January 23, 2023

Weekly Viewpoint

Weak Data and Hawkish Fed Commentary Weigh on the Market

Performance for Week Ending 1.20.2023

The Dow Jones Industrial Average (Dow) finished down 2.70%, the Wilshire 5000 Total Market Index[SM] (Wilshire 5000[SM]) lost 0.62%, the Standard & Poor's 500 Index (S&P 500) dipped 0.66% and the Nasdaq Composite Index (NASDAQ) tacked on 0.55%. Sector breadth was negative with 8 of the 11 S&P sector groups closing lower. The Industrials sector (-3.36%) was the worst performer followed by Utilities (-2.93%) and Consumer Staples (-2.86%). On the upside Communication Services (+2.97%) led the way followed by Energy (+0.74%) and Technology (+0.68%).

Index*	Closing Price 1/20/2023	Percentage Change for Week Ending 1/20/2023	Year-to-Date Percentage Change Through 1/20/2023
Dow	33375.49	-2.70%	+0.69%
Wilshire 5000	39585.93	-0.62%	+3.97%
S&P 500	3972.61	-0.66%	+3.47%
Nasdaq	11140.43	+0.55%	+6.44%

Market Observations: 1/16/23 – 1/20/23

After posting gains during the first two weeks of the new year, the S&P 500 finished the holiday shortened week lower on renewed concern the economy is heading toward recession. Driving the worries was a batch of mixed quarterly earnings reports and economic data signaling the economy ended last year on a weak note. The focal data report was December retail sales which showed growth fell by 1.1% on a month over month basis following a downward revision to the November data. Investors monitor the report very closely as consumer spending is a major driver of US economic growth. The housing market also remains in tatters with existing home sales, which make up most of the housing market, falling 17.8% in 2022 to their lowest level since 2014, as surging mortgage rates made home purchases too expensive for many buyers. On a bittersweet note, wholesale inflation continued to retreat but remained at very elevated levels. According to the Labor Department, the headline producer price index (PPI) fell 0.5% in December, well below the consensus forecast for a 0.1% decline. November's increase was also revised down 0.1ppts to 0.2%. Core producer prices—which exclude food and energy prices—rose

0.1%, falling out of the +0.2% to +0.3% range for first time in sixth months and notching the slowest month over month increase since March of 2021. The headline inflation fell to 6.2% on a year-over-year basis, while core inflation fell to 4.3% y/y, both the slowest pace since March of 2021.

Mixed Fed speak also added to the market's volatile trading. Fed speakers were very active last week to get their message out ahead of the pending blackout period for the upcoming (Jan. 31/Feb 1) FOMC meeting. Cleveland Fed President Loretta Mester, speaking with the Associated Press, said that while there's growing evidence that high inflation is finally easing, further rate hikes are still needed. Mester added "I still see the larger risk coming from tightening too little." Mester stressed her belief that the Fed's key rate should rise a "little bit" above the 5% to 5.25% range that policymakers have collectively projected for the end of this year. Meanwhile, speaking with the WSJ, St. Louis Fed President James Bullard said the Fed should keep rapidly raising interest rates until it gets above 5%. Fed Vice Chair Lael Brainard, speaking at the University of Chicago, said that the central bank is still "probing" for the correct level of interest rates that will both tame inflation and ensure the economy avoids recession, but added that borrowing costs are likely to remain elevated "for some time," even though she favors smaller hikes going forward. That view was echoed in part by Boston Fed President Susan Collins who suggested the Fed Funds rate could be pushed above 5% by the spring and stay there for some time. While the message from the Fed seemed pretty consistent, market forecasts, according to Bloomberg's World Interest Rate Probability tool, are suggesting rates will top out below 5%, with the possibility of a rate cut later in the latter part of the year.

Fourth Quarter Earnings: Q4 earnings season kicked off in earnest last week but will shift to high gear in the weeks ahead. As of Friday 55, members of the S&P 500 have reported results with nearly 69% surprising to the upside. Expectations heading into fourth quarter reporting season are relatively low with the full quarter results expected to show earnings for the S&P 500 contracted at just over a 3.0% year-over-year pace. While its still very early aggregate earnings for the group are currently down by 4.5%. So far, the strongest results have come from the Industrials, Energy and Consumer Discretionary sectors, whereas, Telecom and Technology have delivered the weakest results. With 284 members of the S&P scheduled to release results over the next two weeks, we are likely to get a better sense of how the overall quarter will shape up by then.

The Week Ahead: The US data calendar will be front and center in the upcoming week, with the preliminary Q4 GDP reading being a key highlight. The report follows last week's weak retail sales report that fueled growth and earnings concerns in the market. According to Bloomberg, economists expect a +2.6% annualized reading for real GDP following the +3.2% print in Q3 and a contraction of -0.6% in Q2. The other key piece of data will be the release of the December personal consumption and expenditures (PCE) data. The "core" reading of the PCE report, which excludes food and energy prices, is the Fed's preferred inflation barometer. Economists, according to Bloomberg, are expecting the December core reading to rise by 0.3% with the year-over-year rate coming in at +4.4% (down from 4.7% in November). Other notable data releases include durable goods orders, new home sales and the Chicago Fed national activity index. All will be closely watched for signs of weakness. Fourth quarter earnings season will shift into high gear with 89 members of the S&P 500 scheduled to report results this week followed by 195 members during the following week. The Fed speaking calendar will be quiet as Fed members will be in their traditional blackout period ahead of next week's FOMC meeting.

Definitions

The Dow Jones Industrial Average is a price-weighted average of 30 blue-chip stocks that are generally defined as the leaders in their industry. It has been a widely followed indicator of the stock market since October 1, 1928.

Wilshire 5000 Total Market IndexSM represents the broadest index for the U.S. equity market, measuring the performance of all U.S. equity securities with readily available price data. The index is comprised of virtually every stock that: the firm's headquarters are based in the U.S.; the stock is actively traded on a U.S. exchange; the stock has widely available pricing information (this disqualifies bulletin board or over-the-counter stocks). The index is market cap weighted, meaning that the firms with the highest market value account for a larger portion of the index.

Standard and Poor's 500 Index is a capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The Nasdaq Composite Index is a broad-based capitalization-weighted index of stocks in all three NASDAQ tiers: Global Select, Global Market and Capital Market. The index was developed with a base level of 100 as of February 5, 1971.