Summary

Economic data for the week included the U.S. Producer and Consumer Price Indexes each rising at a monthly pace in line with expectations but continuing to decelerate on a year-over-year basis. Consumer sentiment also worsened, while jobless claims rose.

Global equities were mixed to lower, with U.S. outperforming foreign. Bonds also fell back a bit due to higher yields, and foreign bonds being negatively affected by a stronger dollar. Commodities also lost ground with continued economic concerns.

Economic Notes

(+) The **Producer Price Index** in April rose 0.2% on both a headline and core level, ex-energy and food; headline was a tenth below expected, while core was in line. Food prices fell a half-percent, while costs for energy rose by nearly a percent, along with a rise in retail margins of a half-percent. Overall, services contributed to over three-quarters of the April increase, with goods far less significant—these are in keeping with the composition of current economic activity. On a year-over-year basis, final demand PPI growth decelerated nearly a half-percent to 2.3% on a headline level, while core ex-food and energy PPI fell three-tenths to 3.2%. These represent significantly lower rates of inflation, helped by shelter not being included, unlike the CPI measure.

(0/+) The **Consumer Price Index** for April rose 0.4% for both headline and core, removing the impact of food and energy. Both were on par with expectations. For the single month, food away from home gained nearly a half percent, while food at home offset the impact by declining. Energy commodity prices rose nearly 3%, mostly due to gasoline, while other products fell in price. Shelter costs rose 0.4%, slowing a few tenths from prior months as home price declines and rents have become more integrated. However, used car prices (2.5% of the index) rose 4.4% in April, registering an outsized impact on conditions; this wasn't a surprise, as it reflected several months of rising wholesale car auction prices (which have now since started to reverse). New car prices, though, fell back for the first time in two years, with few supply issues at this point and rising domestic production. Airline fares and lodging prices each pulled back by -3%.

On a trailing 12-month basis, CPI decelerated to a 4.9% rise on a headline level and 5.5% for core. The headline number was at the slowest pace in two years, with an under-5% reading taken as a welcome sign. The past year was highlighted by an 8% rise in food prices (13% of the total CPI index), led by grain and dairy, which has weighed on consumers in a more tangible way. On the other hand, energy prices (7% of CPI) are actually down -5% on net. Shelter, at 35% of total CPI, remains up 8% year-over-year, registering an outsized influence compared to how inflation is measured in many other countries that exclude housing.

Overall, inflation conditions continue to improve, but not at the more rapid pace many economists have hoped for by now. The Fed is especially focused on the niche calculation of core inflation ex-shelter rent, referred to as 'supercore,' which is a timelier reflection of the economy than are the real estate-related segments. Looking out a few years, economist estimates have generally been inching up, from initial expectations of the Fed getting to their 2.0% goal sooner, to now more like a stickier 2.5%. This isn't a deal-breaker by any means, and that small of a margin might not even be noticeable, as some economists argue that 2.0% isn't a realistic or desirable goal anyway (it was chosen arbitrarily by a variety of central banks). But improvement is improvement.

(-) **Import prices** rose 0.4% in April, a tenth higher than expected and reversing a drop in the prior month. Fuel prices (just under 10% of the index) were the main driver, up nearly 5%, along with higher prices for industrial supplies. Outside of petroleum, there was little net change. Year-over-year, import prices were down -5%, and down -2% when removing fuels.

(-) The preliminary **Univ. of Michigan index of consumer sentiment** for May fell by -5.8 points (-9%) to 57.7, well below the expected minor drop to 63.0. Assessments of current conditions declined by -4 points, while expectations for the future fell -7 points. Inflation expectations for the coming year ticked down a tenth to 4.5%, while those for the coming 5-10 years rose 0.2% to 3.2%. Per the release from the Univ. of Michigan, the May numbers reflected worries over what appeared to be the negative trajectory of the economy, which includes the debt crisis standoff. (They likely also include woes in the banking system, which has high media visibility.) The overall index remains down -1% from readings a year ago, due to the expectations component lagging the current component. Expectations for the economy a year out and several years out were both sharply negative. Then again, as conditions shift, sentiment has the habit of changing quickly, making these less reliable far in the future—the index's value is how sentiment might negatively affect spending today.

