

Good morning,

What's in this week's Report:

- The Two Main Reasons Stocks Hit New Highs
- Weekly Market Preview: Can Resilient Economic Data Keep Supporting Stocks?
- Weekly Economic Cheat Sheet: Jobs Week (Jobs Report on Friday)
- Understanding Why OpenAI Concerns Hit the Market
- Future Market Impacts of the Fed Meeting
- "Run-Hot" Economic Data Fuels Fed Policy Uncertainty

Futures are slightly lower as markets digest the latest U.S./Iran headlines, including the implication of "Operation Freedom" and a report that a U.S. Naval vessel was attacked.

On Sunday, President Trump announced "Operation Freedom," in which the U.S. military will help escort trapped tankers out of the Strait of Hormuz.

Iran's reaction to this is unclear, but there are unconfirmed reports that Iranian missiles hit a U.S. naval vessel, and oil is rallying in response (and futures are slipping).

Today's headlines from the Gulf will dominate markets, and if there's a resumption of attacks between the U.S. and Iran, expect oil to spike and stocks to drop. Outside of geopolitics, New York Fed President Williams speaks (12:50 p.m. ET), and for markets, the more dovish he is, the better.

Market	Level	Change	% Change
S&P 500 Futures	7,253.75	-4.25	-0.06%
U.S. Dollar (DXY)	98.18	0.18	0.18%
Gold	4,573.34	-71.16	-1.53%
WTI	103.42	1.48	1.45%
10 Year	4.396%	0.018	0.41%

Stocks

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

Stocks churned sideways through the first half of last week amid simmering geopolitical tensions ahead of both the Fed decision and Mag-7 earnings. A revival in AI optimism powered a late-week rally, sending the S&P 500 up 0.92% for the week.

Equities largely chopped sideways in a trendless manner to start last week as traders digested the breakdown in peace talks between the U.S. and Iran, which triggered an oil rally and sent yields higher. A strong 2-Yr Note auction that curbed the rise in yields and revamped AI optimism amid multiple mega-cap tech investment deals helped the S&P 500 close up 0.12% at a new record.

The market gave back Monday's gains, and then some at the open Tuesday as a WSJ article revealed OpenAI failed to hit internal revenue and user growth targets, which poured cold water on the early week sense of AI enthusiasm. No further progress towards a lasting U.S.-Iran peace deal and a "hawkish hold" by the BOJ were both added drags on the market, leaving the S&P 500 to close down 0.49%.

A sense of "Fed paralysis" fell over the market on Wednesday as traders looked ahead to the afternoon FOMC decision and Powell's final press conference as Fed chair. A sharp, geopolitically fueled rally in oil weighed moderately on stocks before volatility picked up after the Fed statement revealed that the April FOMC meeting had the most dissenting votes since 1992. The S&P 500 stabilized at key support at 7,100 and ended off session lows, still down 0.04%.

Volatility remained elevated early Thursday as mixed mega-cap tech earnings (GOOGL surged, MSFT pulled back, and META fell sharply) roiled markets early in the day. However, largely robust U.S. economic data and news that the U.S. had prepared a new peace proposal aimed at reopening the Strait of Hormuz helped the "rest of the market" mount a month-end rally, and the S&P 500 closed up 1.02% at a new record high.

Stocks gapped up to another set of record highs on Friday, thanks to a blowout earnings release from tech behemoth AAPL and news that the U.S. had prepared yet another peace deal proposal for Iran. The early advance was stopped in its tracks upon the release of the April ISM Manufacturing PMI, which offered a fresh whiff of stagflation amid surging input costs and a sharp decline in the Employment subindex. Stocks spent the balance of the session churning steadily lower but maintained positive territory to end the day up 0.29%.

Two Reasons Stocks Hit New Highs

In last Monday's issue, we noted that earnings results would likely be the most important market catalyst last week, and that proved true: strong earnings drove the S&P 500 to another new high despite deterioration in the U.S./Iran situation.

