Week in Review

Equity Markets:

The NASDAQ and S&P 500 continued their climbs to new record highs last week. The S&P 500 ended the week up 1.6% while the NASDAQ finished up by 3.3%. Large Cap Growth continues to outpace its value counterpart. The Russell 1000 Growth finished the week up 3.48% and the value index fell 1.11% as investors piled into the technology sector[1]. Small caps further lagged the broader last week ending down 0.95% and bringing its year-to-date performance to -0.4%.

The market has shifted its focus to the start of next quarter's earnings. The estimated second-quarter earnings growth rate for the S&P 500 is 9%[2]. If companies continue the string of surprises and meet expectations it would mark the highest quarterly growth rate since the first quarter of 2022. The number of companies issuing negative guidance for the quarter sits at 67 and 44 have issued positive earnings guidance. These numbers are an improvement from prior quarters and could point to another strong quarter for earnings results.

Fixed Income Markets:

For the seventh consecutive meeting, the Federal Reserve left the benchmark unchanged from the current level of 5.25-5.5%. Policymakers remained dovish, and despite improving inflation the dot plot indicated members of the committee expect only one cut this year, but increased the expectations for 2025 from three cuts to four[3]. Market participants still see at least two cuts this year as the Fed Fund's Futures market is pricing in a 62% probability[4].

The bond market saw a second week of significant moves. The 10-year Treasury Yield closed the week at 4.2%, down from the prior week's close of 4.43%. The 2-year Treasury Yield fell 0.2% and closed the week at 4.67%. Despite the recent decline in rates, the 2's/10's spread has remained near the same level as the path has been a parallel shift down in the yield curve.

Economic:

Inflation remains above the two percent target of the Federal Reserve, but the CPI was flat for the month of May. On an annual basis, CPI increased 3.3%. Economists were anticipating a 0.1% monthly increase and a 3.4% annual increase. Core CPI, which excludes food and energy, rose 0.2% in May which was slightly below the estimates of 0.3%. The index rose 3.4% relative to the prior year, which also came in slightly better than the expected 3.5%. The PPI report showed a reversal in prices as the headline reading fell 0.2% in May. The PPI reading is considered to be a leading indicator for the direction of inflation. Consumer sentiment fell through the first half of May. The preliminary reading of the University of Michigan Consumer Sentiment Index fell to 65.6. Economists had forecast a reading of 72. Consumers cited concerns about the continued high interest rate environment, inflation, and weakening incomes. The weekly unemployment claims report saw initial claims of 242,000.

Looking Ahead

Equity Markets:

The recent rally in the market can be attributed to only a handful of names as breadth has continued to be weak. With the market trading at 21.4x forward four quarter earnings[5], narrow breadth could be a tailwind for the market. If the economy remains strong and conditions loosen it could push the market even higher through the end of the year. We believe the lack of market breadth has increased the risk of near-term volatility and the potential for a market pullback. With a small portion of components driving the majority of the market returns, if earnings results miss expectations it could lead to downside.

We have experienced very little volatility this year and we believe this will not be the trend for the remainder of the year. As we move closer to elections, the uncertainty regarding rate cuts, and what we believe to be a very optimistically priced market investors should take a deep look at their current exposures to ensure they do not have more risk exposure than desired.

Fixed Income Market

Unlike the equity markets, the fixed-income markets have experienced their fair share of volatility this year. To start the year, the 10-year Treasury Yield was 3.88%, briefly touched 4.7% in April and is back in the 4.2% range. However, we believe the volatility in the fixed-income markets will settle as we believe the 10-year yield will be ranged bound in the 4.25-4.5% level until later in the year. It is our opinion that the 5% yield that occurred in October of last year is the peak yield for the current cycle, but to a sign, a larger move down in yields will require the Fed to cut rates. As of now, that appears to be in the fourth quarter and is a significant driver for range-bound view of the bond market.

Economic:

Following the surprise drop in consumer sentiment, Tuesday's Retail Sales report will provide a more robust picture of the current consumer. The highlight for the week will be the housing market. The Housing Market Index will be released on Wednesday, followed by housing starts on Thursday, and Existing Home Sales will close the week on Friday. Also being released on Friday will be The Conference Board's Leading Economic Index.

**** *See Important Disclosures on the following page*

Sources:

1)JP Morgan
https://am.jpmorgan.com/content/dam/jpm-am-aem/americas/us/en/insights/market-insights/wmr/weekly_market_recap.pdf

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4) CME Group
https://www.cmegroup.com/markets/interest-rates/cme-fedwatch-tool.html

5) LSEG I/B/E/S
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