JUNE 13, 2022

Weekly Market Update

General Market News

- The U.S. Department of Labor released its May inflation numbers last Friday. The Consumer Price Index (CPI) report showed that inflation increased 8.6 percent year-over-year, coming in above analyst expectations for an 8.3 percent increase. The FOMC has been closely watching CPI for any signs of cooling inflation as we approach the 6/14–6/15 meeting, and it's likely concerned that the numbers remain frustratingly elevated. This latest report certainly bolsters expectations for consecutive 50 basis point (bp) rate hikes at the next two meetings. It also perpetuates worries about the Federal Reserve (Fed)'s ability to engineer a soft landing as inflation persists and economic growth expectations slow. U.S. Treasury yields were up across the curve last week. The 2-year, 5-year, 10-year, and 30-year rose 15 bps (to 2.81 percent), 13 bps (to 3.07 percent), 10 bps (to 3.04 percent), and 8 bps (to 3.17 percent), respectively.

- Global equity markets sold off as a higher-than-expected inflation report on Friday led to added concerns about persistent inflation and the need for more aggressive actions from global central banks. The headline and core reports showed surprising results of 1.0 and 0.6 percent, up by 0.3 and 0.1 percent, respectively. While we've seen inflation for goods slow, food and energy continue to accelerate their pace of inflation as supply chain disruptions—caused by the Russia-Ukraine conflict, Covid-19 lockdowns, and weather—create a challenged supply environment. Goods have slowed as price increases of household furnishings, appliances, and new automobiles have eased. This potentially reflects some of the consumer-related results we've been seeing from Target (TGT) and Walmart (WMT) in recent weeks as product purchases have shifted, leading to heavy markdowns in home furnishings, appliances, and other big-ticket items. The breadth of inflation continues to pick up, which will likely force the Fed to take a September pause off the table.

- On Friday, the May CPI report was released. Headline consumer prices increased 1 percent, which was up from the 0.3 percent increase in April and higher than the expected 0.7 percent. On a year-over-year basis, consumer prices rose 8.6 percent in May against calls for an 8.3 percent increase. This marks a 40-year high for year-over-year consumer inflation, which is disappointing given calls for a potential peak in headline inflation in April. Core consumer prices, which strip out the impact of volatile food and energy prices, rose 0.6 percent during the month and 6 percent on a year-over-year basis against forecasts for 0.5 percent monthly and 5.9 percent year-over-year increases. Consumer prices have faced notable inflationary pressure over the past year, with the initial surge focused primarily on rising costs for goods. We've recently started to see prices for services face more sustained upward pressure, which contributed to larger-than-expected boosts in headline and core inflation.

- Friday also saw the release of the preliminary estimate of the University of Michigan Consumer Sentiment survey for June. Sentiment soured more than expected during the month and the index fell from 58.4 in May to 50.2 in June against calls for a more modest drop to 58.1.
This larger-than-expected decline was due to worsening consumer views on both the current economic condition and future expectations, and it brought the index to a new record low. The primary cause for worsening views was rising concerns about inflation, as 46 percent of respondents attributed their negative views to inflation, up from 38 percent in May. The report also showed that consumer expectations for inflation increased in both the short and long term, which is a potential cause for concern. All in all, this report was another reminder of the negative impact high levels of inflation can have on the overall economy.

Market Index Performance Data

EQUITIES

Index	Week to Date	Month to Date	Year to Date	12 Month
S&P 500	–5.04	–13.62	–17.60	–6.83
Nasdaq Composite	–5.59	–20.12	–27.26	–18.84
DJIA	–4.56	–9.05	–12.78	–7.19
MSCI EAFE	–4.65	–10.51	–15.80	–16.06
MSCI Emerging Markets	–0.53	–7.10	–13.58	–21.88
Russell 2000	–4.37	–12.83	–19.39	–22.04

Source: Bloomberg, as of June 10, 2022

FIXED INCOME

Index	Month to Date	Year to Date	12 Month
U.S. Broad Market	–1.90	–10.65	–10.50
U.S. Treasury	–1.68	–9.87	–9.60
U.S. Mortgages	–2.06	–9.20	–9.58
Municipal Bond	–0.81	–8.22	–8.16

