Truist Advisory Services, Inc.

Market Perspective – Stick with cyclicals with growth scare in rearview mirror

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Our work suggests the economy is moving past the summer growth scare. In today's note, we provide the key factors behind this view and why we favor **cyclical areas of the market** as the economy sets up for positive surprises.

- The Atlanta GDPNow tracker currently suggests the U.S economy only grew 1.2% in the third quarter, down from an estimate near 6% on July 1. Downward revisions coincided with a surge in COVID-19 cases through the summer.
- **The good news is the latest Delta variant wave appears to have crested**, and we expect this should lead to better economic trends in the months ahead.
- **The Citi U.S. Economic Surprise Index**, which measures how economic reports come in relative to expectations, has declined sharply. However, as the COVID-19 numbers improve and economic data firms, we are **already starting to see this index turn up from depressed levels**.

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The market is in sync with our view that we are moving past the summer growth scare as economically-sensitive areas rebound.

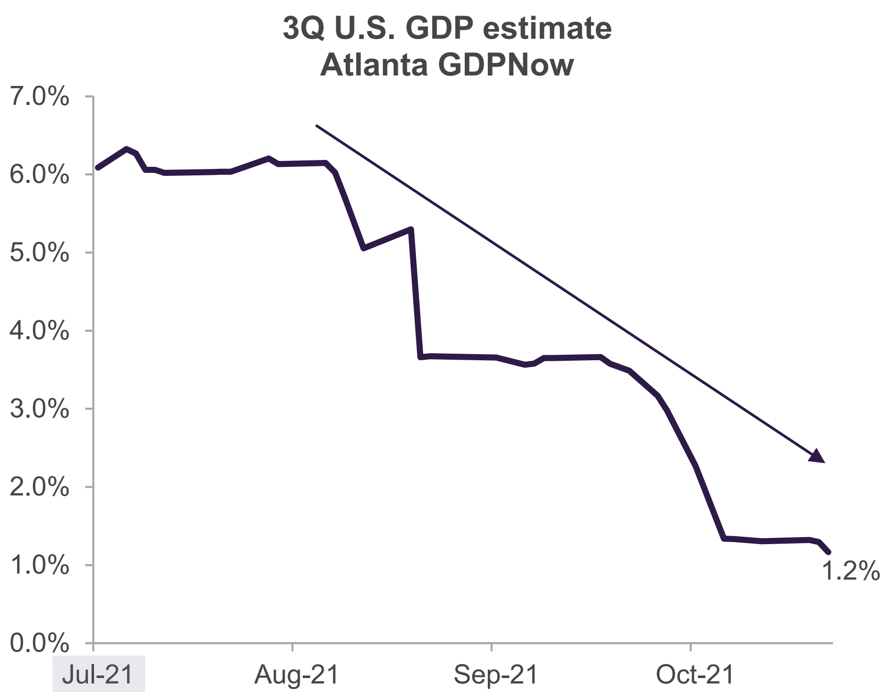
- **Copper** prices are up 15% this month, **lumber** prices are at a multi-month high, the **transportation index** has moved above a multi-month price downtrend, and the **10-year U.S. Treasury yield** has continued to move higher.
- **Classic defensive sectors continue to underperform**, which also suggests investors are looking past the recent economic slowdown. The relative prices of the S&P Consumer Staples and Utilities sectors are near year-to-date lows**. We remain underweight both sectors.**

