THE PRIVATE CLIENT GROUP

BALANCING LIFE & WEALTH

ECONOMIC & MARKET INSIGHTS

An Executive Summary for August 2023

August is typically a time for summer vacation and down-time. Both equity and fixed income markets appeared to be taking time off as well. The S&P 500 decreased as all sectors were down except for Energy. Utilities fell the most, followed by Consumer Staples, Materials, and Real Estate. The Small-cap Russell 2000 index also declined. Yields on U.S. 10-year Treasuries rose for the fourth straight month reaching 4.1%, though mid-month levels reached 4.36%. The 5-year U.S. treasury rose towards 4.5% before retreating to 4.2% by month end. Within fixed-income markets, while U.S. Corporate High-yield bonds rose, the Bloomberg U.S. Aggregate Bond Index and Municipal bonds fell.

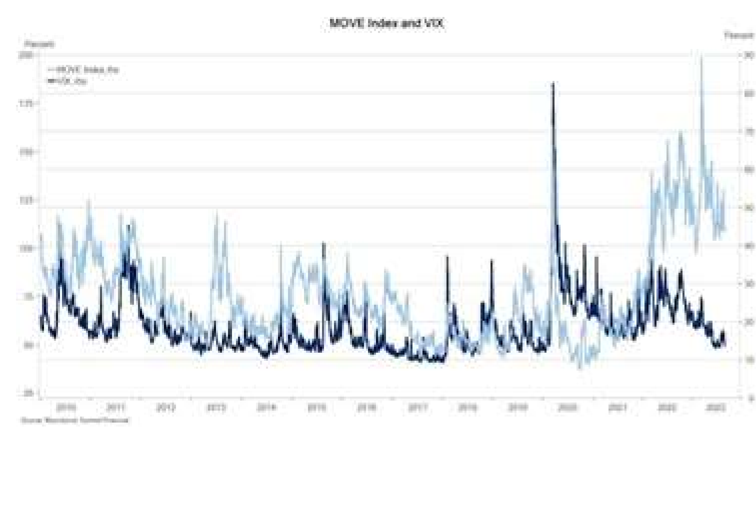
During the Federal Reserve's Jackson Hole Symposium, its annual policy conference, Chair Powell indicated that while inflation has moved down from its peak, "it remains too high" and that returning to the 2% target will "require a period of below-trend economic growth as well some softening in labor market conditions." Powell further indicated that he would like to see sustained progress on reducing goods inflation. With regard to future growth, he stated: "there may be significant further drag in the pipeline." While he did not indicate if the Fed would achieve a soft landing, he did reiterate that the current rate is restrictive and confirmed that policy would return to being data-dependent. A drag in growth, however, does not appear to be the case this quarter. According to the Atlanta Fed's GDPNow estimate, U.S. GDP is forecasted to grow 5.6% in the third quarter. This rate is well above the trend and has been driven by strength in manufacturing, retail sales, and housing starts.

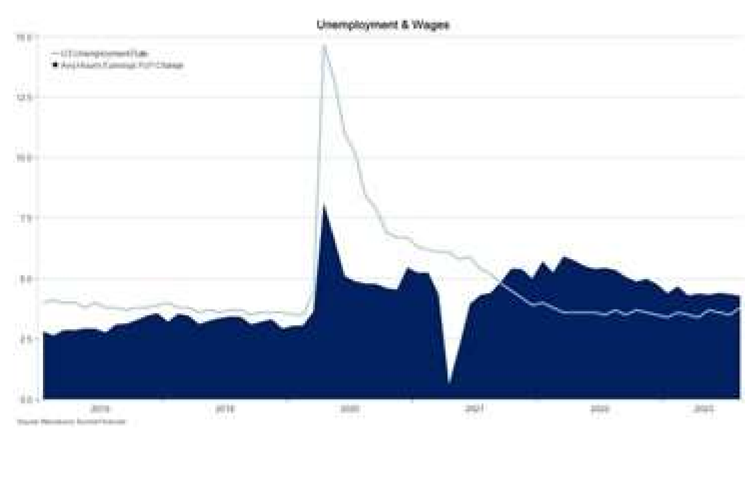
Looking forward, per the CME Fed Futures market, investors forecast that the Fed Funds rate will remain unchanged for the remainder of the year at 5.25% to 5.50%. By year-end 2024, futures markets predict that the Fed is likely to reduce rates by an estimated 75 basis points towards 4.5%. If this forecast holds, rates will remain at their highest levels since the 1999-2000 period.

Within fixed-income markets, the curve remains deeply inverted with short-term treasuries still offering the highest yield, peaking at the 3-month term with a yield of 5.56%. The 1-year U.S. treasury is at 5.37%, then yields drop to 4.85% for the 2-year and 4.23% for the 5-year. Earlier this month, credit rating agency Fitch downgraded U.S. credit from AAA to AA+. The near-term impact seemed muted as neither rates nor credit spreads moved notably in response to the downgrade. Credit spreads for both investment grade and high-yield corporate bonds remain in line with historic ranges from prior cycles. Inflation expectations remain contained with 5-year breakeven rates holding steady at 2.2%, very near the Fed's long-term target of 2%. Given the rise in long-term rates, extending duration, especially for investment-grade bonds, provides a reasonable risk-reward trade-off.

