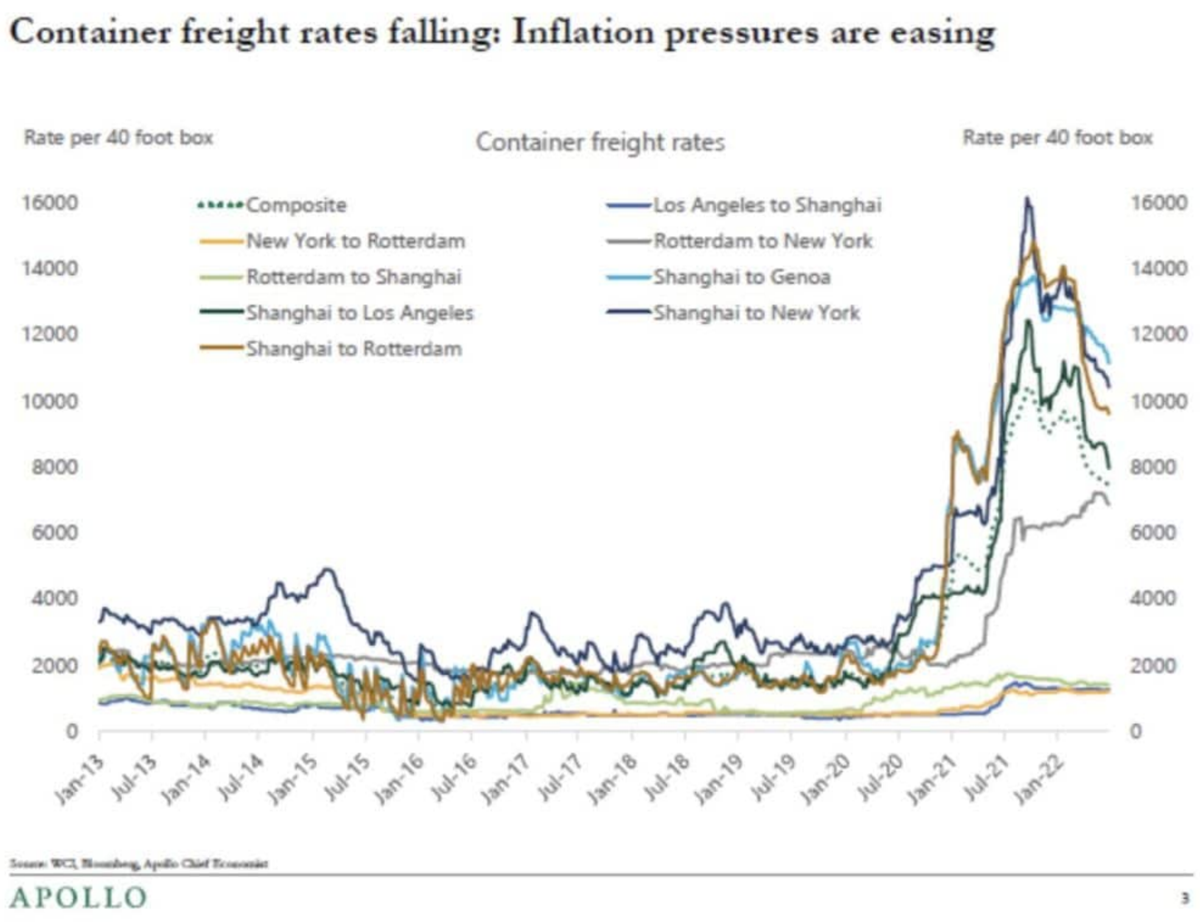
Inflation U-Turn Ahead

There are a growing number of signs that a u-turn in inflation rates may be upon us. For instance, the graph below shows that various significant container freight rates have peaked. Falling shipping costs also imply that the supply and demand for goods are normalizing. Adding to the evidence that inflation may be making a u-turn, metals prices are falling rapidly, as we shared yesterday. Many other commodities, including energy products, are off their all-time highs. Target, Gap, and other retailers are cutting prices to help relieve their troubling high inventories. Further fueling the u-turn theory, used car prices and home price inflation are peaking. The microchip shortage, which greatly limited the supply of new cars, is easing. Peak inflation may be here. Got bonds?



