Midwest Financial

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Brian Johnson, RFC
706 Montana Street
Glidden, IA 51443
www.midwestfinancial.us
brian@midwestfinancial.us
712-659-2156

The SITREP for the week ending 06/03/2022

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SIT REP: n. a report on the current situation; a military abbreviation; from "situation report".

In the markets:

U.S. Markets: **U.S. stocks surrendered a portion of the previous week's strong gains as investors continued to question whether the Federal Reserve would be able to rein in inflation without causing a recession.** All of the major equity benchmarks finished the week to the downside. The Dow Jones Industrial Average shed 313 points, finishing the week at 32,900, down -0.9%. The technology-heavy NASDAQ Composite shed -1% and closed at 12,013. **By market cap, the large cap S&P 500 fared the worst, ending down -1.2%, while the mid cap S&P 400 retreated -0.7% and the small cap Russell 2000 finished down -0.3%.**

International Markets: **International markets were mixed for the week.** Canada's TSX ticked up 0.2% last week, while the United Kingdom's FTSE 100 shed -0.7%. On Europe's mainland, France's CAC 40 pulled back -0.5% and Germany's DAX finished essentially flat. In Asia, China's Shanghai Composite rose 2.1% and Japan's Nikkei rallied 3.7%. **As grouped by Morgan Stanley Capital International, developed markets declined -1%, while emerging markets finished the week up 0.8%.**

Commodities: **Major commodities finished the week mixed.** Precious metals closed to the downside with Gold giving up -0.4% to $1850.20 per ounce and Silver retreating -0.9% to $21.91. Energy had a second week of gains with West Texas Intermediate crude oil rising 3.3% to $118.87 per barrel and Brent crude adding 4.7% to $121.05. The industrial metal copper, viewed by some analysts as a barometer of world economic health due to its wide variety of uses, finished the week up 3.8%.

May Summary:

Despite all the intra-month volatility, the majority of the U.S. benchmark indexes finished the month of May flat. The Dow Jones Industrial Average was essentially unchanged on a percentage basis, finishing down just 90 points for the month. It was a similar story for both the large cap S&P 500 and the small cap Russell 2000. The mid cap S&P 400 managed a 0.6% increase in the month of May, while the NASDAQ Composite ended the month down -2.1%.

For the month of May, Canada declined -0.2%, while the United Kingdom gained 0.8%. France and Germany ended the mixed with France declining -1% and Germany gaining 2.1%. China rallied 4.6% and Japan added 1.6%. Developed markets finished the month up 2%. Emerging markets added 0.6%.

Gold and Silver finished the month of May down -3.3% and -6.1%, respectively, while West Texas Intermediate rallied 9.5%. Brent gained 9%. Copper finished the month down -2.6%.

U.S. Economic News: **The number of people filing for first-time unemployment benefits fell by 11,000 last week to just 200,000, reflecting one of the strongest labor markets in decades.** Economists had expected initial jobless claims to total 210,000. Applications for unemployment benefits have fallen the last two weeks after hitting a four-month high in early May. Claims fell the most in Kentucky, Pennsylvania, Georgia, and Florida. California and Mississippi were the only states to post sizable increases. Meanwhile, the number of people already collecting benefits, **continuing claims, fell by 34,000 to 1.31 million. That number is still at its lowest level since 1969.**

The country added a stronger-than-expected 390,000 new jobs in May, signaling the labor market and the broader economy remain resilient despite mounting macroeconomic pressures. Economists had forecast an increase of just 328,000 new jobs after reports leading up to the release hinted at slower hiring. **The increase in employment was the smallest in 13 months, however**. Overall, the unemployment rate remained unchanged at

3.6%--just a tick below the pre-pandemic low. The size of the labor force grew by 330,000 in May, nudging the participation rate up to 62.3% from 62.2%. **Analysts noted the stronger-than-expected report is likely to allow the Fed to continue hiking rates.** Restaurants and hotels again led the way in hiring, adding 84,000 jobs. Employment also rose by 75,000 at professional businesses, 47,000 in transportation and warehousing, and 36,000 in construction. Chief economist Bill Adams of Comerica Bank stated, "Another month of solid job growth in May is further evidence that the U.S. economy was not in a recession in the spring."