The Q1 earnings season has been very strong, with 80% of companies beating estimates (solidly above the historical average), and if we had to point to one reason the S&P 500 is at new all-time highs, it's earnings. But, if we look specifically at the results, there were two themes in earnings releases last week (and really all season) that powered stocks higher: The economic impact of the ongoing AI data center boom and a resilient consumer.

Starting with the AI data center boom, it's alive, well, and strong. Not only is the insatiable demand for technology parts and capacity (semiconductors, memory, compute power, cloud storage) helping tech earnings grow sharply, but construction of the actual sites (buildings, roads, utilities) is powering numerous other sectors. The AI data center buildout is still acting like an economy-wide stimulus program, benefiting many companies' earnings, not just the tech sector.

Turning to the consumer, spending remains resilient despite geopolitical concerns and more affordability challenges. Companies across the consumer spectrum (banks, credit cards, casual dining, luxury goods, travel) are consistently reporting resilient consumer spending, which has absolutely helped drive strong earnings and higher stock prices.

Bottom line: stocks are at new highs for legitimate reasons beyond just momentum (though momentum is part of it), as earnings growth is better than expected, thanks primarily to the AI data center stimulus and resilient consumer spending. And as long as that's true, it'll be hard for this market to have a sustained decline. However, don't confuse that with a market that can't go down!

The risks to both of these positives are significant and cannot be ignored. On the AI front, the reality is it's not sustainable in the long term unless we start to see better ROI from AI, and we are not seeing that yet. It doesn't mean it won't happen, but it must happen at some point, otherwise the AI building boom will stop, and that will be an earnings and economic headwind.

As for consumers, higher gas prices (really, higher prices on everything) do matter. Low unemployment is keeping the consumer resilient, but it's not indefinite. The longer the Strait of Hormuz remains closed, the longer and more severe the stagflation impact on the economy will be, and that could be a problem in the coming quarters.

Bottom line, this market is stretched in the short term, and there are risks to monitor. But there are real, fundamentally positive reasons for the new highs. So, while this market remains vulnerable to an air pocket on U.S./Iran disappointment, there are legitimate, fundamental financial positives supporting stocks that should limit downside as long as they remain in place.

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

Last Week

Economic data last week continued to point towards a "run-hot" economy of 1) Strong activity and 2) Higher prices, and the market implications of that are higher Treasury yields and cyclical sector outperformance.

Virtually every important economic report last week pointed to the same thing: Strong economic activity and increasing price pressures. The key report was the March Core PCE Price Index, the Fed's preferred measure of inflation, which met expectations at 3.2% y/y, up from 3.0% y/y in February. Positively, that wasn't any worse than feared. Negatively, that's the highest reading since November 2023, and the Core PCE Price Index has now risen solidly above 3.0% from the cycle low of 2.8% back in mid-2025. Bottom line, the Fed's favorite inflation metric is clear: Inflation pressures are building again, and that does mean 1) A greater chance of rate hikes in 2026 or 2027 and 2) Upward pressure on yields (which, at some point, will become a problem for stocks if they keep rising).

Looking at the growth data last week, it was strong. Friday's ISM Manufacturing PMI showed solid activity and a big jump in prices. The headline reading was flat at 52.7 vs. (E) 53.1 while New Orders slipped slightly to 54.1 vs. (E) 54.5. While slight misses vs. expectations, both metrics remained solidly in expansion territory. The price metrics, meanwhile, exploded higher by 26.2 points, to levels not seen since April 2022, when the Fed was reacting to the Covid inflation surge. Bottom line, the ISM Manufacturing PMI price index doesn't directly translate to higher CPI, but it does reflect elevated price pressures in the manufacturing industry.

Durable Goods beat estimates on the headline, rising 0.8% vs. (E) 0.5% while the more important New Orders for Non-Defense Capital Goods ex-Aircraft (NDCGXA) leapt to 3.3% vs. (E) 1.6%. It's probably true that the number is overstating business investment because it's an aggregate figure (so rising prices boost the number even if more investment isn't occurring). However, it's still a strong reading and suggests businesses aren't pulling back.

