Weekly Wire

APRIL 3, 2023

BRINKER CAPITAL INVESTMENTS
AN ORION COMPANY

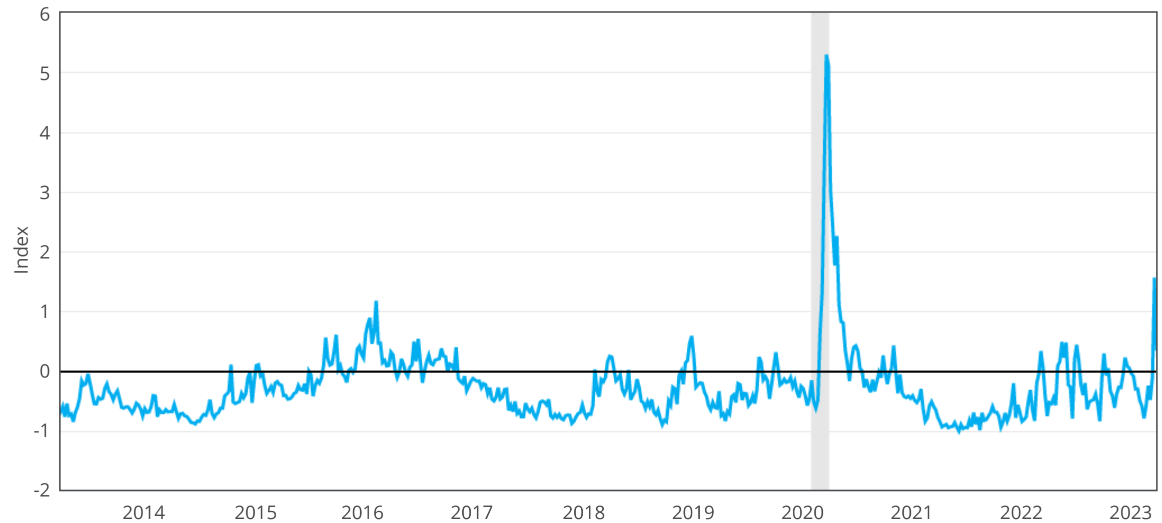
A Rate Hike By Any Other Name Would Tighten Financial Conditions Just the Same

Our apologies to The Bard for this week's title, an admittedly awful take on one of the most famous bits of dialogue penned by the great William Shakespeare - "A rose by any other name would smell as sweet," as said by Juliet to Romeo in the play Romeo & Juliet. While the quality of our prose might be underwhelming, the point about tightening financial conditions is worth making.

As we know, the Federal Reserve has raised rates nine times over the past year in hopes of bringing down historically high inflation. And as we also know, the way high interest rates solve for high inflation is they make capital more expensive for consumers and corporations, which in turn slows consumer and corporate spending, which in turn slows the economy, which in turn brings down inflation. Said differently, the Fed is raising rates to tighten financial conditions. But it isn't just the Fed and higher rates that influence financial conditions. Consumer and corporate sentiment play a part, as does the ability and willingness of banks to extend credit to consumers and companies. This brings us back to the title of this week's piece.

It would seem the failure of Silicon Valley Bank and the ongoing concerns over the banking system should be thought of as a rate hike by another name that has indeed tightened financial conditions just the same. One way to quantify this is the St. Louis Fed Financial Stress Index which measures the degree of financial stress in the markets – zero represents normal market conditions; values below zero represent below-average market stress and values above zero represent above-average market stress. Well, two weeks ago the Index jumped to 1.6, its highest level since the early days of the pandemic (see chart), while Fed Chair Powell, at his post-FOMC March meeting press conference, said a tightening of financial conditions would work in the same direction as rate tightening. We don't think the banking system faces systemic risk, but we do think its struggles of late have tightened financial conditions and have increased the risk of an economic recession.

