The Weekly Market Update – 5/1/23: GDP Misses Final Estimates; Don't Blame Consumers

Major Indices (Price Returns)	Close	Last Week	Quarter-to-Date	Year-to-Date	Trailing 12-Months	All-Time High	% to High
S&P 500	4,169.48	0.87%	1.46%	8.59%	0.91%	4,796.56	15.0%
Dow Jones Industrial Average	34,098.16	0.86%	2.48%	2.87%	3.40%	36,799.65	7.9%
NASDAQ Composite	12,226.58	1.28%	0.04%	16.82%	-0.88%	16,057.44	31.3%
Russell 2000	1,768.99	-1.26%	-1.86%	0.44%	-5.10%	2,442.74	38.1%
MSCI EAFE (USD)	2,143.85	-0.11%	2.45%	10.28%	5.42%	2,398.71	11.9%
MSCI Emerging Markets (USD)	977.05	-0.38%	-1.34%	2.16%	-9.21%	1,444.93	47.9%
Bloomberg Commodity Index	104.31	-1.20%	-1.13%	-7.53%	-19.44%	237.95	128.1%
Barclays U.S. Aggregate Bond	91.47	0.77%	0.42%	2.91%	-2.55%	112.07	22.5%

Source: FactSet

The U.S. economy grew 1.1% in the first quarter of 2023 (1Q23), missing the 1.9% FactSet consensus estimate (from Wall Street economists). The U.S. Bureau of Economic Analysis' (BEA) first measurement of the quarter's real (inflation-adjusted) gross domestic product, or GDP (the annualized growth rate of the value of goods and services produced in the quarter), was also below 4Q22 U.S. GDP of 2.6%, indicating that economic growth deceleration was more than expected. However, consumer spending, the largest component of the U.S. economy in the first quarter (comprising 71% of total annualized real GDP), grew 3.7%, contributing 2.5% (well above the 1.1% reported) to the GDP number. This was the strongest consumer contribution to GDP growth in the past seven quarters as spending on both goods (first quarterly growth since 4Q21) and services (positive for the 11th consecutive quarter) surged. Goods spending was largely driven by automotive sales, while growth in services was spread across multiple categories, including health care, travel, restaurants, and hotels. We view early 2023 consumer spending strength as an unexpected positive surprise, following weaker and decelerating trends to close out 2022. We attribute renewed consumer strength and resiliency to multiple factors, paced by ongoing monthly jobs gains (reported by the Bureau of Labor Statistics, BLS), and also helped by residual pent-up demand following a relatively weak 2022 holiday season, relatively mild winter weather in many U.S. geographies, and excess savings accumulated by many consumers during the COVID-19 work-from-home orders and government stimulus payments. Offsetting the 1Q23 consumer strength, business investment decelerated to its lowest growth in three quarters (investment in equipment was negative) and housing, despite improvement, was negative for the eighth consecutive quarter. The largest negative component of 1Q23 GDP growth was inventories, which subtracted 2.3% from total GDP. This suggests that companies were meeting demand from products previously produced. This could reflect potential slower demand ahead, but also indicates that at some point inventory levels must be replenished. Even consumer spending decelerated during the quarter, as monthly data from the BEA showed that February and March were lower than January, suggesting potential lower GDP growth in 2Q23.

We expect the U.S. Federal Reserve Bank (Fed) will raise its short-term interest rate targets yet again this week. The Fed's Open Market Committee (FOMC) will conclude its third 2023 policy meeting this week on 5/3/23. We agree with consensus expectations that the Fed will lift its overnight bank lending fed funds interest rate target range by 0.25% to 5.00% to 5.25%. This would be the tenth consecutive FOMC meeting with a hike in the rate target as the Fed uses its tool of higher short-term interest rates to slow economic growth and inflation. While Fed hikes have placed pressure on housing (higher mortgage rates) and regional banks (higher deposit rates), consumer spending has remained robust. We are interested in Fed commentary on both the banking sector as well as the pace of consumer spending in March compared to January.

The first week of May includes earnings reports, the Tuesday/Wednesday FOMC meeting and April jobs data on Friday. Through early Monday, 54% of S&P 500 constituents had reported 1Q23 financial results, with 162 companies, or 32% scheduled to report this week. The FactSet consensus now expects a -3.7% earnings decline vs. -6.7% estimated as of 3/31/23. Jobs data from the BLS is expected to show an April gain of 182 thousand (K), a slower pace than 236K in March.

James D. Ragan, CFA
Director of WM Research
(206) 389-4070
jragan@dadco.com

Important Disclosure: The information contained herein has been obtained by sources we consider reliable, but is not guaranteed and we are not soliciting any action based upon it. Any opinions expressed are based on our interpretation of data available to us at the time of the original publication of the report. Assumptions, opinions, and estimates constitute our judgment as of the date of this report and are subject to change without notice. Investors must bear in mind that inherent in investments are the risks of fluctuating prices and the uncertainties of dividends, rates of return and yield, as well as broader market and macroeconomic fluctuations and unforeseen changes in the fundamentals or business trends affecting the securities referred to in this report. Investors should also remember that past performance is not indicative of future performance and D.A. Davidson & Co. makes no guarantee, express or implied, as to future performance. The information is not intended to be used as the primary basis of investment decisions. Because of individual client requirements, it should not be construed as advice designed to meet the particular investment needs of any investor. It is not a representation by us, or an offer, or the solicitation of an offer, to sell or buy any security. Further, a security described in a report may not be eligible for solicitation in the states in which a client resides. D.A. Davidson & Co. does not provide tax advice and investors should consult with their tax professional before investing. Further information and elaboration is available upon request.

Market Indices: The information on indices is presented for illustrative purposes only and is not intended to imply the potential performance of any fund or investment. Indices provide a general source of information on how various market segments and types of investments have performed in the past. Index performance assumes the reinvestment of all distributions, but does not assume any transaction costs, taxes, management fees, or other expenses. You may not invest directly in an index. Past performance is not an indicator of future results. The Russell 2000® Index is a market cap weighted index that measures the performance of the 2,000 smallest companies in the Russell 3000® Index. The S&P 400 Index is a market cap weighted index comprised of U.S. stocks in the middle capitalization range, generally considered to be between $200 million and $5 billion in market value. The S&P 500 Index is a market cap weighted index that is designed to measure the US large-cap equity performance. The index is composed of the 500 leading publically traded US companies based on size, liquidity, industry, and profitability criteria. The Dow Jones Industrial Average is a price weighted index that tracks 30 large, publicly-owned companies trading on the New York Stock Exchange (NYSE) and the NASDAQ. The MSCI EAFE® Index (Europe, Austral, Asia, Far East) is a free float-adjusted market capitalization index that is designed to measure developed market equity performance, excluding the US and Canada. The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets.