Amadeus Wealth Alternatives
Your Compass to Alternative Investments

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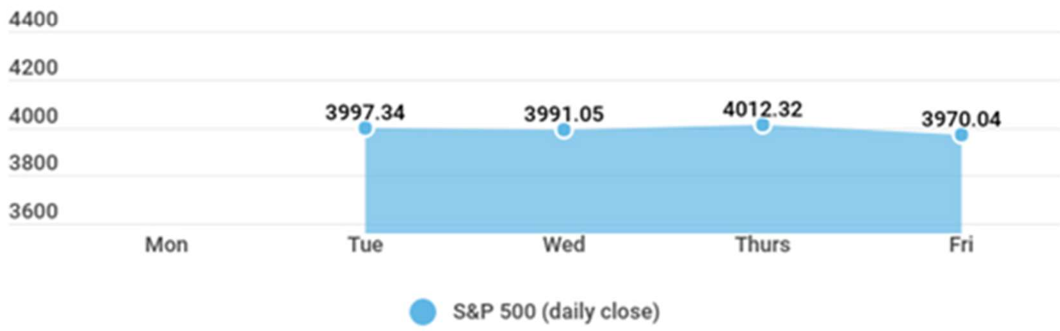
Concerns over a firmer monetary policy were heightened by fresh economic data, touching off a climb in bond yields and a slide in stock prices last week.

The Dow Jones Industrial Average skidded 2.99%, while the Standard & Poor's 500 dipped 2.67%. The Nasdaq Composite index sagged 3.33% for the week. The MSCI EAFE index, which tracks developed overseas stock markets, retreated 1.23%.[1,2,3]

Market Index	Close	Week	Y-T-D
DJIA	32,816.92	-2.99%	-1.00%
NASDAQ	11,394.94	-3.33%	+8.87%
MSCI-EAFE	2,061.45	-1.23%	+6.05%
S&P 500	3,970.04	-2.67%	+3.40%



	Treasury	Close	Week	Y-T-D
	10-Year Note	3.95%	+0.13%	+0.07%

Sources: The Wall Street Journal, February 24, 2023; Treasury.gov, February 24, 2023
Weekly performance for the Dow Jones Industrial Average, Standard & Poor's 500 Index, and NASDAQ Composite Index is measured from the close of trading on Friday, February 17, to Friday, February 24, close. Weekly performance for the MSCI-EAFE is measured from Friday, February 17, open to Thursday, February 23, close. Weekly and year-to-date 10-year Treasury note yield are expressed in basis points.

Stocks Slide

Stocks struggled last week, buffeted by growing fears of further Fed tightening and disappointing forecasts from two major retailers that called into question the consumer's health. The release of the minutes from the Federal Open Market Committee's (FOMC) last meeting did little to assuage investor worries. Reflecting these concerns of a more aggressive Fed was that by Thursday, traders were pricing in a 27% chance that the Fed might lift rates by a half-percentage point at its next meeting, far above the 1.3% chance just one month ago.[4]

Stocks took another leg lower on Friday following the release of January's Personal Consumption Expenditures (PCE) price index, which showed hotter-than-expected price increases and more robust consumer spending.

FOMC Minutes

Minutes from the last FOMC meeting indicated that nearly all members agreed with February's quarter-point rate increase, though some would have supported a 50 basis point rate hike to move quicker towards the Fed's target range. While the minutes suggested another 25 basis point hike is likely at their next meeting, investors remain anxious that more recent economic data may prompt a 0.50% hike instead.[5]

The minutes stressed that inflation was still too high. However, members diverged on the economy, with some members finding the risk of recession elevated. In contrast, others feel the Fed may engineer a soft landing or avoid a recession altogether.[6]

This Week: Key Economic Data

Monday: Durable Goods Orders.

Tuesday: Consumer Confidence.

Wednesday: Institute for Supply Management (ISM) Manufacturing Index.

Thursday: Jobless Claims.

Friday: Institute for Supply Management (ISM) Services Index.

"The first panacea of a mismanaged nation is inflation of the currency; the second is war. Both bring a temporary prosperity; both bring a permanent ruin. But both are the refuge of political and economic opportunists"

– Ernest Hemingway

Of Note

Two important pieces of data came out recently that should be paid close attention to.

On February 16th, the Philadelphia Fed Manufacturing Survey for February was released. According to MarketWatch, the median estimate called for a decline of -7.8. The actual result was a decline -24.3.

