The Weekly Market Update – 5/15/23: Range-Bound Market and Narrow Leadership

Major Indices (Price Returns)	Close	Last Week	Quarter-to-Date	Year-to-Date	Trailing 12-Months	All-Time High	% to High
S&P 500	4,124.08	-0.29%	0.36%	7.41%	-0.19%	4,796.56	16.3%
Dow Jones Industrial Average	33,300.62	-1.11%	0.08%	0.46%	0.98%	36,799.65	10.5%
NASDAQ Composite	12,284.74	0.40%	0.51%	17.37%	-0.40%	16,057.44	30.7%
Russell 2000	1,740.85	-1.08%	-3.42%	-1.16%	-6.61%	2,442.74	40.3%
MSCI EAFE (USD)	2,126.26	-0.86%	1.61%	9.38%	4.55%	2,398.71	12.8%
MSCI Emerging Markets (USD)	973.00	-0.88%	-1.75%	1.74%	-9.59%	1,444.93	48.5%
Bloomberg Commodity Index	101.18	-1.72%	-4.10%	-10.30%	-21.86%	237.95	135.2%
Barclays U.S. Aggregate Bond	91.12	-0.25%	0.04%	2.52%	-2.92%	112.07	23.0%

Source: FactSet

Despite no shortage of concern leaning on investor sentiment, widely followed U.S. equity indices in the second quarter (2Q23) are range-bound with limited volatility. While widely followed, large-company equity indices have posted strong year-to-date (YTD) gains in 2023 (the S&P 500 index was up +7.4%, not including dividends, YTD through 5/12/23), returns in 2Q23 have moderated. As of 5/12/23, the S&P 500 was down -1.1% in May, and still holding a +0.4% gain in 2Q23. One measure of volatility that we watch is the daily price movement of the S&P 500; specifically, the number of individual trading days that the index closing price changes at least 1.0% (up or down) vs. the previous day's closing price. In 2022, the S&P 500 made a plus or minus 1% move on 130 of 250 trading days, or 52%. In 1Q23, the index closing price changed by at least 1% on 47% of trading days, but in 2Q23 (through 5/12/23) just 17% of closing prices reflected a 1% daily change. The drop in daily volatility is perhaps unexpected as markets in general evaluate economic growth concerns, weak corporate earnings performance, and a political battle over the U.S. government debt limit, and we remain concerned about relatively narrow gains (lack of broad participation across companies and sectors). The U.S. economy grew +1.1% in 1Q23 (according to the Bureau of Economic Analysis, BEA; first report of gross domestic product, or GDP). This was below 4Q22 and 3Q22 GDP growth of +2.6% and +3.2%, respectively. The FactSet consensus estimate (from Wall Street economists) for 2Q23 GDP growth is just +0.4%. Through 5/12/23, more than 90% of S&P 500 companies had reported earnings results for the March/April quarter. While percentage Y/Y earnings growth has exceeded the -6.6% decline estimated (FactSet) on 3/31/23, earnings are down -2.5% in 1Q23 vs. 1Q22, the second consecutive quarter of lower Y/Y earnings. In 2Q23, while the market capitalization-weighted S&P 500 (the largest companies comprise a larger portion of the index) has gained +0.4%, the equal-weighted S&P 500 index (all companies have the same weight) was down -2.3%, and for 2023 YTD, the equal weight index was up just +0.1%. The combination of low volatility and narrow participation in YTD gains suggests to us that additional equity market gains could be limited over the medium term.

One reason for reduced equity market volatility in recent weeks is that investors could be waiting for resolution on the approaching deadline for the U.S. Congress to pass an increase in government borrowing capacity. With U.S. federal borrowing coming up against the $31.4 trillion limit authorized by Congress, the House, Senate and President must authorize a higher limit, or risk an inability to pay certain government commitments. While the exact timing is uncertain as the Treasury has the ability to move funds around using accounting measures, Treasury Secretary Janet Yellen has given 6/1/23 as a tentative deadline for an agreement. There is no question that the debt limit must be raised as the U.S. government continues to operate with an annual deficit. We expect a resolution to go down to the wire as a divided Congress (the House controlled by Republicans and the Senate by Democrats) makes a nasty fight all but inevitable, in our view. This increases the risk of heightened volatility as the deadline approaches, especially given the recent lack of volatility as discussed above.

The pace of earnings reports slows this week, but key economic data is expected in the areas of consumer spending and housing. Earnings reports are expected from a few large retailers and Technology companies, but focus will shift to reports on April retail sales and housing starts (both from the Census Bureau).

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