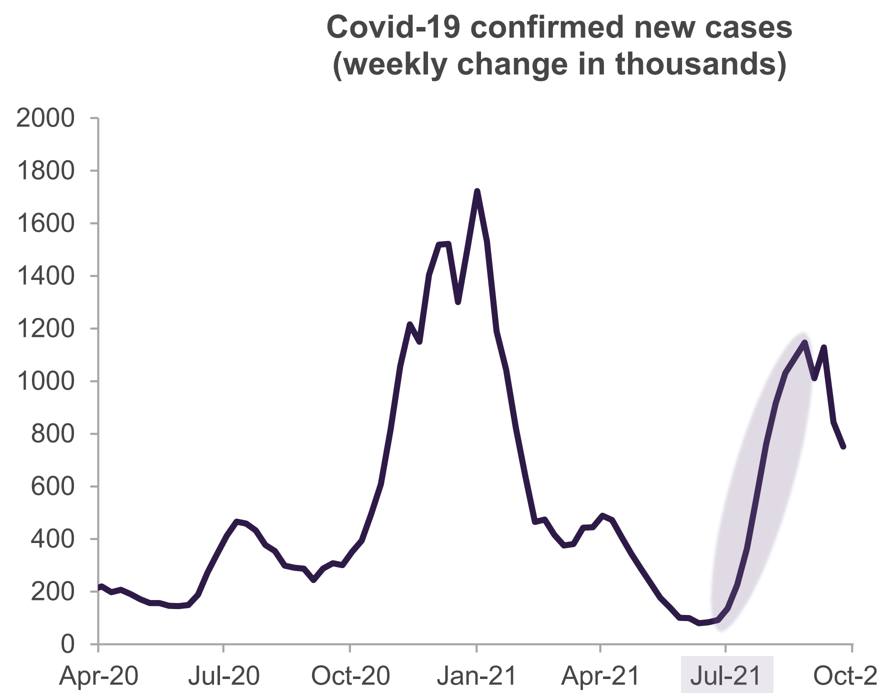
We remain overweight equities and continue to see opportunity in cyclical areas, including the energy and financials sectors, as well as small caps.

- While the **S&P Energy sector** is also up a lot this year, it remains **25% below** where it was three years ago and has lagged oil prices, which are at the highest level since 2014. The sector also still **trails the S&P 500 by 77% over the past three years**. Thus, we still see upside as the economy firms.
- The **S&P Financial sector** made a **fresh high recently**. Improved economic trends and a gradual move higher in yields should remain supportive for the sector.
- **Small caps appear attractive** following extreme underperformance, 20-year lows in relative valuations, and strong earnings trends and should benefit from improved economic trends.

A surge in the Delta variant led to a summer economic slowdown, but we expect activity to improve as new COVID-19 cases decline

The Atlanta GDPNow tracker currently suggests the U.S economy only grew 1.2% in the third quarter, down from an estimate near 6% on July 1. Downward revisions coincided with a surge in COVID-19 cases through the summer. The good news is the latest Delta variant wave appears to have crested, and we expect this should lead to better economic trends in the months ahead.



