

Week in review and ahead (vol.25)



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June 22, 2025

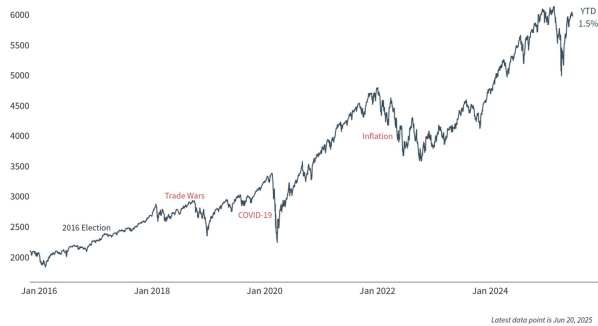
The equity markets were slightly down for the holiday shortened week in the US, but also globally, as the Israel-Iran war is escalating with the US contemplating its involvement to diminish Iran's nuclear aspirations. With geo-political issues in focus, the Fed's decision to keep rates unchanged in the US on Wednesday had initially triggered a rally in equities, before markets closed for Juneteenth on Thursday, however, Fed Chair Powell's statement that it may keep policy unchanged for longer, therefore indicating reduced probability of multiple cuts this year, saw the rally in equities reverse.

The S&P500 declined by 0.2%, while the tech-heavy Nasdaq edged higher by 0.2% and the Dow Jones were flat on the week. Within the S&P500, only the financial, information technology and energy sectors increased for the week by 0.8%, 0.9% and 1.1%, respectively while all other sectors declined.

Internationally, all major markets declined for the week but for the Nikkei index in Japan, and the Sensex and Nifty 50 indices in India. Japan's Nikkei advanced 1.5% for the week, as Q1 GDP data was weaker than expected, contracting -0.7% on a year-over-year ('YoY') basis compared to expectations of a decline of -0.2%, with many market participants (in Japan) anticipating the Bank of Japan may halt its recent interest rate hikes. Besides, the Japanese bond market appears to stabilize as did the Yen which previously had set-off global sell-off of sovereign debt that steepened yield curves, including the US. In contrast, India's indices advancing 1.6%, respectively due to a technical rebound that led to a surge as short covering ensued.

Stock Market Performance

S&P 500 Index, recent period



Sources: Clearnomics,
Standard & Poor's,
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Macroeconomic data in the US continues to point to a slowdown, albeit greater focus (by the markets) was placed on the Fed's FOMC meeting that took place last Tuesday and Wednesday, which left monetary policy and interest rates unchanged.

Retail sales reported on Tuesday were mixed with headline number for May showing a decline of -0.9% compared to an expected decline of -0.6% and down from the decline of -0.1% in April. Excluding autos, retail sales surprised to the downside by declining -0.3% compared to an estimate of increasing by 0.1% and virtually flat in April, and together with

headline pointing to some softening of the US consumer. The core retail sales (excluding auto, gasoline, building materials and food services), however, were up 0.1% compared to expectations of declining by -0.1%. On a YoY basis, the core retail sales in May grew at a solid 3.9% rate.

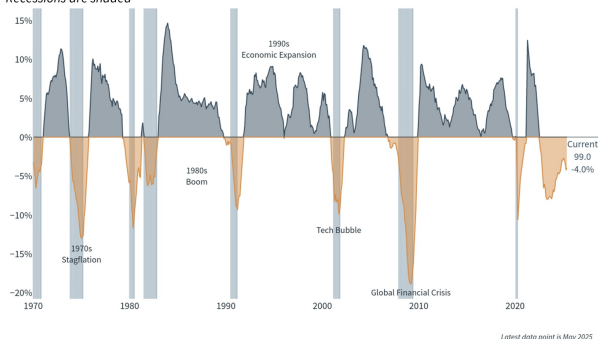
The labor market continues to display some weakness with initial jobless claims declining from 250K last week to 245K this week, in line with expectations of 246K. Similarly, continuing claims of 1.945M were below last week's 1.95M but higher than the expected 1.94M and above the 1.9M-mark now for the 5th consecutive week. Yet while claims, both initial and continuing, are somewhat elevated, claims continue to behave somewhat well without any major spikes, as labor force (participation) continues volatile under this administration's aggressive deportation policy that lead for certain industries, especially the agricultural and hospitality sectors, voice concerns that it is encountering significant labor shortages.

The housing market's weaknesses, on the other hand, continues to deteriorate with housing starts in May at 1.26M well-off expectations of 1.35M and the prior month of 1.39M touching a five-year low. The decline in housing starts was influenced heavily by a sharp drop in multifamily asset classes. Similarly, building permits for May were light, too with 1.39M compared to expectations and prior month's permits of 1.42M, respectively.

