Week in Review

Equity Markets:

All major equity markets were in the red again this week. The S&P 500 ended the week down 0.3% and now, down 2.2% for the year. Technology and consumer discretionary stocks showed some signs of life early in the week, but the NASDAQ ended the week down 0.3%, and down 4.8% so far this year. The growth vs value spread currently stands at ~7%, with the growth index down ~6% and the value index up 1%. Investors' concerns around inflation and interest rates have driven them towards undervalued, lower multiple sectors of the market.

Q4 earnings season kicked off last week, highlighted by a handful of major banks on Friday. Results from JP Morgan, Citigroup and Wells Fargo were mixed and the banks had a lot of price momentum heading into earnings. Of the companies that have so far reported, labor costs and shortages are still having negative impacts on the bottom line.

Fixed Income Markets:

The 10-yr treasury ended the week little changed at 1.77%. Although there were no major moves in the fixed income markets this week, they are still be watched closely as investors prepare for the start of the Fed's tightening plans. The Fed has expressed their most likely course of action, although data dependent. Fed Chair Powell and other Fed officials stated that they are still in support of the tightening policy to keep inflation under control.

This plan is likely to result in:

- Ending asset purchases by March
- Hiking rates over the course of year
- Allowing the balance sheet to run off starting late in the year

Until those play out, uncertainty in the markets will remain. It is one thing to announce your plans, but actions are more important to the markets.

Economic:

The December CPI reading was the major data point released last week. The trend continues with elevated inflation as the reading came in at 7%. This marks eight straight months where inflation exceeded 5%. The January preliminary Consumer Sentiment Index declined more than expected, 68.8 vs 70, on the heels of consumers' concerns over inflation.

Looking Ahead

Equity Markets:

Earnings growth will be a major factor in potentially correcting the current downtrend we have seen so far in 2022. According to FactSet, Wall Street analysts expect companies to report more than 20% increase in net income year-over-year. If companies meet these expectations, the backdrop for an equity market run looks promising.

Next week will put earnings season into full swing. We will continue to see results from other major banks, regional banks, and brokerage firms. Also set to report are Proctor & Gamble, American Airlines, Netflix, and some of the major railroads.

Aside from earnings, inflation and rates will be a major driver and/or risk to the equity markets. If the Fed continues down the path of swift tightening, we would expect to see the pivot to value/cyclical sectors to continue. Historically, these have outperformed growth stocks during times of rising rates.

Fixed Income Markets:

Rates have settled in the current range, but our anticipation is to see rates continue their climb up in the 2% range soon as the Fed is likely to start taking action to keep inflation under control. Once rates break above 2%, we believe that they will stay in the 2% to 2.5% range with a trend upward over the year.

Over the long run, we still don't see rates moving into upper single digits. It's possible to see the 10-yr reach 3% over the next 18 months, but there are long-term factors that should keep a lid on rates. One of these factors includes the deflationary pressures of demographics and our aging population. The aging population may shift more toward risk off assets, such as bonds. The demand for fixed income domestically, along with demand from the international community, will likely help keep yields suppressed longer-term.

Economic:

The housing sector will be the major component of the reports on the economy next week. Housing starts, existing home sales and major applications will be reported. The New York and Philadelphia manufacturing reports will also be released next week.

See following page for important disclosures

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