

Weekly Market Perspectives

August 01, 2022



Anthony Saglimbene

Global Market Strategist
Ameriprise Financial

“Although it would be a stretch to believe assets won’t see added headwinds from tighter monetary policies this year, stock prices are starting to more fully reflect the idea that the Fed’s outsized rate moves are in the process of winding down.”

Will July’s Stock Rally Continue?

Stocks finished higher last week for the second-straight week, capping their strongest monthly performance since November 2020. Despite the Federal Reserve aggressively lifting interest rates last week and a Q2 GDP print showing the U.S. economy contracted for the second straight quarter, investors instead looked through the headwinds and focused on what may lie ahead. The S&P 500 Index gained +4.3% on the week, while the NASDAQ Composite jumped +4.7%. Notably, the S&P 500 is higher by nearly +13.0% since its June low. Growth outperformed Value for the third week in the past four, supported by better-than-feared earnings reports out of Big Tech and declining bond yields. The Dow Jones Industrials Average closed last week higher by nearly +3.0%.

All U.S. Treasury yields within a 10-year duration fell below 3.0% last week, which helped lift stock prices. Additionally, the U.S. Dollar Index declined for the second-straight week after logging gains in six of the previous seven weeks. Copper closed the week higher by +6.6%, Gold gained +3.1%, and West Texas Intermediate (WTI) crude settled higher by +4.1%, closing at \$98.28 per barrel.

Whether simply a bear market rally or the beginning of a more extended recovery, stocks turned in an impressive month of performance. In July, the S&P 500 climbed +9.1%, the NASDAQ surged +12.4%, and the Dow gained +6.7%. All eleven S&P 500 sectors finished the month higher, with Consumer Discretionary (+18.9%) and Information Technology (+13.5%) the standout performers. Semiconductors, casual diners, hotels, casinos, autos, apparel/accessories, and homebuilders drove U.S. stock indexes higher in July, while Consumer Staples (+3.1%) and Health Care (+3.2%) lagged.

During July, the 10-year U.S. Treasury yield slipped over 30 basis points to 2.66%, while WTI crude slumped 6.8%. **Bottom line: Falling yields helped relieve some pressure on growth stocks last month while declining crude prices reduced runaway inflation fears.** Record-high inflation and rising interest rates have sapped investor sentiment all year, causing stock prices to buckle under the pressures. But a little reprieve on both these fronts proved a welcome development last month, giving investors hope that price pressures can eventually subside, and interest rates can find an equilibrium level. In our view, much of the strong stock performance in July can be attributed to the peak inflation narrative gaining more steam. The sell-off across commodities, the decline in medium and longer-term inflation expectations (see July Michigan sentiment survey), and a pullback in price measures in regional manufacturing surveys contributed to the idea that the most significant price increases across the economy may be in the rearview mirror. Notably, an increasing number of investors believe June’s hot consumer and producer inflation prints could be this cycle’s high-water mark. And with July’s inflation data expected to show price pressures easing across a range of areas, stocks drove higher last month.

Stock Prices Reacted to the Federal Reserve’s Expected Rate Hike

Also helping to play into the peak inflation narrative is the bad news is good news theme, where softening demand and weaker economic activity could prompt the Federal Reserve to slow its aggressive rate hiking campaign. Last week, the Federal Reserve lifted its fed funds target rate by another 75 basis points, as expected. Yet,

Fed Chair Jerome Powell said that it would likely be appropriate to slow rate increases at some point and that another 75-basis point increase at the September meeting would depend on the data. After last week's move, the fed funds target rate now stands at 2.25% - 2.50%, up from 0.0% - 0.25% at the beginning of the year.

However, the market currently sees a high probability that the Federal Reserve will only raise rates by 50 basis points at its next meeting. In addition, investors increasingly believe the Fed will need to cut rates by July 2023, given slowing growth trends, to help counteract a potential recession. Here, investors believe Powell and company have gone a meaningful way to frontload rate hikes this year in an effort to curb demand and slow inflation pressures. Moving forward, the Fed may be able to slow the pace of future rate hikes to allow the economy to catch up with tighter policies. **Although it would be a stretch to believe assets won't see added headwinds from tighter monetary policies this year, stock prices are starting to more fully reflect the idea that the Fed's outsized rate moves are in the process of winding down.**

Recession Odds Still in Play, Yet Worst-Case Scenarios for Big Tech Avoided in Q2

Lending evidence to that statement is the fact that the U.S. economy shrank by 0.9% annualized in the second quarter after contracting by 1.6% in the first quarter. Though consumer spending increased in Q2, driven partly by inflation, inventories, residential/nonresidential investment, and government spending acted as significant drags on growth. Notably, two straight quarters of negative economic growth now elevate the growing belief that the U.S. is in or will soon enter a recession. According to a number of surveys, many Americans already believe the U.S. economy is in the midst of a significant downturn, and whether the National Bureau of Economic Research (NBER) official defines the downturn as a recession in hindsight is unimportant to the stock market. Consumer and business activity has slowed, spending is downshifting, and behaviors across the economy already reflect significant negativity. In our view, stock prices primarily looked through the negative Q2 GDP report last week because the market has been contemplating a shallow recession for some time now. Stocks climbed higher last week, in part, based on the assumption a Fed-induced slowdown in the economy is also in the process of winding down. However, much depends on the path of inflation. Thus far, it's unclear whether price pressures have been tamed enough to change sentiment or monetary policy in a more lasting way.

