

Good morning,

What's in this week's Report:

- Were Powell's Comments Really That Bullish?
- Weekly Economic Cheat Sheet: More Focus on Inflation (Core PCE Price Index on Friday)
- Market Concentration Risks Warrant Attention
- Is There Any Value Left in Tech?

Futures are modestly lower, primarily on digestion of Friday's big rally and following a quiet weekend of news.

Economically, the only notable report was German IFO Business Expectations, which jumped to a one-year high (91.6 vs. (E) 90.8).

There was no notable geopolitical news over the weekend.

Today there are two economic reports, Chicago Fed (Prior: -0.10), New Home Sales (E: 628K) and two Fed speakers, Logan (3:15 p.m. ET) and Williams (7:15 p.m. ET), but none of that should move markets as the economic reports shouldn't change the outlook for growth while Powell broadly acknowledged a likely rate cut in September (making other Fed commentary less important).

Market	Level	Change	% Change
S&P 500 Futures	6,463.00	-20.25	-0.31%
U.S. Dollar (DXY)	97.92	0.20	0.20%
Gold	3,415.17	-3.33	-0.10%
WTI	64.07	0.41	0.64%
10 Year	4.286%	0.026	0.61%

Stocks

Last Week (Needed Context as We Start a New Week)

Stocks reversed weakness early last week thanks to Fed Chair Powell's Jackson Hole speech, where he signaled an openness to cutting rates in September, and in doing so confirmed rate-cut expectations. The big Friday rally helped the S&P 500 rise 0.30% on the week.

Stocks traded in a tight range to start last week as focus remained on geopolitics as the Trump administration continued to try to facilitate a ceasefire deal between Russia and Ukraine. The lack of material progress left markets to chop sideways with the S&P 500 ending flat on Monday.

Monday's price action gave way to a downturn on Tuesday, with mega-cap tech stocks beginning to come for sale on profit-taking as traders began to look ahead to Powell's speech on Friday. A solid Housing start headline and steady corporate guidance by HD failed to steady the market, and the S&P 500 fell 0.59%.

The market accelerated lower on Wednesday morning as Trump called for the resignation or removal of the Fed's Cook, rekindling concerns about "Fed independence." The Fed's Waller mentioned the potential for the incorporation of "tokenization" and the use of AI in payment systems, which helped the market stabilize before volatility picked up on hawkishly received minutes from the July Fed meeting. Risk-on money flows persisted into the close, however, leaving the S&P 500 to end the day well off the lows with a modest 0.24% loss.

Stocks gapped lower at the open on Thursday, thanks to hawkish commentary from the Fed's Bostic and Schmid amplifying negative sentiment surrounding an earnings miss from retail giant WMT, which noted measurable inflation pressures being observed during restocking, while pre-market economic data was negative. The S&P 500 caught a bid in the wake of the relatively solid Composite PMI Flash release, but follow-through was limited, and the index ended down 0.40%.

After five consecutive down sessions for the S&P 500, stocks reversed higher in a big way on Friday morning as Fed Chair Powell struck a dovish tone during his speech from Jackson Hole, noting labor market risks are currently outweighing inflation risks. A resurgence in bets for a September rate cut saw the S&P 500 revisit all-time highs into the lunch hour, but the rally lost steam and notably failed to break out to fresh records by a few points. The S&P 500 ended Friday up 1.52%, notably turning positive for the week.

Were Powell's Comments Really That Bullish? No

Markets surged following Powell's more-dovish-than-expected comments on Friday, as his openness to a September rate cut fueled aggressive rate-cut assumptions, and that propelled cyclical sectors and indices as well as the broad markets (Russell 2000 rose 3.9%!).

Given the massive Friday rally, it's reasonable to think that Powell introduced a new, bullish catalyst to the markets, but that is not actually the case. In reality, all Powell did, beyond the short term, was reinforce existing expectations for a September rate cut (remember, Fed Watch had those odds near 100% pre-Powell).