The number of job openings dropped by roughly half a million in April to 11.4 million open positions, according to the latest data from the Labor Department. Furthermore, **the number of people who quit their jobs remained little changed at 4.4 million.** Quits topped 4 million last summer for the first time on record, part of a pandemic-era trend that became known as "the great resignation". Prior to COVID, the number of people quitting jobs averaged fewer than 3 million per month. Analysts note the U.S. labor market may be the economy's saving grace as the Federal Reserve moves to raise interest rates to tame inflation. Higher rates are likely to slow the economy, however as long as workers feel secure in their jobs, they're likely to keep spending—and steady consumer spending should help the economy avoid a recession. Job openings fell the most in health care and social services (-266,000), retail (-162,000) and hotels and restaurants (113,000). Openings rose in manufacturing, transportation and warehousing. **The so-called "quits rate" remained unchanged at 2.9% for the third month in a row.**

Home prices rose again, hitting all-time highs despite mortgage rates also being on the rise. The S&P CoreLogic Case-Shiller 20-city home price index was up a record 21.2% year-over-year in March and up 3.1% from the previous month. Once again, Phoenix had the highest rate of home-prices in the country--up a whopping 32% from the same time last year. Dallas was second with a 30.7% annual increase. However, Rubeela Farooqi, chief U.S. economist at High Frequency Economics noted **that home prices are bound to slow as mortgage rates continue to rise. The rate on a 30-year fixed rate mortgage has almost doubled to 5.25% from 2.75% last fall.**

Manufacturing activity increased in May according to the latest report from the Institute for Supply Management (ISM). ISM reported its Manufacturing Purchasing Managers' Index (PMI) rose to 56.1 in May from 55.4 in the prior month. The reading exceeded the consensus forecast of a decline to 54.5. In the report, the index for new orders rose 1.6 points to 55.1 as demand continues to increase despite higher prices. Employment, however, pulled back 1.3 to 49.6. **All of the six biggest manufacturing industries posted moderate-to-strong growth in May. Ian Shepherdson, chief economist at Pantheon Macro stated, "Fears of a near-term rollover in the sector look overdone, though we think that the ISM index will soften over the next few months before recovering somewhat in the fall."**

The vastly larger 'services' side of the U.S. economy expanded at its slowest pace since early last year, in a similar report from ISM. **ISM reported its Services PMI dropped to 55.9 from 57.1 in May—its lowest reading since February of 2021.** Economists had expected a reading of 56.7. Still the reading signaled growth--numbers over 50 are considered positive, while readings over 55 are considered exceptional. The decline was led by a decline in business activity and slowing supplier deliveries. Business activity slumped 4.6 points to 54.5. Analysts at Contingent Macro Advisors wrote that while service industry growth was decelerating, it remains historically strong. **"There are (so far) few signs that this slowdown is more than just an expected deceleration after heightened activity,"** they wrote.

The confidence of America's consumers dipped in May over worries about higher inflation and a slowing U.S. economy. **The Conference Board reported its Consumer Confidence Index dropped 2.2 points to 106.4 in May. Still, the reading exceeded the consensus forecast of 103.9.** The measure of how consumers feel about the economy right now slipped to 149.6 from 152.9. Some respondents stated the jobs market was not quite as strong as it was a few months ago. A similar gauge that looks ahead six months fell to 77.5 from 79. Lynn Franco, senior director of economic indicators at the board stated **consumers don't "foresee the economy picking up steam in the months ahead." "Inflation remains top of mind for consumers,"** she added.

The Federal Reserve's 'Beige Book', a collection of anecdotal reports from each of its regional banks, found the U.S. economy showed "slight or modest" growth in May, but so did worries about a recession. "Contacts tended to cite labor market difficulties as their greatest challenge, followed by supply chain disruptions," the survey stated. Rising interest rates, inflation, and international conflict rounded out other concerns weighing on respondents. The Federal Reserve has raised its key short-term interest rates twice this year to try to reign in the worst outbreak of inflation in 40 years.

