Summary

Economic data for the week included a surprisingly negative U.S. GDP result for the first quarter. Housing data was mixed, with slower sales, but home prices reached record highs. Consumer sentiment fell back a bit, but durable goods rose, and jobless claims remained positive, and near multi-decade lows.

Global equity markets fell back sharply last week, due to mixed earnings reports, high commodity prices, slowing growth, and Ukraine concerns. Bonds were little changed in the U.S., but were negatively impacted abroad by an especially strong U.S. dollar. Commodities were mixed, with higher energy prices offsetting declines in metals.

Economic Notes

(-/0) Advance U.S. **GDP** for Q1 came in showing an unexpected contraction of -1.4%, in a somewhat mixed report. Although no one expected a repeat of Q4's 6.9% growth, this surprised relative to expectations calling for a small gain of 1.0%. Under the hood, conditions were better than at first glance, with strong personal consumption (2.7% growth, although a percent below expected, contributing to 1.8% of the total GDP growth release), with services and durable goods remaining strong, relative to nondurable goods. Also robust was private sector demand in business fixed investment (up 9.2%) intellectual property, and homebuilding. The negativity was primarily focused on stronger net imports (up 18%). As imports don't add to a nation's production, net exports are what's desired, but trade has been hampered by higher prices and anticipated potential shortages due to Ukraine, causing the sector to account for a negative -2.5% of the total GDP contribution. Government spending also shrunk by nearly -3%, detracting -0.5% from GDP. These naturally offset a good deal of positive contribution on the private side.

The core PCE price index rose at a sharp 5.2% quarter-over-quarter annualized rate in Q1, but was actually a few tenths less than expectations. The GDP price index rose a robust 8.0% on a quarterly annualized basis, in fact the highest rate since 1981, and rising 6.8% over the trailing 12 months.

Of course, later revisions of these results at the ends of May and June could alter this negative result a bit. Based on the cyclical indicators of business investment being positive, especially homebuilding, the odds of this being the first half of a recession reading aren't overly high. (But it's not impossible, although recessions are technically based on a qualitative assessment from the NBER.) Interestingly, based on observations of Moody's, from the period of 1960 through 2008, a quarterly contraction in GDP was almost always associated with a recession ultimately. However, post-GFC, single-quarter instances of negative GDP happened several times without a recession unfolding, twice in 2011 and once in 2014.

The Atlanta Fed's GDPNow indicator had predicted a weak 0.4% just prior to the Q1 release, and it had been deteriorating as of late, so not that far off base. For Q2, the initial GDPNow reading is 1.9%. Expectations for 2022 overall remain in the 2.5-3.0% range, which is still above trend. For 2023-24 and onward, a variety of predictions are tilted toward 2.0-2.5%, which is more in line with the pre-Covid growth pace, as well as a reflection of slower fundamentals, such as demographics, immigration, and productivity.

(0) **Personal income** in March rose 0.5%, a tenth above consensus expectations, and mostly driven by higher wage/salary income as employers are responding to worker shortages. From a higher-level view, income is down nearly -12% over the last 12 months, due to the base effects of large government fiscal stimulus made last spring now falling off. **Personal spending** rose 1.1%, which was nearly double expectations of 0.6%, but reflected some prior month revisions which normalized the net result for 2022. Over the past year, spending remains up 9%, which reflects stimulus spending, but also high goods inflation readings, which reduces the net effect. For March, the personal savings rate therefore fell back by -0.6% to 6.2%—remaining below pre-pandemic rates.

The PCE price index rose 0.9% on a headline level, and 0.3% for core, which was largely in line with expectations. On a year-over-year basis, PCE inflation rose 6.6% and 5.2% on a headline and core level, respectively. The core number shows some deceleration from the prior month, which brings questions about the timing of the inflation peak.

(0/+) **Durable goods** orders for March rose by 0.8%, just short of the 1.0% gain expected, but a reversal of the prior month. Removing transportation orders, the gain improved to 1.1%, and 1.0% on a core capital goods order level. Core capital goods shipments rose 0.2%, less than half that expected by median forecast. In March, orders for autos (up 5%), computers/electronics (up 2-4%), and other machinery and metals led the way. Durable goods orders overall are up 10% over the trailing 12 months. Demand remains strong, seen in the record level of orders that remain unfilled, being hampered by the well-documented supply issues, in nearly all industrial segments. Although recession worries and probabilities have certainly risen, strength in these areas has the potential of keeping economic growth slowing at bay (assuming the orders can be filled).

