

Good morning,

What's in this week's Report:

- Why Did the S&P 500 Hit A New High? (And Is It Sustainable?)
- Weekly Market Preview: Does the Big, Beautiful Bill Pass and Further Support Growth?
- Weekly Economic Cheat Sheet: The Big Three Reports This Week: Jobs Report (Thurs), ISM Manufacturing & Services PMIs
- Mixed Messages from Market Breadth Measures
- What Would Make Markets Care About the Israel/Iran Conflict?

Futures are modestly higher on further progress on passing the "Big, Beautiful Bill" (which would extend and increase tax cuts, further supporting economic growth).

The "Big Beautiful Bill" passed a key procedural vote over the weekend, and passage out of the Senate is expected later today (and it could be law by the end of the week).

Economically, the June Chinese manufacturing and service PMIs were slightly better than expected.

Today, there is one economic report (Chicago PMI (E: 42.7)) and two Fed speakers, Bostic (10:00 a.m. ET) and Goolsbee (1:00 p.m. ET), but they shouldn't move markets. Instead, the focus will remain on Washington. If passage of the Big, Beautiful Bill becomes even more likely (meaning it passes the Senate and there's no major pushback from House members), that should further add to the upward momentum in the market.

Market	Level	Change	% Change
S&P 500 Futures	6,249.75	26.00	0.42%
U.S. Dollar (DXY)	97.25	-0.15	-0.15%
Gold	3,292.92	5.32	0.16%
WTI	65.39	-0.13	-0.20%
10 Year	4.247%	-0.011	-0.26%

Stocks

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

Stocks rallied to fresh record highs last week as traders celebrated the rapid de-escalation of the geopolitical conflict between Israel and Iran, despite mixed economic data and mildly dovish comments from the Fed. The S&P 500 jumped 3.48% on the week.

U.S. equities started last week with a solid rally as markets recovered from a knee-jerk, risk-off reaction to the U.S. airstrikes on Iran's nuclear facilities the prior weekend. The combination of a better-than-expected June Flash PMI and solid Existing Home Sales helped tamp down recession fears, and Iran's counterattack on the U.S. was seen as nominal, allowing the S&P 500 to rally 0.96%.

The rally continued on Tuesday with the S&P 500 rallying another 1.11% to approach record highs, as President Trump formally announced a ceasefire agreement between Israel and Iran. Meanwhile, Fed Chair Powell was no more hawkish than feared during his first day of semi-annual congressional testimony. A soft Consumer Confidence report bolstered dovish money flows, while reports that the U.S. strikes on Iran were unsuccessful kept the rally from "running away" to new highs.

The week's equity rally paused on Wednesday, as logistics giant FDX reported weak Q1 earnings and New Home Sales unexpectedly fell sharply in May. President Trump's commentary on the Middle East turned less optimistic, leaving the S&P 500 to edge down 0.01%.

Stocks resumed their advance on Thursday, with the S&P 500 notably coming within a single point of the February record high but narrowly missing the opportunity to establish new all-time highs. A rise to multi-year highs in continuing jobless claims (a key unemployment rate proxy) and dovish Fed speak supported risk-on money flows into stocks, while geopolitical tensions continued to ease. The S&P 500 rose another 0.80%.

Equities gapped higher on bullish momentum to start the session Friday as trade-deal optimism fueled risk-on money flows and a better-than-expected June Consumer Sentiment headline helped offset a "warm" Core PCE print for May. The S&P 500 surged to new all-time intraday record highs in the middle of the day before the market rolled over in the afternoon, thanks to deteriorating rhetoric from the White House regarding both geopolitics and trade deals. A late-day bounce saw the S&P 500 recover from a late-afternoon dip into negative territory to end the day higher by 0.52% and at a new record closing high.

Why Did the S&P 500 Hit a New High?

Stable economic data, a slightly dovish shift from the Fed, a decline in geopolitical risks, combined with market momentum, pushed the S&P 500 to a new all-time high last week, despite the market still facing a number of potentially disruptive events. These new highs have shocked many investors and analysts who (reasonably) look at the near-constant stream of negative headlines about tariffs, trade wars, debt, deficits, and geopolitics and view those and the stock market at new highs as incompatible. But nonetheless, here we are. Given this widely held sentiment among investors, I want to examine exactly how we got here and whether this is sustainable going forward.

