CROSSMARK
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DOLL'S DELIBERATIONS

WEEKLY INVESTMENT COMMENTARY

EQUITY MARKETS (INDEX TOTAL RETURN)	LAST WEEK	YEAR-TO-DATE
DJIA	-2.85%	-12.54%
S&P 500	-3.23%	-16.78%
NASDAQ	-4.18%	-25.25%
RUSSELL 2000	-4.01%	-18.11%
RUSSELL 1000 GROWTH	-3.88%	-24.07%
RUSSELL 1000 VALUE	-2.78%	-10.36%

S&P EQUITY SECTORS (INDEX TOTAL RETURN)	LAST WEEK	YEAR-TO-DATE
COMMUNICATION SERVICES	-2.36%	-31.19%
CONSUMER DISCRETIONARY	-2.56%	-23.72%
CONSUMER STAPLES	-2.29%	-4.77%
ENERGY	-3.19%	48.14%
FINANCIALS	-2.41%	-14.98%
HEALTHCARE	-1.79%	-10.59%
INDUSTRIALS	-3.49%	-12.17%
INFORMATION TECHNOLOGY	-4.97%	-23.46%
MATERIALS	-4.85%	-17.06%
REAL ESTATE	-3.92%	-19.15%
UTILITIES	-1.44%	5.85%

INTERNATIONAL EQUITY MARKETS (INDEX NET RETURN)	LAST WEEK	YEAR-TO-DATE
MSCI ACWI	-3.07%	-18.37%
MSCI ACWI EX U.S.	-4.28%	-20.22%
MSCI EAFE	-4.78%	-21.70%
MSCI EM	-3.00%	-18.97%

SUMMARY:

U.S. equities were down for the third consecutive week. The S&P 500 (-3.2%) is now off 8.8% since topping 4300 on August 16. The path of monetary policy remained the central question, with expectations firming for a 75bp Fed rate hike in September and a "higher for longer" mindset taking hold. Best sectors were utilities (-1.4%), healthcare (-1.8%); worst sectors were materials (-4.9%) and technology (-5.0%).

KEY TAKEAWAYS:

1. The August unemployment report (315,000 new jobs vs. estimates of 300,000) was slightly weaker and less hawkish than expected. The report is totally inconsistent with recession and unlikely to produce much reassessment at the Fed about its next policy move.

2. In his now infamous speech of August 25, Fed Chair Powell said, "we must keep at it [fighting inflation] until the job is done." Consider the punch bowl removed.

3. After declining for three consecutive months, job openings unexpectedly rose to 11.2 million in July. As a result, the ratio of openings to applicants ticked higher, back to 2.0.

4. The August CPI report will be released on September 13. It is likely to show that inflation continues to fall.

5. U.S. two-year yield crossed 3.50 last week, marking the highest level since November 2007. (The most notable difference is the P/E on the S&P (17x today vs. 14x then) suggesting that stocks might still be expensive.

6. U.S. housing has rapidly become a weak part of the economy with higher mortgage rates deterring demand. But, so far, home prices remain relatively robust.

7. The national average retail gas price has declined 11 straight weeks from a high of $5.01 on June 13th to $3.83 as of August 29th with further declines to come (to a projected $3.29.)

8. Energy contributed 16% of 2Q earnings (but is only 4.5% of equity market capitalization), suggesting energy stocks are still poised to outperform.

9. Dividends will likely play a big part in the return profile for stocks moving forward as we exit a regime of low inflation and loose monetary policy.

10. The 2022 midterm election is becoming a choice between the two parties and not the usual midterm election referendum. This has given the Democrats some momentum.