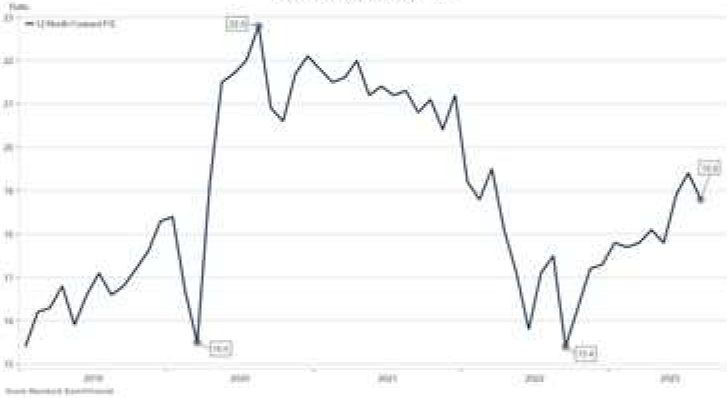
Corporate earnings were in line with expectations, but growth levels varied. In general, earnings across consumer-facing firms were weaker while earnings across enterprise technology and industrials were stronger. Notably, analysts have begun to raise estimates again. After cutting expectations over the past year, Q3 and Q4 2023 EPS estimates have been revised higher as have forecasts for 2024.

Globally, economic growth rates are mixed. Growth in China continues to struggle with Q3 GDP estimates expected to come in at 4.6%, versus 6.3% from the prior year. Expectations are for weaker growth in areas like manufacturing, production, and energy utilization. Eurozone GDP for Q2 came in flat compared to the previous quarter. France and Spain grew slightly at 0.5% and 0.4% respectively, while Germany was flat and Italy declined at 0.3%. GDP growth for Japan increased by 1.5% QoQ, which is the fastest expansion since Q4 2020.



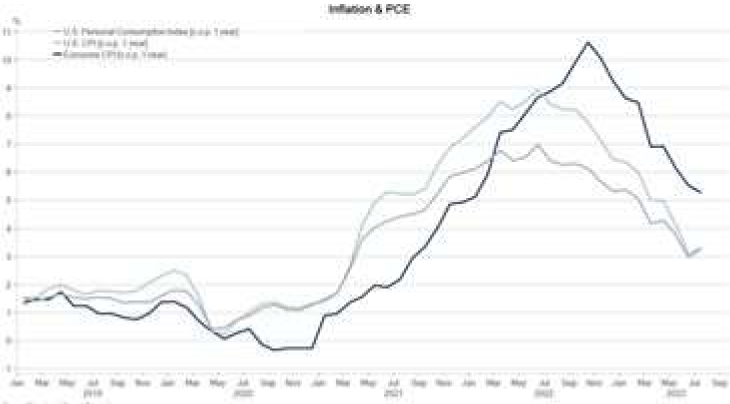


S&P 500 12-Month Forward P/E

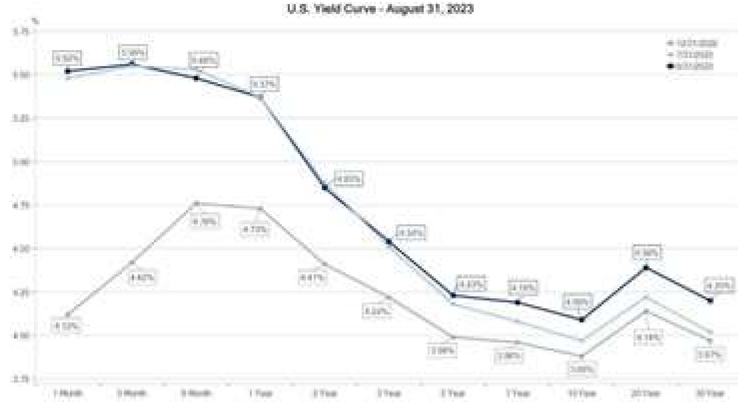


U.S. ISM Indices

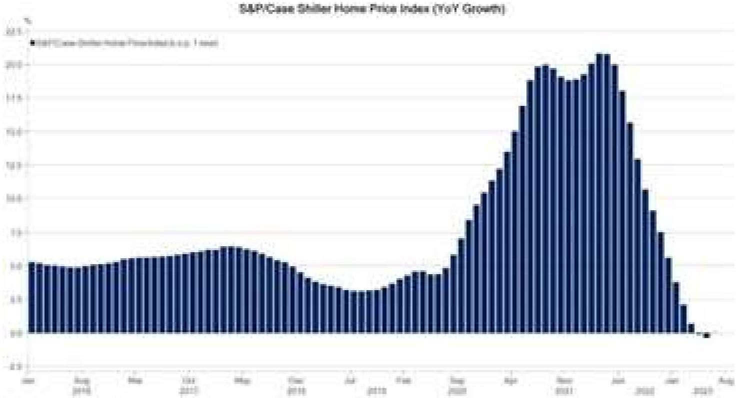
Inflation & PCE



U.S. Yield Curve - August 31, 2023



S&P/Case Shiller Home Price Index (YoY Growth)



Global 10-Year Bond Yields

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