What To Watch Today

Economy

- **MBA Mortgage Applications**, the week ended June 24 (-4.2% prior)
- **GDP Annualized**, quarter-over-quarter, 1Q third (-1.5% expected, -1.5% prior)
- **Personal Consumption**, quarter-over-quarter, 1Q third (3.1% expected, 3.1% prior)
- **GDP Price Index**, quarter-over-quarter, 1Q third (8.1% expected, 8.1% prior)
- **Core PCE**, quarter-over-quarter, 1Q second (5.1% expected, 5.1% prior)

?**Earnings**

Pre-market

- **Barnes & Noble Education** (BNED)
- **Bed Bath & Beyond** (BBBY)
- **General Mills** (GIS)
- **McCormick & Co.** (MKC)
- **Paychex** (PAYX)

Post-market

- **MillerKnoll** (MLKN)

Market Trading - Stocks Fail At First Resistance

Yesterday, several economic measures provided very disappointing outlooks which put stocks on their heels all day. While markets remain on short-term buy signals, the failure at the first level of resistance is not encouraging and suggests the reflexive rally may not have as much life to it as hoped. While the energy sector did well, everything else lagged.

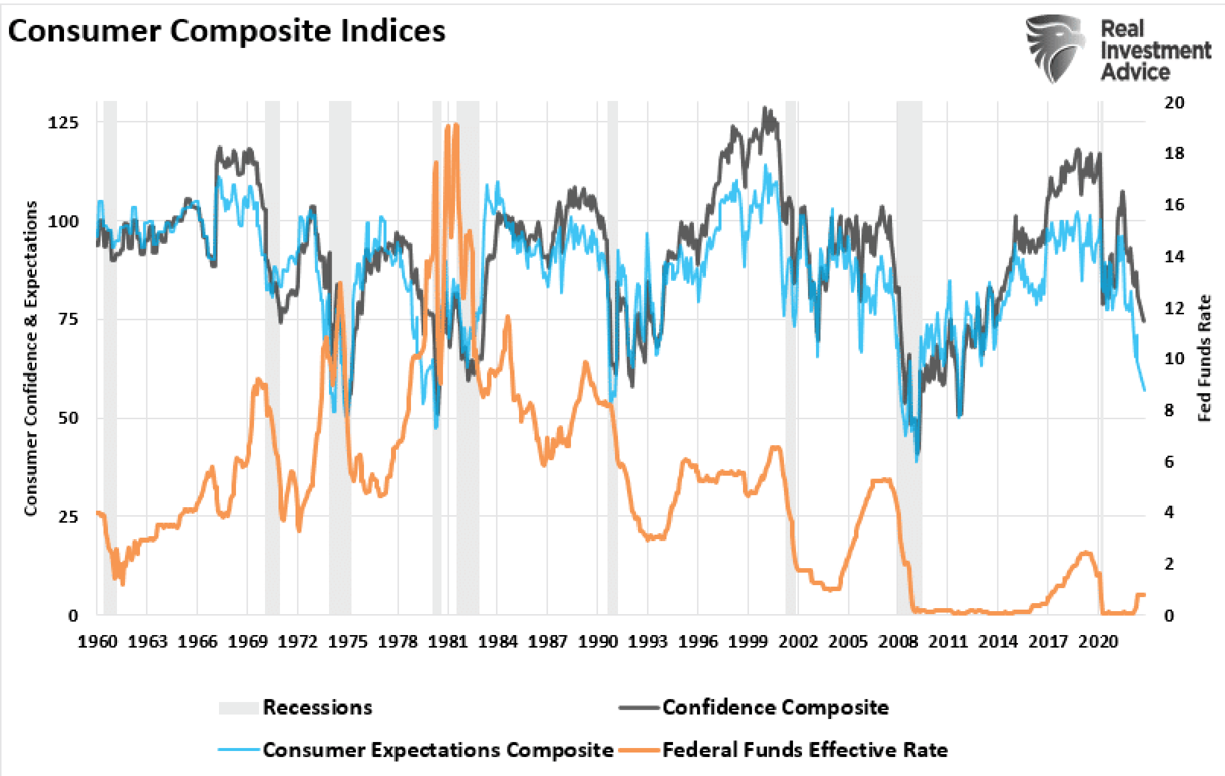
With only a couple of days left in the week to rebalance portfolios, we will see if markets can muster a bit of recovery tomorrow. If not a break below 3800 is the current stop level before retesting previous lows.

Consumer Confidence is Worsening

Tuesday's [Consumer Confidence] Index fell to 98.7 from 106.4, the lowest level since 2021. The decline was led almost entirely by the expectations index, which fell to 66.4, the lowest level since 2013. The present conditions index was marginally lower. The graph below shows the difference between the present situation index and the expectations index is at or below levels consistent with recessions.

