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Weekly Market Flash
A slowly, but most likely surely, economic slowdown

April 23, 2023

Following a busy few weeks, this week was fairly light in terms of data and macro events. Markets took the opportunity to consolidate, and to focus on the earnings season that has just begun—especially in anticipation of the big names in technology releasing earnings next week.

Highlights

▪ The Fed's Beige Book revealed a number of things, which on balance suggest an ongoing economic slowdown after a decidedly strong and above-expected first quarter.

▪ The final release of Q1 GDP should be around 2.5% annualized growth in real terms.

▪ 87 S&P 500 index companies reported their earnings, with an average earnings surprise of +5.3% and average sales surprise of +1.9%. Of the 87 companies, 66 (76%) delivered positive earnings surprises with most of these positive surprises taking place in the consumer discretionary sector (around +20.0%).

▪ Technology was the only sector to-date to deliver on average a negative earnings surprise (-11.9%).

Markets & Macro | A slowly, but most likely surely, economic slowdown

Focus on the US debt ceiling grows.

This week, there were some data releases in the US—but they sent slightly mixed signals. We therefore take a look at the release of the Federal Reserve's Beige Book (published Wednesday), to summarize and describe the state of the US economy:

- Both consumption and manufacturing activity remained stable or declined slightly, as did transportation and residential housing;
- Activity remained roughly stable, with nine districts indicating unchanged or little change and just three districts showing moderate growth;
- Credit volumes and demand for credit fell, and lending standards were tightened in five areas, with particular mention from New York state;
- Job creation has declined, with many districts reporting a less tight labor market and an increase in labor supply. Wage pressures have also decreased (this confirms what we are seeing across other labor market indicators, such as jobless and continuing claims, which point to a slowdown in the labor market);
- Good news on the price front, which continues to fall, in most of the districts analyzed.

"Credit volumes and demand for credit fell, and lending standards were tightened in five areas..."

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Figure 1: Year-to-Date Performance of Major Indices

Equity Indices	Last Value	Week	Ytd
MSCI World	2,823.07	-0.08%	9.26%
Nasdaq	12,072.46	-0.42%	15.64%
S&P 500	4,133.52	-0.09%	8.20%
S&P Equal Weighted	5,885.71	0.18%	3.10%
DJ Industrial	33,808.96	-0.19%	2.65%
Nikkei	28,564.37	0.25%	10.48%
Euro Stoxx 50	4,408.59	0.41%	17.18%
Swiss SMI	11,460.58	1.08%	9.66%
FTSE 100	7,914.13	0.59%	7.58%
Canada	20,693.15	0.55%	7.83%
Shenzen	4,032.57	-1.44%	4.21%
Hong Kong	20,075.73	-1.78%	1.91%
MSCI EM	980.74	-1.95%	3.09%

Equity Sectors	Last Value	Week	Ytd
S&P Value	152.99	0.35%	5.97%
S&P Growth	64.25	-0.46%	10.16%
S&P Defensives	1,576.86	0.94%	3.11%
ARK Fund	37.63	-2.99%	20.45%
FANGS	5,942.87	-1.69%	33.66%
S&P Banks	82.90	-0.05%	-16.97%
Euro Stoxx Banks	84.98	-0.34%	14.65%
S&P Energy	84.98	-2.58%	-1.85%
Gold Miners	33.61	-4.22%	17.27%

Commodities	Last Value	Week	Ytd
BBG Commodities	105.58	-2.08%	-6.41%
BBG Agriculture	68.09	-1.47%	-1.07%
Gold	1,983.06	-1.05%	8.72%
Silver	25.08	-1.04%	4.72%
BBG Brent Crude TR	1,031.92	-5.04%	-2.82%
BBG WTI Crude Oil TR	187.68	-5.21%	-1.89%

FX	Last Value	Week	Ytd
DXY Index	1,225.11	0.27%	-1.72%
EUR/CHF	0.9806	-0.22%	-0.90%
GBP Index	635.51	0.37%	2.03%
EM FX Index	1,689.48	-0.59%	1.74%
USD/JPY	134.16	0.28%	2.32%
USD/CNY	6.89	0.32%	-0.10%
Bitcoin	27,259.50	-10.54%	64.81%

Bond Indices	Last Value	Week	Ytd
US Inv Grade	109.00	-0.36%	4.39%
US High Yield	74.99	-0.39%	3.43%
Euro Corps	231.65	-0.02%	1.75%
JPM Europe Govies	9,549.94	-0.45%	3.47%
US Treasuries	2,246.54	-0.25%	2.66%
China Aggregate	260.69	-0.50%	2.12%
EMBI Global	782.40	-0.95%	1.84%
EMBI Local	129.88	-0.44%	5.00%

Source: Bloomberg, as at April 21, 2023. Performance figures in indices' local currencies.

Our view: The balance, thus far, seems to be that of an ongoing economic slowdown after a decidedly strong and above-expected first quarter, which should see the final release of Q1 GDP (released next week) around 2.5% annualized growth in real terms.

On the other hand, the focus on the debt ceiling continues to grow after the US Treasury released data on tax payments that were significantly lower than expected. The Treasury should run out of funds as early as June, whereas previously it was estimated that the deadline would come in September. Now, this is certainly not the first time that the US would come close to the brink of default, and usually the political conflict is resolved with a watered-down compromise. However, this matter is always used as a blackmail tool and wall-to-wall can end up unnerving the market—as happened not too long ago in August 2011, when volatility exploded, partly due to low summer liquidity.