(-) **Initial jobless claims** for the May 6 ending week rose by 22k to 264k, above the 245k median forecast Continuing claims for the Apr. 29 week rose 12k to 1.813 mil., below the 1.820 mil. level expected. Initial claims jumped to their highest level since Oct. 2021, but were led by a substantial jump in Massachusetts (6k). This is in keeping with gains in the last few weeks from that state, which appear to be largely due to fraudulent claims applications.

(0/-) The Q1 2023 Federal Reserve **Senior Loan Office Opinion Survey** (with responses collected in late March and early April) noted a slight tightening in credit conditions compared to the prior Q4 report. While the changes weren't as dramatic as might have been expected, bankers surveyed did expect conditions to get worse, which could skew current loan decisions. In general, higher interest rates or uncertainty about the path of rates (for variable-rate loans) plays an unsurprisingly large role in borrower demand.

For commercial/industrial loans, just under half of banks noted tighter standards for larger- and medium-sized firms, and loan spreads widened, while demand also weakened from such companies. The reasons for tightening remained mixed, with a less favorable/uncertain economic outlook being primary, followed by reduced tolerance for risk, worsening of industry-specific problems, and bank liquidity (which rose over 20% from Q4).

For commercial real estate loans, standards tightened for both construction/development as well as multi-family projects, while demand for such loans fell again (likely related to higher interest costs). Residential mortgages were little changed from the credit side, with tightening minimal, except for jumbo and sub-prime. Consumer loans and credit cards saw tighter standards generally, with weaker demand for auto loans specifically (which could be related to both higher interest rates and auto availability).

Market Notes

Period ending 5/12/2023	1 Week %	YTD %
DJIA	-1.04	1.19
S&P 500	-0.24	8.07
NASDAQ	0.44	17.74
Russell 2000	-1.04	-0.65
MSCI-EAFE	-0.67	10.95
MSCI-EM	-0.86	2.42
Bloomberg U.S. Aggregate	-0.23	3.30

U.S. Treasury Yields	3 Mo.	2 Yr.	5 Yr.	10 Yr.	30 Yr.
12/31/2022	4.42	4.41	3.99	3.88	3.97
5/5/2023	5.26	3.92	3.41	3.44	3.76
5/12/2023	5.25	3.98	3.45	3.46	3.78

U.S. stocks were dominated early in the week by the Tuesday meeting between President Biden and Congressional leadership to find common ground about the upcoming U.S. debt limit; a follow-up meeting later in the week was postponed. Weaker consumer sentiment and higher inflation expectations also appeared to weigh on market sentiment, as did continued concerns over several banks. By sector, communications led the way with gains of over 2% (led by Alphabet/Google's artificial intelligence bot release), while materials and energy each declined by -2%. Real estate fell back around a percent, along with rates moving upward.

Through this week, one surprising thing has been the strong performance of U.S. stocks despite a variety of headwinds, including potential recession, slowing earnings, and the debt limit. Then again, the largest group of 7 or so FAANG stocks has led the way, along with 'growth' over 'value', which has driven the Nasdaq index higher. Removing that segment, the S&P minus those key tech names is down so far this year.

Foreign stocks underperformed U.S. stocks generally, with no help from a stronger dollar. The Bank of England raised interest rates by 0.25% to 4.50%, as expected, although the vote was far from unanimous, while the ECB continued hawkish comments noting there is 'more to do' on the inflation front. European manufacturing data also declined, which raised recession fears. Japanese equities were the only region ending positively due to stronger earnings results, while emerging markets were down over -2%. In EM, China led the way downward with continued concerns over economic growth not exploding to the degree first anticipated upon the post-pandemic reopening. Interestingly, inflation has fallen so fast in China that outright deflation has become a future concern, with the most recent year-over-year CPI number coming in at only 0.1%.

Bonds fell back a bit last week as interest rates ticked higher across the yield curve. Investment-grade corporates fared best, while high yield bonds fell back nearly a half-percent. Unhedged foreign bonds were negatively impacted by an over 1% rise in the U.S. dollar, while dollar-hedged debt was little changed on the week.

Commodities fell back last week, with declines in energy but an even more sizable drop in industrial metals (especially nickel). Crude oil rose a few percent mid-week before ending down -2% last week to $70/barrel. This losing streak has been due to larger U.S. inventories (despite falling rig counts), debt default concerns, as well as the recovery in China looking less consistent than expected.

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, 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.

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