The reason Powell's comments sparked that rally was because they helped diffuse what was pretty "hot" inflation data last week (and for most of August). Numerous inflation metrics have run hot in the last few weeks, including the CPI, the price indices in the August flash PMIs, as well as some insight from retailers (Walmart especially, which said tariffs are now pushing prices higher and that will continue for the next few months).

Powell signaling an openness to a September cut pushes back on those inflation concerns and instead lets investors enjoy the solid economic data from last week (the headline flash PMIs were strong, as were most other metrics). Point being, Powell's openness to a September rate cut allowed investors to enjoy this market environment, i.e., stable growth, some inflation pressures, and the Fed still cutting rates in the coming weeks. That's a positive recipe for stocks in the short term, and combined with some momentum, that's what drove Friday's rally. And with the S&P 500 at new highs, clearly market momentum is higher in the short term.

But the risk profile for this market has not changed beyond the short term. And in reality, it's probably a bit worse than it was. I say that because stagflation risks are actually rising, not falling.

Price metrics are seeing upward pressure, while the labor market is showing more signs of losing momentum (continuing jobless claims and the monthly jobs report are going in the wrong directions).

None of this is bad enough, yet, to impact the markets. But I don't want anyone to be blindsided by rising stagflation risks, and that's why I want to make sure, amidst all this bullishness, that we are staying focused on stagflation risks because if we do get a stagflation scare, the S&P 500 will fall 5%-10% (and more if we actually get some stagflation).

Bottom line, this market wants to go higher right now, and Powell's openness to a rate cut helped to reinforce a largely stock-positive near-term setup. But don't confuse that with an environment where stagflation risks are falling. They are not. And while they aren't big enough to disrupt the rally, they are moving in the wrong direction, and we will continue to watch them closely because the impact on this market if stagflation becomes a real worry will be substantial.

Economic Data (What You Need to Know in Plain English)

Last Week

Economic data was decidedly mixed last week, but had enough of a stagflationary impulse to it to keep stagflation fears alive, and that did slightly add to the downward pressure on stocks last week.

The key reports from last week were the August flash composite PMIs, which gave us the first look at national economic data for August, and the numbers were good. The flash manufacturing PMI jumped to 53.3 vs. (E) 49.7, while the flash services PMI modestly beat estimates at 55.4 vs. (E) 54.2, which helps push back on economic slowdown fears. However, the price components rose in the surveys and supported some of the recent inflation concerns. The other growth metric last week, the Philly Fed manufacturing survey, was more traditionally stagflationary as growth slowed (down to -0.3 vs. (E) 8.0), while New Orders, the leading indicator in the report, dropped to -1.9 from 18.4. However, the prices paid index jumped to 66.8 from 58.8, contributing to the stagflationary reading.

Completing the mixed view from economic data last week, weekly jobless claims rose to 235k vs. (E) 224k, but it was a big jump in Continuing Claims that caught people's attention, as Continuing Claims rose to 1.972k vs. (E) 1.960k. That's a three-year high, and it further supports the idea that the labor market is losing momentum and, more practically, that companies are not yet actively laying workers off. Still, they are not hiring workers either (which is why it's taking unemployed people longer to find a job).

Bottom line, none of last week's data should be viewed as that negative, as growth metrics were mixed (but not bad), while inflation pressures were elevated (but not extreme). So, last week's data doesn't mean that stagflation is more likely or that inflation is rebounding more than the market previously expected.

But last week's data does reinforce that it's possible, and the risk of either slowing growth or elevated inflation (or both) is real and needs to be monitored. That, combined with tech weakness, led to some pullbacks in the major averages last week.

The takeaway is that we need to continue to watch economic data closely (and we will) because while the valuation of the S&P 500 implies there's no risk of a slowdown or inflation spike, the data does not confirm that and that means this market is vulnerable to either a "growth scare" (which would likely come via the next jobs report) or a hot inflation surprise that alters rate-cut expectations (this week's Core PCE Price Index and next month's CPI are the two numbers to watch).