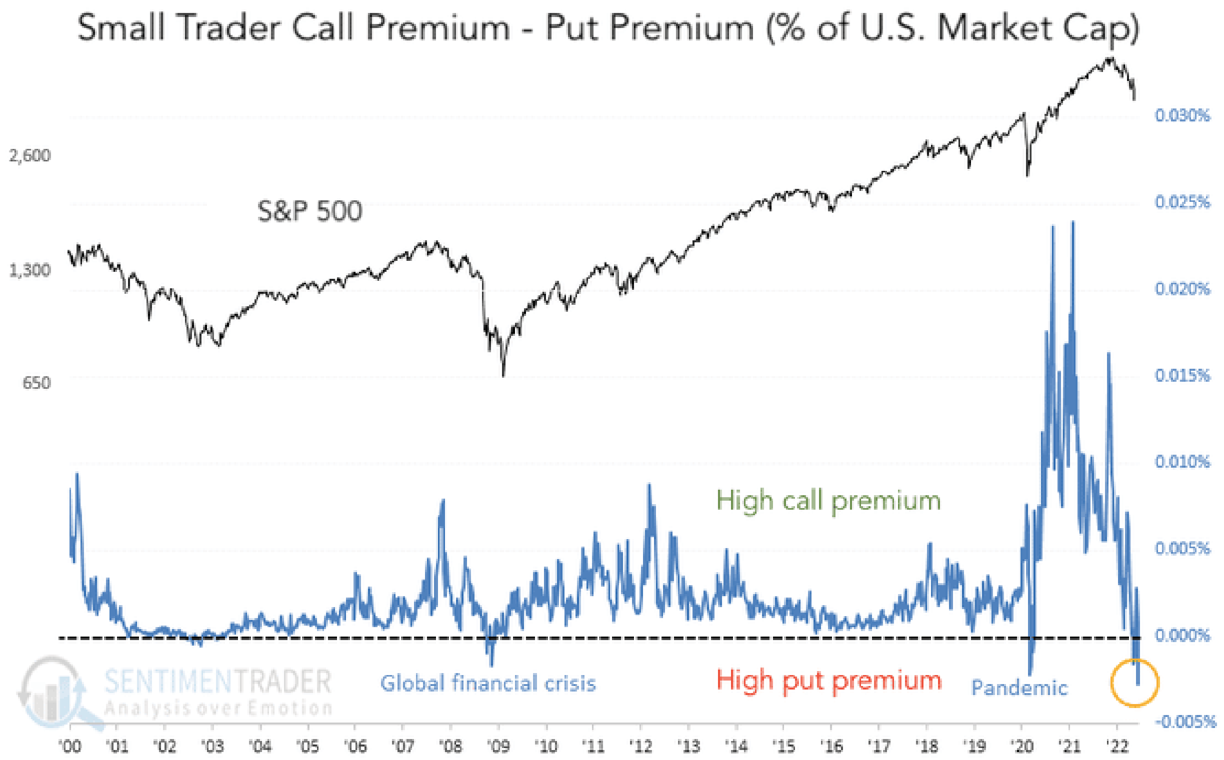
> Per the Conference Board: ?*While the Present Situation Index was relatively unchanged, the Expectations Index continued its recent downward trajectory?falling to its lowest point in nearly a decade. Consumers? grimmer outlook was driven by increasing concerns about inflation, in particular rising gas and food prices. Expectations have now fallen well below a reading of 80, suggesting weaker growth in the second half of 2022 as well as the growing risk of recession by yearend.?*

Our composite consumer confidence measure (which averages both the Conference Board and UofM indices) is plunging rapidly. Currently, both the current and future expectations measures are at levels that previously marked recessions. It is also at levels where both a Fed rate and inflation u-turn occurred.



Small Traders are Very Bearish

Small traders are betting on a stock market decline more so than in 2008 and 2020. Per Sentimentrader, the small trader options premium shows an unprecedented level of the put premium. The put premium measures the amount of money spent on put options. Is retail right this time? Or are institutional investors taking advantage of them once again?