The week concluded with the US leading economic indicators ("LEI") improving significantly in May to -0.1% from -1.4% in April, in line with expectations, primarily as stock prices continued their sharp recovery from the early April lows. For the six-month period that ended in May'25, the LEIs decline was 2.7%, at a greater rate than the 1.4% decline for the previous six-month period.

Leading Economic Indicators

Conference Board LEI year-over-year percent change
Recessions are shaded



Latest data point is May 2025

Sources: Clearnomics,
Conference Board,
NBER, ISG
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The focus last week, however, besides the geo-political risks that did and continue to take center stage, was the FOMC meeting which left monetary policy unchanged as widely expected, drawing, as expected, the POTUS' ire. Markets initially were rallying on the announcement as well as the beginning of Fed Chair Powell's prepared comments and subsequent Q&A.

While the Fed projections (known as the "dot plot") did indicate that the FOMC voting members appear increasingly more divided, it did maintain median projections of two rate cuts of 25 basis-points ('bps') this year, which would reduce the Fed Funds Rate to 3.9%, again in-line with

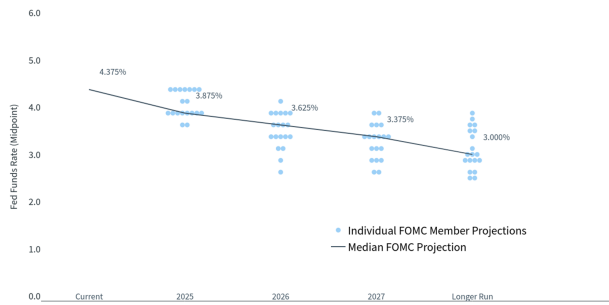
recent market expectations. Keeping expected rate cuts the same was interpreted favorably, particularly since the dot plot increase projected PCE inflation index to 3.1% by the end of the year, compared to the projections of 2.8% in March, amidst reduced projections for 2025' GDP growth, down from the estimated 1.7% in March. The markets may have interpreted that if the Fed's dual mandate diverge, which many expect to occur during the second half of 2025, the FOMC may favor unemployment over price stability and proceed with rate cuts, or easing of monetary policy.

The markets appeared initially to ignore the fact that more FOMC members appear to expect or favor no rate cuts for 2025, or 7 out of 19 members (nearly 37%), as the initial rally just after the announcement in equities demonstrated. It was not until Fed Chair Powell emphasized during Q&A that if inflation accelerates the FOMC may leave rates unchanged that markets reversed. Regardless, the Fed's announcement, including reaffirmation of the wait and see approach, was widely expected by the markets.

It should be noted that concerns about inflation reaccelerating, particularly given the last two CPI reports for April but particularly for May, which reported better than expected inflation amidst tariffs taking hold, continue. Apollo on Friday raised red flags over the same CPI data. Specifically, the Bureau of Labor Statistics ("BLS"), compiles approximately 90,000 price quotes over 200 categories across 75 urban areas, collected by field agents. Generally, about 10% of these data values that feed into the CPI are estimated, as data may not be (readily) available. For the last two months, however, these data sets have seen elevated levels of estimates, with both April and May approaching 30% (see chart on: https://www.apolloacademy.com/wp-content/uploads/2025/06/062025_Chart_v2.pdf).

Federal Reserve Dot Plot

FOMC Participants' Projections of the Federal Funds Rate



Sources: Clearnomics, Federal Reserve
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Next week's focus will remain on geopolitical events, which will continue to influence volatility and markets. Fed Chair Powell is scheduled to testify to congress on Tuesday and Wednesday, and the week concludes with May's data on personal consumption and expenditures ('PCE'), including the Fed's preferred inflation gauge, the core PCE inflation index projected to increase 0.1% month-over-month and 2.6% YoY.

Additionally, S&P will issue its preliminary estimates for June's service and manufacturing PMI's, together with additional data on the US housing market, specifically, existing home sales, expected

at just below 4M, and new home sales for May, which is expected to decline by nearly 8% from April's 743K to 689K. Finally, consumer confidence for June is scheduled to be reported on Tuesday, with Thursday, to provide an update on weekly and continuing jobless claims.

As of writing this weekly newsletter, news of the US conducting airstrikes on three nuclear facilities in Iran broke and the next 48 hours will somewhat determine if the conflict escalates, likely with US involvement, or if diplomatic discussions, which were unsuccessful thus far and seen as less likely, can resume somewhat.

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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