Reason 1 for New Highs: The Administration. This may come as a surprise to many, given the administration's chaotic and aggressive tariff policy. And undoubtedly, the way the administration operates will keep this market more volatile than it has been in recent years (as we saw on Friday with the Canada headlines). But while the reciprocal tariff announcement rightly shocked markets, since early April the administration has taken a series of actions to "step back" from the brink and the most important part of that is the market believes the administration will not pursue any policies that will materially hurt the economy, regardless of what President Trump may say or threaten. That's the key. And yes, markets can call this "TACO" (Trump Always Chickens Out), but that's an oversimplification. Instead, Trump employs a negotiating strategy that involves threatening a near absurdity and then getting people to move in his direction (so the worst case doesn't happen, but he still exacts gains). Ultimately, the primary reason the S&P 500 has returned to its

February highs is that the market has confidence that the administration won't take any actions that could materially harm the economy. This belief is the foundation upon which the Q2 rebound was built.

Reason 2: No Evidence of Stagflation. Central to the declines in stocks in March and April was the concern that tariffs would lead to stagflation (slowing growth and high inflation). However, neither has occurred, as the economy has proven much more resilient than analysts feared, once again. While there are some minor signs of softening, the economy is holding up reasonably well, and more importantly, there has been no sizable increase in inflation. The market now believes that any inflationary effects of the tariffs will be more than offset by cooling housing and energy prices. As a result, neither the CPI nor the PCE Price Index is expected to rise materially. Meanwhile, the market still expects two Fed rate cuts in 2H'25 to support growth, reducing the chances of a slowdown. Bottom line, the market is no longer afraid of tariff-driven stagflation.

Reason 3: AI Enthusiasm. In a repeat of 2023 and the majority of 2024, AI enthusiasm has again propelled the tech sector to outperform the rest of the market substantially, pulling the S&P 500 to new highs. The DeepSeek drama from January created a buying opportunity in AI names, and in April, as tariff reduction and exemption followed, it only benefited those tech names more. So, once again, AI enthusiasm is a powerful force behind the new highs, and tech and tech-aligned sectors have done the heavy lifting in the Q2 rebound.

Factor 4: Valuations. Again, this may seem surprising, as the market is trading at 23 times the 2025 earnings of \$260-\$265. However, as we alluded to a few weeks ago, analysts are quickly pivoting to using 2026 earnings estimates, which range between \$290 and \$300 per share. Based on that valuation math ($6,141/\$295$), the S&P 500 is trading at just 20.8X earnings, a reasonable number (as long as you agree with all the assumptions built into this rally).

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

Last Week

Economic data mainly remained resilient last week, and the message from the Fed took a slight dovish turn. These factors combined to push the S&P 500 to a new all-time high. Last week brought the first major economic report for June via the flash manufacturing and service PMIs, and both were better than expected. The flash manufacturing PMI was 52.0, compared to 51.2 (E), while the services PMI registered 53.1, compared to 52.9 (E). These were two notable positives, given that the ISM PMIs from May fell below 50, which pushes back on the idea that the economy is losing momentum.

However, not all the economic news was good last week, as there were more signs of deterioration in the labor market. Weekly jobless claims were better than expected and declined to 236k vs. (E) 244k, but Continuing Claims jumped to 1,974k vs. (E) 1,950k. That increase brings Continuing Claims to the highest level since 2021. The practical takeaway from this data is that employers aren't actively laying off workers. Still, they aren't hiring either, so it's becoming more difficult for unemployed people to find a job. Typically, this is a leading indicator of labor market weakness, and we'll need to continue watching it closely because the current market levels do not account for a potential growth scare (and if we experience one, it could shave 5%-10% off the S&P 500, quickly).

Finally, on the Fed front, Powell's semiannual testimony to Congress provided little new information, as he largely reiterated the Fed's "wait-and-see" approach. But importantly, he didn't materially push back on comments from other Fed leaders (Bowman and Waller) about a possible July rate cut. So, while a July cut remains unlikely, the expectation for a September rate cut is rising, which helped the stock and bond markets last week.

Bottom line, most economic data continued to show a resilient economy. At the same time, the Fed made a very slight dovish shift, and this combination helped push stocks higher (along with falling oil prices following the Israel-Iran ceasefire). However, there are growing signs that the labor market is losing momentum, so we cannot be complacent about economic risks, as a growth scare would likely impact this market.

Important Economic Data This Week

This week brings the “big three” monthly economic reports, and it will be another condensed schedule due to the July 4th holiday and an early close on Thursday.

The key report this week is Thursday’s jobs report, and the key here is stability. There have been several labor market indicators that have lost momentum lately. If we see a lackluster jobs report (solidly below 100k), that will spike economic concerns, which is something this market is vulnerable to.

The other two key reports this week are the ISM Manufacturing and Services PMIs. They are released on Tuesday and Thursday, respectively, and the key to these reports is clear: At least one needs to jump back above 50. Last month (May), both PMIs fell below 50 for the first time since mid-2024. One month of sub-50 numbers for both isn’t a big deal, but two consecutive months are more substantial. That wouldn’t be enough to declare a warning sign on the economy, but it leaves this data set open to a third or fourth straight sub-50 reading, and if that occurs, then it will be enough to declare an economic warning sign!

