June 6, 2022

# Weekly Viewpoint

## Jobs Data Keeps Fed on Track for a June Hike

### Performance for Week Ending 6.3.2022

The Dow Jones Industrial Average (Dow) finished down 0.94%, the Wilshire 5000 Total Market Index℠ (Wilshire 5000℠) fell 1.08%, the Standard & Poor's 500 Index (S&P 500) slumped 1.20% and the Nasdaq Composite Index (NASDAQ) closed off 0.98%. Sector breadth was negative with 8 of the 11 S&P sector groups closing lower. The Healthcare sector (-3.14%) was the worst performer followed by Real Estate (-2.23%) and Financials (-2.14%). On the upside, Energy (+1.18%) was the best performer followed by Industrials (+0.04%) and Consumer Discretionary (+0.01%).

| Index* | Closing Price 6/3/2022 | Percentage Change for Week Ending 6/3/2022 | Year-to-Date Percentage Change Through 6/3/2022 |
|---|---|---|---|
| **Dow** | 32899.70 | -0.94% | -9.46% |
| **Wilshire 5000** | 40945.40 | -1.08% | -15.51% |
| **S&P 500** | 4108.54 | -1.20% | -13.80% |
| **Nasdaq** | 12012.73 | -0.98% | 23.22% |

### Market Observations: 5/30/22 – 6/3/22

The major market indices finished the holiday shortened week lower as solid jobs data and hawkish commentary from Fed officials reinforced expectations of aggressive tightening of monetary policy. Strong job growth gives the Federal Reserve more runway to continue hiking interest rates in order to address hot inflation. Sentiment was also hurt by a report that Tesla's Elon Musk may be considering job cuts on worries over the economic outlook. Musk's uncertainties followed comments earlier in the week from J.P. Morgan's Jamie Dimon, who said he foresees an economic "hurricane" ahead from the war in Ukraine and the Fed's tightening policies.

**Payroll Report:** The Labor Department reported that nonfarm payrolls during May rose by a better than anticipated 390K, suggesting that the economy remains in good shape. The strength in payrolls was widespread, with solid gains in professional & business services employment (+75K), leisure & hospitality (+84K), as well as a decent 36K gain in construction payrolls and an 18K rise in manufacturing payrolls. The one weak spot was retail, where employment fell by 61K, with losses concentrated in the big general merchandise stores, reflecting the recent struggles at Walmart and Target. The unemployment rate was unchanged at 3.6%. Amid signs that labor shortages are easing, average hourly earnings rose by a relatively muted (at least by recent standards) 0.3% in May for a second month running, bringing the annual rate down to 5.2% from 5.5%. The deceleration in wage growth is encouraging because it suggests that the broader cyclical price pressures in the economy may be close to peaking. However it will take a further slowdown in annual wage growth before the Fed can claim it is making significant progress towards its inflation goal. As such, the report supports the Fed raising the fed funds rate by 50bps at each of its June and July meetings.

**Pause Not Likely:** Last week Fed Vice Chair Lael Brainard said expectations for half-percentage-point increases in interest rates this month and next were reasonable, and saw no case for pausing the central bank's tightening campaign afterward. "From where I sit today, market pricing for 50 basis points, potentially in June and July, from the data we have in hand today, seems like a reasonable path," Brainard said in an interview with CNBC. "Right now it's very hard to see the case for a pause. We've still got a lot of work to do to get inflation down to our 2% target." Meanwhile, Cleveland Fed President Loretta Mester said she favors raising interest rates by 50 basis points this month and next but cautioned that pace could speed up or slowdown from September, based on what happens with inflation. "If by the September FOMC meeting, the monthly readings on inflation provide compelling evidence that inflation is moving down, then the pace of rate increases could slow," Mester said, adding that "if inflation has failed to moderate, then a faster pace of rate increases could be necessary."

**Q1 Earnings – It's a Wrap:** First quarter earnings has come to an end and results ended up better than feared with nearly 76% of the S&P 500 companies beating expectations. Aggregate earnings growth for the quarter rose by 9.5% on a year-over-year basis, solidly better than the 5.7% pace that analysts were forecasting at the start of April. On the sector level, nine of the eleven of the S&P sector groups have delivered positive growth with the strongest gains coming from cyclical sectors like Energy, Industrials and Materials. On the weak side, Consumer Discretionary and Financials saw year-over-year growth fall.

**Tale of Two Halves?** While the near-term outlook for the markets will remain clouded by the situation in Ukraine, elevated levels of inflation and concerns over the Federal Reserve's response to inflation, we think as we move forward fundamentals will ultimately outweigh fears. The US economy remains in good shape and the probability of a recession in the coming quarters remains low. Consumer balance sheets are strong and net worth is near all-time highs. Money market mutual have over $4.5 trillion in cash and corporate buyback activity is expected to remain strong. Supply chain issues have also started to ease. Importantly, the earnings environment remains solid with high single digit growth expect this year and next. If there has been a silver lining to the recent market weakness, it's been that valuation levels have moved lower with the S&P selling for just over 16x the 2023 estimate and 15x the 2024 estimates. While still not a cheap market, it is much less expensive than we've seen in recent years.

**The Week Ahead:** Inflation data will be front and center with the May Consumer Price Index report due out on

Friday. According to Bloomberg, headline inflation is expected to rise by 0.7% for the month and by 8.3% on a year-over-year basis. Other data reports of interest include: the April trade balance, wholesale inventories during April, initial jobless claims, and the University of Michigan consumer sentiment data. The Fed speaking calendar will be nonexistent reflecting the blackout period ahead of the June 14 & 15 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 Index**SM 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.



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