MARKSGROUP WEALTH MANAGEMENT

PERSPECTIVES & OUTLOOK

May 2022

Inflation, Fedwinds Weigh on Stock Prices

Sobering realities of 8.5% inflation, less favorable Fed policy, and Russia's invasion of Ukraine have battered stock prices this year. The S&P 500 has fallen ~15% from its early January peak. Stocks with the highest valuations proved especially vulnerable.

US Equity Valuations Near 2-Year Lows

As of April 30, the forward P/E ratio for the S&P 500 had fallen to 18.1, its lowest point since April 2020. US stock valuations have dropped 22% from their peak 18 months ago. This suggests a good chunk of the coming "Fedwinds" are priced into equities.

Yield Curve Inversion is Not a Sell Signal

The 2-year US Treasury yield rose higher than the 10-year yield in late March. This "inversion" is often promoted as a recession warning, but the last 4 times it happened, the S&P 500 rose an additional 29% on average and did not peak for another 17 months.

The Earnings Bar has been Raised

After four consecutive quarters showing annual earnings growth of 20% or more, forward expectations are more modest. S&P earnings are projected to increase 5-7% in Q1. As labor and material costs increase, profit margins have come under pressure.

Rising Rates do not Dictate Market Losses

The latest futures indicate the market is expecting 9 interest rate hikes this year. Since WWII, we've had 11 periods with 5 or more rate hikes by the Fed. The S&P 500 was positive in 8 of those, with median returns of 5.6% per year.

Labor Shortage is a Challenge

The latest employment data shows 5 million more job openings in America than unemployed workers. In addition to hurting productivity, the labor shortage also contributes to inflation since employers must pay higher wages to fill open positions.

Hot Housing Market Could Cause Burns

The latest Case-Shiller data shows home prices nationally have increased 20% in the last 12 months. 30-yr mortgage rates have doubled and are now above 5%. An unbalanced housing market and low affordability create hurdles to a healthy economy.

COVID Will Not Drive Market Returns

COVID variants are a reminder the pandemic is not over, but the impact of COVID on financial markets will be minimal in 2022. Widespread shutdowns will not occur in the US, and consumers' comfort level (and buying habits) have adapted.