MARKET REVIEW & OUTLOOK

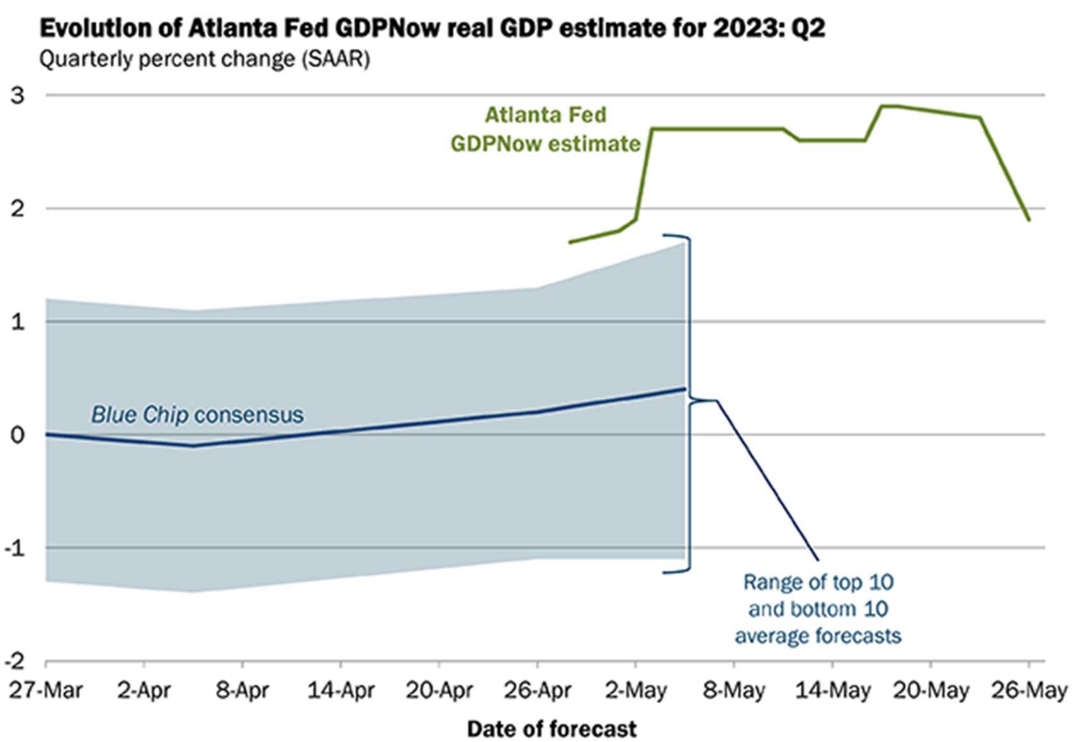
MAY 2023

KEY TAKEAWAYS

- The broad markets still seem stuck, though the AI (artificial intelligence) mania has Tech or things that used to be known as Tech, like Amazon and Google going to the moon. The non-Tech sectors on the other hand dropped.
- The bond market, Fed, can't decide whether Fed fund rates will pause or go up in June. The Fed might just flip a coin as that is as reliable as the daily Fed speak. 😊
- Crude oil continues to trade lower on current fears of slowing demand rather than future expected supply constraints.

The U.S. Economy

The second report for 1st quarter GDP came in at 1.3%, up modestly from the first look. Further, core PCE, the imbedded inflation measure, continued beating expectations, and rose again to 5.0%. The 2nd quarter GDP estimate from GDPNow was looking better mid-month, but seems to be settling into similar performance of 1st quarter in the high 1% growth range, while the Blue-Chip consensus is creeping just above 0%, as shown in the chart below. The Fed continues to face firming inflation, and a "middling" economy. Meanwhile credit is tightening, the Fed's path forward appears treacherous, hence all the hemming and hawing on the next move.



Sources: *Blue Chip Economic Indicators* and *Blue Chip Financial Forecasts*
Note: The top (bottom) 10 average forecast is an average of the highest (lowest) 10 forecasts in the *Blue Chip* survey.