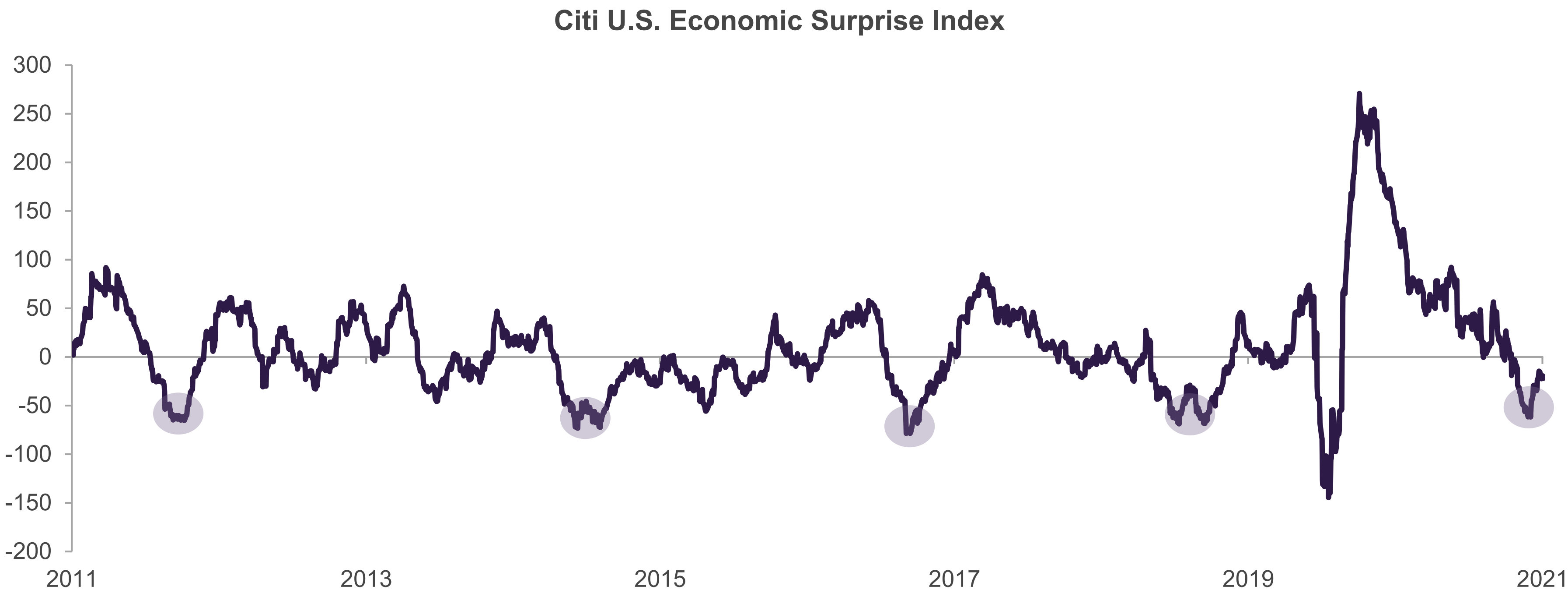


Data Source: Truist IAG, Federal Reserve of Atlanta, Bloomberg.

Past performance does not guarantee future results.

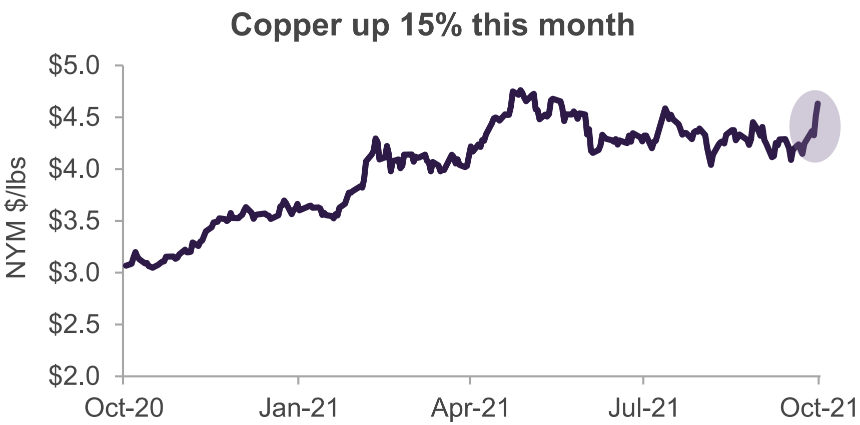
Economic surprise index already turning up as COVID-19 trends improve

