0%
Altria Group, Inc.	MO	$47.63	$44.62	-6.3%	12.2.22	0.9%	-7.2%
Celanese Corp.	CE	$122.12	$108.89	-10.8%	2.6.23	0.0%	-10.8%
Diamondback Energy, Inc.	FANG	$145.46	$135.17	-7.1%	12.2.22	0.9%	-8.0%
Henry Schein	HSIC	$78.31	$81.54	4.1%	3.1.23	4.0%	0.1%
Kroger Co.	KR	$47.57	$49.37	3.8%	12.2.22	0.9%	2.9%
McKesson Corp.	MCK	$313.34	$356.05	13.6%	6.10.22	5.3%	8.3%
ONEOK Inc.	OKE	$68.20	$63.54	-6.8%	2.6.23	0.0%	-6.8%
Pulte Group	PHM	$57.48	$58.28	1.4%	2.6.23	0.0%	1.4%
Skywork Solutions Inc.	SWKS	$93.96	$117.98	25.6%	12.2.22	0.9%	24.6%
						AVERAGE	0.5%

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Centene Corp. (CNC: $63.21, close 3.31.2023)

- Centene Corporation is a leading managed healthcare enterprise focused on administering government-sponsored and commercial healthcare programs, concentrating on under-insured and uninsured individuals with more than 27 million members. CNC recently acquired WellCare Health Plans Inc.
- Trades at a Forward P/E (TTM) of 9.75 and at a 32% discount to its 52-week high.
- CNC has the third-highest expected return forecast for April (+1.86%) from our Gamma Company Model for the S&P 500. That was a substantial increase from the previous month's (March) forecasted gain of +0.85%.
- Analyst coverage: 21 analysts cover CNC and the recommendations are 7 strong buys, 7 buys and 6 holds and 1 underperform. The price target ranges from $71.00 - $110.00.
- Centene's CEO recently purchased nearly $2MM of stock. Over the last 12 months, other insiders have been buying shares.
- The company has a strong balance sheet and trades at a much lower forward P/E of 9.75 than the industry average of 13.9.
- CNC announced it is expanding the use of Evolent Health, Inc.'s EVH oncology solution, strengthening the specialty care partnership between the two. Evolent's value-based specialty care platform provides innovative solutions to payers and providers.
- Centene has a solid nationwide presence securing numerous contract wins and deal renewals. The company has used an organic growth route to increase its capabilities and provide revenue growth. Partnerships with regional healthcare providers allows CNC to deliver effective healthcare services and to local markets.
- CNC repurchased 17 million of its shares worth $1.4 billion. As of Feb 7, 2023, the company had a leftover share buyback capacity of $2.5 billion.
- Centene's membership has been growing over the past few years due to additional Medicaid and Medicare businesses, contract wins, and expansion across different regions. Total membership was 27.1 million as of Dec 31, 2022, an annual gain of 4.8%. The growth came on the back of strength in Medicaid and Medicare businesses.
- CNC is the largest Medicaid health insurer in the US, with 16 million members. The company is forecasting to lose 2+ million enrollees during the unwinding of the so-called "Medicaid unwind" as federal COVID-19 pandemic protections prohibited states from dropping anyone from Medicaid since 2020. But Centene expects between 200-300K people who lose Medicaid coverage to sign up for a Centene ACA marketplace plan. With states poised to start disenrolling Medicaid enrollees in April who no longer qualify, insurers hope to retain enrollees who are still eligible and capture those who lose coverage with the Affordable Care Act marketplace plans. Moving members to an ACA plan could boost the profits.
- A possible negative, several Wall Street analysts have expressed some concern about 2024 earnings estimates with potential significant negative future revisions both to guidance and Street estimates. In

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addition, the near-term Medicare Advantage rate outlook is disappointing with the Centers for Medicare and Medicaid Services announcing a 2% preliminary rate cut next year versus the market's expectation for an increase in the range of 0%-2%.

-Karl Chalupa and N. Claude Colabella

Mr. Chalupa is the CEO and Co-Founder of Gamma Investment Consulting and Editor of the Gamma Intelligence Reports. He is also President of Gamma Capital LLC, a quantitative global macro investment firm. Mr. Chalupa developed the Gamma Investment Program used for previously trading the firm's $400 million global macro program. He was previously Director of Risk Management at Titan Advisors LLC, a $4.5 billion alternative investments firm. Mr. Chalupa was also Managing Director of the Currency and Alternative Investment Strategies Groups at State Street Global Advisors (SSGA) where he developed a $9 billion currency overlay program and launched SSGA's first hedge fund based on his Gamma Model. Mr. Chalupa spent 13 years at ABN Amro Bank where he traded interest rate and currency derivatives and was Manager of the Proprietary Trading and Economic Research Desk. He began his career as an economist for the Federal Reserve Bank of Chicago. Mr. Chalupa holds an MA in Economics from Brown University, graduated magna cum laude from Northern Illinois University with BAs in Economics and Political Science, and is Series 3 registered.

Mr. Colabella is the Chief Operating Officer, Co-Founder of Gamma Investment Consulting and Co-Editor of the Gamma Equity Intelligence Report. He was previously Director of Communications and Investor Relations at Titan Advisors, LLC, a $4.5 billion alternative assets solutions firm. Mr. Colabella has equity research experience with working at Petroleum Research Group, Inc. (Rye, NY), an independent energy equity research boutique and at John S. Herold, Inc., a leading petroleum research and consulting firm. He was a Managing Partner at Alpha Beta Alternative Investments, Inc., an alternative investment boutique that managed Alpha Beta Partners, LP, a multi-strategy "fund of funds". Mr. Colabella holds an MBA in Finance from Duke University, Fuqua School of Business. He graduated magna cum laude from Manhattan College, with a BS BA in Economics.

