The Longo Group

Independent Financial Firm

Week Ahead

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The Longo Group
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Week of
June 20, 2023

Peak Inflation, Peak Rates, Earnings Improving, Bearish Positioning = Markets Higher

Last week, both the Consumer Price Index (CPI) and the Producer Price Index (PPI) came in softer than expected. After 10 consecutive rate hikes, the Federal Reserve decided to pause this month and not raise rates again BUT with the caveat that they are likely not done raising rates.

The Fed did say they remain "data dependent" month to month. While the market is already pricing in an additional 25-basis point rate hike in July, it is really looking beyond these actions, believing that we are coming to the end of the higher rate cycle. What's fueling this belief? In part: all the positive earnings estimates we're seeing. Global markets have also gotten excited and rallied because China is stimulating its economy by cutting rates. Why? Its economy is not recovering as expected and remains weak.

CPI Year on Year Has Peaked

Source: Bloomberg, June 16, 2023

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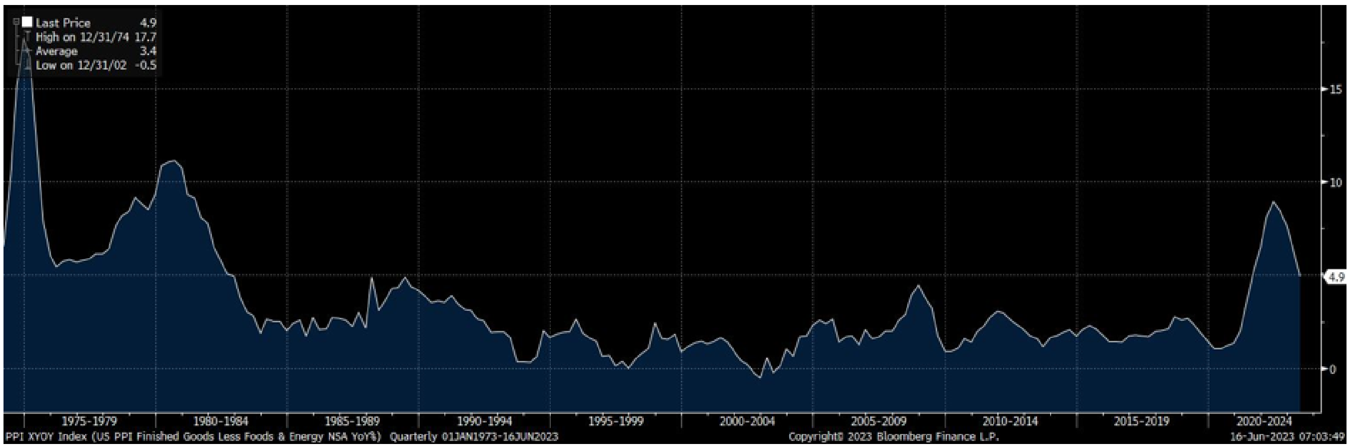
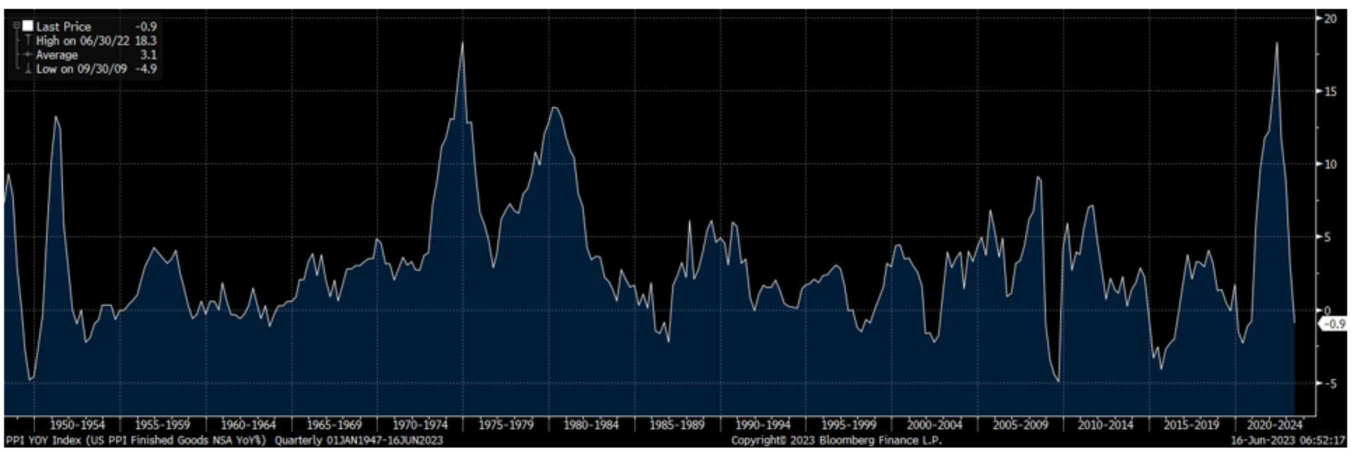
PPI Finished Goods Less Food and Energy Year over Year Has Peaked