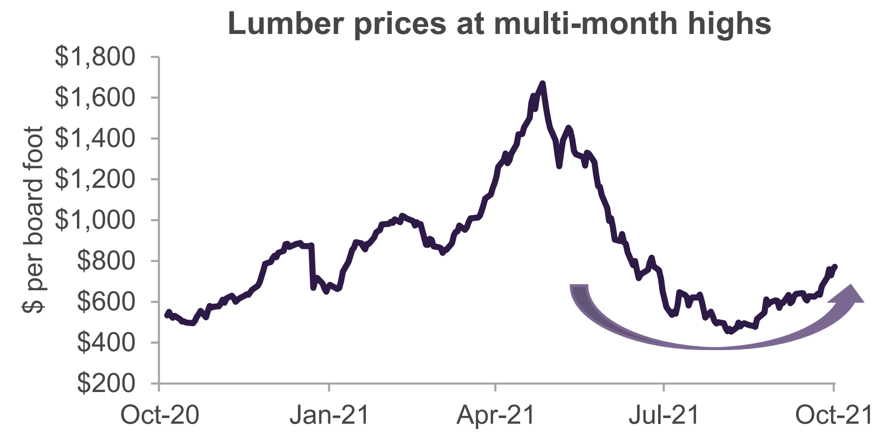
The Citi U.S. Economic Surprise Index, which measures how economic reports come in relative to expectations, has declined sharply. However, as the COVID-19 numbers improve and economic data firms, we are already starting to see this index turn up from depressed levels.

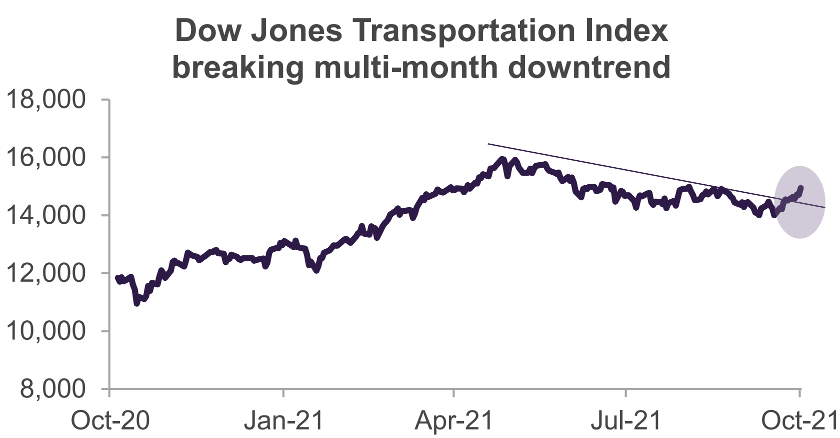


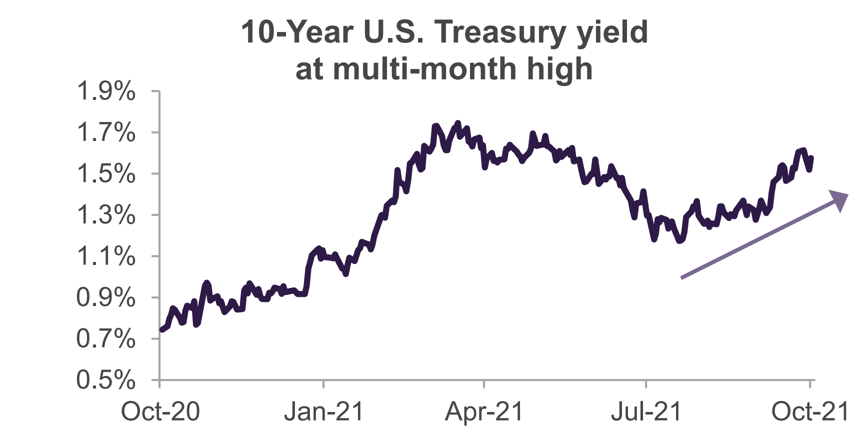
Data Source: Truist IAG, FactSet. Past performance does not guarantee future results.

