Summary

Economic data for the week included the FOMC meeting ending in no action, as expected, with dovish undertones at the press conference. Both ISM manufacturing and services fell back into contraction, while the employment situation report came in weaker than expected. Home prices continued their stretch of gains by several measures.

Stocks gained ground globally last week, with strong corporate earnings, but also weaker economic data that pointed to interest rates eventually dropping down the road. Bonds fared positively along with lower yields. Commodities fell back sharply, as oil prices declined for a variety of market and geopolitical reasons.

Economic Notes

(0) The **FOMC meeting** ended with the expected no action. However, market (and Fed) expectations have shifted noticeably over the past few months, from a possible ease this summer to perhaps one cut at most the rest of this year. In fact, fears of even another hike bubbled to the surface, with a sentence added to the formal statement noting the lack of progress made toward lowering inflation, which could be taken hawkishly at first glance. Though, at the press conference, Fed Chair Powell took on a much more dovish tone, calming markets by confirming that another rate at this stage was “unlikely.” He further elaborated that such a decision to hike down the road, if necessary, would be based on the “totality” of a variety of measures, if they didn’t show sufficient tightness—but current conditions certainly don’t warrant that, as he “did not see signs of reheating.” (The stock market cheered the response immediately by turning around and rising over a percent, before reversing again later.) In response to questions, he also noted that policy is currently “well-positioned,” appears balanced, given what looks to be a probability-based analysis of the “different paths the economy might take.” He did pull back on putting a timeline on cuts, which was also no surprise. He added an almost-flippant contextual answer in response to rising worries over a stagflation scenario—noting that today’s environment obviously looks far different than the comparative to the 1970s that featured double-digit percentage levels in both inflation and unemployment.

The only political mention during the presser was a reminder that the Fed does not take elections or their timing into consideration at all for policy decisions. There has been concern in the background, based on comments from a few political strategists about the possibility of amending the Fed’s rules to allow future Presidents to have greater influence on interest rate policy. The prospect of something like this is very unpopular in the economic community, as it no doubt introduces non-economic influences into a fairly quantitatively-based monetary process. No doubt, like their constituents, politicians all seek long regimes of strong economic growth and high employment—both of which could point to a perpetual bias toward lower interest rates. At the same time, voters also dislike high prices, which can be a byproduct of too-high growth, leading to the need of a correctional upward bias if inflation remains too high. As with all interest rate matters, there is no policy magic bullet, but if additional considerations are included in rate policy, greater yield volatility in the system could result. Another issue at play is that a Fed chair can be fired only ‘for cause,’ as opposed to for political or personal reasons. Chair Powell’s term is up in 2026, with apparent reluctance by either Presidential candidate to discuss a reappointment, even if he did want to stay in the job, as opposed to declaring victory over inflation for the most part and gracefully exit. So, this could be a moot point. Down the road, focus would turn to possible replacements, and the potential dovishness or hawkishness of respective new chairs.

(-) The **ISM manufacturing index** fell by -1.1 points in April to 49.2, reversing back into a slight contraction, and below the median expectation of a 50.0 neutral reading. The report was fairly balanced, with half of the industries reporting expansion, and most of the other half in contraction, with a handful at neutral. According to the report, new orders fell by several points back into contraction, although it’s been in that condition for much of the past two years. On the other hand, employment improved by over a point, but stayed in contraction. Supplier deliveries also fell back, while prices paid rose 5 points to a stronger expansionary level of 61. It was noted anecdotally that the order backlogs, which have been shrinking and reflect weaker demand for manufactured items, should continue to boost activity for the next six months or so at least. Overall, the foray into expansion for a month was short-lived, although the minor differences from month to month lately are generally within the 'neutral' range, pointing to neither sharp slowdown nor stronger expansion.

(-) The **ISM services/non-manufacturing index** fell -2.0 points in April to 49.4, below expectations calling for a minor increase to 52.0. This represented a reversal from light expansion back into contraction, for the first time since a brief stint at year-end 2022, and before that, during early 2020 during the early pandemic period. However, underlying data was mixed with two-thirds of industries still showing expansion, with the other third in contraction. New orders fell -2 points but remained in expansion, while employment fell a few points further into contraction. Business activity fell sharply but landed just above the neutral 50 level. Prices paid ticked up sharply also, ending near a solidly-expanding 60 level. This shows signs of slowing in the largest segment of the economy that has been in expansion solidly for years, but future reports will be required to see if this persists into an extended trend lower.