Source: Bloomberg, June 16, 2023

PPI Finished Goods Year on Year Has Peaked and Has Moved Negative!!!



Source: Bloomberg, June 16, 2023

Interest Rates Are Peaking

10-Year Treasury Yield – Expecting a Fall to 2.5%

Source: Bloomberg, June 9, 2023

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2-Year Treasury Yield – Forming a Top? We Think So – Rates to Fall

Source: Bloomberg, June 16, 2023

Dressing Up is Always Fun

Kids love to dress up and so do the markets -- buying what is working and selling what is not working, it's all just window dressing. And it's happening now as the equity markets continue to rally. Many investors remain underweight or short the equity market as we approach 2Q performance. We believe investors are dressing up their portfolios to have more exposure to stocks – notably the winners that have been surging in the equity market.

Earnings are Coming Back!

The equity markets discount future data – especially earnings – and earnings are forecast to come back!!! Equity markets don't move sustainably on economic data, they move on earnings. According to FactSet, analysts project earnings growth to return in the second half of 2023. For Q3 2023, the estimated earnings growth rate is 0.8%. For Q4 2023, the estimated earnings growth rate is 8.2%. If 8.2% is the actual growth rate for the quarter, it will mark the highest year-over-year earnings growth rate reported by the S&P 500 since Q1 2022 (9.4%). What is driving the expected improvement in earnings growth in Q4 2023?

At the sector level, 9 of the 11 sectors are predicted to report year-over-year earnings growth in Q4 2023. Five of these 9 sectors are expected to report double-digit earnings growth for the quarter: Communication Services (36.3%), Utilities (26.2%), Consumer Discretionary (21.3%), Information Technology (12.4%), and Financials (11.2%). The Communication Services and Information Technology sectors are expected to be the largest contributors to earnings growth for the fourth quarter of all 11 sectors. If these two sectors were excluded, the estimated earnings growth rate for the S&P 500 for Q4 2023 would fall to 3.9% from 8.2%.

At the company level, Amazon, Meta Platforms, Alphabet, and NVIDIA are expected to be the largest contributors to earnings growth for the S&P 500 for Q4 2023. Amazon, Meta Platforms, and NVIDIA are expected to report year-over-year EPS growth of more than 100% in Q4 2023. In addition, analysts have increased EPS estimates for all four companies for the fourth quarter since December 31. If these four companies were excluded, the estimated earnings growth rate for the S&P 500 for Q4 2023 would fall to 4.2% from 8.2% but would remain positive!!!