Market in sync with our view that we are moving past the summer growth scare as economically-sensitive areas rebound





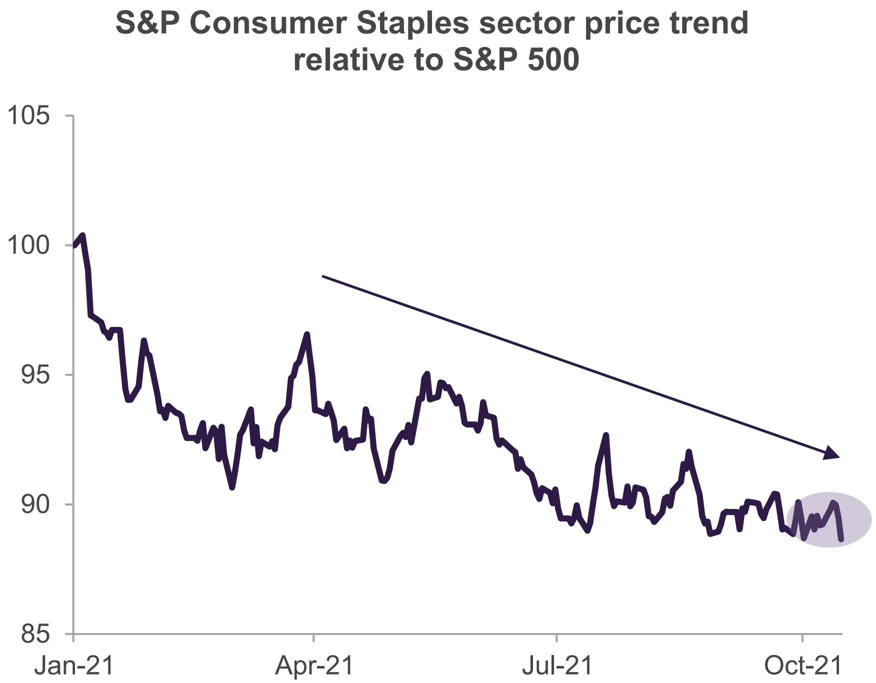


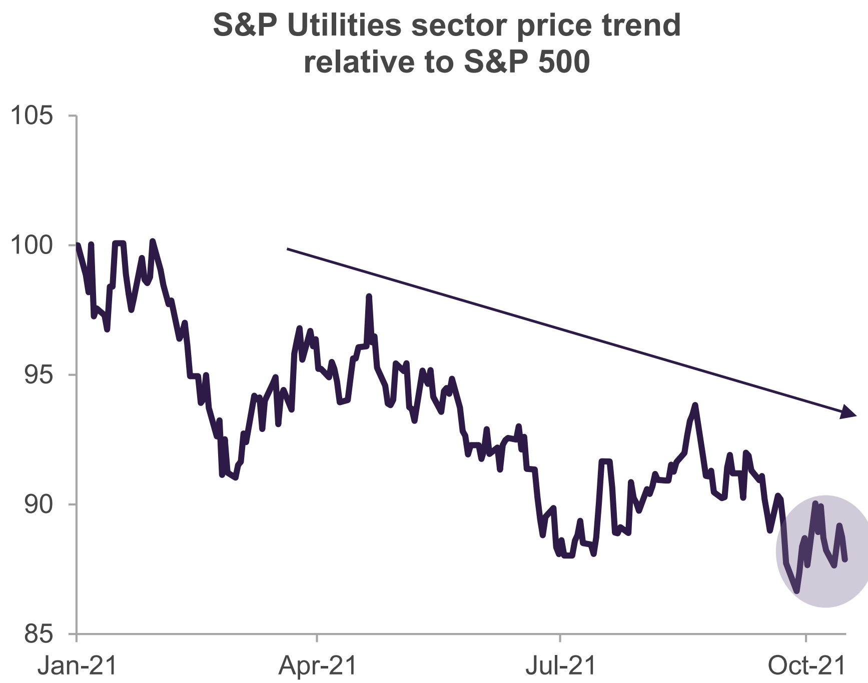


Data Source: Truist IAG, FactSet. Copper = Continuous futures contract; Lumber = Continuous futures contract; Past performance does not guarantee future results

Classic defensive sectors continue to underperform, which also suggests investors are looking past recent economic slowdown

Consumer staples and utilities tend to do better as investors become more concerned about the economy as their businesses tend to be somewhat less sensitive to the economic cycle relative to more cyclically-oriented areas. With both sectors trading near their lowest levels of the year relative to the broader market, this suggests markets are looking past the summer slowdown**. We continue to advise an underweight position to both sectors.**



