Market Monitor: July 2023

Markets finished the second quarter on another positive note as investors around the globe seem to be willing to maintain their risk appetite even in the face of potential interest rate increases ahead and inflation that remains stubbornly high. Stocks overcame many obstacles in the first half of 2023, but through it all, consumers continue to spend, and unemployment remains historically low. In the second half of the year, we will learn whether slowing corporate earnings growth and the specter of a looming recession predicted by many market analysts will bring the party to an early close.

2nd Quarter Highlights

- The S&P 500 Index of large U.S. companies ended the quarter up 16.9% for the year, one of the best first half performances in recent memory. Non-U.S. developed stocks rose 11.7%, as measured by the MSCI EAFE Index.
- Growth stocks, specifically technology names, continue to lead the market higher. The Vanguard Information Technology index increased over 39% for the first two quarters of 2023. Large capitalization tech names drew investor attention, and a positive surprise from AI chip vendor, NVIDIA, turbocharged the buying spree mid-quarter.
- The Bloomberg Aggregate Bond Index finished the quarter with an increase of 2.1% for the year. Bonds may be suffering from a double headwind of rising rates still to come and an increased appetite for equity risk taking among investors. Still, yields remain attractive for investors looking to position themselves for inflation to continue its slow decline.
- Shorter term bonds continue to offer higher yields than longer term bonds, a condition known as *yield curve inversion*. This situation has persisted much longer than economists would have expected and tends to be a predictor of economic recessions. 6-month Treasury bills were yielding nearly 5.5% at mid-year.
- Recession seems a ways off with unemployment at 3.7% in May and U.S. GDP still showing growth of 2.0% in the 1st quarter of 2023. Recall that the technical definition of recession involves two sequential quarters of GDP declines.

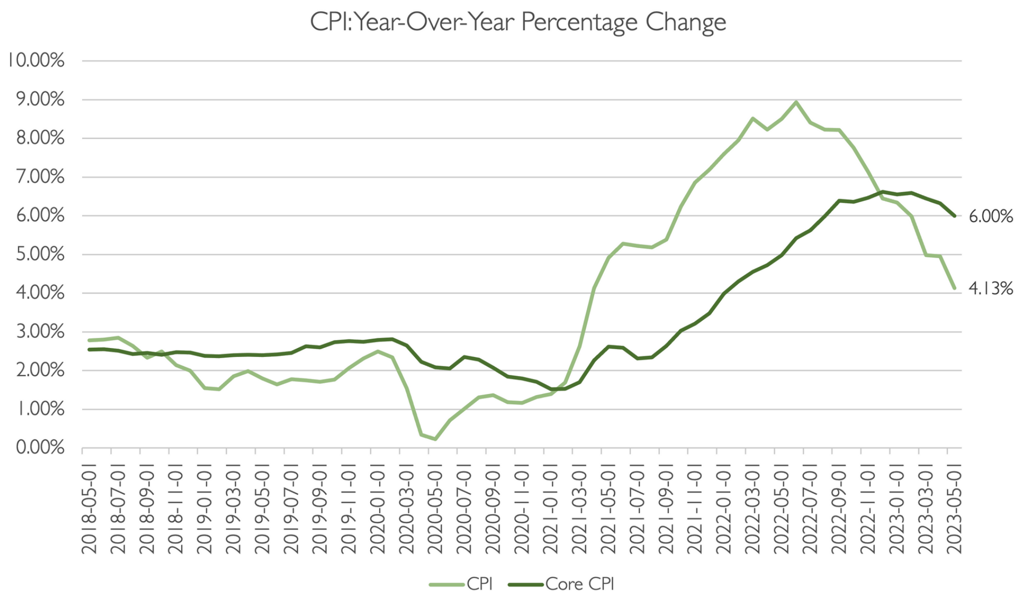
- The Consumer Price Index rose 4.1% in May compared to the prior year (see chart below). This number continues to slow with each reading. The Federal Reserve took a break from raising rates at the June meeting, but the rate increases may not be done. In the eyes of many investors, recession fears have stolen the show from the nagging worries of rising inflation.

Three Big Things

Here we review some emerging trends that may be important for investors and their portfolios. We show recent trends in the CPI, S&P 500 corporate earnings, and a bit of perspective on where we are in the current market cycle.

