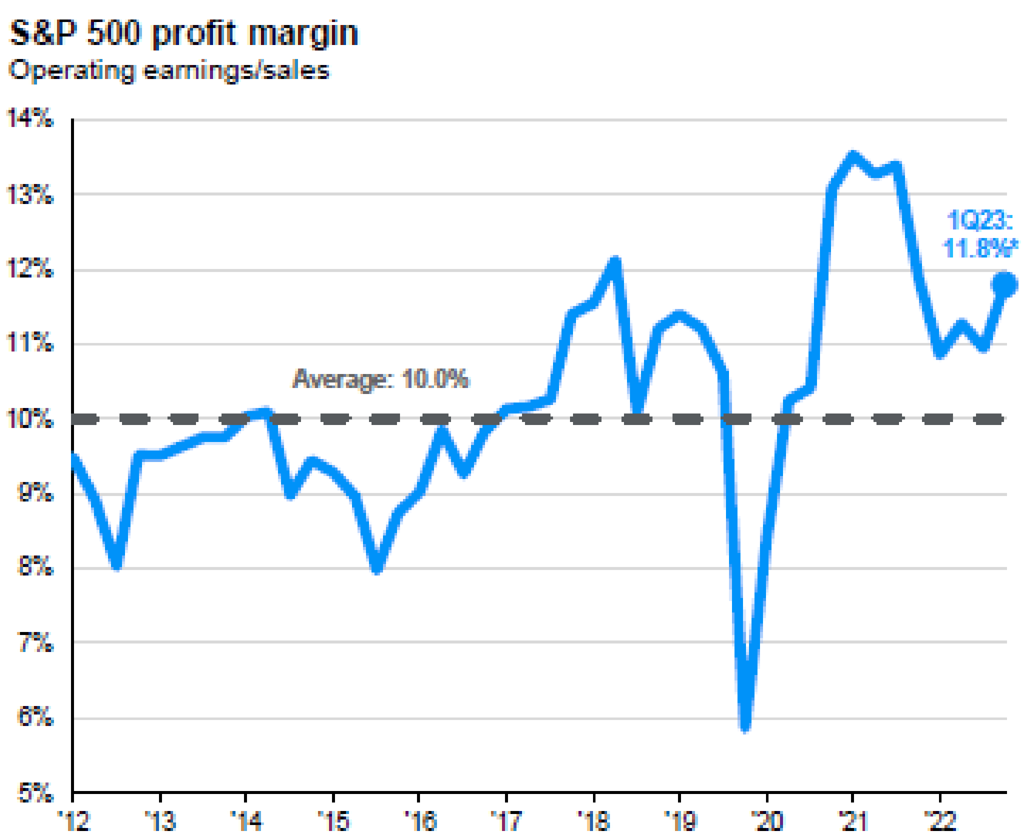
Monday, May 22, 2023

Good afternoon:

Stocks were mixed last week with this year's strongest sectors again leading the way higher. S&P 500 added 1.71% while Technology, Communications Services, and Consumer Discretion sectors helped the NASDAQ gain 3.08% on the week. Despite slower economic growth, 1Q23 S&P 500 earnings have surprised to the upside as economic momentum at the beginning of the year supported an expansion in profit margins. With over 90% of the S&P 500's market cap having reported, profit margins currently stand at 11.8%, a level of profitability that had only been eclipsed once in the pre-pandemic period.



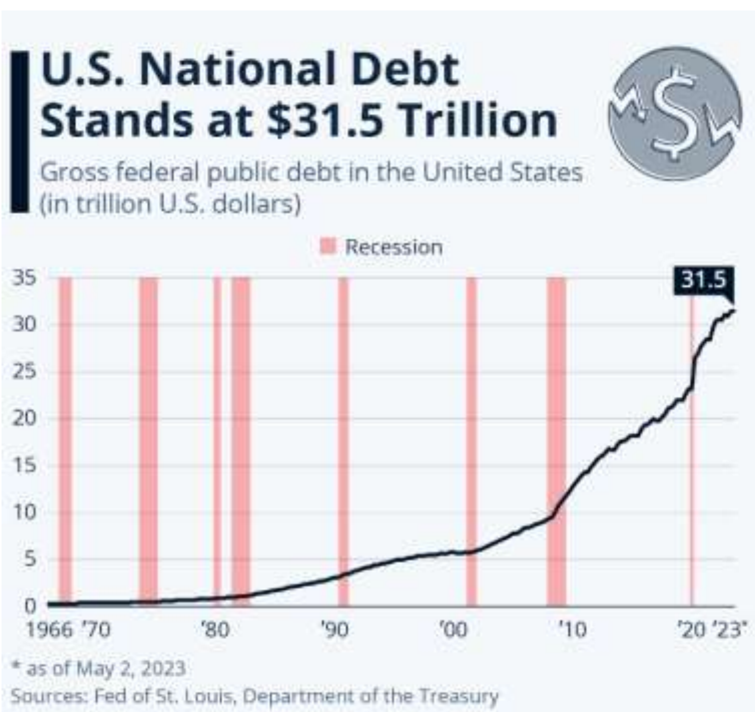
Source: J.P. Morgan Asset Management

Much of these better than anticipated results can still be attributed to strong and resilient consumer demand. Household spending comprises more than two-thirds of U.S. GDP, so the health of the economy is largely dictated by the combination of consumers' income and attitude. While the two are connected, they are not always in sync. This seems to be the case currently, with disposable personal income rising significantly this year while the Consumer Confidence Index has declined year-to-date. With the widely anticipated economic slowdown on the near-term horizon, recent banking turmoil, and pervasive high inflation, it may be reasonable to expect some reduction in consumer spending as well.

Source: FactSet

With remaining post-pandemic pent-up consumer demand, particularly for services like travel and entertainment, the forthcoming economic contraction may not look or feel like past recessions. It may turn out to resemble 2001 where the downturn was fueled by a drop in business spending. Meanwhile, consumer spending pulled back but not materially, helped by little damage to the strong labor market. The result was a short and shallow recession.

In the interim, markets are still anxiously awaiting a resolution to the debt ceiling debate in Washington. While most realize that a default is an unthinkable outcome that will almost certainly be ultimately avoided, the longer these negotiations take, the more we are likely to experience heightened volatility.



If we do see a more definitive recession this year, it will likely result in a return to favor of Value stocks, while this year's winning tech trades give back some of their recent outsized gains. Consumer staples, healthcare, and utility sectors are often shown to be outperformers during recessionary periods due to their more stable businesses, lower valuations, and generally higher dividend yields. Our strategy for long-term investment success is to take a diversified approach to investing in the asset class of equities, allocating capital to both growth *and* value sectors with a strong bias towards high-quality companies and asset managers. This has enabled us to help our clients successfully navigate through all kinds of varying market and economic climates on their way to achieving their investment and financial planning goals.

Have a great week!

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