Market Perspectives

April 2023

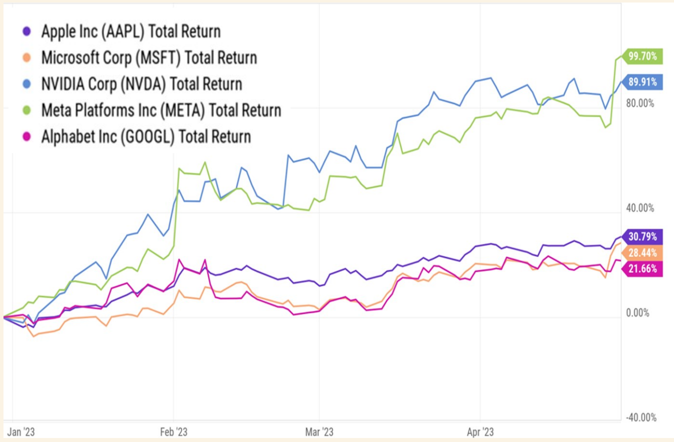
TURTLE CREEK
WEALTH ADVISORS

KEY HIGHLIGHTS

- April was a positive month for stocks except for small caps and emerging markets.
- Inflation continues to fall but remains far above the Fed's 2% target.
- The yield curve becomes even more inverted.
- Banking issues persist.
- S&P earnings better than feared so far.

APRIL PERFORMANCE

The Dow Jones Industrial Average rose 2.6%, the S&P 500 added 1.6% and the Nasdaq posted a slight gain of 0.1% for the month. Emerging markets and U.S. small-caps slipped 1.1% and 1.8% respectively with the Russell 2000 index falling for the third consecutive month. Breadth in the market has been narrow with technology and communication services sectors accounting for the lion's share of the S&P 500's gain. In fact, the combined year to date appreciation in Apple, Microsoft, Nvidia, Meta Platforms and Alphabet have contributed approximately 67% of the $2.2 trillion of additional market cap added to the S&P 500 in 2023. All five are in the top eight in market capitalization weighting in the index and when they do well so goes the index. As illustrated below, each has handily outpaced the year-to-date S&P 500 gain of 9.17%.



Source: YCHARTS

Breadth in the market has been narrow with the technology and communication services sectors accounting for the lion's share of the S&P 500 gain this year.

Index	MTD	QTD	YTD	1 Year	2022
S&P 500	1.56	1.56	9.17	2.66	-18.11
Dow Jones Industrial Average	2.57	2.57	3.53	5.64	-6.86
Russell 2000	-1.80	-1.80	0.89	-3.65	-20.44
NASDAQ Composite	0.07	0.07	17.12	0.02	-32.61
Europe, Australia, & Far East (EAFE)	2.93	2.93	11.80	9.00	-14.05
MSCI Emerging Markets	-1.11	-1.11	2.86	-6.09	-19.78
Bloomberg Barclays U.S. Aggregate Bond	0.61	0.61	3.59	-0.43	-13.04

As of 4.30.23; Returns in percent

INFLATION ON THE DECLINE

Inflation is moving in the right direction although not as quickly as expected or hoped for. March CPI was released on April 12th and declined to 5.0% year-over-year compared to 6.04% last month, however inflation has remained persistently above the Fed's 2% target. In an effort to tame stubborn inflation, the Fed has embarked on an incredibly aggressive tightening cycle. Markets oscillate up and down depending on current views of how the inflation fight is playing out. The economy continues to provide mixed signals with a strong labor market, and a near all-time low for unemployment juxtaposed with weakening manufacturing data, negative earnings growth, and tepid GDP. We believe inflation likely continues to come down but is unlikely to touch the 2% target for some time. Might it be prudent for the Fed to target 3% inflation while allowing the data to play out? There is a lag effect of monetary policy on the economy that takes many months to penetrate the broader economy. In our view, anchoring to the 2% target (today) heightens the probability of a policy error.

EVEN MORE INVERTED

The yield curve continued to become more inverted in April with the 3-month Treasury and 10-year Treasury spread closing the month at -1.66%, the greatest negative spread ever. As mentioned in our March Perspectives, an inverted yield curve has historically been quite accurate in foretelling recessions, however actual timing is unpredictable, and many other factors play a role in determining recessions such as employment. As the yield curve inversion has widened, the probability of recession over the next 12 months has increased to 68.22% per the Federal Reserve Bank of New York. While seemingly troubling, there is no guarantee that the U.S. economy will end up in a recession and it bears remembering not all recessions are of the Great Financial Crisis (GFC) version and some are quite mild. Additionally, opportunities abound during slowing economic times and during inversions. Today, fixed income has become much more desirable sporting attractive yields and even once abandoned cash is considered an asset class again with money market funds yielding 4.60%.

BANKING ISSUES

The banking issues that surfaced in March seemed to be relatively under control for most of April with many regional banks posting results that were better than feared. However, late in the month, First Republic Bank (FRCB) also became a calamity and was expected to go into FDIC receivership. Early on Monday, May 1st the bank was seized by regulators and sold to JP Morgan Chase. FRCB is now the second largest bank failure in the U.S. and the third midsize bank to fail in less than two months. Banks are now tightening lending standards which will lead to less lending and a potential slowdown in the economy. The banking issues are assisting the Fed in its job to fight inflation (slow the economy) as it is estimated that tightened lending is akin to a 0.50% hike in rates. We expect there to be more fallout in the banking sector with the largest of the banks benefiting from the turmoil while small and mid-size banks with challenged balance sheets will remain under stress.

EARNINGS

The overarching theme for Q1 earnings has been that earnings are coming in better than expected albeit hurdling a lower bar. On March 31st the projected Q1 earnings decline was 6.7% and so far, earnings are on track to fall only 3.7% for the period. Earnings, however, typically don't bottom out until after the Fed's last hike. which is likely nearing. The Fed announced on May 3rd a 0.25% hike and meets again in late June. In our view, we are very near the finale of this tightening cycle. Looking ahead, earnings and inflation data will continue to determine the direction of markets.

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