“In absolute terms, however, the index is reporting the largest year-on-year decline in earnings since Q2 2020.”

Equities | Waiting for Godot…

Big Tech guidance in the spotlight next week.

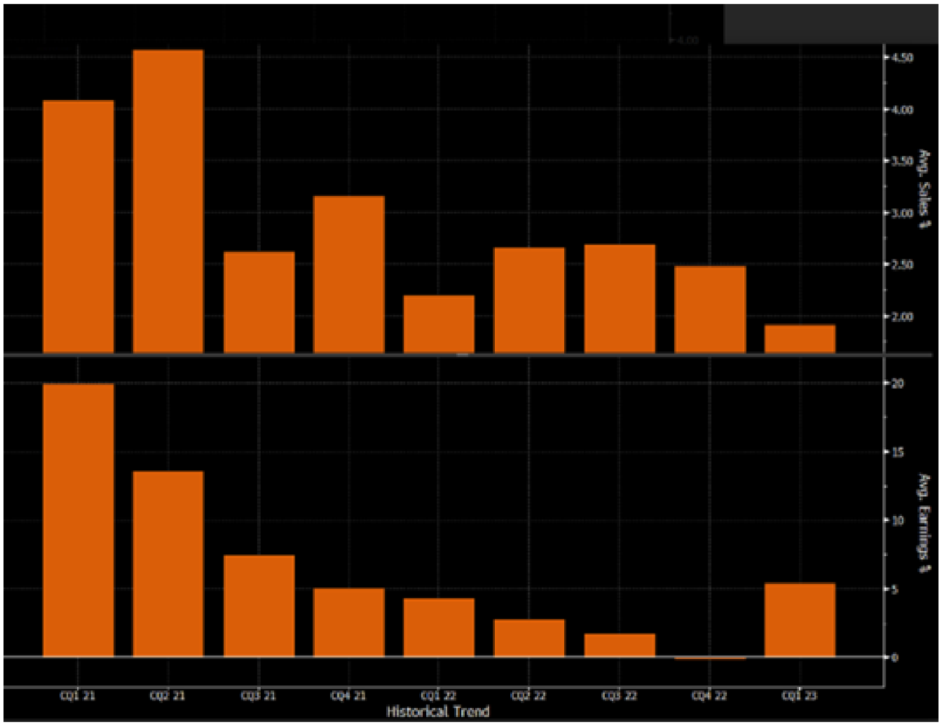
In a week relatively void of economic data, the Q1 earnings reports took center stage. According to Bloomberg, 87 S&P 500 index companies reported their earnings as of Friday, with an average earnings surprise of +5.3% and average sales surprise of +1.9%.

Of the 87 companies, 66 (76%) delivered positive earnings surprises with most of these positive surprises taking place in the consumer discretionary sector (around +20.0%). Technology was the only sector to-date to deliver on average a negative earnings surprise (-11.9%). On balance, the earnings season has, so far, been fairly positive with the magnitude of earnings beats coming in higher relative to the last four quarters. In absolute terms, however, the index is reporting the largest year-on-year decline in earnings since Q2 2020.

"We expect next week to be very dynamic with 180 S&P 500 index companies scheduled to report their Q1 earnings..."

One notable report for the week came from Procter & Gamble (PG US), which gave some interesting insight into consumer behavior. P&G delivered a solid beat and raised its 2023 sales guidance. Net sales for Q1 were up 4%, with organic sales up 7%. Volumes, however, fell 3% for the fourth consecutive quarter as cost-sensitive consumers opted for cheaper alternatives. A 10% year-on-year price increase helped offset that volume decline. Management noted, however, that volumes are improving from last quarter; in the US volumes increased and are beginning to pick up in China.

Figure 2: Average Sales and Earnings



Source: Bloomberg, as at April 21, 2023.

Our view: Since the beginning of April, the S&P 500 index has been range bound between the 4,056 and 4,133 levels, and unable to break out of the psychologically-important 4,200 level. Meanwhile, the CBOE Volatility Index (VIX) is at its lowest level since late 2021. We expect next week to be very dynamic with 180 S&P 500 index companies scheduled to report their Q1 earnings, including Alphabet, Microsoft, Visa, Meta and Amazon.

"With investors seemingly reluctant to decide if signs of labor market weakness are positive or negative, we expect markets to focus intently on the guidance of Big Tech..."

Semiconductor companies and semiconductor equipment manufactures' Q1 reporting season raised more concerns than hope. ASML's solid print was overshadowed by order book lumpiness, suggesting that customers might be looking to cut their CapEx. TSMC pushed out their expectation of the sector's inventory rebalancing to Q3 of this year instead of Q2. This warning came on the heels of IDC's gloomy estimate for PC sales in Q1; 29% worldwide shipment contraction, with Apple faring the worst with a 40.5% year-on-year drop.

With investors seemingly reluctant to decide if signs of labor market weakness are positive for equities (as it suggests a reduced chance of further rate hikes), or negative (as it also suggests a higher chance of a recession), we expect markets to focus intently on the guidance of Big Tech and to look for confirmation of their earnings resiliency. Microsoft, we think, will be particularly important with Artificial Intelligence expectations lately overriding the reality of softer demand, especially in PC sales.

Week Ahead | Key events to watch for

- **It will be a heavy week with both macro data and corporate earnings** (with almost all the Big Techs reporting).
- **In Europe there will be inflation data**; in Japan the central bank reunites, and there is a possibility that the new governor will make some innovative decisions.
- **In the US, first quarter GDP**, and Employment Cost Index and consumer confidence will be published.

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