July 22, 2019

Weekly Viewpoint

Stocks take a Breather as they Await the Fed Decision

Performance for Week Ending 7.19.19

The Dow Jones Industrial Average (Dow) lost 0.65%, the Wilshire 5000 Total Market Index℠ (Wilshire 5000℠) fell 1.21%, the Standard & Poor's 500 Index (S&P 500) dipped 1.23% and the Nasdaq Composite Index (NASDAQ) shed 1.18%. Sector breadth was negative with 9 of the 11 S&P sector groups finishing lower. The Communication Services sector (-3.06%) was the worst performer followed by Energy (-2.70%) and Real Estate (-2.29%).

Index*	Closing Price 7/19/2019	Percentage Change for Week Ending 7/19/2019	Year-to-Date Percentage Change Through 7/19/2019
Dow	27154.20	-0.65%	+16.40%
Wilshire 5000	30608.71	-1.21%	+18.87%
S&P 500	2976.61	-1.23%	+18.74%
Nasdaq	8146.49	-1.18%	+22.78%

Market Observations: 7/8/19–7/12/19

The major market indices finished the week modestly lower as optimism around the prospects for looser monetary policy was offset by the spotty start to second quarter earnings season and signs the US/China trade talks are making little progress. The Energy sector sharply underperformed the broader market reflecting a sharp pullback in the price of oil. Oil fell by nearly 7%, its worst weekly decline since late-May, on signs of building inventory levels and weakening demand.

Economic Data Solid … Economic reports out of the manufacturing sector this week suggest the recent swoon may prove temporary. Of note, the Fed's regional manufacturing survey from the Philadelphia region came in much stronger than anticipated and the highest level this year. The strong report followed a rebound in the New York regional manufacturing index. Elsewhere, the closely watched monthly retail sales report also surprised to the upside. According to the Commerce Department, retail sales during the month of June rose by a better than expected 0.4%, exceeding economists' expectations of a 0.2% gain. Retail Sales ex-Autos jumped by 0.7%, also well ahead of forecasts. With almost two-thirds of domestic economic growth coming from consumer spending, the report suggests that consumers remain optimistic likely due to the tight labor market conditions.

… But is Good News, Bad News? With expectations of Fed rate cuts at very elevated levels, a big risk for the market is that the Fed policy underwhelms. During the week, NY Fed President Williams said that central banks should take swift action once there are signs of economic distress. Following the comments, markets began to price in a more aggressive cut at this months Fed meeting. In a very unusual move, the NY Fed actually attempted to walk-back the comment from Williams, noting that the speech should be viewed as an academic discussion and not a signal of near-term policy. Meanwhile, St. Louis Fed President Bullard said in an interview he would support a quarter point rate cut but doesn't think anything larger is needed at this time. While a quarter point reduction in rates now seems like all but a done deal, the market is currently placing increased odds that a half-point reduction in rates could occur. The latter bet, however, seems at odds with the recent rebound in June payrolls, the budding recovery in regional manufacturing, and the stronger than expected reading on retail sales.

Q2 Earnings Season – Early but Mildly Better: Despite a few high-profile earnings misses, overall second quarter earnings season is off to a mostly better than feared start. While still early (only 77 of the 500 companies have reported as of Friday), the initial results have been mildly encouraging. Of the companies that have released results, nearly 78 percent have met or exceeded expectations with the aggregate upside surprise at nearly 5 percent. As expected, earnings growth has been weak (aggregate growth is up only 2.1 percent), but still better than the feared 1.9 percent decline forecast by FactSet Research. Revenues are posting aggregate growth of 2.6 percent. We should get a better handle on the overall quarter over the coming two weeks as nearly 300 companies are scheduled to release results.

Market View: In light of the strong year-to-date gains, the ongoing uncertainty surrounding the trade spat with China, and signs the global economy is slowing, we have tempered our near-term outlook for risk assets. We are not bearish on the equity market, but with the S&P 500 recently reaching a new all-time high, the overall risk/reward outlook has now become less compelling. In the near-term, market price seems to have outdistanced underlying fundamentals as the strong year-to-date performance has resulted solely from the expansion in the market's P/E multiple. This scenario could leave the market vulnerable to earnings disappointment or negative developments in trade. Earnings growth will be the key driver of forward performance and until revisions begin to move higher, upside from current levels will likely be limited. Better buying opportunities will likely emerge down the road, but now is not the time to be chasing the market higher.

The Week Ahead: Q2 earnings season will begin to hit full stride with nearly 140 members of the S&P 500 scheduled to report. Amongst this group are ten members of the Dow Average. Data reports of interest include; June existing home sales, June new home sales, June durable goods orders and the first estimate of second-quarter GDP. The Fed speaking calendar is nonexistent this week reflecting the traditional blackout period ahead of the scheduled Federal Open Market Committee (FOMC) meeting on July 30 &31.

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.