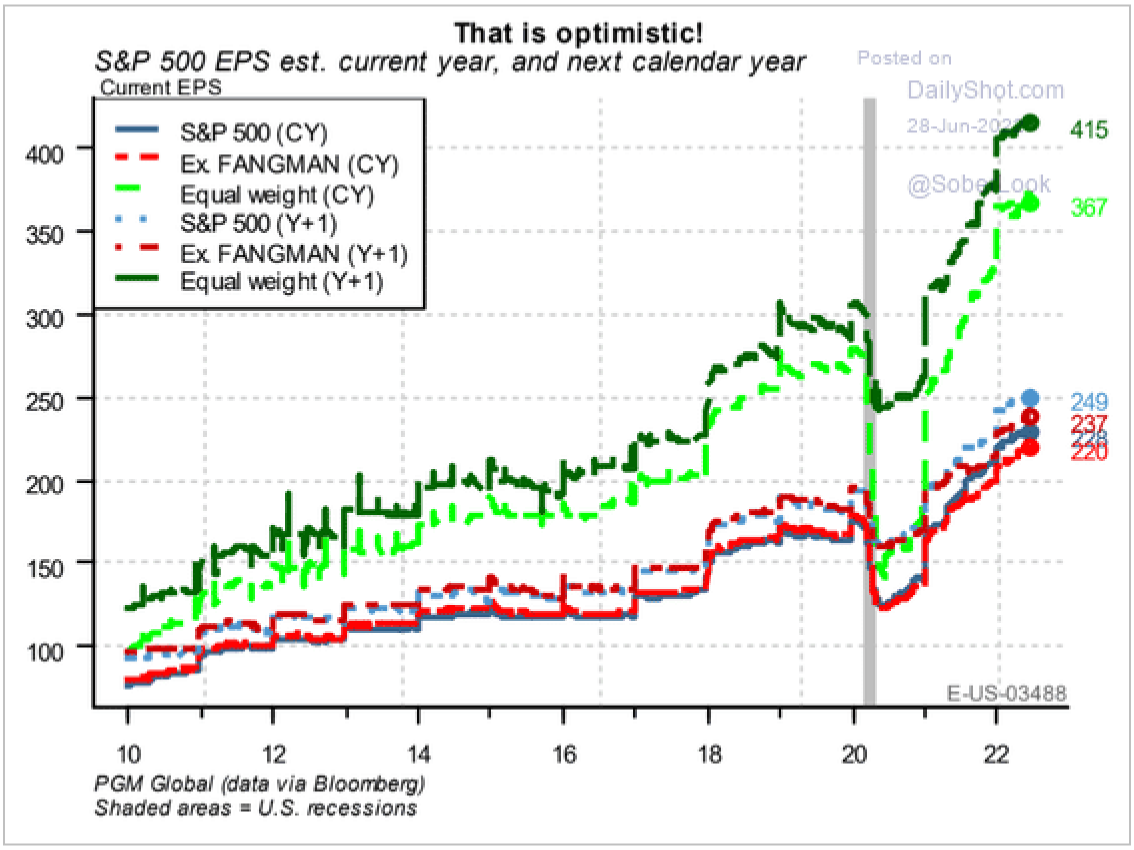
Meta, An Unexpected Value Play

What do Berkshire Hathaway, J&J, Exxon, JP Morgan, and Meta have in common? Those are the top five holdings of the iShares Russell 1000 Value ETF. Meta, aka FaceBook, is likely the shocker in the group as most investors probably classify it as a growth stock. That was the case for the last ten years, but double-digit earnings growth coupled with a 55% decline in its stock price puts it squarely in the value camp. Meta has a P/E ratio of 12.82 (shown below) and a Forward P/E of 13.27. Other valuations stats, such as PEG (2.02) and Price to Sales (3.88), may not be as appetizing for value hunters but are not too high. However, the takeaway is that the market has reduced the price of many stocks by 50% or more. As a result, some companies with solid growth potential are trading at more traditional value stock valuations.

All of Meta's valuations shared above are better than J&J, which many consider a tried and true value company. J&J comparable stats: P/E 18.43, Forward P/E 17.39, PEG 5.52, and Price to Sales 5.12.

What Recession?

Despite growing signs the economy is slipping into a recession, corporate earnings estimates continue upward. As shown below, courtesy of the Daily Shot, Wall Street estimates for the S&P 500 and two variations of the S&P 500 show earnings are expected to climb this year and next year. Helping expected earnings climb, as shown in the second graph, are widening expectations for net margins. This expectation implies that companies, in the aggregate, will be able to pass on higher input costs successfully. Barring a reversal of Fed policy, a sharp u-turn in inflation, and a surge in economic activity, these optimistic estimates will likely be revised lower. For more on future earnings expectations, please read ***Earnings Recession Coming As Fed Hikes Rates***.



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