Source : https://www.frbatlanta.org/cqer/research/gdpnow

Stocks and Bonds

Interest rates had a lot of volatility the first 10 days of the month as a clear direction on economic growth and inflation was elusive. However, firming inflation data reasserting itself along with the Fed speak regarding a pause is not a stop and we may raise rates later, lead to a steady march higher in rates, ending with a relief rally on the apparent settlement of the debt ceiling to finish the month. The 10-year yield once again tested just under 3.30%, before moving as high as 3.85%. The Fed meets next month, but the market, or is it the Fed, changes its' mind every day as to whether June is a hike or a pause. The modest increase in yields created a headwind for High Quality fixed income, which as measured by the iShares US Aggregate Bond ETF lost -1.08% for the month. The U.S. 10-year Treasury bond yield ended the month at 3.64%, up from April's close of 3.45%.

The Dow Jones Industrial Average lost -3.49%, the S&P 500 increased +0.25%, and the small cap Russell 2000 declined -1.09%. The international markets traded relatively in line with the U.S. ex-Large Cap Tech. The MSCI EAFE iShares Core International Developed Markets ETF Index fell -3.90%, and the MSCI Emerging Markets iShares Core ETF Index slumped -1.78%.

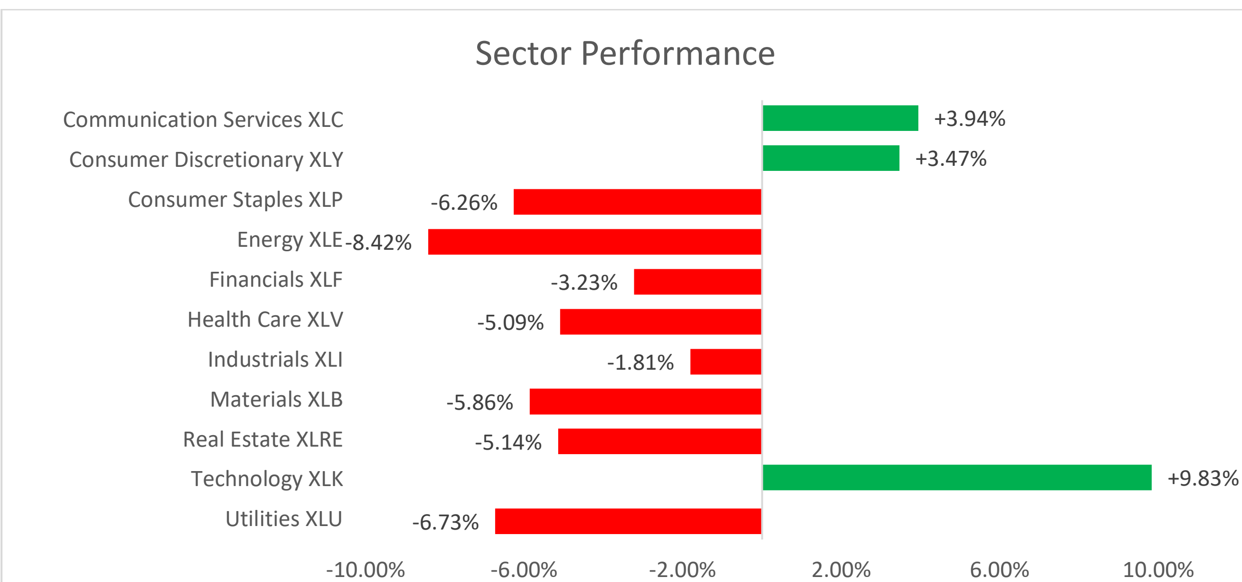
May's performance was to own Tech or names formally known as Tech, like Amazon and Google.