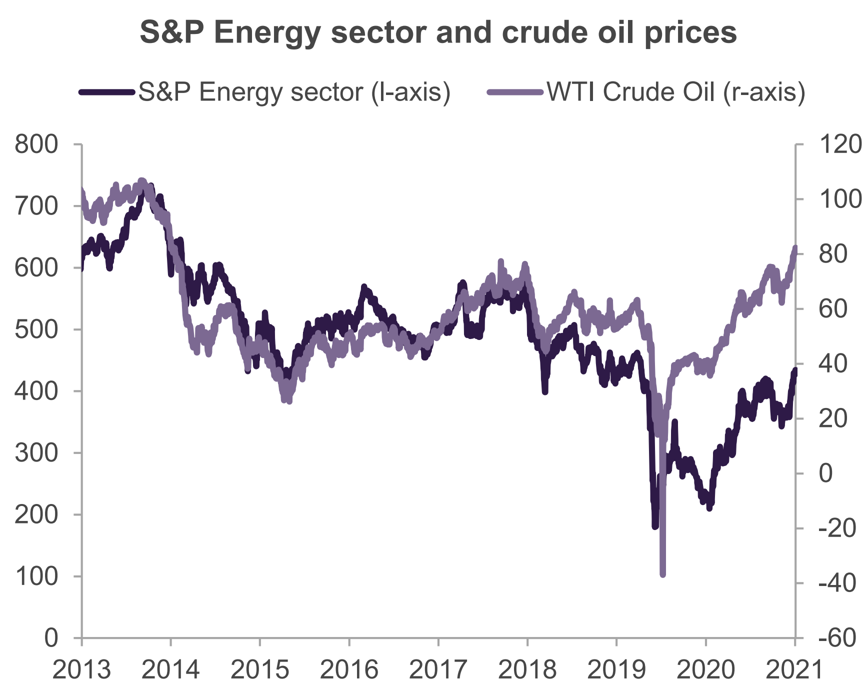


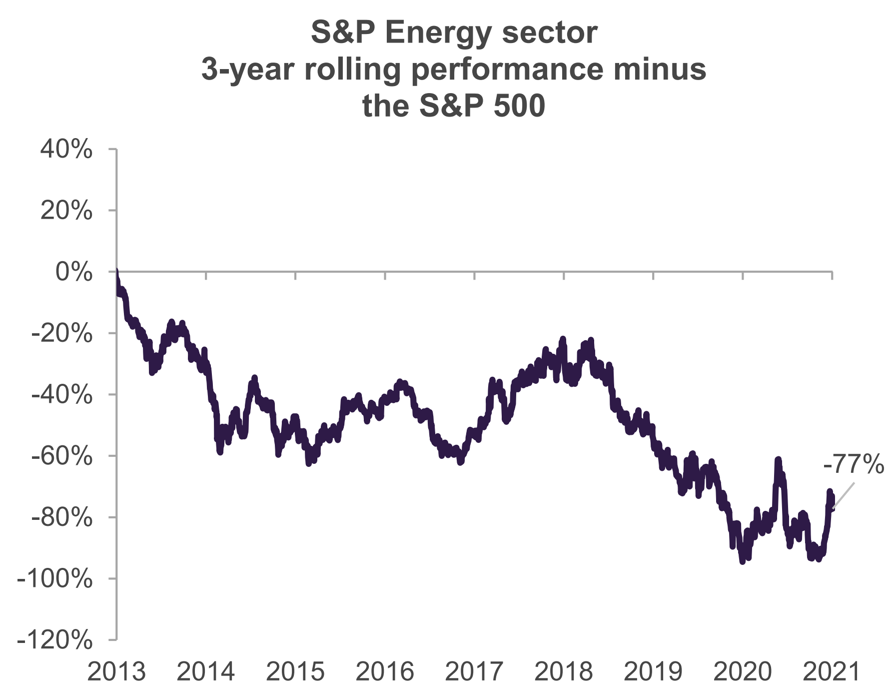
Data Source: Truist IAG, FactSet

Past performance does not guarantee future results

We remain overweight the energy sector – upside potential remains

While the S&P Energy sector is also up a lot this year, it remains 25% below where it was three years ago and has lagged oil prices, which are at the highest level since 2014. The sector also still trails the S&P 500 by 77% over the past three years. Thus, we still see upside as the economy firms.