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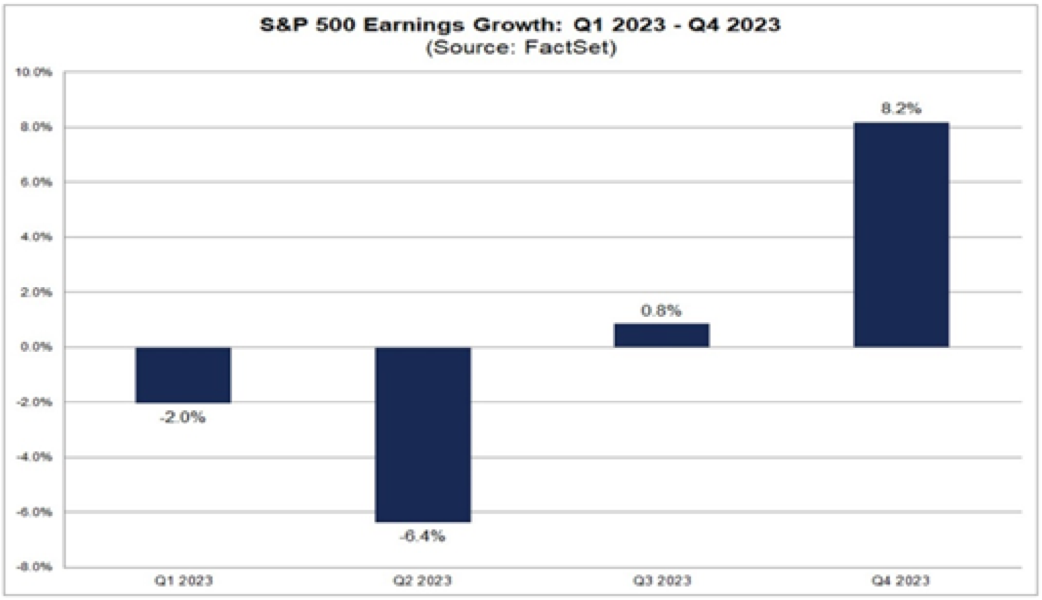
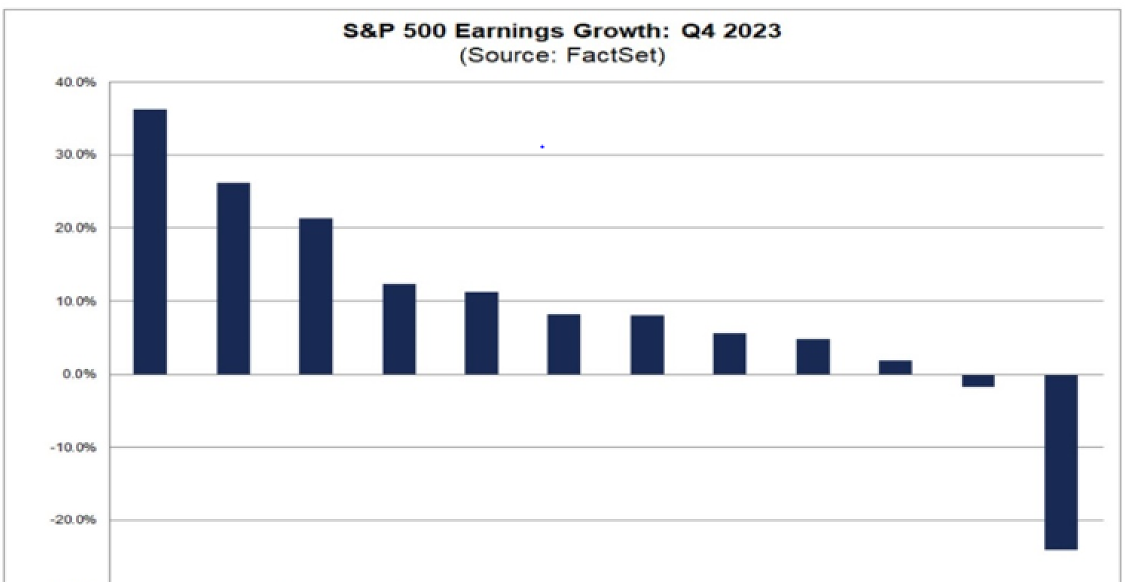


Source: FactSet, June 9, 2023



	Comm. Services	Utilities	Consumer Disc.	Info. Technology	Financials	S&P 500	Industrials	Consumer Staples	Real Estate	Health Care	Materials	Energy
■Earnings	36.3%	26.2%	21.3%	12.4%	11.2%	8.2%	8.0%	5.6%	4.8%	1.9%	-1.7%	-24.1%

