Summary

Economic data for the week included the index of leading economic indicators continuing a long stretch of declines, pointing to ongoing recession risks. Industrial production and retail sales slowed, as did sales and starts in the housing sector.

U.S. stocks saw gains last week, coupled with mixed results abroad. Bonds were little changed in the U.S. with a stable yield curve, while foreign bonds suffered from a weaker dollar. Commodities were also mixed, with gains in energy offset by weaker prices for industrial metals.

Economic Notes

(-) The Conference Board's **Index of Leading Economic Indicators** for June showed a decline of -0.7%, which follows a -0.6% drop the prior month, and continues a stretch of 15 straight negative reports (the longest stretch since 2007-08). In June, the decline was led by weaker results in new orders, consumer sentiment, moderately higher jobless claims, and lower building permits. For the six-month period ending in June, the LEI is down -4.2%, which exceeds the -3.8% decline for the six-month period that ended in Dec. 2022. The six-month period has been characterized by weaker non-financial components, such as consumer sentiment and slower new orders, although the inverted yield curve was also a negative contributor. In their view, this continues to flash a recessionary signal—particularly for Q3-2023 to Q1-2024.

(-/0) **Retail sales** rose 0.2% in June, below the 0.5% rise expected. Removing the more volatile components (autos, building materials, and gasoline), the core/control measure gained 0.6%, as several of those particularly volatile sectors experienced declines. The most powerful positive influences came from non-store/online retail, misc. stores, furnishings, and electronics, while auto sales also gained during the month. Food/beverage sales fell, which appeared to be in conjunction with extended pandemic food stamp benefits expiring. Year-over-year, retail sales are up 1.5%; when this nominal figure is adjusted to an after-inflation real figure, the 'growth' obviously turns negative. Core sales, without the downward commodity pressures, remain up nearly 5% year-over-year. On net, consumer spending remains less robust than earlier in the post-pandemic recovery cycle, but is also still positive, with spending on goods now having transitioned toward services.

(-) **Industrial production** fell -0.5% in June, relative to expectations for no change. By category, manufacturing and mining production each fell by a few tenths, while utilities production fell by -2.5%—a category largely driven by weather and summer cooling needs. On the negative side, auto manufacturing fell by -3%. On a year-over-year basis, industrial production has fallen into the negative, at -0.4%, for the first time in two years, after spending the past several months hovering just above zero. This is similar to the slowdown path of mid-2019, when economists similarly debated the economy's future path into or avoiding recession, before the pandemic provided the more conclusive answer. Capacity utilization fell by -0.5% to 78.9%.

(0) The **Empire state manufacturing index** fell by -5.5 points in July to a still-positive level of 1.1, above expectations of a decline into a contractionary -3.5. New orders moved further into expansion slightly, while employment moved back into expansion, and shipments fell but stayed solidly in expansion. Prices paid also declined by over -5 points, yet still expanded, albeit to the slowest pace in 3 years. The six months-ahead business conditions index rose nearly five points to further expansionary territory as well.

(-) The **Philadelphia Fed manufacturing index** rose 0.2 of a point in July to a still-contractionary -13.5, slightly below the -10.0 level forecast. New orders fell back further into contraction, with shipments falling by -20 points, falling from expansion into contraction, with employment falling slightly further into a minor contraction. While prices paid ticked down a point, remaining in expansion, prices received moved by 23 points higher, into expansion. On the positive side, expected business conditions six months out rose 16 points, further expansionary to 29.

(-) **Existing home sales** for June fell -3.3% to a seasonally-adjusted annualized rate of 4.16 mil. units, below the median forecast of a -2.3% decline, with sales falling for both single-family and multi-family. Regionally, the South and West saw declines of around -5% each, while the Northeast saw small gains. Existing sales are down -18% over the past year. The median sales prices rose a bit to $410,200, which is down -1% on a year-over-year basis, but still remains one of the highest prices registered since the NAR began tracking this data in 1999. The months' supply inventory measure came in at 3.1 months, which remains about half of the long-term average level. Despite this being in the prime summer season for home sales, only two months in the last 22 years have seen fewer new listings.

(-) **Housing starts** fell -8.0% in June to a seasonally-adjusted annualized level of 1.434 mil. units, slightly better than the -9.3% median forecast decline. This was a reversal of the very strong May figure, even though that result was revised downward from an over-20% gain down to 16%. Both single-family and multi-family fell at similar rates. The Midwest saw a -33% drop, followed by less severe negativity in the other three regions. **Building permits** also reversed course by falling -3.7% to a level of 1.440 mil. units, below expectations for a 0.2% rise. Here, single-family permits rose 2%, while multi-family fell by -13%. Hopes continue for new home inventory to come on board (or even construction to begin), but the outlook remains mixed.

(0/+) The **NAHB homebuilder sentiment index** rose a point to 56 in July, on par with expectations, up to the highest reading in a year. This is a diffusion index, like ISM, where numbers over the neutral 50 level indicate positive sentiment. Readings over the past decade range from a pessimistic 30 to a very optimistic 90, and tend to track fairly closely with single-family housing starts. By segment, potential buyer traffic led, by being up 3 points, followed by future sales, and present sales up a point. The index has been moving straight up this year, with a stronger base of decent demand and very low supply. These fundamentals have helped sustain homebuilder confidence relative to conditions a year ago as interest rates were just starting to rise, as well as relative to higher rate environments in years past.

