Week in review and ahead (vol.19)

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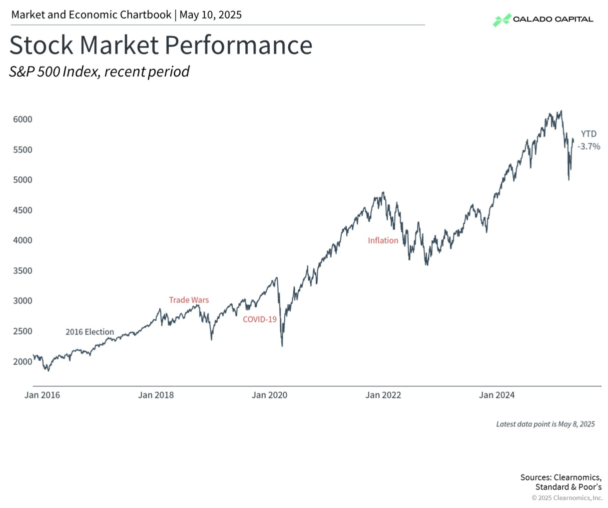
The Fed's FOMC kept US monetary policy unchanged as expected by many, but described risks for higher inflation and unemployment to have risen. The POTUS announced the first trade deal with the UK that kept for the most part the 10% tariff rate imposed on (UK) imports in place. Negotiations for a trade deal with the UK have been underway since Brexit (Jan.31, 2020), or for more than five (5) years and considering it is the US' closest ally, there may have been some disappointment among market participants.

The earnings season continued to see stronger than expected earnings as nearly 83% of the Companies belonging to the S&P500 that reported this past week beat consensus. Similarly, nearly 66% of the S&P500 companies that reported saw revenues exceed consensus, while guidance continued to be mixed. Earnings season is tapering off with only 10 companies belonging to the S&P500 reporting next week.

Equity markets fell for the week as positive sentiment on trade deals, including discussions with China this weekend, and stronger earnings weren't enough to offset growth concerns and arguably some realization that US tariffs may remain and may not just be used as negotiation leverage as the trade announcement with the UK demonstrated. The S&P500 fell 0.5% for the week, while the Down Jones and tech-heavy Nasdaq slipped 0.2% and 0.3%, respectively. Accordingly, the indices continue to be negative on a year-to-date basis.

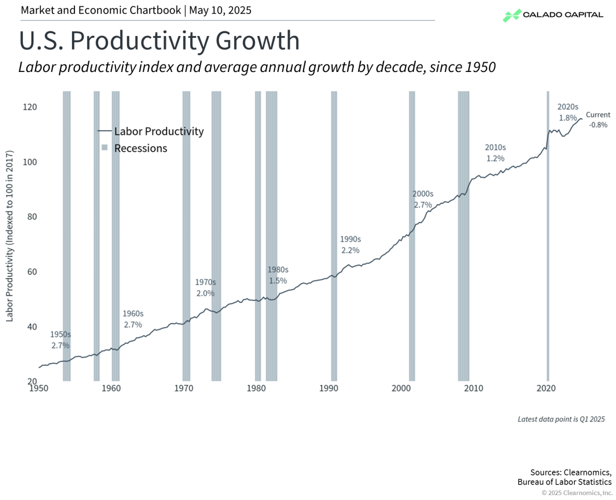
Internationally, key markets continue to advance higher with the German DAX closing the week just below the intraday high during Friday's trading session. In Asia, China and Hong Kong closed the week higher as a scheduled meeting with the US is seen as positive. London, similar to the US, closed the week down by 0.5% despite the announcement on Thursday of a US-UK trade deal.



The Fed maintained its monetary policy stance, in large part as macroeconomic data in the US continues to display some resilience despite low consumer sentiment and elevated inflation expectations for the broader US economy. Last week's key macro data seems to support the Fed's stance.

