Beacon Trust
INNOVATING WEALTH STRATEGY

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Beacon Weekly Investment Insights

It was another eventful week for the economy and markets, with a variety of economic data releases, corporate earnings reports, geopolitical developments, as well as additional comments from various members of the Fed, ultimately culminating in a positive week for equity markets. The S&P 500 closed the week up marginally by 0.36%, with the Nasdaq meaningfully outpacing and closing up 2.1% for the week. Treasury yields increased substantially off the back of a very strong jobs report, which we discuss further in our commentary below. The 2-year and 10-year treasury yield curve inverted further (2-year yield above the 10-year yield) with the 2-year treasury yield climbing all the way back up to 3.24%, retracing roughly 0.35% higher in just one week (a substantial move in a short period of time). The 10-year treasury yield ended the week at 2.83%.

As we noted last week, the Federal Reserve Open Market Committee increased interest rates by 0.75% on July 27th. During the press conference that followed the announcement, Chairman Jerome Powell's comments about potential future rate hikes were interpreted as more dovish by the market, with equity markets subsequently rallying. This was alongside the notion that was communicated during the press conference that although interest rates remain below where they ultimately need to be to stave off inflation, we are perhaps close to a "neutral" level for interest rates with the hikes that have occurred thus far. It is difficult to square this notion with persistently high levels of inflation, and with the labor market as strong as it is. To that end, several members of the Fed followed up those comments last week with a more hawkish tone, walking back the idea that we are close to "neutral" as far as interest rates, and reaffirming the Fed's commitment to aggressively tighten financial conditions to fight inflation. St. Louis Fed President James Bullard said last week that he is in favor of front-loading larger interest-rate hikes, ending the year with the Fed funds rate in the 3.75% - 4.00% range (currently at 2.25% - 2.50%). The Minneapolis Fed President Neel Kashkari, along with others, also reiterated the Fed's commitment to being aggressive in fighting inflation through further tightening of financial conditions.

In what was certainly the most impactful economic data for markets last week, the Labor Department released their jobs report for July which showed a substantial surprise to the upside. The report showed that the U.S. economy added 528,000 jobs in July, vs. expectations for 250,000 jobs added. In addition, the unemployment rate ticked down from 3.6% to 3.5%, matching the level seen before the onset of the coronavirus pandemic. Average hourly earnings increased 0.5% and 5.2% on a month-over-month and year-over-year basis, respectively (both outpacing expectations). The labor force participation rate did tick down from 62.2% to 62.1%. All in all, it was a very strong jobs report that will likely further embolden the Fed to be more aggressive with rate hikes, and calls into question the recent narrative in the markets as to the expectation that the Fed may pivot to a stance of actually cutting interest rates in the middle of next year. It is for this reason that equity markets turned negative after the report was released on Friday, despite what was positive news for the broader economy. The odds of a 0.75% interest rate hike increased meaningfully after the jobs report, with the Fed funds futures market pricing in a 70% probability of a 0.75% interest rate hike in the September meeting, and now projecting that the Fed funds rate will end the year at 3.75%. This dynamic has the potential to drive further volatility in equity and bond markets, as more interest rate hikes and a potentially extended time-frame for keeping higher interest rates in place, is priced into the markets.

Additional economic data released last week included the ISM (Institute for Supply Management) Manufacturing and Services PMI (Purchasing Managers Index) reports. Although still signifying growth with a reading over 50 percent, the Manufacturing PMI for July came in at 52.8 percent, ticking down from the prior month's reading of 53 percent and representing the lowest reading since June of 2020. The report showed new orders and employment contracting, alongside a slower rate of price increases. In contrast, the Services PMI report showed a surprise reading to the upside, coming in with a reading of 56.7 percent for July, up 1.4 percent from the June figure. The report denoted robust overall activity and growth in new orders, and also showed a moderation in prices.

Speaker Pelosi's visit to Taiwan last week was a large topic of conversation and controversy, at a time when geopolitical tensions are already elevated. The stock market took the visit in stride with the S&P 500 closing higher subsequent to Speaker Pelosi safely landing in Taipei last Wednesday, as China's initial response was not as aggressive as Chinese officials had warned could be the case. China subsequently responded by conducting military drills around Taiwan. The Foreign Ministry announced new measures later in the week including suspension of climate talks with the U.S. as well as on cooperation relative to a host of other issues, and announced sanctions against Speaker Pelosi. In addition, OPEC announced last week that they would be increasing oil production by 100,000 barrels/day, a far cry from the magnitude of production increases the Biden administration was hoping for off the back of President Biden's visit to Saudi Arabia. Ultimately, oil prices have moderated recently, and broke below $90/barrel for the first time since February.

As we referenced in last week's piece, an agreement was struck between Senate Majority Leader Chuck Schumer and West Virginia Senator Joe Manchin on a major health care, tax, and climate bill amounting to $740 billion, known as the Inflation Reduction Act. The bill aims to create a 15% corporate minimum tax rate, as well as to tax stock buybacks (a provision aiming to tax carried interest which affects how hedge funds and other asset managers are taxed looks like it will be removed), in an effort to somewhat blunt the impact of inflation on households, make healthcare and prescription drugs more affordable, and make energy security and climate change investments. The bill was narrowly passed in the Senate with Vice President Kamala Harris casting the tie-breaking vote, and is expected to be passed by the House later this week. We will continue to provide updates on this front.

Corporate earnings reports for the 2nd quarter continued to roll out last week, with the likes of semiconductor company Advanced Micro Devices (AMD), large-cap biotech companies Amgen and Vertex Pharmaceuticals, and travel and leisure companies Airbnb, Booking Holdings, and Expedia all reporting. AMD showed solid results that beat expectations for the 2nd quarter and was generally constructive looking ahead, but did warn on slowing PC demand. Amgen and Vertex pharmaceuticals likewise posted strong results that beat expectations, with the stocks reacting positively. We continue to assess our biotech holdings in the context of their financial models, the overall outlook for their drug portfolios and pipelines, and any potential impacts from the new bill we discussed above. The travel and leisure companies generally showed solid results amidst a significant recovery in travel demand, which the management of each of these companies broadly saw continuing in the 2nd half of the year. Overall, 87% of the companies in the S&P 500 have reported earnings for Q2 2022 as of the time of this writing, with 75% of companies reporting earnings above expectations. This improved from 73% of companies having exceeded expectations as of the prior week, but remains below the five-year average of 77%. As far as revenues, 70% of companies have reported revenues above expectations, which is above the five-year average of 69%. Broadly speaking, "better than feared" is the best way to characterize results thus far.

There will be no hiatus in the inflation discussion, with the CPI (consumer price index) and PPI (producer price index) reports due out on Wednesday and Thursday, respectively. In addition, the University of Michigan consumer sentiment index data is due out on Friday.

Market Scorecard:	**8/5/2022**	**YTD Price Change**
Dow Jones Industrial Average	32,803.47	(9.73)%
S&P 500 Index	4,145.19	(13.03)%
NASDAQ Composite	12,657.55	(19.10)%
Russell 1000 Growth Index	2,501.90	(18.64)%
Russell 1000 Value Index	1,516.14	(8.43)%
Russell 2000 Small Cap Index	1,921.82	(14.41)%
MSCI EAFE Index	1,941.71	(16.88)%
US 10 Year Treasury Yield	2.83%	132 basis points
WTI Crude Oil	$88.38	17.51%
Gold $/Oz.	1,791.00	(2.06)%