Bottom line, one (or ideally both) of these PMIs needs to return above 50, and the sooner, the better. While this is a holiday-shortened week, it’s important, as we will receive key updates on the labor market and activity in the manufacturing and service sectors. Solid readings will help support this market and reinforce that tariffs are not causing an economic slowdown.

Special Reports and Editorial

Mixed Messages from Market Breadth Measures

The level of participation in a given rally or selloff in the stock market can offer key insight as to whether the move in question is sustainable or counter to the underlying trend. Put simply, when stocks are rallying, bullish investors want to see participation elevated or rising to bolster the conviction that the move is sustainable. Conversely, low or fading participation or thinning leadership during a stock market advance can highlight rising risks that the rally is becoming exhausted and increasingly dependent on just a few mega-cap names (a dynamic we have seen frequently in recent years).

NYSE Advance-Dcline Line

Starting with a traditional favorite measure of market breadth, the NYSE Advance-Dcline Line, which is derived from a relatively simple calculation: subtracting the number of declining stocks during a given timeframe (usually a daily or weekly period) from the number of advancing stocks in a particular index or basket. The measure can be calculated for any group of stocks, but the NYSE Advance-Dcline Line provides the most comprehensive look at total stock market breadth.

Encouragingly, the daily NYSE Advance-Dcline Line reached an all-time high last week, as the S&P 500 tested its record highs from February, indicating that the recent advance towards record territory is broad-based and should be considered both historically healthy and likely sustainable.

Percentage of S&P 500 Stocks Trading Above Their 200-Day Moving Averages

Another widely followed measure of market breadth is the “Percentage of S&P 500 Stocks Trading Above Their Respective 200-Day Moving Averages.” This alternative measure of breadth offers a good idea of how many stocks are not only “advancing” or rallying on a given day, but arguably more importantly, how many stocks are in long-term uptrends as defined by whether the stock is trading above or below its 200-day moving average. In this case, a stock above its 200-day MA can be considered to be trending higher, and a stock below its 200-day MA can be regarded as trending lower.

This insight helps know if the “advancers” supporting the new highs in the NYSE A-D Line are in full “bull market mode” or instead amid respective counter-trend, bear market rallies. Ideally, we would like to see the A-D Line rising or at new highs alongside a healthy percentage of S&P 500 stocks trading above their respective 200-day moving averages, historically somewhere between 65% and 80% (anything above 80% can be a signal of an overbought market or overcrowded long side of the market at risk of a pullback).

In contrast to the bullish state of the NYSE A-D Line, the current reading on the Percentage of S&P 500 Stocks Trading Above Their Respective 200-Day Moving Averages remains stuck to the 50% level, and notably below the early May highs, a divergence that is a source of concern for this test of all-time highs in the S&P 500 this week.

Bottom line, the divergence between the bullish NYSE A-D Line reading and recently heavy action in the Percentage of S&P 500 Stocks Trading Above Their Respective 200-Day Moving Averages is a source of concern that the rally off the April lows has been due to a combination of real strength in some corners of the market, but counter-trend, bear market rallies in others. For the bulls, the best-case scenario is for the Percentage of S&P 500 stocks trading above their respective 200-day moving averages to rise beyond the May highs of 55%, underscoring that this rally is broad and should be viewed as sustainable.

What Would Make Markets Care About the Israel/Iran Conflict?

Many investors (and advisors) have been surprised by the limited impact on the markets from the Iran/Israel conflict, and most recently, the direct U.S. strikes on Iranian nuclear facilities. However, while these events have not yet moved markets, I don’t want that to be confused with the idea that this conflict can’t move markets, as this situation is not a risk that should be ignored. As such, I wanted to cover the two ways this conflict could negatively impact markets.