International Economic News: **The Bank of Canada appears to have concluded it will need to lift its benchmark interest rate to at least 3% to counter rising inflation.** Canada's benchmark rate is currently 1.5% following a half-point increase on June 1. Before the pandemic, Canada's benchmark interest rate was at 1.75%--which was the highest policymakers managed to achieve following the 2008 financial crisis. Following the 'Great Recession', inflation hadn't been an issue for many of the world's developed economies. But, as Paul Beaudry, one of the central bank's deputy governors, said in a speech on June 2, the "situation today is totally different." The consumer price index between 2010 and 2020 never increased more than 3.7% on a year-over-year basis. In April, the index surged 6.8%, the second-biggest increase since the early 1980s. **Inflation has now exceeded the high end of the Bank of Canada's comfort zone of 1-3% for 12 consecutive months--unprecedented since the central bank adopted the index as its guide for policy in 1991.**

Across the Atlantic, **the United Kingdom marked a milestone in trade relations with the United States by signing its first state-level trade and economic development Memorandum of Understanding (MoU) with Indiana. The MoU creates a framework to remove barriers to trade and investment, paving the way for the United Kingdom and Indiana businesses to invest, export, expand and create jobs.** The UK is the seventh largest export market for Indiana, and the state buys $1.4 billion worth of goods from the UK. In Indiana, International Trade Minister Ranil Jayawardena said, "With the signing of this MoU, British businesses can capitalize on the great opportunities for collaboration in areas like innovation and manufacturing." In the United Kingdom, Secretary of State for International Trade Anne-Marie Trevelyan said, "This is Global Britain in action, making innovative deals on the world stage--and will help UK companies grow faster, innovate more and support jobs and economic growth."

On Europe's mainland, **inflation in France continued to rise in May, reaching an annualized 5.2%--up 0.4% from April. As in previous months, inflation is primarily driven by energy prices, up 28% year-on-year mainly due to higher oil prices. However, price increases were across the board with food prices up 4.2% year-over-year, manufactured goods up 2.9%, and services up 3.2%.** In all major categories, inflation was well above the ECB's intended target of 2%. France's national statistics agency INSEE reported gross domestic product contracted by 0.2% in the first three months of the year. **France's worse-than-estimated performance puts an end to the country's strong economic rebound from the pandemic and poses a challenge to President Emmanuel Macron, who was re-elected just last month.**

Germany's annual inflation rate accelerated to 7.9% in May, its highest level in nearly 50 years, according to Germany's Federal Statistics Office. Inflation jumped 0.5% from April, with **energy prices more than 38% higher than the same time last year.** Germany's current inflation rate is the highest since the winter of 1973-1974 when an oil crisis fueled sharply higher energy prices. In comments shortly before the latest inflation figure was released, Finance Minister Christian Lindner said that the top priority must be fighting inflation. "Inflation is an enormous economic risk, and we must fight this inflation so that no economic crisis grows out of it, so that no spiral develops through which inflation feeds itself," Lindner said.

In China, **the city of Shanghai has lifted its two-month lockdown, much to the relief of its 25 million residents. Citizens of Shanghai have spent the last two months under a ruthlessly enforced lockdown. The prolonged isolation fueled anger and rare protests inside China's most populous metropolis, battered**

the city's manufacturing economy, and disrupted supply chains around the world. Shanghai Port is the world's largest container port and a major transportation hub. Jubilant residents took to social media to celebrate with comments such as one WeChat user wrote: "We often said Shanghai was 'liberated' in 1949. Today, it's another 'liberation'!"

Japan's parliament enacted a 2.7 trillion yen ($21 billion) extra budget to tackle soaring fuel and food prices. The extra budget is for the current fiscal year that started April 1 and will fund part of a 6.2 trillion yen ($48 billion) emergency economic package that Prime Minister Fumio Kishida's government adopted in late April. Nearly 1.2 trillion yen ($9.4 billion) will be used to extend the current oil subsidy program through the end of September. Crude oil prices have risen sharply due to fears of disruptions in supplies from Russia due to its invasion of Ukraine. Wheat and corn prices are also up significantly, prompting food prices to soar.