Source: FactSet, June 9, 2023

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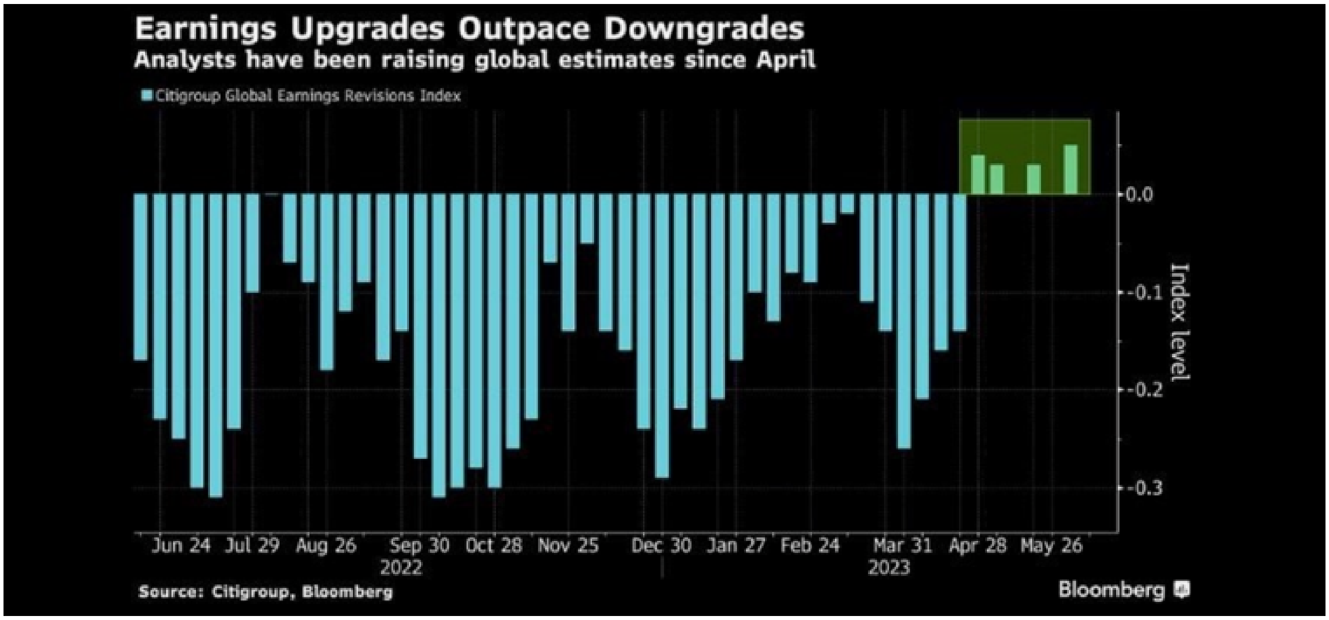
Global Earnings Revisions Are Positive – Positive for Global Equities