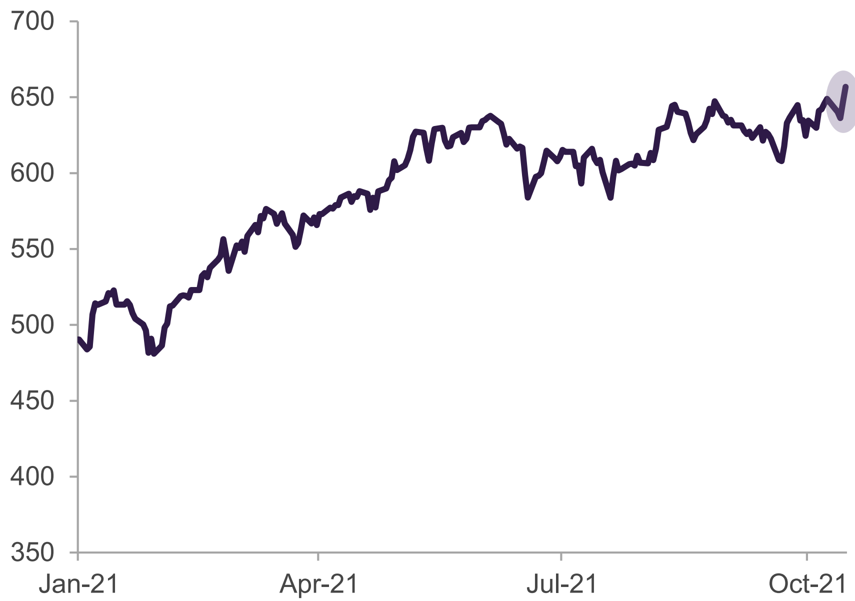
Data Source: Truist IAG, FactSet

Past performance does not guarantee future results

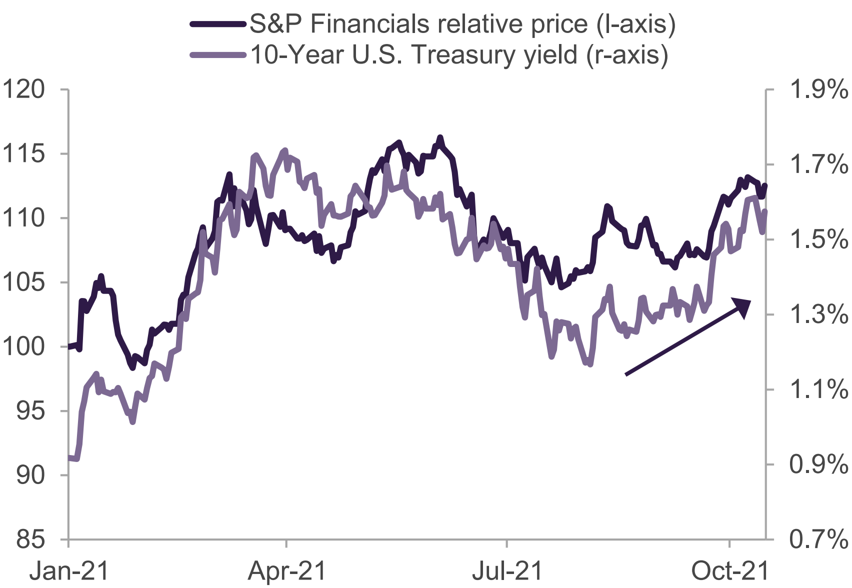
We remain overweight financials – these companies should benefit as the economy firms and interest rates gradually rise

The financial sector made a fresh high recently. Improved economic trends and a gradual move higher in yields should remain supportive. Indeed, the performance of the financial sector relative to the S&P 500 has tracked the direction of interest rates closely this year.