Also, helping stock prices to close the month out on a high note was better-than-feared Q2 earnings reports out of some of the biggest companies on the planet. Notably, Visa and Mastercard highlighted resilient consumer trends in their Q2 results, particularly across travel spending. In addition, though Alphabet and Microsoft posted somewhat disappointing earnings results in the second quarter, the stocks reacted positively to better-than-feared metrics in cloud computing. Investors also responded positively to Amazon highlighting a strong consumer in their Q2 profit report, while Apple rallied on solid iPhone demand in the previous quarter. **Bottom line: Big Tech earnings are slowing, but secular trends look intact, and companies in the space continue to navigate a challenging environment well.** With so much negativity built into share prices coming into last week's Big Tech earnings releases, the market breathed a sigh of relief that the worst-case scenarios were avoided in Q2.

In the Week Ahead: Q2 Earnings Season is Halfway Through and a Myriad of Economic Data Will Be Released

Looking ahead to this week, roughly 30% of the S&P 500 will report Q2 earnings results, including two Dow 30 components. According to FactSet, Q2'22 S&P 500 blended earnings per share (EPS) growth is higher by +6.0% year-over-year on sales growth of +12.3%. Of the 56% of S&P 500 companies that have reported Q2 results thus far, 73% have surpassed EPS estimates, while 66% have beaten sales forecasts. Both measures are below the five-year average. Common themes noted on the latest batch of earnings calls point to slowing demand, shifting spending patterns, high input costs, and cautious outlooks. However, the net profit margin for the S&P 500 is expected to hold above +12.0% in Q2, which would mark the fourth-highest level since FactSet began tracking the metric in 2008.

In addition to a busy week of earnings reports, the economic calendar is also heavy. Investors will receive final looks at July manufacturing and services activity, which has been declining for several months, and a preliminary look at July auto sales. June construction spending and the June Job Openings and Labor Turnover Survey (JOLTS) report are other items of note on the week. But Friday's July nonfarm payrolls report will receive the bulk of the economic focus this week. July nonfarm payrolls are expected to grow by +244K, downshifting from June's +372K hiring pace. The unemployment rate is expected to hold steady at 3.6% for the fifth consecutive month. In June, the job market remained tight, despite cooling employment trends in manufacturing and construction and wage pressures that appeared to be moderating.

A strong labor market has been an area of focus for the bulls and is inconsistent with the concept that the U.S. economy is in or on the edge of falling into recession. After Friday's jobs update, we'll see if the bulls can continue to draw support from this point. Or is the labor market just one of the last shoes to drop in an economic downturn and before the bears say we told you so?

Important Disclosures:

The views expressed are as of the date given, may change as market or other conditions change, and may differ from views expressed by other Ameriprise Financial associates or affiliates. Actual investments or investment decisions made by Ameriprise Financial and its affiliates, whether for its own account or on behalf of clients, will not necessarily reflect the views expressed. This information is not intended to provide investment advice and does not account for individual investor circumstances.

Some of the opinions, conclusions and forward-looking statements are based on an analysis of information compiled from third-party sources. This information has been obtained from sources believed to be reliable, but accuracy and completeness cannot be guaranteed by Ameriprise Financial. It is given for informational purposes only and is not a solicitation to buy or sell the securities mentioned. The information is not intended to be used as the sole basis for investment decisions, nor should it be construed as advice designed to meet the specific needs of an individual investor.

Stock investments involve risk, including loss of principal. High-quality stocks may be appropriate for some investment strategies. Ensure that your investment objectives, time horizon and risk tolerance are aligned with investing in stocks, as they can lose value.

A **10-year Treasury note** is a debt obligation issued by the United States government that matures in 10 years. The 10-year yield is typically used as a proxy for mortgage rates, and other measures.

The fund's investments may not keep pace with **inflation**, which may result in losses.

A rise in **interest rates** may result in a price decline of fixed-income instruments held by the fund, negatively impacting its performance and NAV. Falling rates may result in the fund investing in lower yielding debt instruments, lowering the fund's income and yield. These risks may be heightened for longer maturity and duration securities.

Commodity investments may be affected by the overall market and industry- and commodity-specific factors, and may be more volatile and less liquid than other investments.

Past performance is not a guarantee of future results.

An index is a statistical composite that is not managed. It is not possible to invest directly in an index.

The Standard & Poor's 500 Index (S&P 500® Index), an unmanaged index of common stocks, is frequently used as a general measure of market performance. The index reflects reinvestment of all distributions and changes in market prices but excludes brokerage commissions or other fees. It is not possible to invest directly in an index.

The S&P 500 Financials Index is an index containing companies included in the S&P 500 that are classified as members of the financials sector.

The NASDAQ composite index measures all NASDAQ domestic and international based common type stocks listed on the Nasdaq Stock Market.

The Dow Jones Industrial Average (DJIA) is an index containing stocks of 30 Large-Cap corporations in the United States. The index is owned and maintained by Dow Jones & Company.

Definitions of individual indices and sectors mentioned in this article are available on our website at ameriprise.com/legal/disclosures in the Additional Ameriprise research disclosures section.

The U.S. Dollar Index (DXY) measures the dollar's value against a trade-weighted basket of six major currencies.

West Texas Intermediate (WTI) is a grade of crude oil commonly used as a benchmark for oil prices. WTI is a light grade with low density and sulfur content.

University of Michigan Consumer Sentiment Survey is a rotating panel survey based on a nationally representative sample that gives each household in the coterminous U.S. an equal probability of being selected. Interviews are conducted throughout the month by telephone. The minimum monthly change required for significance at the 95% level in the Sentiment Index is 4.8 points; for Current and Expectations Index the minimum is 6.0 points.

Third party companies mentioned are not affiliated with Ameriprise Financial, Inc.

Investment products are not insured by the FDIC, NCUA or any federal agency, are not deposits or obligations of, or guaranteed by any financial institution, and involve investment risks including possible loss of principal and fluctuation in value.

Ameriprise Financial Services, LLC. Member FINRA and SIPC.