MARKET COMMENTARY

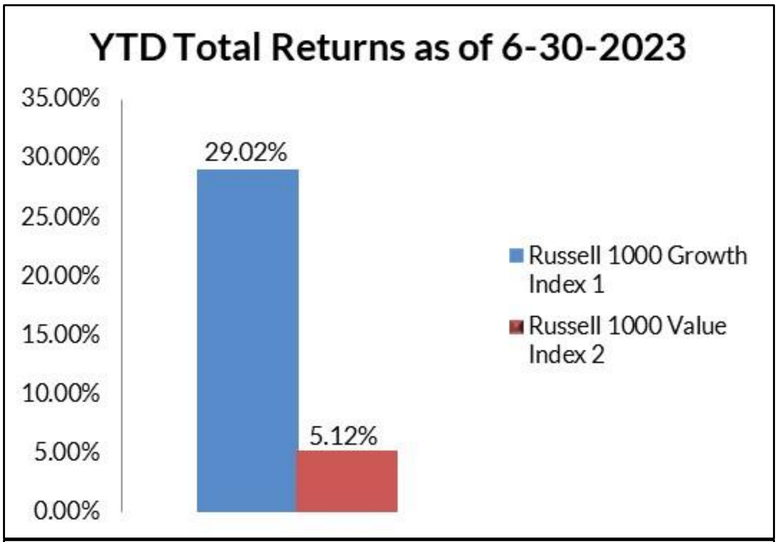
Q2 2023 COMMENTARY

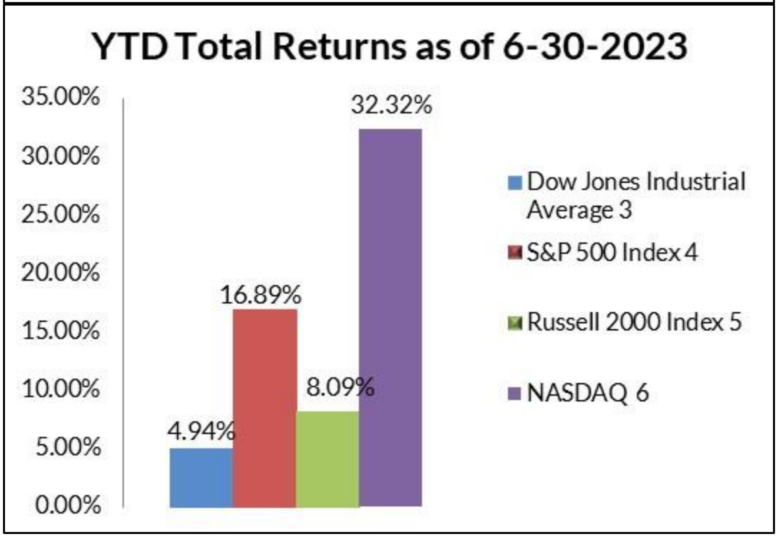
Economic Summary

It seems like a U.S. recession has been anticipated for years now, with pundits espousing various datapoints, while the yield curve has remained steeply inverted. The continued rise in interest rates leads us to believe that inflation will be stickier than most are anticipating. Additionally, the strong stock market performance seems to diminish the likelihood of a serious recession on the horizon.

The Stock Market

It's no secret that money creation by the Federal Reserve (the Fed) as well as the profligate fiscal policy of the Biden administration has produced an enormous quantity of cash in the system. Estimated at $6 trillion or more, it's likely that some of those dollars will find their way into the stock market which may further boost stock prices. Add in corporate balance sheets which are currently stuffed with liquidity, and the possibility of large stock buybacks could provide reasons to believe that the current bull market has legs. 2023 has been a banner six-month period for large-cap technology and growth stocks as the Russell 1000® Growth Index has outperformed the Russell 1000® Value Index by 24% (Chart 1). The technology and mega-cap heavy NASDAQ Composite has nearly doubled the return of the S&P 500® year-to-date (Chart 2).





Charts 1 & 2
Source: Morningstar Direct

[1]The Russell 1000® Growth Index measures the performance of the large-cap growth segment of the U.S. equity universe. It includes those Russell 1000® companies with higher price-to-book ratios and higher forecasted growth values. [2]The Russell 1000® Value Index Measures the performance of the large-cap value segment of the U.S. equity universe. It includes those Russell 1000® companies with lower price-to-book ratios and lower expected growth values. [3]The Dow Jones Industrial Average is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the NASDAQ. [4]The S&P 500® Index is a capitalization weighted unmanaged index of 500 widely traded stocks, created by Standard & Poor's. The index is considered to represent the performance of the stock market in general. [5]The Russell 2000® Index is an unmanaged index of the smallest 2,000 stocks in the Russell 3000® Index. [6]The NASDAQ Composite is a stock market index that includes almost all stocks listed on the Nasdaq stock exchange (more than 2500 stocks). You cannot invest directly in an index.
Past performance does not guarantee future results.

The Stock Market (continued)

Of note, roughly 80% of the NASDAQ's performance was driven by only eight stocks, and those eight stocks made up nearly 50% of the Index market value at quarter-end. Value indexes were impaired by their underweighting of Technology and Consumer Discretionary stocks which were up 49% and 40%, respectively, in the Russell 1000® Growth Index year-to-date.

Analysts are expecting corporate earnings in the S&P 500® to decline -7.2% in the second quarter, down from -4.2% forecasted at the end of March. From a historical perspective, the S&P 500® forward P/E ratio is 18.9, in line with the 5-year average and over one turn above the 10-year average. Corporate earnings, and more specifically the outlook will likely be the driver of market movements in the next few months.

The Bond Market

The 10-year U.S. Treasury Note marched higher during the quarter as the market ingested macro-economic data and rhetoric from the Fed. Ultimately, the 10-year finished the second quarter at 3.8%, up from where it started the quarter at 3.5%. Yields in the short-to-intermediate portion of the yield curve increased more than the Fed Fund's rate. This indicates the market is expecting higher interest rates for longer. The Fed continues its quest to tame inflation, as the economy remains stronger than expected. While inflation has come down, it was reported at 4%, which is twice the Fed's 2% target.

Corporate credit spreads tightened modestly during the first half of the year as investors were more optimistic about the economic landscape. Currently, spreads are right near historical averages (Chart 3), making this a reasonable time to add exposure to select corporate credits in our view.

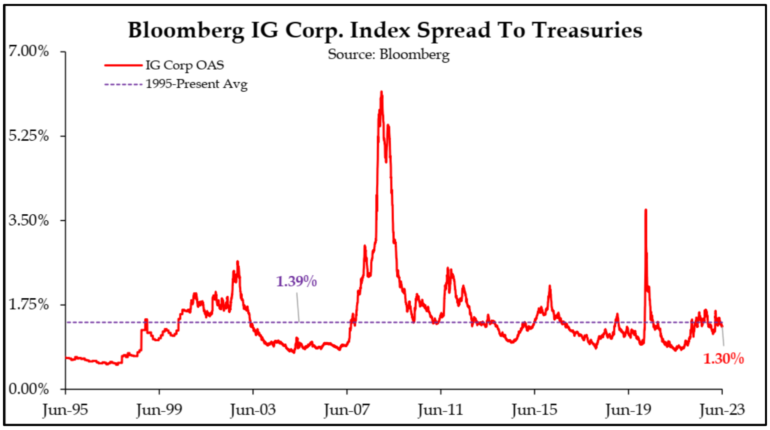


Chart 3

Source: Strategas Research Partners, "Quarterly Review in Charts", 7/5/23

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