S&P Financials - price at new high



S&P Financials relative price to S&P 500 overlaid with the 10-year U.S. Treasury yield



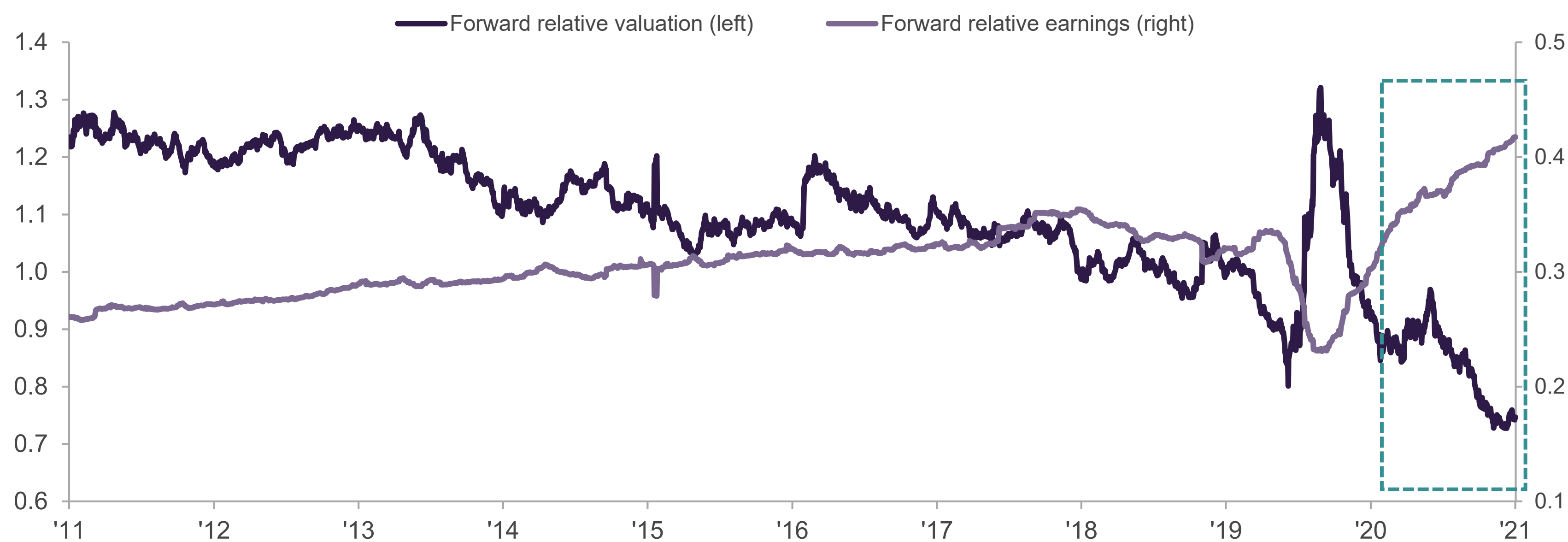
Data Source: Truist IAG, FactSet

Past performance does not guarantee future results

We are overweight small caps – this asset class should benefit from better economic trends, attractive valuations, and strong earnings

Our work suggests a compelling relative opportunity is at hand following extreme underperformance, 20-year lows in relative valuations, and strong earnings trends. Small caps should also benefit as we move past the summer economic growth scare.

Small cap trends relative to large caps



Data Source: Truist IAG, FactSet. Small caps = S&P Small Cap 600, Large caps = S&P 500. Past performance does not guarantee future results.

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