(+) The **S&P/Case-Shiller home price index** for February rose by 2.4%, which was the largest single-month gain in the history of the series, and beat expectations of 1.5%. All 20 cities saw a gain for the month, led by West Coast markets San Diego, Seattle, and LA—each up 3.0-3.5%. Year-over-year, the index accelerated higher by 1.3% to 20.2%, which was also a new historical high for that measure.

(+) The **FHFA house price index** rose 2.1% in February, also surpassing the 1.5% expected by consensus. All nine national segments experienced positive results, led by the South Atlantic and Mountain regions—up 2.5-3.0%. Year-over-year, the rate of change rose by 1.2% to 19.5%, which was a new high as well.

(-) **New home sales** in March fell back by -8.6% to a seasonally-adjusted annualized level of 763k units, well below the median forecast calling for a -0.6% decline. However, sales for the prior two months were revised notably higher. Every region experienced a decline in March, with results most negative in the South and West. The median new home price was up 21% from last year at $436,700, with the average price up 26% at $523,900. The months' supply of new homes ticked up by 1.2 to 6.4, as sales slowed and inventories continue to refill (most of the inventory remains under the category 'homes under construction'). Interestingly, new home sales are down -13% from levels a year ago. As with existing home sales, higher mortgage rates and higher prices (per the Case-Shiller and FHFA data), not to mention still-low inventories, have resulted in mixed housing data on a month-to-month basis. It appears new single-family homes under construction is at its highest level in over 15 years; however, it remains at only three-quarters of the more 'normal' building levels at the turn of the century in 2000ish era.

(-) **Pending home sales** for March declined by -1.2%, just further than the -1.0% forecasted by consensus. Year-over-year, pending sales fell by -9%. While sales rose in the Northeast, the Midwest saw declines of over -5%. As usual, these tend to act as a leading indicator for upcoming month existing home sales.

(-) The Conference Board's **index of consumer confidence** for April fell by -0.3 of a point to 107.3, below the expected 108.2. Assessments of current conditions fell back by over a point, while expectations for the future improved by almost half a point. The labor differential, measuring the ease in finding jobs, fell back a few points, but remains close to a record level of strength.

(-) The final **Univ. of Michigan index of consumer sentiment** for April showed a tick down of -0.5 of a point to 65.2, below the unchanged 65.7 expected. The underlying data showed that the assessments of current conditions rose, while expectations for the future fell back by nearly -2 points. Inflation expectations for the coming year were unchanged at 5.4%, as were those for the next 5-10 years at 3.0%. Perhaps surprisingly, inflation expectations, which are closely watched by the Fed, and remain somewhat of a riddle to economists, have stayed fairly static over the last few months.

(0/+) **Initial jobless claims** for the Apr. 23 ending week fell by -5k to 180k, which was on target with median expectations. **Continuing claims** for the Apr. 16 week fell by a meager -1k to 1.408 mil., which was a bit above the 1.399 mil. consensus estimate. With claims at such low levels, room for improvement remains contained, as company layoffs seem to be minimal, with a need for more workers rather than less.

Market Notes

Period ending 4/29/2022	1 Week (%)	YTD (%)
DJIA	-2.47	-8.73
S&P 500	-3.26	-12.92
NASDAQ	-3.92	-21.00
Russell 2000	-3.94	-16.69
MSCI-EAFE	-2.20	-12.00
MSCI-EM	0.08	-12.15
Bloomberg U.S. Aggregate	-0.01	-9.50

U.S. Treasury Yields	3 Mo.	2 Yr.	5 Yr.	10 Yr.	30 Yr.
12/31/2021	0.06	0.73	1.26	1.52	1.90
4/22/2022	0.83	2.72	2.94	2.90	2.95
4/29/2022	0.85	2.70	2.92	2.89	2.96

U.S. equities experienced a volatile week, falling back near -15% correction territory from peak levels, with April returns coming in as the poorest month since March 2020. Results during the week were largely driven back and forth by earnings news during one of the busier reporting segments for S&P 500 companies. Stocks bounced back slightly early on, partially driven by positive sentiment (for non-financial reasons to some extent) surrounding Elon Musk's bid for Twitter, before suffering again early in the week with additional bad news from China—lockdowns were continuing with the potential for spread to Beijing and other cities. Most directly, the zero-Covid policies in China have cut manufacturing and shipping activity dramatically, which continues to have far-reaching global consequences. However, the Chinese government has been moving toward additional stimulative measures in attempts to offset the slowdowns, countercyclically to most other world nations at this stage. Increasing nuclear rhetoric from Russia, in response to Ukrainian weapons shipments and severe sanctions, also weighed on sentiment.

