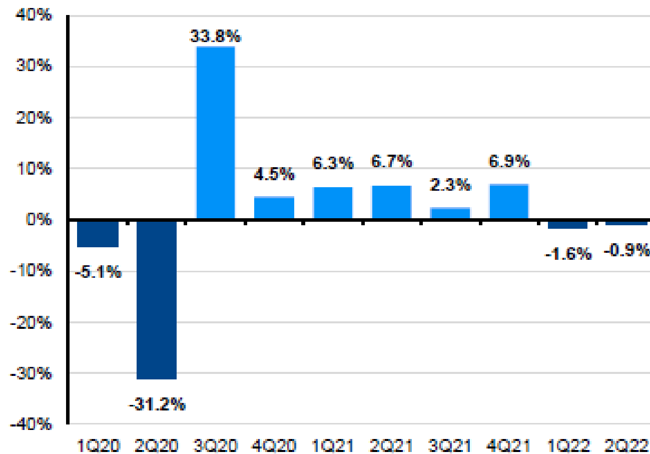
Monday, August 1, 2022

Good afternoon:

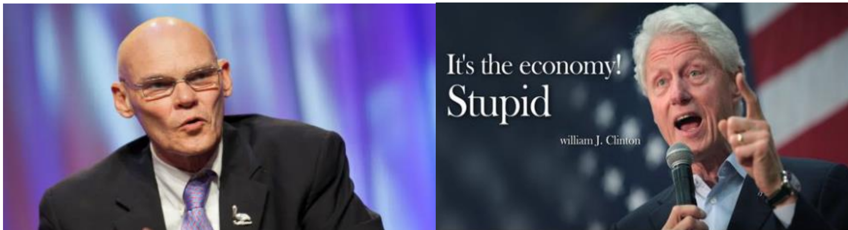
Major stock indices closed out July with another week of solid gains of nearly 3-4¾% amidst a bevy of market-moving earnings and economic data announcements. Investors rewarded several major tech stocks that reported better than expected Q2 results, while punishing those that missed their targets. Meanwhile, the Fed raised rates another 0.75%, which was widely anticipated, in their efforts to curb inflation.

Perhaps grabbing the spotlight from all of these significant reports last week was the confirmation of what most people already knew. The U.S. economy declined for the second quarter in a row with real GDP being reported at -0.9% for Q2. Ahead of this report, a concerted effort was initiated to frame the impending negative result as something other than the long-standing and fairly simple definition of a recession (two or more consecutive quarters of negative GDP). The counterargument is that last month's strong jobs figures, coupled with positive personal incomes, consumption, and industrial production do not *currently* resemble conditions traditionally seen during a recession. After further data is analyzed and additional time has passed, historians will determine whether this the start of a "real" recession or not.



From our perspective, the slowdown is clear, regardless of semantics. Although some of the impact may be delayed, particularly in the data, it is obvious that the consequences of high inflation, and the Fed's response to it by raising borrowing costs, are having a dampening effect on the economy. And while we believe the Fed will continue with its plan to continue to hike rates for the next year or so, it's worth noting that the bond market is currently pricing in rate *cuts* by the Fed after that in two years.

We should also recognize that like most things these days, politics may be having an impact on how the economy is perceived and described. It's really nothing new, though. Thirty years ago in 1992, Governor Bill Clinton's campaign strategist for President James Carville was famously quoted as saying, "It's the economy, stupid!" With midterm elections coming up this fall, expect such sentiments and slogans once again.



Despite the market's strong bounce in July, we remain cautious for the next few months. The historically higher volatility months of August and September (often due to lower volume) may again prove challenging. One potential catalyst to a move in the market in *either* direction will be the next two CPI reports. If inflation starts to moderate in the wake of declining energy and commodity prices, traders will have further justification to buy. However, if it stays at current levels, or goes higher, it could mean the Fed will need to be even more aggressive, likely prompting a retreat from recent equity levels.

It is important to stay focused on longer-term objectives and strategies during periods of volatility and uncertainty.

Have a great week!

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Market return and statistical data obtained from: https://am.jpmorgan.com/blob-gim/1383452890099/83456/weekly_market_recap.pdf?segment=AMERICAS_US_ADV&locale=en_US
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