(0/-) **Initial jobless claims** for the Jul. 15 ending week fell by -9k to 228k, below the median forecast of 240k. Continuing claims for the Jul. 8 week rose by 33k to 1.754 mil., above the 1.722 mil. expected. There still appear to be some seasonal adjustment issues registering in the data, as well as concerns over possibly fraudulent applications in OH and expanded eligibility in MN.

Market Notes

Period ending 7/21/2023	1 Week %	YTD %
DJIA	2.13	7.54
S&P 500	0.70	19.24
NASDAQ	-0.57	34.69
Russell 2000	1.52	12.23
MSCI-EAFE	-0.57	14.06
MSCI-EM	-1.31	7.94
Bloomberg U.S. Aggregate	0.01	2.30

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
7/14/2023	5.49	4.74	4.04	3.83	3.93
7/21/2023	5.50	4.82	4.09	3.84	3.91

U.S. stocks were mixed last week, with continued positive sentiment from the prior week's better inflation readings and optimism about potential avoidance of a recession—seen by improved outlooks from some prominent economists. However, in earnings season, results are often stock-specific. Growth sectors ended in the negative, in contrast to recent strength, while value names gained over 2%. Small cap stocks outperformed large caps, to make up some of their lost ground in 2023, with some investors acknowledging their multi-year valuation discounts relative to larger companies. By sector, gains were had in energy and financials (for example, better than expected earnings for some firms, and Charles Schwab losing deposits at a slower rate than feared) as well as more defensive sectors health care and utilities. On the negative side, communications (Alphabet/Google) and consumer discretionary (Amazon and Tesla) each fell -2% to -3%. The reconfiguring of the Nasdaq 100 today (along with its popular tracking funds like the QQQ) will serve to trim weightings from the largest seven firms, while boosting the relative sizes of the rest, which may have also influenced some pre-emptive trading.

Insofar as Q2 earnings are concerned, per FactSet, nearly 20% of S&P firms have reported so far, with 75% showing positive earnings surprises. Of course, with the quarterly earnings cycle being how it is, and earnings expectations often set low, the surprise statistic isn't really that 'surprising.' Though, the blended expectation for year-over-year earnings growth (which includes combining actual results so far with remaining estimates) has fallen from -7% on June 30 to now -9%. On the positive side, estimated earnings gains of 30% in consumer discretionary and 14% in communications are at the top, while declines of -51% in energy, -34% in materials, and -29% in healthcare represent the low end. Revenue growth is strongest in financials, at 8%, and lowest in energy, at -29%. The poor energy results are in line with a drop in crude oil prices over the past year of over -20%, although that acts as a positive for other sectors that count petroleum as an input cost.

In addition to revenue and earnings results vs. expectations, management commentary and 'outlook' during quarterly calls remain additional wildcards that can end up boosting or working against individual company stock prices. This hasn't been a completely smooth ride, with results from usually-boring firms such as State Street Bank coming in slightly better than expected, yet the share price fell in the double-digits. Net interest income, a key factor in banking revenue, has again risen in focus with the ongoing treasury yield curve inversion (which works against how banks tend to make money when the yield curve is in its normal positive, upward-sloping state). Markets are very fickle, and naturally want it all. Another concern this earnings season is the ability for firms to maintain their high profit margins, which have been running several percent above long-term average levels for several years. One of the few positives about higher inflation is that it boosts revenue and earnings, as those are measured in nominal terms, not in 'real' after-inflation terms like GDP. (This is one of the reasons why stocks are considered an adequate inflation hedge over long periods of time, as inflation gets embedded into these nominal growth results.) Now, though, PPI and CPI have swung into disinflation, which threatens the high levels at which these margins are running. This coming week is the busiest for earnings releases, which could offer more interesting insights.

Foreign stocks were mixed, with developed markets ending with small gains in local terms pulled down by a rise in the U.S. dollar. Gains in the U.K. were helped by decelerating inflation readings, which were offset by flat returns in Europe and Japan, and declines in emerging markets. Interestingly, eurozone economic growth for Q1 was revised up from -0.1% to flat, which avoids a technical recession, although the difference is minimal. EM results were largely led by a drop in China, and related markets South Korea and Taiwan. Concerns linger in China about the strength of their post-pandemic growth recovery, with a disappointing quarterly growth pace of an unannualized 0.8% in Q2, below the Q1 pace of 2.2%, and continued very high youth unemployment, which concerns government officials perhaps as much as any other economic statistic.

Bonds were little changed last week, along with minimal changes in the U.S. treasury yield curve. Investment-grade and high yield corporates outperformed, as credit spreads tightened. Foreign bonds generally fell back as the U.S. dollar rose over a percent.

Commodities gained ground in energy and agriculture, while industrial metals declined by several percent. Crude oil rose over 2% last week to $77/barrel. Natural gas rose 7%, with the continued U.S. heat wave ramping up the need for air conditioning.

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, National Association of Realtors, 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.

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