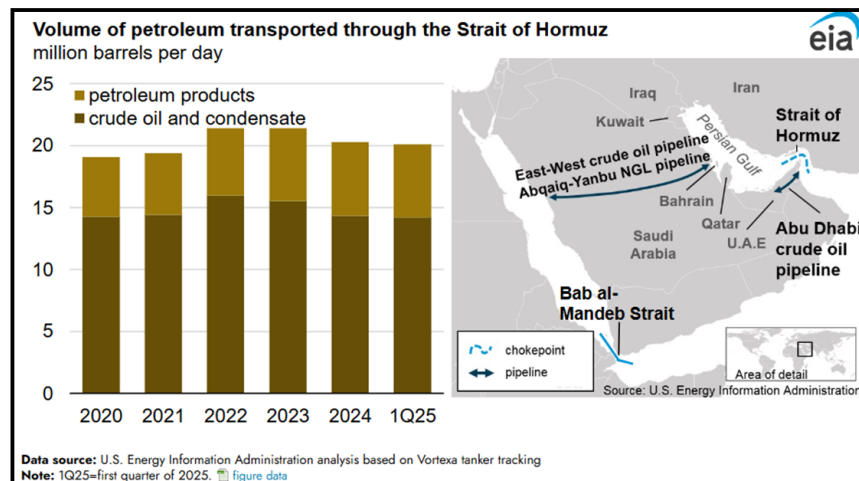
Before I cover those two scenarios, I want to ensure that we all understand why the Iran-Israel conflict hasn’t sent the price of oil sharply higher or stocks sharply lower. It’s because the markets don’t think the conflict will materially disrupt oil production from the Middle East or the flow of oil through that region. That is the only reason the markets haven’t “cared” about this situation and why the market reaction (which has been muted) is so disjointed from the media headlines (which are scary and worrisome).

For this conflict to impact markets, something must occur that makes markets believe oil production and transit could be disrupted. There are two ways this could happen.

First, Iran disrupts transit through the Strait of Hormuz. The Strait of Hormuz is a narrow waterway located between Oman and the UAE to the south and Iran to the north. Every day, 20 million barrels of oil and refined products transit the Strait, as it is the key waterway that transports oil from Saudi Arabia, Iraq, the UAE, Oman, and Iran —a region that produces 25 million barrels of oil per day.

The 20 million barrels per day of oil that runs through the Strait represents 20% of global oil consumption, so we are talking about a substantial amount. If Iran were to attempt to disrupt the movement of oil from those countries out of the Strait and into open water, it would sharply boost oil prices (at least 10% and more, depending on the severity of the disruption), which would negatively impact stocks.

They could accomplish this in several ways. Laying mines in the Strait, attacking merchant ships via missiles or rockets, utilizing small, fast boats to harass ships exiting the straight or via more technological means, including jamming GPS signals (which there are some reports they've done sporadically). Importantly, Iran does not have to block the Strait. Instead, they have to make it dangerous enough that the shipping companies refuse to travel. *Why this is unlikely:* There are several reasons this is unlikely. First and foremost, it would hurt Iran, as Iranian ships also transit the Strait. Additionally, the vast majority of the oil leaving through the Strait is heading east towards China, India, and Japan.



Strait of Hormuz: The Strait is the exit path for most of the Gulf's oil, as 20 million barrels per day transit the waterway. Unless Iran takes action to disrupt much of that production or transit, markets will likely continue to mostly ignore the conflict between Iran and Israel.

China needs that oil, and disrupting maritime traffic through the Strait would hurt China and other Asian countries worst, not the U.S. (other than peripherally through higher oil prices). Bottom line, it's not in Iran's interests. Second, this is unlikely due to the presence of the U.S. 5th Fleet. The U.S. 5th fleet is stationed in Bahrain and tasked with ensuring maritime security in the region. The 5th fleet includes a carrier group along with numerous support vessels. If there were some blockage or disruption in transit, it's reasonable to assume the response from the U.S. military would be punitive on Iran. So, again, it's likely not in their best interests financially or practically.

Second, a regional conflict erupts that endangers oil production. Suppose Iran were to stoke a broader, regional war by attacking oil facilities in Saudi Arabia or another Gulf state that disrupts the flow of oil, turning the conflict from an asymmetrical one (Iran vs. Israel) that could cause a spike in oil prices and impact markets. *Why this is unlikely:* Iran doesn't have any allies in the region that could come to its aid. Hezbollah in Lebanon and Hamas in Gaza have been largely destroyed by Israel and U.S. strikes on the Houthis in Yemen have made them less likely to back Iran's actions. Even Qatar, which has decent relations with Iran, was the target of the missile attack last week (admittedly, it was U.S. bases in Qatar, but Iran still shot missiles into that country). So, a regional conflict would likely resemble Israel, the U.S., and numerous Gulf states versus Iran, rather than a broader regional conflict.

From a market standpoint, this situation remains largely about oil, and as long as the flow of 20 million barrels per day out of the Gulf is not materially disrupted, oil prices are unlikely to rise sustainably. Consequently, this situation is unlikely to have a dramatic impact on U.S. markets.

Finally, don't be surprised if there are reports of sabotage on individual tankers or pipelines transporting crude out of Saudi Arabia or the UAE/Iraq. It's reasonable to expect Iranian groups to create some mischief/trouble to strike back at Israel and the U.S. via oil prices. However, unless it results in a widespread disruption of millions of barrels per day, these attacks are unlikely to create a sustainable increase in oil prices.

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Richard Rose AIF®
917-597-7432
rrose@nationwideplanning.com