Every industry sector lost ground for the week, with consumer discretionary declining over -7% (led downward by Amazon following a poor earnings report, and Tesla, with worries over potential owner distractions and stock technicals in the acquisition of Twitter), followed by financials and communications. Leaders were a mixed bag of energy and materials, with sustained minimal losses for the week in keeping with their recent leadership, as well as technology and consumer staples. Real estate also declined over -5% for the week.

Foreign stocks were mixed, with emerging markets ending flat for the week and Japan faring well, with minimal losses, outperforming Europe and U.K. European governments are contemplating additional sanctions against Russia, as well as cultivating plans to wean off petroleum imports from the region entirely (timeframe to be determined). The re-election of French president Macron provided a bit of relief to markets uncertain about policies of the potential replacement Le Pen. In emerging markets, returns were all over the board, with declines in Brazil, Mexico, and Asia, offset by gains in China. As mentioned, due to Chinese economic weakness, news from government meetings has focused on fiscal stimulus, including tax cuts, new infrastructure plans, and consumption support.

As of Friday, per FactSet, 55% of S&P firms have reported Q1 earnings results. Although it might be a surprise considering recent market volatility, 80% of firms have reported a positive surprise on the earnings side, and over 70% on the revenue side. Earnings growth on a year-over-year basis is just over 7%, which is close to the 30-year average, but below the 9% average rate of the past ten years. Recent weaker price activity and better earnings have brought the 12-month forward P/E to 18.1 (above the 10-year average of 16.9). Interestingly, due to the concentration of the larger members of the S&P, if Amazon were excluded, earnings growth would have risen to over 10%. Of course, this pales in comparison to the year-over-year number of over 90% from March 2021, which reflected the impact of Covid in both directions, but remains solidly expansionary.

Stock market volatility rattles many investors, as it the first worry is often 'crash', but underlying context is helpful. If one believes that financial markets are at least partially 'efficient', securities prices on any given day should reflect the net effect of all investor opinions: bullish, bearish, and neutral. If there is seeming agreement on or at least stability in broader fundamentals, such as future earnings growth, inflation, interest rates, commodity prices, or geopolitics, market prices are less likely to see extreme day-to-day movement. However, when there is greater disagreement on near-term outcomes, or a wider span of possibilities (good and bad), the 'price discovery' function of markets takes over, creating greater volatility. This may last for a short time or longer, based on the uncertainty of the underlying inputs. Note that this is different than a 'crash', which is tends to exhibit a sell-first-and-ask-questions-later behavioral panic, where such a probabilistic evaluation is not conducted in that short a time span. Obviously, today's inputs include a variety of data to digest, such as the Ukraine war and impact on commodity prices and inflation, not to mention chances of a wider conflict, underlying inflation prior to the war, Covid continuing into an endemic stage (it seems) but including Chinese lockdown duration, central bank monetary policy, and the impact of all onto upcoming economic growth and corporate earnings. There is a lot here to digest, and conditions continue to change by the week, causing prices to change in line with changing news and assumptions.

U.S. bonds were stable last week, as interest rates calmed a bit, perhaps with a bit of buying pressure from flows away from equities. Treasuries earned positive returns, outperforming both investment-grade and high yield corporates, which lost a bit of ground, along with a typical positive correlation of credit spreads to equity prices. Foreign bonds lost a percent or more in both developed and emerging markets, with rising rates and the U.S. dollar gaining another two percent for the week. The U.S. dollar has reached another peak not seen since 2016, largely due to 'carry' considerations. For example, as the U.S. Federal Reserve has moving to a higher rate regime, large investors looking for places to park spare cash will choose a higher-rate environment, rather than a static low-interest rate currency like the Japanese yen or euro.

Commodities were mixed for the week, with gains in energy offset by declines in industrial and precious metals. The price of crude oil rose by over 2% to nearly $105/barrel, and natural gas prices rose another 9%. The surge in natural gas was on the heels of global supply concerns following Russia's stoppage of exports to Poland and Bulgaria as a punishment for their refusal to pay in rubles. Natural gas supply dynamics have been one of the largest wildcards affecting the European economy over the past two months, and it's expected will continue to be so.

Have a good week.

Ryan M. Long, CFA
Director of Investments
FocusPoint Solutions, Inc.

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, Moody's, Morgan Stanley, MSCI, Morningstar, Northern Trust, PIMCO, Standard & Poor's, StockCharts.com, The Conference Board, Thomson Reuters, T. Rowe Price, 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.

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