Consumer Price Index (CPI) Growth

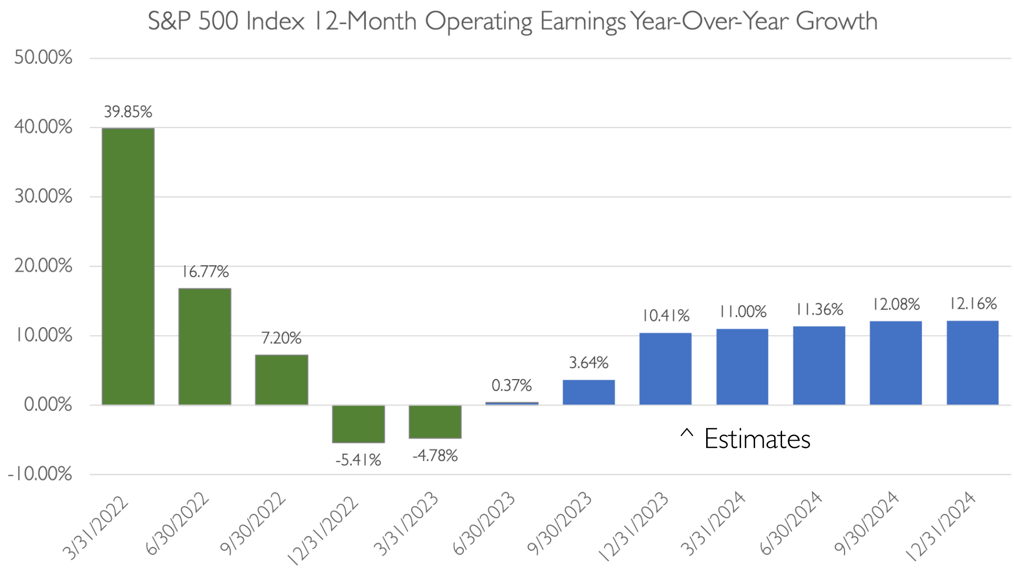
CPI growth has been slowing consistently since a 9.1% reading in July of 2022. While inflation is certainly headed in the direction of the Fed's 2.0% target, investors may wonder if the Fed has done too much in the effort to slow the economy. If so, then growth may slow significantly as time goes on. At the moment, strong consumer spending and employment trends are telling a different story.



Source: U.S. Bureau of Labor Statistics, Consumer Price Index for All Urban Consumers: All Items in U.S. City Average [CPIAUCSL], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/CPIAUCSL, July 4, 2023.

S&P 500 Corporate Earnings Growth

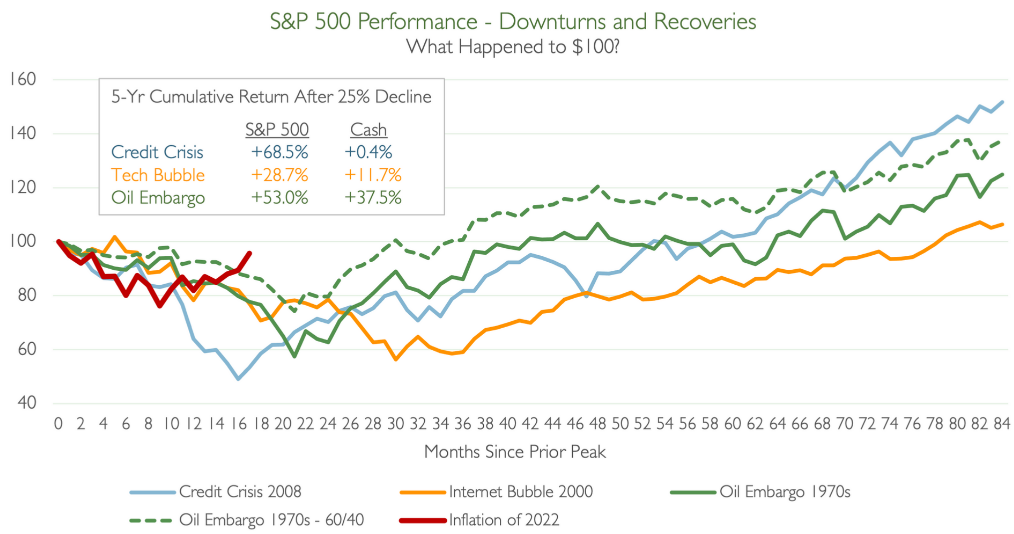
Perhaps the biggest area of debate among economists and market strategists is the future path of corporate earnings. Many estimates look like the chart below, indicating that the decline has already occurred and we are now looking at a steady recovery. But the headlines would suggest otherwise, with a wide range of expected outcomes in the analyst community. Some dire predictions assume a major decline in earnings over the next year.



Source: S&P Global, www.spglobal.com, Capital IQ Consensus

The Current Market Cycle

The chart below provides some context for how this downturn and recovery is playing out relative to others that we have seen in the past. After a significant and abrupt decline in stock performance during 2022, the market has bounced back with a vengeance. The chart tracks the path of a $100 investment starting at the peak prior to each downturn and shows the change in value over the ensuing seven years. Note that the initial downturn was steeper than others we have seen, but the recovery has also been steeper, and after 18 months, the $100 investment is now worth almost $96.



Source: Morningstar Direct. Oil Embargo 60/40 line is 60% stocks (S&P 500 Index) and 40% bonds (U.S. Intermediate Term Treasury Index). For illustrative purposes only. Past performance is no guarantee of future results.

We look forward to the opportunity to review your wealth management plan in the coming months. As always, please do not hesitate to reach out to us at any time.

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