Important Economic Data This Week

This week, the calendar is somewhat sparse from a data standpoint, but the few reports we get will provide notable updates on inflation and growth. The key report this week is Friday's Core PCE Price Index. This is the Fed's preferred measure of inflation and if it rises to or through 3.0% (it was 2.8% in July), that will echo the hot CPI (and other recent price metrics) and regardless of Powell's speech, will inject some doubt into the September rate cut (which would be a negative for stocks as a rate cut in September is priced in at this point).

Looking at the growth data this week, Durable Goods (tomorrow) will be notable to see if business investment has stayed on an upward trajectory through the tariff uncertainty of July (if it has, that's an economic positive as it implies tariffs are not altering business spending/investment, which is positive for growth). The other notable growth report this week is weekly jobless claims, which popped modestly last week. The bigger issue is Continuing Claims, however, as that hit a three-year high. If we see that move closer to 2 million, it will increase concern that the labor market is weakening (which would translate into weaker economic growth).

Bottom line, there are not a lot of economic reports this week, but the few updates we do get will be important for (hopefully) pushing back on stagflation fears, as that would be positive for markets and further support the S&P 500 at these levels.

Special Reports and Editorial**Market Concentration Risks Warrant Attention**

During the market's latest advance that has seen the S&P 500 trade up to fresh record highs this summer, the topic of thinning leadership and historically extreme levels of "market concentration" has been widely discussed and also, importantly, has become an emerging source of concern regarding the sustainability of the bull market in H2'25. Here are some quick facts on current levels of stock market "concentration" and market breadth.

- The top 10 largest U.S. companies, based on market capitalization, now make up ~40% of the S&P 500's total value, an all-time high.
- The top five largest U.S. companies, again based on market cap, now account for ~25% of the S&P 500's total value, more than 10% above the long-term average of 14% since 1990.
- NVDA alone accounts for ~8% of the entire S&P 500, a record high level of concentration for one stock in the broad market index (which actually holds just over 500 names).
- ~70% of the S&P 500's positive "economic profit" (which is essentially the net source of increasing shareholder value in the S&P 500) is generated by the top 10 largest names in the index.
- The top 10 S&P 500 stocks trade at an average Price-to-Earnings Ratio of 26X (2025 earnings) vs. 20X for the "rest of the market."

The fact that 2% of the S&P 500 Index's holdings account for 40% of the 500-company index's total market-capitalization value is not only an attention-grabbing statistic, but it should be concerning because this bull market is now more dependent on the continuation of the rally-supporting AI narrative than ever before. And considering that those same 10 mega-cap stocks account for 70% of economic profit, which is effectively a measure of total S&P 500 shareholder value growth, a correction in any (much less all) of the 10 largest stocks in the S&P 500 could be very detrimental to equity performance.

We have recently been discussing the possibility that an “AI bubble” has formed in equity markets. The fact that indexes have only seen concentration levels even close to current levels during previous bubbles supports the case that a bubble has formed or is forming in stocks. That doesn't mean it will “pop” in the very near future, but it is a dynamic to be aware of and not something to ignore right now.

The level of concentration of the largest stocks in the S&P 500 as a share of the total value of the broad-based, cap-weighted index is only one measure of market breadth that is concerning right now. Still, there are others to be aware, and they are concerningly not in contradiction with the concentration statistics above but instead add to the list of market breadth concerns right now.

The first of the other two measures of market breadth we will look to explore is the percentage of S&P 500 stocks trading above respective, widely-followed moving averages such as the 50-day MA and the 200-day MA, both of which are common timeframe moving averages that everyone from the most experienced market technicians at quant-funds to the most novice investors just starting keep tabs on regularly. When the percentage of stocks above their respective 200-day MAs is on the rise, market breadth can be considered to be improving, as more single-name stocks can be considered in long-term uptrends based on the fact that they are above their 200-day MA. Similarly, a rising number of stocks above their respective 50-day MAs suggests more S&P 500 stocks are in “tactical” or shorter-term uptrends, regardless of their long-term trend status.