Finally: The Biden administration is at once demanding that U.S. oil producers pump more in order to lower prices at the pump, while at the same time the administration is blasting U.S. refiners and producers for "gouging" and looking at punishing them with a "windfall tax". To address these concerns, Chevron CEO Mike Wirth appeared on Bloomberg TV stating that adding refinery capacity is incredibly difficult, especially in the current environment. Wirth stated, "You're looking at committing capital 10 years out, that will need decades to offer a return for shareholders, in a policy environment where governments around the world are saying: we don't want these products." "We're receiving mixed signals in these policy discussions," Wirth added. The United States hasn't had a new refinery built since the 1970's. As the following graphic shows, the rate of price increases for refined products like jet fuel, diesel, and gasoline, have surged far higher than the price of crude oil.

(**Sources:** All index- and returns-data from Yahoo Finance; news from Reuters, Barron's, Wall St. Journal, Bloomberg.com, ft.com, guggenheimpartners.com, zerohedge.com, ritholtz.com, markit.com, financialpost.com, Eurostat,0020Statistics Canada, Yahoo! Finance, stocksandnews.com, marketwatch.com, wantchinatimes.com, BBC, 361capital.com, pensionpartners.com, cnbc.com, FactSet.)

The SITREP | Glossary of Terms

Index, Exchange and Investment Definitions:

- **Barclays Aggregate Index -** An unmanaged index of fixed rate investment grade securities with at least one year to maturity combining the Barclays U.S. Treasury Bond Index, the Barclays U.S. Government-Related Bond Index, the Barclays U.S. Corporate Bond Index, and the Barclays U.S. Securitized Bond Index.
- **Barclays US Corporate Index** is a broad-based benchmark that measures the investment grade US dollar- denominated, fixed-rate, taxable corporate bond market. It includes USD denominated securities issued by US and non-US industrial, utility, and financial issuers that meet specified maturity, liquidity, and quality requirements.
- **Barclays Aggregate Bond Index** (formerly known as the Lehman Brothers Aggregate Bond Index), an unmanaged, market capitalization weighted index of government and corporate bonds, mortgage-backed securities, and other asset-backed securities, with interest reinvested. This index commonly serves as a proxy for the U.S. bond market.
- **The Bloomberg Commodity Index** is designed to be a highly liquid and diversified benchmark for the commodity futures market. The Index is composed of futures contracts on 19 physical commodities and was launched on July 14, 1998.
- **CBOE Volatility Index** shows the market's expectation of 30-day volatility. It is constructed using the implied volatilities of a wide range of S&P 500 index options. This volatility is meant to be forward looking and is calculated from both calls and puts. The VIX is a widely used measure of market risk and is often referred to as the "investor fear gauge."
- **The DJ Equity All REIT Total Return Index** measures the total return performance of the equity subcategory of the Real Estate Investment Trust (REIT) industry as calculated by Dow Jones.
- **The S&P 500** is a market-cap weighted index composed of the common stocks of 500 leading companies in leading industries of the U.S. economy.
- **The Dow Jones Industrial Average** is a price-weighted index of 30 actively traded blue-chip stocks.
- **The NASDAQ Composite Index** is an unmanaged, market-weighted index of all over-the-counter common stocks traded on the National Association of Securities Dealers Automated Quotation System.
- **The Russell 2000 Index** measures the performance of the small-cap segment of the U.S. equity universe: market-cap weighted index composed of 2,000 U.S. small-cap common stocks.
- **The CAC-40 Index** is a narrow-based, modified capitalization-weighted index of 40 companies listed on the Paris Bourse.
- **The ISEQ Overall Index** is a capitalization-weighted index of all official list equities in the Irish Stock Exchange, excluding U.K.-registered companies.
- **The FTSE MIB** (Milano Italia Borsa) is the benchmark stock market index for the Borsa Italiana, the Italian national stock exchange.
- **The IBEX 35** is the benchmark stock market index of the Bolsa de Madrid, Spain's principal stock exchange.
- **The DAX 30** is a Blue-Chip stock market index consisting of the 30 major German companies trading on the Frankfurt Stock Exchange.
- **The FTSE 100 Index** is a share index of the 100 companies listed on the London Stock Exchange with the highest market capitalization.
- **The STOXX Europe 600 Index** is derived from the STOXX Europe Total Market Index (TMI) and is a subset of the STOXX Global 1800 Index.
- **The RTS Index** (abbreviated: RTSI, Russian: Индекс РТС) is a free-float capitalization-weighted index of 50 Russian stocks traded on the Moscow Exchange.
- **The SSE Composite Index** is an index of all stocks (A shares and B shares) that are traded at the Shanghai Stock Exchange.