Turning to the Fed, it met expectations by holding rates steady and keeping an easing bias in the statement, but three dissents wanted to change forward guidance to a neutral stance. The practical impact of the statement was the removal of expectations for a rate cut in 2026 (which were already low, so it wasn't a new negative). However, the Fed seems to be drifting more hawkish, and if the idea of rate hikes gains more traction, that will be a new negative for markets.

In sum, the data and Fed decision weren't negative for stocks in the near term, as the data was solid. And despite the dissents, the Fed didn't alter forward guidance. But the Fed is moving in a hawkish direction, and inflation pressures are continuing to build. If that continues, we will be dealing with rate hikes over the medium term, and that is not priced into this market.

Important Economic Data This Week

This week's focus will be on the labor market and Fed speak, with Friday's jobs report as the key event. We will have our regular Jobs Report Preview in Thursday's Report. Still, markets will want to see a Goldilocks reading that 1) isn't so strong it increases Fed worries that the labor market may contribute to inflation, and 2) isn't so weak that stagflation concerns increase.

Beyond Friday's jobs report, it's "jobs week," which means we get JOLTS tomorrow and Challenger layoffs and jobless claims on Thursday. By the end of the week, we should have a good idea of the state of the labor market, and for the data to support stocks, we need to see solid but not spectacular activity (because too strong growth will increase inflation concerns).

The most important growth metric this week is tomorrow's ISM Services PMI. This remains one of the most important monthly economic reports, and the key is that it stays above 50. That said, the price indices will be closely watched because if we see a spike there, it'll raise concerns that higher oil/gas prices are starting to "seep" in to other parts of the economy and boost overall inflation (presumably, service inflation shouldn't be directly impacted by higher gas prices but if service prices are rising sharply, that's a bad sign for inflation). A headline number at or below 50, with elevated prices, would be a worst-case stagflation reading.

Finally, on inflation, the University of Michigan Consumer Sentiment survey comes out Friday, and we'll be watching the inflation expectation metrics. The one-year isn't very important (it's volatile and tied to oil prices), but the five-year is important, and if it continues to rise, that will get the Fed's attention.

Bottom line, the economic data of that past month has shifted the focus from growth (which is strong) to inflation (which is rising). If this week's data pushes back against rising inflation concerns (via Goldilocks growth and price readings), that will help support stocks.

Special Reports and Editorial

Understanding Why OpenAI Concerns Hit the Market

A report on Tuesday by the WS stating that OpenAI missed internal revenue and user growth metrics didn't just cause weakness in the tech sector (which would be expected). It also caused industrials and materials to sell off, and given rising concerns about OpenAI's performance, we must understand how disappointment could impact the broader markets.

To keep things in plain English, OpenAI has committed to spending so much money on building data centers and computing power that its spending intentions now affect several major companies and sectors. More specifically, to complete and execute Project Tigris, OpenAI's global AI infrastructure buildout initiative, OpenAI will need massive amounts of materials and supplies from multiple industries tied to tech and infrastructure.

That translates to massive incremental demand for semiconductors, cloud computing, processor power, and infrastructure, as well as computing power and memory. In fact, the demand from primarily OpenAI is so big that it's spawned businesses that secure these supplies (semiconductors, cloud space, and processing power) and then lease them to OpenAI (and others).

However, the demands for AI infrastructure aren't limited to silicon and compute. Buildings have to be built, they have to be air-conditioned, roads must be constructed to reach these buildings (in some cases), power supply must be secured, and on it goes. The practical reality of OpenAI's massive spending intentions has been to create a de facto "OpenAI" of publicly traded stocks, not just in the tech sector but also in the industrial, materials, and utilities sectors.

The fear here is that if OpenAI is failing to meet internal sales and revenue goals, it may have to scale back its spending intentions. If that occurs, it'll reduce future demand for those sectors I just listed, negatively impacting their earnings growth outlooks.

To be clear, the WSJ article didn't say that's happening, but the reality is that a lot of the market, in tech and beyond, has rallied on expected earnings growth fueled by OpenAI's spending spree (among other AI companies). If OpenAI has to scale it back, it's an unexpected negative for numerous sectors, not just tech.