During sustainable, long-term uptrends in the broader equity market, equity bulls should be looking for a concurrent rise to new highs in market breadth readings as a source of technical confirmation for the market advance. Additionally, the percentage of stocks above their 200-day MA should be above the more tactical 50-day MA. If stocks are pressing on to new record highs amidst these key, moving-average-based market breadth indicators moving sideways or lower, that is a technical warning sign that participation in the rally is fading and leadership is thinning, ultimately resulting in a rise in concentration into the largest names in the index. And those dynamics are precisely what we are seeing from both the percentage of stocks above their 50-day MA reading, and above their 200-day MA, as the former is in a measurable downtrend with lower-lows and lower-highs on the daily chart. At the same time, the latter stalled in late-July as the January high readings were approached (near 64%) with no new highs to offer breadth-confirmation pointing to a sustainable rally.

The final market breadth measure, and most recent to flash a “Breadth Warning,” was the NYSE Advance-Decline Line, which measures the number of stocks on the entire NYSE that are rising on a given day compared to the number of stocks on the exchange that are falling. A positive reading means more stocks are rising than falling in any given time period, something we would expect to see when the market is rising to signal strong participation in the advance. Conversely, when we see the Advance-Decline Line begin to diverge lower as the major equity indexes continue to rise, it's another technical reading that suggests fading participation and thinning leadership driving the advance.

Right now, the daily NYSE Advance-Decline Line is continuing to rise to new highs, pointing to solid breadth and widespread participation in the latest leg higher of the bull market. However, the weekly timeframe chart, which tends to offer a more reliable read on the underlying breadth trends, has actually begun to roll over, failing to make a new high since the first week of June, and likely more concerningly, fell to the lowest since mid-April as of last Friday's close. The last time we saw a three-plus-month low registered on the weekly NYSE A-D Line was late February, when the H1'25 selloff was only just beginning after new records, albeit incremental all-time highs were established.

Bottom line, multiple market breadth measures and extreme, record high levels of market concentration in the biggest companies of the S&P 500 are dual, but related warning signs from under the market's surface that there are meaningful

and underappreciated downside risks to this market, which has become dependent on the performance of only a handful of mega-cap tech names trading at optimistic valuations. For context, a “valuation reset” that saw the top 10 stocks in the S&P 500 go from trading with an average P/E ratio of 26, down to match the rest of the market at a 20 P/E, would mean a 12% drop in the S&P 500 based on current levels of concentration, and that’s assuming the other 490 names in the S&P 500 remain unchanged.

Is There Any Value Left in Tech?

Investors have significantly benefited from the impressive performance of the tech sector, not only so far in 2025, but also over the past several years, as massive demand for semiconductors and AI infrastructure, combined with the promise of AI-driven leaps in profitability, has caused the sector to lead the S&P 500 higher.

But these gains have also stretched the bounds of what most investors would call reasonable valuations in the tech space, and recently we’ve seen certain AI-darling stocks trade at extreme valuations. The most obvious example of this is Palantir (PLTR), a stock that is the best performer in the S&P 500 YTD but also trades at a quasi-absurd 212X forward earnings!

However, the phenomenon doesn’t just apply to some of the most aggressive AI stocks. Even broad-based tech ETFs such as XLK are trading at historical highs (XLK is currently trading above 29X earnings, a level that hasn’t proven historically sustainable).

Now, we’ve seen a slight alleviation of stretched valuations given this week’s decline in AI-related tech, a decline that has been driven mainly by negative AI-related corporate news and the anticipation of cyclical headwinds given looming rate cuts.

Specifically, CoreWeave (CRWV), Applied Materials (AMAT), and Cisco (CSCO) all posted decent earnings, but the stocks were sold hard afterwards, implying the “bar” to impress investors in the AI names is high.

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