Week in Review

Equity Markets:

The S&P ended the week down 1.2% after a strong rally the week prior. Q1 earnings season is nearly complete with 99% of S&P companies having reported. 77% have beat earnings expectations and 73% have beat revenue expectations according to FactSet. These numbers are on pace with the 5-year average. Despite the solid earnings numbers for the quarter, the S&P is down ~9.9%.

Earnings beats have been smaller relative to the 5-year average. Companies that have beat earnings, on average, have beat by 4.6%. This is below the 5-year average beat rate of 8.9%, according to FactSet. Corporations have held up strong despite the inflationary pressures, but the numbers indicate growth is slowing.

Fixed Income Markets:

The 10-year Treasury saw selling pressure last week. The yield ended the week at 2.94% after starting the week at 2.74%. Strong employment data contributed to the rise in yields on Friday. A strong labor market is a positive for the economy, but the fixed income markets focused on the impacts the data may have on Fed policy decisions going forward. If the labor market remains strong, fixed-income investors have concerns that the Fed will have no choice but to continue its rate hikes at an elevated level.

According to T-Rowe Price traders, international policy developments had a large impact on the short end of the yield curve. Traders observed that higher-than-expected inflation readings in the Eurozone and the announcement of the European Union's plan to ban Russian oil had influenced the sharp yield increase last week.

Economic:

The labor market remains strong, with nonfarm payrolls increasing 390,000 versus the expected growth of 320,000. The labor market is not yet indicating an impending recession; historically unemployment starts to rise prior to a recession. The ISM Services Index remained in expansion territory, but unexpectedly declined month-over-month.

Looking Ahead

Equity Markets:

Q1 earnings season is nearly complete and the focus will now shift to expected future earnings. According to FactSet, analysts have lowered S&P Q2 2022 earnings expectations by 1.3%. The energy sector has contributed greatly to the S&P quarterly earnings growth rate. For Q1, the S&P 500 earnings growth is 9.2% so far. The energy sector saw 268% growth. Excluding the sector, the S&P would have seen 3.3% growth. These numbers could point to corporate profits being lower in the future.

The rally we saw last week was a reprieve for investors, but it should not be seen as an all-clear sign. We believe volatility will continue as the Fed's tightening policy moves into the latter stages. This is a time for investors to stay disciplined, and keep a long-term perspective. Systemic rebalancing could greatly benefit long-term investors as areas of the market have seen heavy selling pressure. For long-term investors, we see opportunities if one can have the ability to weather the volatility that is still likely to come.

Fixed Income Markets:

We won't hear from any members of the Fed as they go silent before the June 14-15 FOMC policy meeting. Any move in yields will likely be contributed to the CPI reading and the market's expectation for Fed action.

We still believe the majority of the move up in yields has already occurred. Our target range is 3.25-3.5% over the next 12-18 months. We are anticipating another move up in yields to this range in the short term. As yields move closer to our range, we believe fixed-income oriented investors will see these levels as opportunities and will pull yields back before making the move back up. There could be short periods above our range, but we see that as a buying opportunity and expect it to be short-lived.

Economic:

The May CPI release will be closely watched by all investors as the ability of the Fed to dampen inflation without slowing the economy remains in question. The preliminary University of Michigan Consumer Sentiment Index will provide timely insight into the health of consumers.

See following page for important disclosures

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