Bottom line, the article was a reminder that while tech has had an impressive rebound, "AI Anxiety" remains alive and well, and sooner or later, investors will need more proof that massive AI infrastructure will produce a positive ROI, otherwise we will see a repeat (or worse) of the weakness in tech as we saw in late-2025 and early 2026.

Future Market Impacts of the Fed Meeting

The net result of the Fed's decision last week was that it met market expectations and made no changes to rates or to the statement. While there was little market reaction to that result, the reality is that the stage is being set for more monetary policy volatility in the coming months, and we need to be aware of it.

For context, there were three "hawkish" dissents to the FOMC decision, with three regional Fed presidents wanting to remove the easing bias from forward guidance and instead signal to markets that the next move won't be a cut; it could be a cut or a hike. Those three dissents weren't enough to change the statement (they were outvoted at least 8-3), but they underscore two important points.

First, we should all view the Fed as being "on hold" from a policy standpoint, because while the FOMC didn't alter the statement, they likely will in the next month or two. Positively, that isn't a major problem for markets right now because it basically meets market expectations for either zero or maybe one rate cut very late in 2026. But if this hawkish trend continues, the market will have to begin pricing in a greater chance of rate hikes, and that is absolutely not priced into stocks at current levels. Bottom line, this isn't a problem yet for the markets, but it is moving in that direction, and we need to watch it (and we will).

Second, this hawkish trend at the FOMC risks creating even more division within the Fed once the more dovish Warsh becomes chair. None of us has ever seen a Fed this divided. Normally, the Fed speaks with one voice and makes unanimous decisions. This is far from that, and it's likely to get worse, as the dovish Warsh will likely clash with the more hawkish part of the Fed.

That potentially more intense conflict within the Fed isn't automatically a negative, and markets will try to focus on what the Fed does rather than what its members say. But we'd be naïve to think a Fed that could be constantly contradicting itself wouldn't be at least a peripheral negative for this market.

Practically, that would show up in higher bond yields, and the No. 1 fundamental risk we need to worry about over the coming months is higher yields negatively impacting the market multiple, earnings, and growth. That's a problem for the simple reason that it can't be addressed by policy changes (at least near term), and it risks undercutting the two core supports for this market: Economic and earnings growth.

To be clear, we are not there yet. But given divisions at the Fed, oil prices that remain very elevated, inflation metrics that were rising even before the U.S./Iran war, and general market volatility, rising yields is a real risk to watch as we move forward in 2026.

"Run-Hot" Economic Data Fuels Fed Policy Uncertainty

There were multiple economic reports last week, but three were particularly noteworthy: The Advanced Q1 GDP release, Jobless Claims, and the March Core PCE Price Index, which is the Fed's preferred measure of consumer inflation utilized for policy decisions.

While some of the details of the various releases sent mixed signals, the data revived the idea that the U.S. economy is trending towards a "run-hot" dynamic with above-target inflation, high-frequency labor data signaling the jobs market is as tight as it has been in decades, and broader economic growth trends that remain solid with consumer spending holding up better than most feared given geopolitical uncertainty emanating from the ongoing U.S.-Iran war.

The reason all of this matters is the Fed. Wednesday's FOMC meeting saw the highest number of dissents among voting FOMC members since 1992, leaving the market with limited conviction as to which direction the Fed will move policy rates in the coming months and quarters. Case in point: Fed funds futures have priced in the risk of rate hikes in 2027 (17.5% odds).

Monetary policy uncertainty, by itself, is not a bearish game changer that will derail the latest leg of this historic, respectable stock market rally. But markets prefer to have a good idea of what lies ahead, particularly about monetary policy, and the prior consensus view that the Fed is "on hold" for now, with the eventual next change to policy rates being a rate cut, *not a hike*, is poised to be challenged by the latest run-hot economy showing up in the latest "hard data" reports. And while a run-hot economy is widely preferred over either stagflation or a sudden contraction, the uncertainty around rate policy will leave the risk of relatively violent bouts of market volatility increasingly elevated as we continue to navigate 2026.

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