

Beacon Weekly Investment Insights

The shortened week last week saw continued volatility in the equity markets, with the S&P 500 ultimately ending the week up 1.45%. The Dow also finished the week positive in positive territory, up 1.46%, with the Nasdaq up 0.98%. We continue to see downward pressure on commodities, and oil declined -8% for the week with WTI crude now trading at about \$73/barrel. The 10-year yield moved down from 3.88% to 3.56% to close the week.

The market's focus last week was primarily on the minutes released for the most recent Fed meeting in December, as well as on a variety of labor market data, including the closely watched payrolls report released last Friday. Markets initially retreated from positive territory after the release of the Fed minutes last Wednesday, before closing positive. The market was reacting to the minutes which ostensibly had a more hawkish tone than anticipated. The Fed minutes reflected that none of the 19 top Federal Reserve officials expected that it would be appropriate to cut interest rates this year. While Fed officials welcomed recent reports that showed moderating inflation data, they made it clear that they will want to see a lot more evidence that inflation is on a sustained downward trajectory before considering any kind of pivot in policy. With that said, we continue to see somewhat of a disconnect between what the Fed is saying, and what markets believes is likely to occur. Fed Funds futures, which show the market's expectation for the future path and level of the Fed Funds rate, are pricing in further interest rate increases in upcoming Fed meetings. At present, 0.25% increases are being priced in for both the February and March meetings which would bring the Fed funds rate to the 4.75%-5.00% level. However, the market currently expects that the Fed will pause further rate hikes thereafter, and is pricing in a potential 0.25% rate cut as soon as November.

There was also a significant amount of labor market data released last week. The JOLTS (job openings and labor turnover survey) showed job openings coming in just shy of 10.5 million, which was ahead of expectations for 10.1 million openings, and down a little from last month's reading. The report did show a slight decrease in hiring and a tick up in layoffs. However, for the time-being, the report is still showing a tight labor market and high demand for employment with open positions outnumbering available workers about 1.7 to 1. The ADP employment report came in significantly hotter than expected, with 235,000 jobs added in December, up substantially from the prior month's reading of 127,000 and well above expectations of 153,000 for this month. Likewise, the more closely watched nonfarm payrolls report last Friday showed an upside surprise as far as jobs added, coming in at 223,000 vs. expectations for an increase of 200,000. The market ultimately viewed the report favorably, keying in on moderating wage pressures with average hourly earnings up a less than expected 0.3% in December, while the unemployment rate moved down to 3.5%. This reading was down slightly from the prior 3.6% figure, and lower than the expected tick up to 3.7%. The moderation in average hourly earnings alongside a decrease in the unemployment rate adds some fuel to the fire for the discussion around a potential soft landing (moderating inflation and slowing growth, while avoiding a full-fledged recession) for the economy, although it is important to remember that this is of course only one report.

ISM Service Index data was also released last week, which showed a sharp decline in the services side of economy. The reading came down significantly to 49.6% from a prior reading of 56.5%, and was well below expectations of 55.1%. This is notable in that the reading turned negative for the first time since early on in the pandemic, and has now joined the recent ISM Manufacturing data in showing contraction in the economy with a reading below 50%.

The 4th quarter earnings season will kick off in earnest this week, with many of the large banks reporting earnings at the end of the week. Consensus estimates are for overall S&P 500 earnings to decline for Q4 '22. Although overall earnings growth is still expected to be moderately positive (future revisions to estimated earnings growth after Q4 earnings are reported notwithstanding) for 2023, earnings are expected to decline in the first half of the year. We think it important to note that slowing earnings growth or even a decline in earnings in a given year does

not necessarily correlate to negative market returns in that year, and that there are many historical examples of market returns being divorced from either earnings growth or declines. By way of example, looking back to what occurred as recently as 2020 during the height of the pandemic, S&P 500 earnings dropped precipitously by -32%, however the market finished the year up over 18% in the midst of highly accommodative monetary policy and stimulus. The converse occurred in 2018 in which S&P 500 earnings growth was 20+%, but the market was down by roughly -4%. Amongst many others, 2015 provides us with another example, in which earnings were down -15%, but the market finished in positive territory. With continued pressures on corporate profit margins and the expectation for a period of earnings declines being a meaningful focus for markets this year, we think it important to bear this in mind.

This week will be a lighter week in terms of economic data releases. Importantly, markets will be focusing on upcoming inflation data with the CPI report due out on Thursday. In addition, the University of Michigan consumer sentiment index reading is due out on Friday.

Market Scorecard:	1/6/2023	YTD Price Change
Dow Jones Industrial Average	33,630.61	(1.46)%
S&P 500 Index	3,895.08	(1.45)%
NASDAQ Composite	10,569.29	(0.98)%
Russell 1000 Growth Index	2,165.04	(0.32)%
Russell 1000 Value Index	1,533.98	(2.46)%
Russell 2000 Small Cap Index	1,792.80	(1.79)%
MSCI EAFE Index	1,995.78	(2.67)%
US 10 Year Treasury Yield	3.56%	-32 basis points
WTI Crude Oil	\$73.77	(8.09)%
Gold \$/Oz.	\$1,869.70	(2.38)%



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