Source: Morningstar Direct, as of June 10, 2022

What to Look Forward To

On Tuesday, the Producer Price Index report for May is set to be released. As was the case with consumer inflation, producer inflation is expected to remain high. Headline producer prices are expected to increase 0.8 percent during the month and 10.8 percent on a year-over-year basis. Core producer prices, which strip out the impact of food and energy prices, are set to increase 0.6 percent during the month and 8.6 percent on a year-over-year basis. Producer prices have faced persistent inflationary pressure over the past year, driven, in large part, by rising material costs and tangled global supply chains. If estimates hold, this report would be another sign that inflationary pressure remains high throughout the economy despite recent efforts from the Fed to tighten monetary policy to combat inflation. Given the prospects for continued high inflation in the months ahead, the Fed is expected to focus on tighter policy throughout the year and into 2023.

On Wednesday, the May retail sales report will be released. Retail sales are expected to increase 0.2 percent during the month, following a 0.9 percent increase in April. Core retail sales, which strip out the impact of volatile auto and gas sales, are set to increase by a more solid 0.5 percent following a 1 percent increase in April. Retail sales have held up well in 2022 following a lull in sales last December. If estimates hold, this would mark five consecutive months of retail sales growth. The consistent sales growth is a positive sign for the health of the economy given the importance of consumer spending on overall economic activity. The sales growth throughout the year has been especially impressive given the headwinds created by health risks at the start of the year, sinking consumer confidence, and persistently high levels of consumer inflation.

Wednesday will also see the release of the National Association of Home Builders Housing Market Index for June. This measure of home builder confidence is

What to Look Forward To (continued)

expected to decline modestly during the month, with the index set to drop from 69 in May to 68 in June. This is a diffusion index where values above 50 indicate expansion, so this anticipated result would be a sign of continued growth for the home building industry. Home builder confidence had previously been well supported by high levels of home buyer demand and a low supply of existing homes for sale during the past two years. That said, we've seen confidence falter in 2022 due to rising material and labor costs along with signs of slowing prospective home buyer demand. Builder backlogs remain long, so new home construction should continue at a strong pace in the months ahead; however, rising mortgage rates and continued high housing costs could serve as headwinds for notably faster construction growth.

The third major release on Wednesday will be the FOMC rate decision from the Fed's June meeting. The central bank started raising interest rates back at its March meeting, with a 25 bp hike to the federal funds rate that was followed by an additional 50 bp hike at the May meeting. Economists and markets expect to see another 50 bp hike at the June meeting. This will be a widely monitored release given the higher-than-expected consumer inflation in May and the Fed's ability to cause potential market volatility. Looking forward, markets anticipate another 50 bp hike at both the July and September FOMC meetings, which signals tighter financial conditions ahead. Given the continued strength of the labor market and the high levels of inflation, the Fed is expected to focus on combating inflation with tighter policy throughout the rest of the year.

On Thursday, the May building permits and housing starts reports will be released. Permits are expected to decline 1.8 percent during the month, while starts are set to drop 1 percent. While both of these measures on new home construction are expected to decline in May, they are expected to remain well above pre-pandemic levels and near post-pandemic highs. Demand for new houses has started to fade given the increase in mortgage rates this year, but it remains relatively strong on a historical basis. Given the continued lack of supply of existing homes for sale, new home construction is expected, although we may see a slowdown in the months ahead due to the headwinds currently affecting the housing sector.

We'll finish the week with Friday's release of the May industrial production report. Production is set to grow 0.4 percent following a 1.1 percent increase in April. Hotter-than-normal weather caused utility production to increase notably, which should help support overall industrial production. We've also seen mining and drilling output increase with the rise in oil and gas prices. Manufacturing production is also expected to show continued growth during the month, with economists calling for a 0.2 percent increase in May following a 0.8 percent rise in April. If estimates hold, this would be the fifth straight month with increased industrial production and the fourth straight month with rising manufacturing production. High levels of consumer and business demand for manufactured goods have helped support the improvements in production we've seen so far this year. But looking forward, the industry is expected to face headwinds from rising prices and supply chain constraints.

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