(-) **Construction spending** declined -0.2% in March, a tenth of a percent below expectations, and included a revision upward to flat for Feb. and negative for Jan., which appear to cancel each other out. Private residential spending declined by the greatest degree, which offset gains on the public construction side in both residential and non-residential. Construction costs also rose in March by several tenths, pushing 'real' spending even further negative.

(+) The **S&P Case-Shiller 20-city home price index** rose 0.6% in February, beating expectations of only a 0.1% rise. Prices rose in all but one of the 20 urban centers, led by gains of at least a percent in Seattle, Chicago, and New York, while Tampa saw a decline. The year-over-year rate of increase nationally reaccelerated by 0.7% to 7.3%, to another new all-time high plateau.

(+) The **FHFA home price index** for February rose an even sharper 1.2%, exceeding the 0.1% expected. The single-month results by region were led by a 3% rise in New England (from CT north), while West South Central (OK south to LA) rose 0.4%. The national year-over-year rate of increase reaccelerated in this index as well, from 6.5% to 7.0%, led by 11% in the Mid Atlantic. The FHFA is a more comprehensive data series, including fewer urban regions, but showing a similar pace of strength reasserting itself over the past year in an environment of meager housing supply.

(-) The Conference Board's **index of consumer confidence** fell -6.1 points in April to a level of 97.0, well below the expected increase to 104.0. This was the lowest level in two years, with assessments of the current situation down but even further in expectations for the future. The labor differential also fell back, with jobs slightly less plentiful and a bit harder to get. Based on respondent opinions, the perceived likelihood of a recession in the next year ticked up a percent to 66%—staying sharply higher than predictions from institutional economists.

(0) **Initial jobless claims** for the Apr. 27 ending week were unchanged at 208k, just below the 211k forecast. Continuing claims for the Apr. 20 week were also strangely unchanged at 1.774 mil., below the 1.790 mil. expected. This was about as uneventful as it can get, although some layoffs have been announced in selected sectors, such as tech and communications, which could eventually filter through to claims.

(-) The **JOLTS** job openings report for March saw a decline of -325k to 8.488 mil., below the median forecast of 8.680 mil. openings. By industry, gains were seen in information (+43k), government (+39k), and leisure and hospitality (+10k), while the largest drops were in construction (-182k), financial (-144k), and professional/business services (-41k). The job openings rate fell by -0.2% to 5.1%, along with a similar -0.2% decline in the hiring rate to 3.5%; on the departure side, the layoff rate fell a tenth to 1.0%, as did the quits rate to 2.1%. A decline in

(-) The employment situation report for April came in a bit weaker than expected, which is never desired from a labor market standpoint, but was cheered by markets wanting some signs that the conditions aren't reaccelerating further into re-inflationary territory. **Nonfarm payrolls** came in at 175k, well below the 240k expected by consensus, which included -22k in revisions for the prior two months. It also fell below the trailing 12-month trend level of roughly 240k. By segment, gains were strongest in health care (56k, mostly health services), social assistance (31k), transportation/warehousing (22k), as well as retail (20k). On the more lackluster side were construction (9k), manufacturing (8k), government (8k), and leisure/hospitality (5k), while information jobs lost ground (-8k).

The **unemployment rate** ticked up again by a tenth to 3.9%, versus expectations of no change, and no change in the labor force participation rate, with the household survey showing gains of 87k. The U-6 underemployment rate also rose a tenth to 7.4%. Based on some common rules of thumb, the unemployment rate remains above the 12-month moving average, but has not yet triggered the 'Sahm Rule,' based on a similar recency metric relative to the past year. So, signs remain mixed, as we've become used to. **Average hourly earnings** rose 0.2%, decelerating a tenth from the prior month as well as expectations of 0.3%. Year-over-year earnings decelerated by -0.2% to 3.9%, confirming some easing in inflationary wage pressures. **Average weekly hours** also fell a tenth to 34.3.

Before that report, nonfarm **productivity** for Q1 was released, showing a rise of only 0.3% on an annualized basis, below the 0.5% expected and well below the prior quarter's 3.5% gain. Over the trailing 12 months, productivity increased 2.9%. This compares to an annualized 1.5% rate of productivity growth over the last five years. **Unit labor costs** rose at an annualized 4.7% pace in Q1, exceeding the 4.0% rise expected; the year-over-year increase decelerated by almost a half-percent to 4.3%.