St. Louis Fed Financial Stress Index



Stocks, bonds, and commodities (3/31/2023)

Security name	Last	QTD chg	YTD chg	12mo chg
S&P 500	4109.31	0.00%	7.03%	-9.60%
MSCI AC World ex USA	298.68	0.00%	6.18%	-7.52%
MSCI EAFE	2092.60	0.00%	7.65%	-3.62%
MSCI EM	990.28	0.00%	3.54%	-13.58%
Bloomberg Barclays US Agg	91.09	0.00%	2.48%	-6.61%
Crude Oil WTI	75.70	0.04%	-5.68%	-23.74%
Natural Gas	2.17	-2.26%	-47.22%	-62.13%

Treasury rates (3/31/2023)

	Price	Yield
2Y	99.22 / 99.2	4.023
3Y	102.0 / 102	3.788
5Y	100.0 / 100	3.578
7Y	100.1 / 100	3.536
10Y	100.0 / 100	3.470
30Y	99.15 / 99.1	3.651

Weekly reports

This week (4/3/2023)

- Feb JOLTS Job Openings
- Mar Nonfarm Payrolls SA

Week of 3/27/2022

- Jan FHFA Home Price Index 393.2
- Mar Chicago PMI SA 43.8

Source: Federal Reserve Bank of St. Louis

Brinker Capital Market Barometer

MARCH 2023

Equity markets couldn't continue the strong gains to start the year as global markets declined in February. Fixed income markets also saw losses as rates rose across the yield curve. The extremely hot January jobs number marked the year-to-date peak for risk assets. The Federal Reserve continues to stick to its hawkish tone, noting that further rate increases are needed and rates will need to remain higher for longer. The fourth-quarter earnings period all but wrapped up with fewer than average companies beating expectations and the first YoY decline in earnings since Q2 2020. While domestic earnings are under pressure, developed foreign markets managed a slight increase and have seen smaller downward revisions to future earnings estimates. The trend of lower inflation readings took a pause during the month as most data was slightly above expectations and led to a renewed fear that inflation may prove to be stickier than many hoped. The 2Y/10Y yield curve remains highly inverted and the 1-Yr Treasury yield crossed above 5% for the first time since 2007. Economic data during the month generally proved more resilient than some had feared. While this may put additional pressure on the Fed to destroy demand, recession fears continue to be kept at bay. The market environment remains highly uncertain, but the opportunity set for multi-asset class portfolios continues to expand on a forward-looking basis.

SHORT-TERM FACTORS (< 6 months)

	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	
Momentum			●		Six month returns remain positive despite the February pullback; choppy market environment persists
Trend			●		Markets remain above long term moving averages but are testing upward trend of shorter averages
Investor sentiment				●	Survey data bearish but off extremes; fund flows remain tepid
Seasonality				●	Strong January as well as 3rd year of presidential cycle tends to bode well for forward returns

INTERMEDIATE-TERM FACTORS (6-36 months)

	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	
Fiscal policy			●		Spending increases unlikely; debt ceiling debate bears watching
Monetary policy		●			While the pace of rate hikes has slowed, rhetoric from Fed remains fairly hawkish
Inflation		●			Negative January surprise drives importance of next few months in establishing inflation trend
Interest rate environment		●			Deep curve inversion signals growth warning; higher short term rates affecting cost of capital
Macroeconomic			●		Global PMIs show contraction; labor market strength continue despite slowdown/recession fears
Business sentiment		●			Business confidence measures remain subdued as a growth slowdown is expected
Consumer sentiment		●			Consumer sentiment has rebounded over the past few months but remains depressed
Corporate earnings			●		Q4 earnings were first YoY decline since Q3 2020; foreign earnings and revisions proving resilient
Credit environment				●	Level of credit spreads at or below long-term averages; defaults remain low; credit conditions modest

LONG-TERM FACTORS (36+ months)

	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	
Valuation			●		U.S. equity valuations near long-term averages; overseas markets below average valuations
Business cycle			●		Q4 GDP came in higher than expectations but underlying components stoke slowdown fears
Demographics			●		Emerging markets possess more favorable trends overall than developed markets

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