CROSSMARK GLOBAL INVESTMENTS

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DOLL'S DELIBERATIONS

WEEKLY INVESTMENT COMMENTARY

EQUITY MARKETS (INDEX TOTAL RETURN)	LAST WEEK	YEAR-TO-DATE
DJIA	-1.82%	-6.42%
S&P 500	-2.74%	-9.99%
NASDAQ	-3.83%	-17.77%
RUSSELL 2000	-3.20%	-13.28%
RUSSELL 1000 GROWTH	-3.76%	-17.34%
RUSSELL 1000 VALUE	-2.03%	-3.11%

S&P EQUITY SECTORS (INDEX TOTAL RETURN)	LAST WEEK	YEAR-TO-DATE
COMMUNICATION SERVICES	-7.74%	-22.51%
CONSUMER DISCRETIONARY	-1.77%	-14.08%
CONSUMER STAPLES	0.49%	3.65%
ENERGY	-4.56%	38.59%
FINANCIALS	-1.97%	-7.00%
HEALTHCARE	-3.59%	-4.78%
INDUSTRIALS	-1.54%	-6.62%
INFORMATION TECHNOLOGY	-2.53%	-17.66%
MATERIALS	-3.72%	-5.01%
REAL ESTATE	1.24%	-4.14%
UTILITIES	-2.36%	4.56%

INTERNATIONAL EQUITY MARKETS (INDEX NET RETURN)	LAST WEEK	YEAR-TO-DATE
MSCI ACWI	-2.66%	-10.58%
MSCI ACWI EX U.S.	-2.23%	-9.96%
MSCI EAFE	-1.53%	-10.02%
MSCI EM	-3.33%	-12.22%

SUMMARY:

U.S. equities were down last week, with the S&P 500 falling 2.7%. The week's slide was broadly attributed to increasingly hawkish central bank commentary by the Fed and the ECB. Q1 earnings so far are outpacing expectations. The only positive sectors were REITs (+1.2%) and consumer staples (+0.4%); the worst performing sectors were communication services (-7.7%) and energy (-4.6%).

KEY TAKEAWAYS:

1. Economic data surprise indicators have been positive even as the recession chatter has picked up. All the weakness in headline GDP growth in Q1 is being driven by net exports and inventory, the two most volatile components (meaning, the overall economy is in pretty good shape).
2. An economic slowdown will eventually be a headwind to profits which could fall in 2023.
3. The rise in interest rates is weighing on housing demand, which should facilitate pushing inventory on the market and arrest the housing price climb.
4. The violent selloff in U.S. and G7 government bonds reflects the beginning of a capitulation by both central banks and bond bulls. It is typical of what occurs at the start of a significant structural trend change for an asset class.
5. Inflation is likely peaking on a year-over-year basis, but it will remain way above the Fed's target. We expect core inflation to settle out at around 4%.
6. Corporate America is in good shape. Corporate profits and cash flow are at record highs. Profit margins are near record highs despite rising costs. And balance sheets are flush with cash.
7. The main concern facing most businesses in America is a chronic labor shortage. Businesses are responding by spending more on capital equipment and technology to boost productivity.
8. A watered-down Build Back Better (BBB) bill still has less than a 50% chance of passing. A deal would be good for green energy and bad for the drug industry.
9. The dollar has seen unexpected strength due to the war in Europe, enhanced supply chain problems, diverging monetary policies, improving fiscal conditions, and rising real rates.
10. The latest AAII investor survey reports the fewest percentage of bullish respondents since 1992 – only 15%. A deterioration in investor sentiment is typically good news for stocks.

FIXED INCOME MARKETS (INDEX TOTAL RETURN)	LAST WEEK	YEAR-TO-DATE
BLOOMBERG U.S. AGGREGATE BOND	-1.04%	-9.49%
BLOOMBERG U.S. CORP HIGH YIELD	-0.88%	-7.38%
BLOOMBERG U.S. GOV/ CREDIT	-0.92%	-9.89%
BLOOMBERG U.S. T-BILL 1-3 MONTH	0.01%	0.04%

ALTERNATIVES (INDEX TOTAL RETURN)	LAST WEEK	YEAR-TO-DATE
FTSE NAREIT (REAL ESTATE)	0.97%	-3.80%
DJ COMMODITIES	-2.13%	29.68%
RED ROCKS GLOBAL LISTED PRIVATE EQUITY	-3.62%	-21.17%
DB G10 CURRENCY FUTURES	-0.83%	7.09%

VALUATIONS CONTINUE TO SUFFER FROM INFLATION UPTURN DESPITE DECENT ECONOMY AND EARNINGS

Equity markets remain trendless despite positive early signs from first-quarter earnings reports and indications that the global economic expansion is progressing despite various headwinds. The deteriorating inflation outlook remains a formidable risk factor for stocks along with, to a lesser degree, the ongoing economic restrictions in China, the war in Ukraine, and high energy, food, and commodity prices. In recent decades, government bond markets benefited when equities were weak, but that era ended when inflation returned. Short-term inflation expectations have already spiked, but worries that a return to the 2% inflation world might be in jeopardy are starting to creep in. A full-blown upshift in longer-term inflation expectations would be very disruptive for all asset classes and, eventually, the global economy. There is some near-run hope for a reprieve in that rampant goods price inflation will soon cool. However, even this positive is likely to provide only temporary relief since service sector inflation will continue to advance as mobility improves and spending strengthens. Inflation will pull back from current unsustainability high readings but will remain well above levels recorded in recent decades.

While stretched technical conditions suggest a pause or brief countertrend decline in bond yields may soon develop, the cyclical backdrop remains bearish for government bonds. Equities have not yet reached a dead end because corporate earnings remain supportive, although sustained upside will be difficult unless bond yields calm.

The business cycle is advanced, although bear markets do not usually occur when employment conditions are positive, and unemployment is falling. However, the environment has several unique elements and is not sufficiently positive for stocks to warrant an aggressively positive stance, especially given the ongoing bond bear market. Credit spreads are still not signaling trouble for equities, but the unprecedented liquidity boom that brought forward risk asset returns has passed now that inflation is rising. This, in turn, warns that the cyclical risks for stocks are increasing. Investors have not had to deal with a sustained higher level of inflation in 40 years and will continue to change the investment landscape profoundly.

Never having witnessed negative-yielding bonds, even in the Depression, a sizable part of the global debt market saw yields drop below zero. The unprecedented policy response to the pandemic triggered a massive liquidity boom and rampant and broad-based inflation. The downside of this boom, and the subsequent solid global economic recovery, is that inflation has gained a solid toehold.

CONCLUSION:

The global economic expansion is proving to be durable despite recent hits to sentiment. The cyclical bear markets in bonds are not over, but a pause or yield decline is increasingly likely on technical grounds. Equities need a pause in bond yields to move higher. Corporate profit trends remain supportive, but rising bond yields will continue to pressure stock market valuations.

Data from Morningstar Direct, as of 04/25/2022.

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