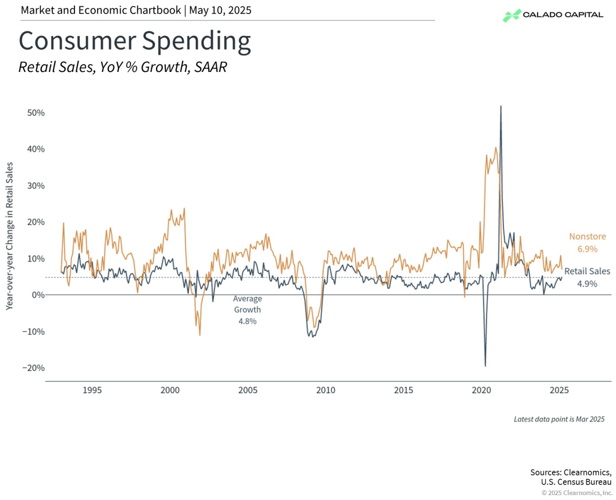
The Institute for Supply Management ('ISM') reading for the service sector surprised at 51.6 for April compared to 50.4 expected, continuing expansionary trend at the highest reading since February 2024. Within the service ISM, however, readings for prices paid rose to the highest since January 2023 (at 65.5) while employment (at 49.0) fell into contractionary territory, dropping to the weakest since June 2024. Initial jobless claims fell back to 228K, after reaching 241K the previous week, and just below expectations for 230K. Similarly, continuing claims fell below 1.9M (to 1.88M), after continuing claims of 1.92M for the previous week did not see any revisions, marking last week the first time it exceeded the 1.9M threshold since the pandemic. US productivity for Q1'25 declined by -0.8% for the first time since Q2'22. The decline surprised as consensus expected an increase of 0.7%, after seeing stronger productivity gains recently, including 1.7% in Q4'24.

While most of the macroeconomic data continues to display resilience, some cracks are creeping into the economic data set that may have caused the Fed to highlight elevated risks of inflation and unemployment in the US, and seen as 'hawkish' by markets while leaving policy unchanged. Inquiries as to which of its goals the Fed would prioritize were not entirely answered, rather theoretical, in stating that the Fed would assess which of the data set would be furthest from its goal and implications for the broader US economy. Regardless, given the Fed's assertion of higher risks to inflation and unemployment (without updating its projections or 'dot plots' which is expected to be released next in June), emphasized concerns of stagflation in the US. Those concerns did mute trade sentiment and otherwise offset positive sentiment from stronger earnings and the prospect of trade deal announcements, including China.



The week will begin with digestion of the US-China discussions in Switzerland over the weekend. While no announcements have been made on Saturday evening (the time of writing this update), markets are expecting the two largest economies to agree at a minimum to lower tariff rates from current levels seen as unsustainable by both parties. Anything different may influence sentiment, however, the market appears to be positioned to "sell the news" after "buying the rumor" leading up to the meeting this weekend. Discussions are expected to address complex trading issues and to take considerable time to yield a new trade agreement.

From a macroeconomic perspective, markets will focus on retail (CPI) and wholesale (PPI) inflation for April in the US with the core inflation expected to be 2.8% (same as in March) and 3.6% (from 3.4%), respectively. Retail sales for April are expected on Wednesday, with the year-over-year expected at 1.1% and 0.5% ex-auto, well below the 4.9% and 3.1% ex-auto growth recorded in March, after weak consumption during January and February. While consumer sentiment is at the lowest levels, overall consumers appear to have kept spending and a positive surprise on retail sales ex auto (as auto sales may have seen strong demand ahead of tariffs) may alleviate concerns on the US consumer somewhat. Similarly, initial jobless claims are expected to be at 225K while continuing claims are expected to remain below 1.9M. Fed Chair Powell is expected to speak on Thursday and markets will pay attention if its stance may have changed from this past week, considering data for April. The week concludes with reports on building permits and housing starts as well as preliminary reading of consumer sentiment by the University of Michigan.



If you have questions about how this may impact your investments, or how you should be positioned, please do not hesitate to contact us at claudio@caladocapital.com.

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