DAVIS EXECUTIVE WEALTH MANAGEMENT
at Steward Partners

Market Update

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There have been rumblings in the financial press recently about the possibility that the U.S. is at risk of falling into a Stagflationary environment where inflation continues to persist and economic growth stalls out. The reason why this is a concern is because in a Stagflationary market, it's tough to invest in stocks or bonds. In a literal sense, you have "Stag" – Stalled Growth & "Flation" – Inflation runs high. This is what the United States experienced in the 1970's and no one wants to go back there. Fed Chairman Powell has been on record of saying that he did not understand the concerns about inflation because the economy is still growing and inflation is coming down. You can see some of those comments here. Unfortunately, this is the same Fed Chair that said inflation was "transitory" and predicted a few Fed rate hikes before embarking on the most aggressive rate hike campaign in two generations. So, lets take a look at the data to see where we currently stand.

"Stag" –

- In an absolute sense, the economy is still growing with Q1 GDP at a solid 1.6% annualized per CNBC. Not huge but far from zero.
- Both the ISM Manufacturing & ISM Services PMI's are now below 50 which is something that doesn't happen very often and signals a contraction in both the services (spending) and manufacturing (making stuff) parts of the economy.
- Durable Goods have been flat for a year.
- Unemployment – Remains below 4% but is threatening to move above that number on a sustained basis for the first time since well before Covid.

"Flation" –

- CPI has recently gotten "stuck" around 3.5% year-over-year (this is very heavily influenced by shelter costs & auto insurance so it must be taken with a grain of salt) and the University of Michigan Inflation Expectations have snuck up to 3.5% for 1-Year & 3.1% for 5-Years.
- Price Indices for the ISM Manufacturing & Services PMI's have also jumped to multi-month highs.
- There is a lot of "noise" in the inflation data that is still somewhat conflicting but many of the Core items ex-auto insurance & shelter costs are BELOW trend. See Tom Lee's comments here on CNBC recently.

Add it all up and we are far, far away from the 1970's. The main concern for this market, however, is with the multiple on the S&P 500 at 21x earnings, per Bloomberg, there is zero room for error as the market is priced for perfection. This week will be very telling with April CPI being reported on Wednesday morning. Keep a very close eye on the housing & auto insurance inputs. These inputs are the ones that have weighted most heavily on the headline CPI number, and we need them to contract. Either way, we are laser-focused on this topic and will be monitoring it closely in the coming weeks and months. Thank you to Tom Essaye of the 7's Report & Tom Lee of Fundstrat for the inspiration and data points reflated in this update. I find their research to be some of the best out there.

Please feel free to reach out to me with any comments or questions. I always enjoy the opportunity to engage with clients and friends on the things that matter to them most.

Regards,
Tim

PS – Per Fundstrat: 460 companies that have reported earnings so far (92% of the S&P 500):

- Overall, 81% are beating estimates, and those that "beat" are beating by a median of 8%.
- Of the 19% missing, those are missing by a median of -5%.
- On the top line, overall results are beating estimates by a median of 5% and missing by a median of -4%, and 60% of those reporting are beating estimates.

Listen to my interview on Sirus XM's Business Briefing:
https://youtu.be/URCkH5TQpa4?si=TzpkZdtKEvQnWDio

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