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Gamma Equity Model Forecasts for April 2023 (as of 3/31/2023)

TABLE 1

1 MONTH STOCK INDEX MODEL FORECASTS (%)

Country	Stock Index	Price	1 Mo Forecast	Previous Forecast	Position	Trade	Updated
USA	S&P 500	4,050.83	0.00%	0.00%	Neutral	Hold	3/31/23
USA	Nadaq	12,085.12	0.00%	0.00%	Neutral	Hold	3/31/23
Canada	S&P/TSX 60	1,205.72	0.00%	0.00%	Neutral	Hold	3/31/23
Mexico	IPC	54,508.61	0.20%	1.47%	Long	Hold	3/31/23

TABLE 2

1 Mo Stock Sector Index Forecasts (%)

Sector	Ticker	1 Mo Forecast	Previous Forecast	Change
Consumer Staples	XLP	0.84%	-0.10%	0.94%
Energy	XLE	0.72%	1.06%	-0.34%
Health Care	XLV	0.58%	-0.13%	0.71%
Gold Miners		0.50%	-1.29%	1.79%
Utilities	XLU	0.31%	0.17%	0.14%
Real Estate	XLRE	0.11%	-1.02%	1.13%
Materials	XLB	0.02%	-0.12%	0.14%
Communications Services	XLC	-0.22%	-1.41%	1.20%
Technology	XLK	-0.29%	-1.47%	1.18%
Industrials	XLI	-0.37%	-0.65%	0.29%
Consumer Discretionary	XLY	-1.16%	-2.20%	1.04%
Financials	XLF	-1.16%	-1.14%	-0.02%

TABLE 3

S&P 500: LARGE CAP STOCKS | **Top 25 Picks Based on Expected Return and Factor Momentum** | **Forecast for: Apr 2023**

1 Month Company Stock Price Forecasts (%) — **Updated: Mar 31, 2023**

Company	Ticker	Closing Price	1 Mo Forecast	Previous Forecast	Change	% Off 52 Wk High	Forward P/E	Dividend Yield	Factor Momentum
PULTEGROUP	PHM	$58.28	2.79%	2.75%	0.04%	0.0%	7.68	1.10%	Positive
ADVANCED MICRO DEVICES	AMD	$98.01	2.35%	1.10%	1.24%	-3.8%	29.03	0.00%	Positive
CENTENE	CNC	$63.21	1.86%	1.02%	0.85%	-32.0%	9.75	0.00%	Positive
STEEL DYNAMICS	STLD	$113.06	1.85%	1.52%	0.33%	-10.3%	9.53	1.50%	Positive
GENERAL ELECTRIC	GE	$95.60	1.72%	1.17%	0.55%	0.0%	38.71	0.33%	Positive
FIRST SOLAR	FSLR	$217.50	1.61%	0.28%	1.33%	0.0%	24.84	0.00%	Positive
AMERISOURCEBERGEN	ABC	$160.11	1.58%	1.57%	0.01%	-6.2%	13.15	1.21%	Positive
NVR	NVR	$5,572.19	1.56%	1.31%	0.25%	0.0%	14.65	0.00%	Positive
F5	FFIV	$145.69	1.47%	0.35%	1.12%	-13.0%	11.59	0.00%	Positive
JUNIPER NETWORKS	JNPR	$34.42	1.46%	0.91%	0.55%	0.0%	14.43	2.56%	Positive
D R HORTON	DHI	$97.69	1.45%	1.41%	0.04%	-1.0%	10.29	1.02%	Positive
ALIGN TECHNOLOGY	ALGN	$334.14	1.36%	0.35%	1.00%	0.0%	36.87	0.00%	Positive
GEN DIGITAL	GEN	$17.16	1.34%	0.14%	1.20%	-31.5%	8.22	2.91%	Positive
ALTRIA GROUP	MO	$44.62	1.26%	1.04%	0.23%	-19.7%	8.70	8.43%	Positive
CAMDEN PROPERTY TST.	CPT	$104.84	1.26%	0.39%	0.87%	-33.2%	63.64	3.82%	Positive
ULTA BEAUTY	ULTA	$545.67	1.20%	1.11%	0.10%	0.0%	20.90	0.00%	Positive
MGM RESORTS INTL.	MGM	$44.42	0.98%	0.40%	0.58%	0.0%	52.41	0.02%	Positive
LENNAR 'A'	LEN	$105.11	0.97%	0.52%	0.45%	0.0%	10.03	1.43%	Positive
TERADYNE (XSC)	TER	$107.51	0.96%	0.94%	0.03%	-1.6%	29.42	0.41%	Positive
ARTHUR J GALLAGHER	AJG	$191.31	0.85%	0.76%	0.09%	-3.9%	20.96	1.15%	Positive
AUTOZONE	AZO	$2,458.15	0.80%	0.08%	0.72%	-4.7%	17.33	0.00%	Positive
PG&E	PCG	$16.17	0.80%	0.28%	0.52%	-0.6%	12.76	0.00%	Positive
NORFOLK SOUTHERN	NSC	$212.00	0.77%	0.23%	0.54%	-17.8%	14.93	2.55%	Positive
INTL.FLAVORS & FRAG.	IFF	$91.96	0.74%	0.49%	0.25%	-30.4%	17.76	3.52%	Positive
PAYPAL HOLDINGS	PYPL	$75.94	0.73%	0.51%	0.23%	-18.7%	14.67	0.00%	Positive

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