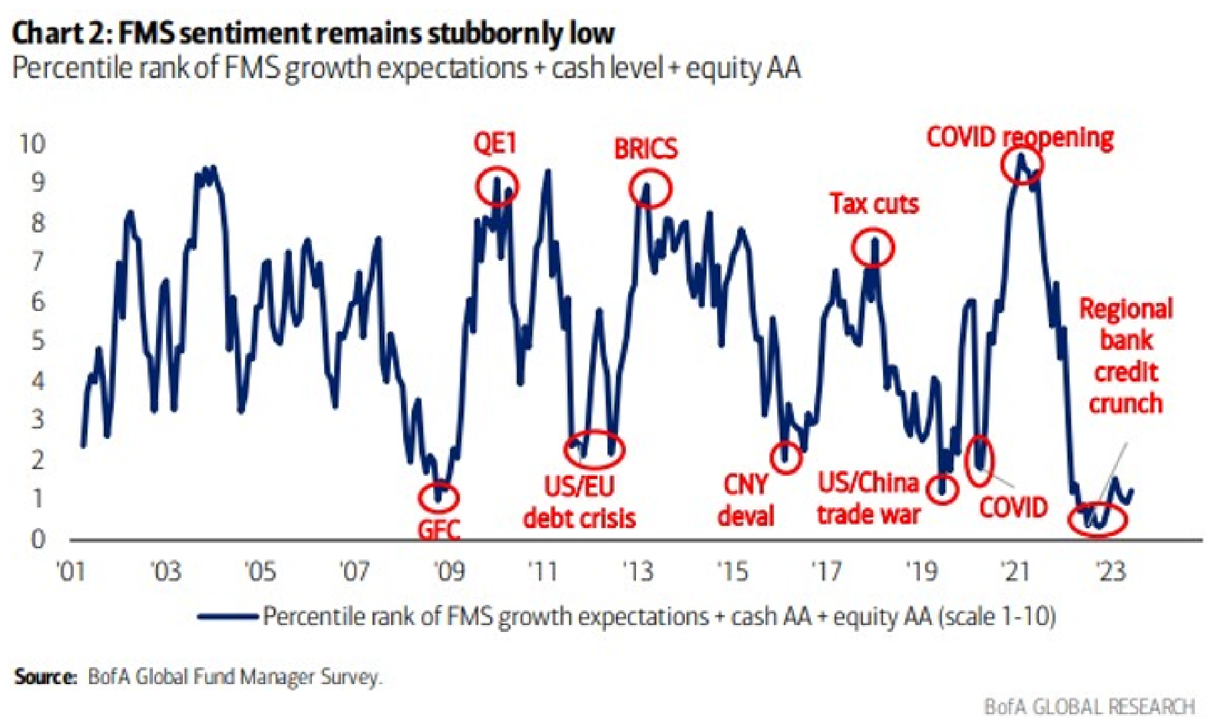


Source: Bloomberg, 2023

Sentiment and Positioning Remain Bearish – Which Is Bullish For Equities

Markets don't peak on pessimism, they peak on optimism. When we look at Bank of America's Global Fund Manager Survey for June, we see that positioning remains extremely bearish. There is a tremendous amount of room for money to come into the market, with the potential to drive the S&P 500 to its old high near 4800 and possibly to new highs.

Growth Expectations + Cash Levels + Asset Allocation Near Record Lows



Source: Bank of America June Global Fund Manager Survey

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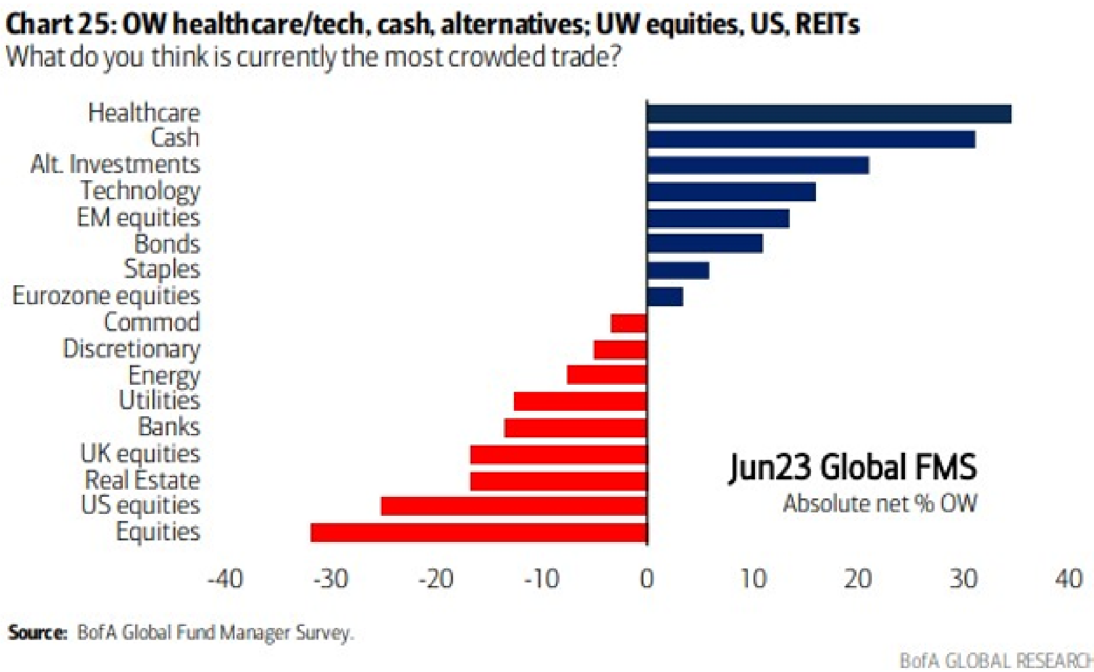
Equities and the US Equity Markets Remain Underweight – Contrary Bullish!!!