Market Notes

Period ending 5/3/2024	1 Week %	YTD %
DJIA	1.14	3.21
S&P 500	0.56	7.99
NASDAQ	1.44	7.85
Russell 2000	1.71	0.85
MSCI-EAFE	1.63	4.44
MSCI-EM	2.03	4.43
Bloomberg U.S. Aggregate	1.17	-2.06

U.S. Treasury Yields	3 Mo.	2 Yr.	5 Yr.	10 Yr.	30 Yr.
12/31/2023	5.40	4.23	3.84	3.88	4.03
4/26/2024	5.46	4.96	4.68	4.67	4.78
5/3/2024	5.45	4.81	4.48	4.50	4.66

U.S. stocks turned the corner on a negative April, with gains last week. Softness early in the week appeared related to poor consumer sentiment and the looming Fed decision, as well as the attached message. On Wed., after the Fed meeting, markets had started down nearly a percent but completely reversed to up a percent by the time the press conference had started, before reversing backwards again. The discussion took on a more dovish tone than expected, highlighted by the answer of rate hikes 'not really on the table'—removing a key tail risk markets had been worried about. The rally Fri. was directly related to a weaker-than-expected jobs report, and moderating wage pressures, that also restrained the 'too hot' economy risk and kept hopes for rate cuts alive.

By sector, utilities led the way, up over 3% (based on strong Q1 earnings, lower interest rates, and expectations for rising AI-fueled electricity demand), followed by technology (Apple was boosted by better-than-expected earnings and announcement of a record buyback program), and consumer discretionary (Tesla's tentative agreement with the Chinese government for use of self-driving technology). On the downside, energy declined -3% along with lower oil prices. Real estate also gained over a percent, in keeping with a drop in yields. Small caps outpaced large caps, getting back into positive territory on a year-to-date basis.

Earnings season has continued to progress, with 80% of S&P 500 companies now having reported for Q1, per FactSet. The blended year-over-year earnings growth rate has come in at a decent 5.0%—the best in a few years—and up from expectations of 3% a month ago. Analysts have also increased EPS estimates more than normal, rather than decreasing them in light of slowdown fears, as was earlier assumed. The strongest earnings growth results have come from communications, utilities, consumer discretionary, and technology—all up over 25% or better year-over-year. Energy and healthcare have continued to lag, each down around -25%. Also interestingly, stocks with more than half of their revenues earned domestically in the U.S. have only seen earnings growth of 0.5%, while stocks with the majority of revenues from abroad have seen 13.2% earnings growth. (Overall, as has been the case for a while, roughly 40% of S&P 500 revenues are foreign-sourced.)

Foreign stocks rose last week as well, as sharp gains in Japan and the emerging markets outweighed flattish results in Europe. Euro area GDP came in at a surprisingly 'strong' 0.3%, after a year of stagnant growth. It still appears the ECB is poised to cut rates beginning in June, although the pace might not be necessarily quick or substantial given the economic improvement. The Japanese government appeared to intervene in currency markets over the prior weekend, to stabilize the plummeting yen somewhat, although they didn't admit to it—helping boost Japanese asset returns for the week. Chinese markets were closed much of the week for the May holiday, but exposure through China ETFs saw a sharp rise along with hopes for holiday consumer spending and additional government stimulus, along with stronger manufacturing data.

Bonds experienced gains broadly last week, led by investment-grade corporates, with yields falling towards the end of the week, based on cooling economic and labor data. Foreign bonds fared positively along with a falling U.S. dollar.

Commodities were down broadly last week, despite the weaker dollar, led by energy and precious metals. Crude oil fell by nearly -7% last week to $78/barrel, as signs of some U.S. economic slowing, a fade in Middle East tensions, and higher U.S. supply have weighed on pricing. Interesting, current high crude prices caused the Biden administration to halt plans to refill the U.S. Strategic Petroleum Reserve in the near-term.

Have a good week.

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Sources: FocusPoint Solutions, American Association for Individual Investors (AAII), Associated Press, Barclays Capital, Bloomberg, Citigroup, Deutsche Bank, FactSet, Financial Times, First Trust, Goldman Sachs, Invesco, JPMorgan Asset Management, Marketfield Asset Management, Morgan Stanley, MSCI, Morningstar, Northern Trust, Oilprice.com, PIMCO, Standard & Poor's, StockCharts.com, The Conference Board, Thomson Reuters, T. Rowe Price, Univ. of Michigan, U.S. Bureau of Economic Analysis, U.S. Federal Reserve, Wall Street Journal, The Washington Post. Index performance is shown as total return, which includes dividends. Performance for the MSCI-EAFE and MSCI-EM indexes is quoted in U.S. Dollar investor terms.

Notes key: (+) positive/encouraging development, (0) neutral/inconclusive/no net effect, (-) negative/discouraging development.