Week in Review

Equity Markets:

The S&P 500 remained rangebound last week following a late rally into the close on Friday, ending the week slightly negative by 0.3%. The market has been stabilized by the mega-cap technology names that have surprised on the earnings front. Market breadth remains narrow as we enter the end of the first-quarter earnings season.

There are portions of the market that have weakened, but earnings have continued to surprise to the upside. With roughly 92% of the S&P 500 already reported, 78% have beaten earnings expectations and 75% have beaten revenue expectations[1]. Earnings have continued to decline, with the Q1 blended earnings growth standing at -2.5%, but this is much better than the expected earnings decline of 6.7% going into the quarter, according to data collected by FactSet[1].

Fixed Income Markets:

Despite the concerns around the debt ceiling, the 10-yr Treasury saw little movement last week, ending 4 basis points higher at 3.47%. The short end of the yield curve sold off slightly as talks regarding the debt ceiling saw little movement. The 1-month treasury bill spiked at the end of the week with a yield of 5.66%. This is the highest yield on the bill in over 20 years[2].

The 2's/10's spread remains negative but has tightened from the 1%+ spread from last year. Currently, the spread is -0.51%. This spread has historically been a forward-looking indicator; once inverted the likelihood of a recession in the near to intermediate term is high.

Economic:

The headline reports for the week were the Consumer Price Index and the Producer Price Index. As we are likely near the end of the Fed's rate hiking cycle, inflation has remained somewhat sticky. Core CPI, which excludes food and energy, rose 5.5% which was in line with expectations. The headline number rose 4.9% year-over-year. PPI, which is the prices paid by producers, slowed to 2.3% in April. This is positive news for consumers because historically PPI has been a leading indicator for the inflation outlook. The May Preliminary University of Michigan Consumer Sentiment Index dropped to a six-month low, coming in at 57.7, missing expectations. Concerns around the debt-ceiling and regional banks[3] contributed to the downside miss.

Looking Ahead

Equity Markets:

The first quarter earnings are nearly complete and have come much better than expected. Analysts may have gotten ahead of themselves with earnings write-downs, but full-year 2023 earnings have remained lower with slight growth of 1.2%[4].

With the current rate environment, we believe a period of slower growth is likely. The equity risk premium has tightened and for a sustained rally in the markets, we will need to see earnings growth. The higher cost of capital will make this more difficult for corporations to accomplish than in the previous cycle. We believe investors should remain committed to their long-term strategic allocations because a pivot to an accommodative environment can happen quickly. With that being said, investors should realign their expectations over the short to intermediate term. We still believe there are attractive opportunities for Investors with a multi-year timeframe but volatility should likely persist as we move through a slowing economic environment.

Fixed Income Markets:

We believe the fixed-income markets are likely to stay in a tight range until a catalyst forces them to adjust. The macroeconomic backdrop and debt ceiling battle in Washington are the major factors in the fixed-income markets. The debt ceiling could cause short-term volatility and have the potential to put upward pressure on rates, as we have seen on the very short end of the curve, as of late. The weakening macroeconomic environment is a tailwind for fixed-income investors. A pivot, rather than a pause, from the Federal Reserve would push bond prices higher, ultimately reducing rates.

We remain in the lower for longer camp but acknowledge short-term disruptions could cause a jump in rates. The belief is that disruptions should be short-lived and rates will settle in the 3-3.25% range within 6-12 months after.

Economic:

This week's economic news will see housing data from the NAHB's Housing Market Index and existing home sales from the National Association of Realtors. Following the lower-than-expected consumer reading last week, we will see a retail sales report on Tuesday. The Conference Board will release the Leading Economic Index on Thursday. The index has fallen for 12 straight months and market participants will likely be watching the release closely.

**** *See Important Disclosures on following page*

Sources:

1)FactSet
https://advantage.factset.com/hubfs/Website/Resources%20Section/Research%20Desk/Earnings%20Insight/EarningsInsight_050523.pdf

2)Federal Reserve Bank of St. Louis
https://fred.stlouisfed.org/series/DGS1MO

3)Reuters
https://www.reuters.com/markets/us/us-consumer-sentiment-drops-six-month-low-may-2023-05-12/

4)Lipper Alpha/Refinitiv
https://lipperalpha.refinitiv.com/wp-content/uploads/2023/05/TRPR_82221_697.pdf