Bank of America Fund Manager Survey Shows Defensives OW & Equities Underweight



Source: Bank of America June Global Fund Manager Survey

S&P 500 Has a Major Breakout – Test of the Highs and New Highs Should be Expected

The S&P 500 has traded in a range for the past year, forming a very large base which measures future demand for stocks. The resistance (first box) is supply (i.e., future potential selling pressure) and the demand box is larger than the supply box. The demand box is larger than the supply box meaning that market highs should be tested, and new highs are possible. This illustration further confirms to us that we are indeed back in a Bull market.

S&P 500 Index

Source: Bloomberg, June 9, 2023

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The Bull is Charging Back

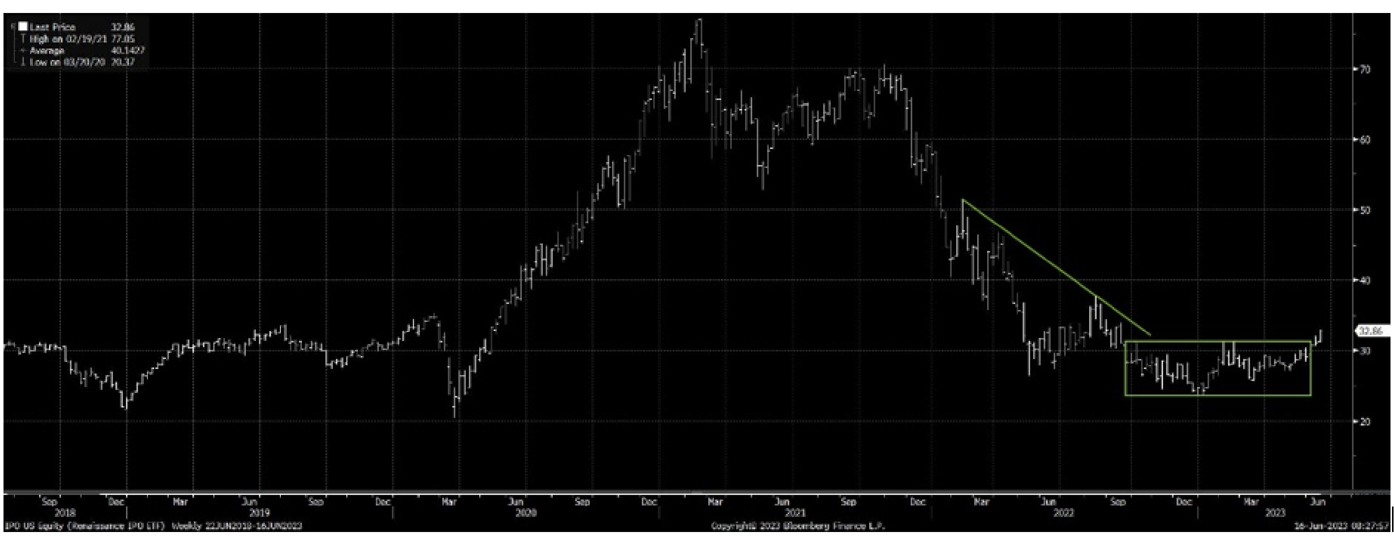
IPOs Are Back

Shares of CAVA Group (CAVA), the Mediterranean fast-casual restaurant chain, closed at $43.30 on June 15th on its Initial Public Offering (IPO), valuing the company at roughly $4.8 billion. That's almost twice what the company priced at on last Wednesday evening at $22 per share, which valued the company at $2.5 billion. Having such strong demand for this new IPO tells us that investors are hungry to feast on new investment ideas. (All puns intended!)

Take a look at the Renaissance IPO ETF (IPO). This ETF consists of a portfolio of new IPOs. The chart shows that Renaissance has reversed its downtrend and has broken out of its base consolidation, indicating a rally is underway – more evidence that there is demand for future IPOs.