The best performers were…

- Technology: +9.83%
- Communication Services: +3.94%
- Consumer Discretionary: +3.47%

The worst performers were…

- Energy: -8.42%
- Utilities: -6.73%
- Consumer Staples: -6.26%



Source: https://www.morningstar.com

Oil Report

The oil market held above the $70 mark for most of the month but slipped below as the month ended; with the slowing economic data out of China being blamed as the culprit and the resultant likely waning demand for oil. The OPEC+ announced additional production cuts at the beginning of April are now a distant memory as talks of any future cuts remains on hold. The current NYMEX WTI Crude Oil futures settled at $68.09 posting a loss of just over 11% from the prior month's close of $76.78 a barrel. The decline in crude oil hampered RBOB gasoline, as RBOB gasoline finished with a loss of over 3% vs April's close. The current 6-month range bound trading has ended at the bottom of the range. Will concerns of economic slowing result in a new trend lower? Crude oil may be near the lower end of the range, but prices at the pump have climbed steadily reminding me of last year's high prices!

The Rest of the Data

The April ISM Manufacturing Index increased to 47.1 from March's reading of 46.3. Additionally, the ISM Services Index increased to 51.9 in April, from March's print of 51.2. The prices paid component for Services remained at modestly elevated levels and Manufacturing prices firmed. Any reading below 50 generally indicates deteriorating conditions and any reading above 50 generally indicates improving conditions. Consumer confidence decreased to 102.3 in May, which compares to an upwardly revised figure of 103.7 in April. The unemployment rate declined to 3.4%, and the economy added a strong 253,000 jobs in April, which solidly beat expectations, for the 13th month in a row, of 185,000 jobs. The Consumer Price Index for All Urban Consumers (CPI-U) jumped to +0.4% in April, on a seasonally adjusted basis. Over the last 12 months, the All-Items Index rate further eased to +4.9% on a non-seasonally adjusted basis. The CPI ex Food and Energy, eased modestly to 5.5% over the last year. The economy seems to be coasting in a low growth manner. On the other hand, inflation is showing signs of stabilizing at a rate far above the Fed's stated target of 2%. We will continue to monitor economic activity along with inflation reports and now bank run concerns and how that may impact Fed policy.

Summary

The broad markets across many asset classes are seeing meaningful weakness both in the U.S. and International Markets. If not for a handful of AI mania driven stocks, broad indices would be meaningfully lower, please see the chart on the following page. The Fed speakers have been beating the pause/stop/hike not done mantra all month and the interest rate futures market has been reflecting the, all over the map, Fed speak. The narrowness of the market is usually a sign of a tired market, where the new money coming in is limited to the last ones standing. Will that be the case once again or will there be a new catalyst that drives another round of money flows that helps the broader market. As we mentioned last month, the market really doesn't seem to have a good read on what's next. Hence the lack of a sustained direction and the constant swings up and then back down. We still have a couple of more weeks until the next Fed announcement, but their recent confusing Fed speak is unlikely to be cleared up next month. Maybe the Debt Ceiling being fixed will be the answer to all our problems! 🤣

Source: https://www.zerohedge.com/markets/watch-yield-curve-when-stocks-begin-price-recession-risk

As always, the markets can be emotional, so we retain our focus on what we can control, which is the amount of equity risk that is taken in a clients' portfolio in concert with the clients' risk tolerance and long-term goals. The markets will always face different "worries", today it is inflation/war vs. waning growth expectations, tomorrow it will be something else. We have built our asset allocation models with dynamic features and quarterly rebalancing, both in fixed income and equities. The non-Large Cap Tech weakness resulted in the Mid-Cap strategy shifting back to T-Bills. The tactical Fixed Income allocation started transitioning to High Yield bonds at the end of the month.

If you have specific questions about your portfolio or financial situation, we are here to help. Long-term financial planning is designed to deal with uncertainty like those we discussed above. Our portfolio management process is to design a prudent allocation across many asset classes. Equities are for long-term growth and several vehicles that we utilize offer defensive mechanisms to mitigate equity market declines.

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