FIXED INCOME MARKETS (INDEX TOTAL RETURN)	LAST WEEK	YEAR-TO-DATE
BLOOMBERG U.S. AGGREGATE BOND	-1.40%	-11.28%
BLOOMBERG U.S. CORP HIGH YIELD	-2.19%	-11.72%
BLOOMBERG U.S. GOV/ CREDIT	-1.49%	-12.09%
BLOOMBERG U.S. T-BILL 1-3 MONTH	0.04%	0.43%

ALTERNATIVES (INDEX TOTAL RETURN)	LAST WEEK	YEAR-TO-DATE
REAL ESTATE (FTSE NAREIT)	-2.59%	-17.18%
COMMODITIES (DJ)	-4.36%	21.03%
GLOBAL LISTED PRIVATE EQUITY (RED ROCKS)	-4.86%	-35.90%
CURRENCIES (DB G10 CURRENCY FUTURE)	0.83%	6.74%

MIXED CROSSCURRENTS

The Jackson Hole August 25 Fed speech was hawkish and thus bearish for risk assets. The Fed Chair reaffirmed the goal of returning inflation to low levels (2%) in line with their mandate. Nevertheless, we anticipate that the major central banks, including the Fed, will back off before taking significant economic risks; that is, we believe they are not yet willing to push policy rates well into restrictive territory and trigger a recession over the next 6-12 months. The Fed is likely to pause by year-end to assess whether the economy is still holding up and if the budding deceleration in inflation seems likely to prove meaningful. So, while we think a risk-off posture makes sense, stocks have quickly become oversold and could rally inside the trading range bounded by June lows and August highs.

Economic risks are higher now than at the start of the year, albeit mostly due to non-monetary factors. China remains mired in a sluggish, choppy recovery because of its pursuit of COVID-zero, made worse by droughts. While droughts are also impacting Europe, the larger drag on activity and economic sentiment remains the war-related energy crisis. Both China and euro area economies have sufficiently robust foundations that a return to decent growth is possible if these non-monetary headwinds ease. Despite an inverted yield curve, the U.S. economy continues to progress with notable tightness in labor markets. The overall picture is mixed but a slide into recession is unlikely, unless central banks proceed to hike interest rates aggressively in the next 6-12 months or exogenous forces worsen.

U.S. inflation, although coming off the peak, will not be easily returned to 2%. Headline inflation will move steadily lower due to an unwinding of the post-pandemic spike in some goods prices and with gasoline/oil prices down significantly. Importantly for the Fed (and for wage pressures and, therefore, inflation), labor market indicators are holding up. The housing market is cooling steadily in the face of higher mortgage rates, although it is likely that high house prices have been a depressant on demand. Importantly, we believe the reprieve on the U.S. inflation front over the next six months will be temporary in nature and a return in core CPI to levels that would reverse the rate-hiking cycle are unlikely. In recent decades, inflation would periodically flare, but it never became entrenched and quickly declined. No such benign outcome is probable this cycle.

Despite holding a view that is more upbeat on the global economy than the consensus, we also fear that equity markets are in a trading range, suggesting that it could be quite difficult to generate positive returns. Two possibilities: 1) either the global economy holds up well and corporate earnings continue to provide underlying support, in which case central banks will likely be forced to continue tightening policy and bond yields may well eventually overshoot, resulting in a further de-rating of equities such as occurred in the first half of 2022 or, 2) economic activity weakens and corporate profits falter, which would cause central banks to back off but would also result in an earnings downturn that would undermine equity prices. The equity rebound (more than 15% from mid-June to late August) stalled as bond yields started to rise again. The still low level of credit spreads suggests that a bearish earnings outcome is not yet likely.

CONCLUSION:

The Fed may have room to pause its rate-hiking cycle by year-end, as U.S. headline inflation will steadily decelerate and the central bank will eventually want to see how its policy has impacted the economy. However, the recent risk-on phase ended as government bond yields have firmed due to ongoing hawkish central bank rhetoric and somewhat better-than-expected economic activity. Meanwhile, equities are likely in a trading range, bounded by June lows (S&P 500 3636) and August highs (4325).

Data from Bloomberg, as of 09/02/2022.

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