- **The Shanghai Composite Index** tracks the biggest and most important public companies in China.
- **The Hang Seng Index** is a free float-adjusted market capitalization-weighted stock market index that is the main indicator of the overall market performance in Hong Kong.
- **The IDX Composite** or Jakarta Composite Index is an index of all stocks that are traded on the Indonesia Stock Exchange (IDX).
- **The Korea Composite Stock Price Index** or KOSPI is the major stock market index of South Korea, representing all common stocks traded on the Korea Exchange.
- **The Asia Dow** measures the Asia equity markets by tracking 30 leading blue-chip companies in the region.
- **The S&P/ASX 200 Index** is a market-capitalization weighted and float-adjusted stock market index of Australian stocks listed on the Australian Securities Exchange from Standard & Poor's.
- **Nikkei 225 (**Ticker: ^N225) is a stock market index for the Tokyo Stock Exchange (TSE).
- **The Nikkei Average** is the most watched index of Asian stocks.
- **The BSE SENSEX** (Bombay Stock Exchange Sensitive Index), also-called the BSE 30 (BOMBAY STOCK EXCHANGE) or simply the SENSEX, is a free-float market capitalization-weighted stock market index of 30 well-established and financially sound companies listed on the Bombay Stock Exchange (BSE).
- **Karachi Stock Exchange 100 Index** (KSE-100 Index) is a stock index acting as a benchmark to compare prices on the Karachi Stock Exchange (KSE) over a period.
- **The Dow Jones Americas Index** measures the Latin American equity markets by tracking 30 leading blue-chip companies in the region.
- **The Mexican IPC Index** (Indices de Precios y Cotizaciones) is a major stock market index which tracks the performance of leading companies listed on the Mexican Stock Exchange.
- **The Bovespa Index** is a gross total return index weighted by traded volume & is comprised of the most liquid stocks traded on the Sao Paulo Stock Exchange.
- **The S&P/TSX Composite Index** is an index of the stock (equity) prices of the largest companies on the Toronto Stock Exchange (TSX) as measured by market capitalization.
- **The Global Dow** is an equally weighted index of 150 widely traded blue-chip common stocks worldwide.
- **The MSCI World Index** is a free-float weighted equity index that includes developed world markets and does not include emerging markets.
- **The MSCI EAFE Index** is recognized as the pre-eminent benchmark in the United States to measure international equity performance. It comprises the MSCI country indices that represent developed markets outside of North America: Europe, Australasia and the Far East.
- **The MSCI Emerging Markets Index** is a float-adjusted market capitalization index consisting of indices in more than 25 emerging economies.
- **The US Dollar Index** measures the performance of the U.S. dollar against a basket of six currencies.
- **Corporate BBB 1-3-year Index** - as represented by the BBB rated component of the BofA Merrill Lynch 1-3 Year U.S. Corporate Index, comprised of U.S. dollar-denominated investment-grade corporate debt securities publicly issued in the U.S. domestic market with between one and three years remaining to final maturity.
- **High Yield Index** - as represented by the Bank of America Merrill Lynch U.S. High Yield Master II Constrained Index, a market value-weighted index of all domestic and Yankee high-yield bonds, including deferred-interest bonds and payment–in-kind securities.
- **10 -Year US Treasury Index** - This index represents a theoretical rolling 10-year U.S. Treasury note, renewed semiannually to a new higher coupon based on the indicated rise in rates.

Index Disclosures:

"An index is a composite of securities that provides a performance benchmark. Indexes are unmanaged, do not incur management fees/costs/expenses, and cannot be invested-in directly. Past performance is not a guarantee of future results."

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Brian D Johnson

Brian Johnson, RFC
Managing Member
712-659-2156
706 Montana St.
Glidden, IA 51443