Note: IPOs do well in Bull markets not in Bear markets. Yet another sign that we're back in a Bull market!

Renaissance IPO ETF (IPO)



Source: Bloomberg, June 16, 2023

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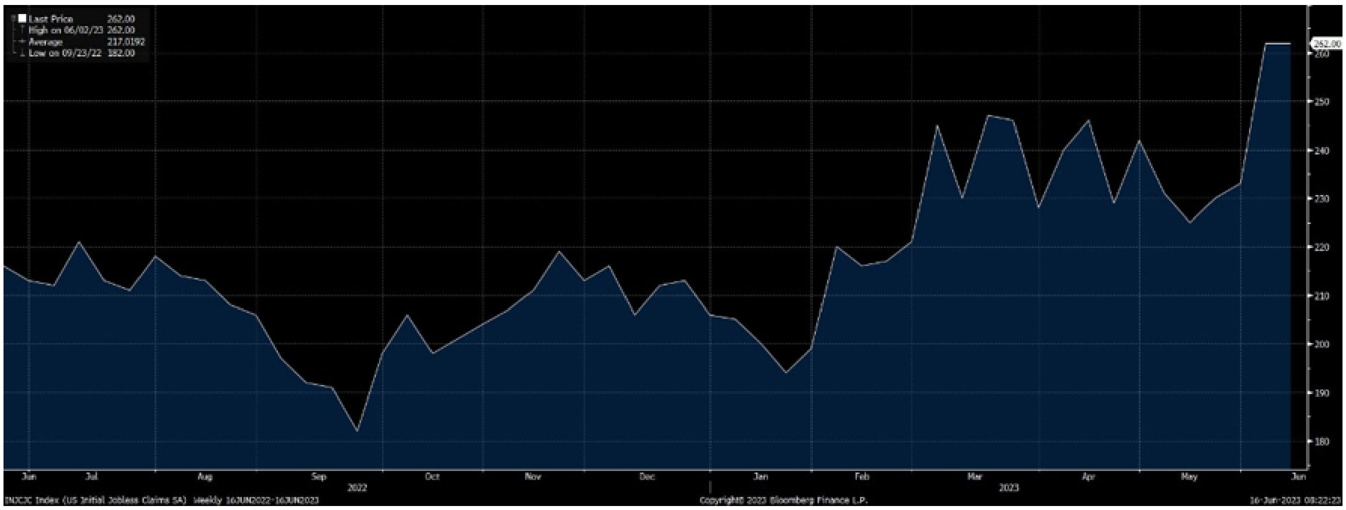
Initial Jobless Claims Remain Elevated

Last week, Initial Jobless Claims, a leading indicator of the labor market, came in above 250,000 for the second consecutive week, suggesting that softness should be coming to the labor market. This is what the Fed has been looking for. This data point was also a factor in last week's rally.

Initial Jobless Claims



Source: Bloomberg, June 16, 2023

Dressing Up for Quarter End

This is the week that seasonal behavior may outweigh weekly data.

In a shortened and relatively quiet week, all eyes will be on housing data and initial jobless claims. But what we'll also be watching is the S&P 500. With the equity market extremely overbought, a correction can happen at any time.

Still, jumping on the bandwagon of surging stocks is part of the ramp up towards the end of Q2. The rally is here, the Bull is running. Let's see who will blink first.

Calendar

Mon.

Juneteenth Day holiday, all markets closed

Tue.

8:30 am: Housing starts
11:45am: New York Fed President John Williams speaks
Earnings: FedEx, La-Z-Boy

Wed.

10:00 am: Fed Chair Powell testifies to House panel; Senate nomination hearing for Fed Govs. Jefferson and Cook and nominee Kugler
Earnings: KB Home, Korn/Ferry, Steelcase, Winnebago

Thu.

8:30 am: Initial jobless claims
10:00am: Existing home sales, Fed Chair Powell testifies to Senate panel
Earnings: Accenture, BRP, Commerical Metals, Darden, FactSet, GMS, Smith & Wesson Brands

Fri.

8:30 am: S&P flash U.S. services PMI
Earnings: CarMax

Source: MarketWatch/Kiplinger