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June 19, 2023

OBSERVATIONS: *Stock Market gets a technical lift, Inflation softer (but high), macro data still mixed*

- Last week the S&P 500 had its best week since March after rallying +2.6% and breaking above a key technical level (more in today's One More Thought). The yield on the 10-Year US Treasury was mostly unchanged on the week, while the 2-Yr US Treasury yield reached 4.7%—the highest level since mid-March amid continued Fed hawkishness.[1]
- Core inflation (CPI ex. food and energy) rose +0.4%, in line with expectations, in May on a month-over-month basis (MoM) and increased +5.3% on a year-over-year basis (YoY)—slightly higher than expectations of +5.2% but lower than last month's reading of +5.5%. Perhaps a better proxy for interest rate policy, core services excluding housing and energy rose by +4.6% YoY in May, the smallest YoY increase in 15 months.[1]
- US Wholesale prices (Producer Prices Index or PPI) fell -0.3% (vs expectations of -0.1%) in May MoM and have risen +1.1% on a YoY basis—below expectations of +1.5% and the lowest YoY change since December 2020. On a YoY basis, PPI peaked at +11.7% in early 2022.[1]
- Consistent with the contractionary readings from the manufacturing PMIs, the Cass Freight Index—a measure of the trucking volume in the US—decreased in May -5.6% YoY. As activity in the manufacturing sector has softened, shipping rates have fallen as well and trucking costs are down approximately -10.0% YoY in May.[1]
- The NFIB Small Business Optimism Index inched up 0.4 points in May to 89.4—representing the 17th consecutive month below the 49-year average of 98. Perhaps more worrisome, the number of small business owners who expect better business conditions over the next six months declined again in May.[1]
- Retail sales moved up modestly in May (+0.3%) from April and are +1.6% higher than last year, but excluding gasoline sales—*oil prices have been falling recently*—retail sales moved up +4.1% YoY.[1]
- Industrial production moved lower in May as both the mining and utilities sectors registered declines, while manufacturing ticked up a meager 0.1%. Overall capacity utilization also moved lower to 79.6%.[1]

EXPECTATIONS: *Monetary policy divergence: China cuts, Fed holds (for now), and ECB hikes*

- As expected, the Federal Reserve kept interest rates unchanged after ten consecutive rate hikes leaving the target Fed funds range at 5.00-5.25%. The Fed's new Summary of Economic Projections now implies two additional rate hikes by the end of 2023. The European Central Bank (ECB), meanwhile, raised its policy rate by +25bps (as expected) and despite recent data suggesting the Eurozone entered a technical recession in Q1 with GDP contracting -0.1%, which follows a similar economic contraction in Q4-2022.[1]
- In stark contrast to most Western central banks, China's central bank, the Peoples Bank of China, cut its overnight reverse repo rate by 10 basis points and its 1-year benchmark interest rate by the same amount last week. This makes it likely that it will cut its long-term lending benchmark rate later this month and could foreshadow additional monetary stimulus later this year as the Chinese economy struggles in the face of slowing global trade and manufacturing as well as deleveraging from its property markets.[1]