The official press release noted the following: “The diffusion index for current activity fell from a reading of -8.9 last month to -24.3 this month, its sixth consecutive negative reading and lowest reading since May 2020.”

You might wonder, “What is the Philadelphia Fed Manufacturing Survey, and why does it matter to me?”

The Manufacturing Business Outlook Survey (official name) is a monthly survey of manufacturers in the Third Federal Reserve District. Participants indicate the direction of change in overall business activity and in the various measures of activity at their plants: employment, working hours, new and unfilled orders, shipments, inventories, delivery times, prices paid, and prices received. The survey has been conducted each month since May 1968.

Why does it matter? Here is a good synopsis provided by TheStreet.com: The survey, conducted each month since May 1968, is the oldest among the 12 Fed banks monitoring regional manufacturing activities and is often viewed as accurately reflecting the pace of growth in manufacturing nationally. The survey’s influence as a leading economic indicator has pushed other regional banks to publish their own polls for their districts. A reading greater than zero suggests expansion in manufacturing, while a reading of less than zero indicates contraction. Because the data span more than 50 years, the index reliably provides an early indication of whether the economy might be slipping into recession. The Philadelphia Fed asserts that its survey leads other indicators by weeks and correlates strongly with lagging indicators such as employment and industrial production.

A monthly reading of the data since inception of the index in 1968 leads to a few interesting observations:

• In six of the eight recessions since the 1960's, when the index fell to -24.3, or lower, the US economy was already in a recession.
• In the two instances where this was not the case, September '79 & January '01, the US economy entered a recession 4-months and 2-months later, respectively.

Some will argue that the US economy has transitioned more towards a "service-based" economy vs. a "manufacturing-based" economy over the last several decades, and while that is a true statement, McKinsey & Company noted the following in August '22:

"US manufacturing may be poised for an overhaul and a rebound, with a potentially significant impact on the nation's overall economy. In the United States, manufacturing accounts for $2.3 trillion in GDP, employs 12 million people, and supports hundreds of local economies. Although that represents just 11 percent of US GDP and 8 percent of direct employment, the sector makes a disproportionate economic contribution, including 20 percent of the nation's capital investment, 35 percent of productivity growth, 60 percent of exports, and 70 percent of business R&D spending."

So, yes, the US has moved more towards a "service-based" economy over the last 40+ years, yet, since "peak manufacturing" in 1979, we've had six recessions where the two bullet points above hold true. So, this time has to be completely different than history, or we should expect the US economy to enter a recession in the future.

This week's second piece of important data was The Conference Board Leading Economic Index (LEI), released on February 17th. As the name would imply, this index looks at 10 different components that The Conference Board believes are predictive, or "leading", with respect to the direction of the US economy.

The LEI fell by -0.3% in January, following a decline of -0.8% in December. The Conference Board made the following observations in their press release:

"The LEI is now down 3.6% over the six-month period between July 2022 and January 2023 – a steeper rate of decline than its 2.4% contraction over the previous six-month period (January – July 2022)."

Further, they note: "The US LEI remained on a downward trajectory, but its rate of decline moderated slightly in January," said Ataman Ozyildirim, Senior Director, Economics, at The Conference Board. "Among the leading indicators, deteriorating manufacturing new orders, consumers' expectations of business conditions, and credit conditions more than offset strengths in labor markets and stock prices to drive the index lower in the month. The contribution of the yield spread component of the LEI also turned negative in the last two months, which is often a signal of recession to come. While the LEI continues to signal recession in the near term, indicators related to the labor market—including employment and personal income—remain robust so far. Nonetheless, The Conference Board still expects high inflation, rising interest rates, and contracting consumer spending to tip the US economy into recession in 2023."

As discussed in "Reading the FOMC Tea Leaves" and in "Layoffs…What Are They Telling Us?", the goal isn't to spark fear or panic, rather, to prepare for what may be coming. Investors often get caught up in acting as though a recession means the world is coming to an end, but recessions should be looked at as a natural part of the cleansing process that allows markets to reset and move directionally more towards fair value. Further, a recession often presents a generational buying opportunity for risk assets. The key though is having the capital available to do so when the time comes.[7]

Footnotes and Sources

1. The Wall Street Journal, February 24, 2023
2. The Wall Street Journal, February 24, 2023
3. The Wall Street Journal, February 24, 2023
4. The Wall Street Journal, February 22, 2023
5. The Wall Street Journal, February 23, 2023
6. CNBC, February 22, 2023
7. zerohedge.com/markets/do-not-be-fooled-it-return-normal

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Please consult your financial professional for additional information.