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WEEKLY MARKET RECAP | August 21, 2023

Week in Review

Equity Markets:

The major markets experienced steep sell-offs last week. The S&P 500 ended the week down 2.6% and the NASDAQ finished the week down 2.6%. The first half of the year was dominated by Large-Cap Growth, specifically the technology sector, but the tide has shifted so far this quarter. The Russell 1000 Growth Index is down 2.61% compared to the Russell 1000 Value Index which is down a modest 0.5%[1].

Second quarter earnings season is nearing completion. 95% of S&P 500 companies have reported thus far and results have been far better than analyst's expectations. 79% of companies have exceeded earnings expectations and 63% have beaten revenue expectations. The earnings beat rate is well above the long-term average of 66% and the prior four-quarter average of 73.4%. On the other hand, the revenue results are in line with the long-term average of 62% but below the previous four-quarter average of 70%[2]. The expected year-over-year earnings growth rate currently stands at -3.4%.

Fixed Income Markets:

The fixed-income market sold off last week and the 10-year put in a new cycle-high closing yield. The 10-year finished the week yielding 4.26% after exceeding 4.3% intraday on Thursday. The sell-off was fueled by strong-than-expected economic data and the Atlanta Fed's GDP forecast. The GDPNow forecast model indicated the economy is likely to grow at 5.8% for the third quarter[3]. Market participants believe this could lead to the Fed keeping the policy rate higher for longer than initially expected.

The yield curve continued its steepening trend that began in early July. The 2's/10's spread finished the week at -0.66%. On July 3rd of this year, the spread was -1.03%.

Economic:

The Conference Board's Leading Economic Index fell for the 16th consecutive month in July. The decline was heavily influenced by consumer expectations which had a decline of 1.33% in July. Retail sales rose 0.7%, handily exceeding economists' expectations. The consumer remains one of the bright spots of the economy. The consumer has stayed resilient despite the high inflationary environment of the past two years. Weekly unemployment claims fell 11,000 week over week to 239,000. The labor market has somewhat cooled but still remains at historically tight levels.

Looking Ahead

Equity Markets:

On the surface, earnings reports have largely appeared upbeat and optimistic. But, as we dig deeper, weakness is still present. Analysts started the quarter with a very pessimistic view, anticipating an earnings decline of 5.7%. Coming out of the Covid-19 Pandemic, corporations were in an extremely healthy position. Corporate profit margins and balance sheet strength has allowed them to absorb the high inflationary environment, and the strength of consumer has been beneficial as well.

The recent drawdowns have moved valuations back down, and the forward four-quarter S&P 500 P/E is at 18.9x. This is still somewhat elevated, but as earnings estimates have stabilized it is an encouraging sign. We believe the recent drawdown has been influenced by overly optimistic sentiment and stretched valuations. Both of these have come down in recent weeks and we do not see this being the start of a long-term downtrend, but more of a recalibration. We do anticipate bouts of volatility throughout the end of the year following the strong performance in the first half of the year. Investors should remain broadly diversified as we have experienced quick pivots to various corners of the market. Broad diversification will help in capturing these shifts, as the majority of the time they come unforeseen. A thoughtfully developed strategic allocation, that matches your specific risk tolerance, will not only help you capture the upside but can also provide protection during risk-off environments.

Fixed Income Markets:

Following last week's jump in yields, the Economic Policy Symposium at Jackson Hole will garner the majority of attention this week. Fed officials will speak about the current environment and is often used as a platform for the Federal Reserve Chairman to announce any significant change in policy outlook.

With rates at cyclical highs, our positive view of the fixed-income markets still remains. The 10-year yield is at its highest level in over 15 years[5] and presents an attractive multi-year risk/return profile for fixed-income investors. In the near term, should be prepared for short bouts of volatility and upward pressure on rates as the Fed enters the final innings in the fight against inflation, but we see any further jump in rates will be short-lived.

Economic:

The economic calendar is light this week and much of the focus will be on the commentary from the Jackson Hole Summit. The housing market will kick the week off. On Tuesday the National Association of Realtors will release existing home sales; followed by new home sales on Wednesday. The University of Michigan will release the final August reading for the Consumer Sentiment Index on Friday. S&P will release its flash PMI for the services and manufacturing sectors on Wednesday.

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

Sources:

1)JP Morgan
https://am.jpmorgan.com/content/dam/jpm-am-aem/americas/us/en/insights/market-insights/wmr/weekly_market_recap.pdf

2)I/B/E/S Refinitiv
https://lipperalpha.refinitiv.com/wp-content/uploads/2023/08/TRPR_82221_711.pdf

3)Reuters
https://www.reuters.com/markets/us/atlanta-fed-model-lifts-us-third-quarter-gdp-view-58-2023-08-16/

4)KPS Research

5)St. Louis Federal Reserve
https://fred.stlouisfed.org/series/DGS10