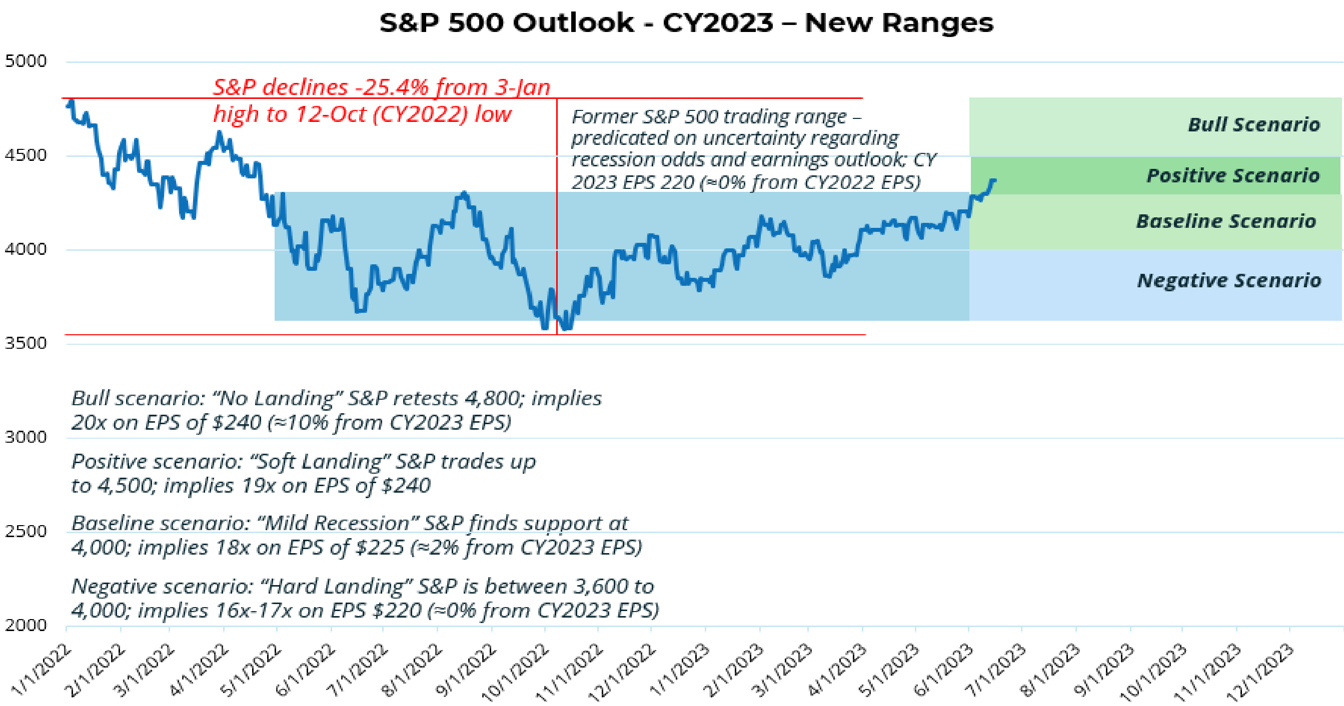
ONE MORE THOUGHT: *Market Momentum: A New Bull or a False Dawn*[1]

Equity markets have been trading up in recent weeks and the S&P 500 has risen more than 20% since its previous low set on October 12, 2022—the technical definition of a new bull market. Additionally, the gains that propelled the S&P 500 into a new bull also pushed it above the price level of 4,300, which is significant in that this was a level that the S&P 500 has had difficulty breaching since May-2022 when the beginning of a series of negative earnings revisions sent the index lower. Since May of 2022, as we have noted several times in past Research Corners, the

[1] *Bloomberg LP*

S&P 500 has been range bound largely between 3,600 to 4,300, with the index confined to an even narrower range of 3,800 to 4,000 for most of that time. However, over the past week, the S&P has held above the 4,300 level which suggests to us there is momentum to potentially take the index even higher over the coming weeks and months. This then begs the question, is this the start of a truly new, long-lived bull run, or a false start ultimately on the way to new lows. We are reminded that in both bear markets of 2000-2003 and 2008-2009, there were several instances where the S&P 500 rose more than 20% from its near-term bottom only to trade lower and ultimately set new bear-market lows. Time will tell, though the near-term momentum of the stock market is likely to be positive as the Fed rate hiking cycle takes a pause and Q2 earnings announcements remain a few weeks away. In the meantime, we adjust our expectations for the S&P 500 year-end range up from 3,600 to 4,300 to 4,000 to 4,500—representing the bottom end of our baseline and the top end of a positive scenario. Lastly, increasing differences in the performance between asset classes—fixed income and equities—and within asset classes—small cap to large cap, growth to value—means rebalancing opportunities exist and investors should be taking advantage of these opportunities.

CHART OF THE WEEK



Source: Bloomberg LP, Clearstead, daily data as of 6/15/2023; Past performance is not an indicator of future results.

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