MIDWEST FINANCIAL

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The SITREP for the week ending 07/08//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. equities erased much the previous week's losses** on optimism that the Federal Reserve will be able to slow inflation without tipping the economy into recession. The gains pulled the benchmark S&P 500 index out of bear market territory, leaving it down 19.1% from its January peak. The Dow Jones Industrial Average retraced most of last week's decline, rising 0.8% to 31,338. The technology-heavy NASDAQ Composite rallied 4.6% and finished at 11,635. **By market cap, the large cap S&P 500 added 1.9% while the mid cap S&P 400 and small cap Russell 2000 gained 1.1% and 2.4%, respectively.**

International Markets: **Almost all major international markets finished in the green as well**. Canada's TSX rose 0.9%, while the United Kingdom's FTSE 100 added 0.4%. On Europe's mainland, France's CAC 40 and Germany's DAX rose 1.7% and 1.6%, respectively. China's Shanghai Composite had its first down week in six, however, pulling back -0.9%. Japan rose 2.2%. **As grouped by Morgan Stanley Capital International, developed markets gave up -0.5%, while emerging markets finished up 0.6%.**

Commodities: **Major commodities finished the week in the red. Precious metals sold off** with Gold falling -3.3% to $1742.30 per ounce, while Silver retreated -2.2% to $19.24. **Energy retraced all of last week's rebound and then some.** West Texas Intermediate crude oil declined -3.4% to $104.79 per barrel, while Brent crude declined -3.9% to $107.15. The industrial metal copper, viewed by some analysts as a barometer of world economic health due to its wide variety of uses, finished down -2.3% - its fifth consecutive weekly decline.

U.S. Economic News: **Employers added 372,000 new jobs in June, well above the consensus forecast** of around 250,000. The much better-than-expected reading signaled the economy is still powering ahead despite an avalanche of predictions of an impending recession. **Hiring in professional employment led the way rising by 74,000**, while bars, restaurants, hotels and other hospitality businesses created 67,000 new jobs. Corporate economist Robert Frick at Navy Federal Credit Union remarked, "June's strong job growth, especially in the teeth of high inflation, shows that the expansion remains on solid ground." **However, one concern was that the size of the labor force fell for the second time in three months.** The labor force tends to stagnate when hiring slows or jobs become harder to find. The unemployment remained unchanged at 3.6%.

The number of Americans filing first time unemployment claims rose to a six-month high last week, a sign the labor market may finally be slowing. The Labor Department reported 235,000 people applied for initial jobless benefits last week, an increase of 4,000 over the previous week. Economists had expected initial claims to total 230,000. Most of the increase in raw or actual jobless claims was concentrated in just a handful of states: New York, Michigan, California and Georgia. The increase in Michigan is likely tied to temporary furloughs among automakers**. Meanwhile, the number of people already collecting unemployment benefits rose by 51,000 to 1.38 million**. That's the biggest one-week increase since September.

The U.S. economy by many measures appears to be cooling, but the labor market remains quite robust. The Labor Department reported job openings fell slightly in May to a still-high 11.3 million. **Layoffs remained near a record low.** Job openings have slipped for two months in a row after peaking in March, but they've topped 11 million for six consecutive months. Job openings fell the most at white-collar profession businesses (-325,000) and manufacturing (-208,000). Technology companies in particular are scaling back. Meanwhile, the number of people who quit their jobs fell slightly to 4.27 million. **The closely watched 'quits rate' slipped to 2.8% from 2.9%.** Analysts view the quits rate as a more reliable view of the state of the economy as it is assumed that one would only quit a job in lieu of a more lucrative one. **Nick Bunker, director of economic research at Indeed Hiring Lab noted, "This is not what a recession looks like".** The May job openings data "obviously lags what's happening in the labor market presently, but all signs are that it remains strong."

Orders for U.S. factory goods jumped 1.6% in May, bucking a string of recent data showing a softening in the economy. However, some analysts were quick to point out the increase was primarily due to petroleum-related products whose prices have risen sharply. The increase in orders exceeded the 0.6% forecast by economists. However, a survey of senior manufacturing executives signaled a slowdown in June. The Institute for Supply Management (ISM) reported its **national factory activity index slipped to a two-year low** as orders contracted for the first time since the start of the pandemic in the spring of 2020. Manufacturing accounts for 12% of the U.S. economy and is being held up by strong demand for goods even as overall spending rotates more toward the services sector.

In a similar survey, **ISM reported its barometer of business conditions at service-oriented companies such as restaurants, hotels, and retailers, dipped to a two-year low of 55.3 in June—another sign of a slowing U.S. economy.** However, the reading exceeded the consensus forecast of 54. Still, while numbers over 50 signify expansion over contraction, the index has fallen three months in a row. "Inflation is definitely taking a bite from our sales," a retail executive told the Institute for Supply management. Furthermore, the situation doesn't appear likely to improve anytime soon. **The new orders index dropped 2 points to 55.6—a 16 month low**, while the employment index fell 2.8 points to 47.4. That's the third negative reading in employment over the past five months—and the lowest in almost two years.

Federal Reserve officials remained resolute about the need to continue their interest rate hiking trajectory according to the minutes of its June policy meeting released this week. Fed officials "recognized that policy firming could slow the pace of economic growth for a time, but they saw the return of inflation to 2% as critical to achieving maximum employment on a sustained basis," the minutes said. Officials agreed to a rare 75 basis point hike in the Fed funds rate in June – the largest rate hike since 1994 – and "judged that an increase of 50 or 75 bp would likely be appropriate at the next meeting." The central bankers agreed that **"the labor market was very tight, inflation was well above the Committee's 2% inflation objective and the near-term inflation outlook had deteriorated since the time of the May meeting."** In June, Fed officials penciled in getting the policy rate up to near 3.5% by the end of this year and close to 4% in 2023.

International Economic News: **Economists at the Royal Bank of Canada (RBC) warned that Canada was going to enter a 'moderate and short-lived' recession next year as it copes with rising interest rates and rising inflation.** In its latest report, the bank said Canada's unemployment rate is now almost a full percentage point below RBC's assumption of the longer-run, non-inflationary level. "(Recession) has become, in our view, the most likely outcome," Nathan Janzen, one of the report's authors, said. The report predicts the Bank of Canada will follow the lead of the U.S. Federal Reserve, which hiked rates by 75 basis points in June, during its meeting next week. **RBC now expects the Bank of Canada to lift rates to 3.25% by the end of 2022, which they noted is high enough to significantly restrict growth, particularly in Canada, where household debt is very high.**

Across the Atlantic, **British PM Boris Johnson was forced to resign** as dozens of members of his party quit the government after one ethics scandal too many. Outside of parliament, his popularity was also in shambles as surging inflation and stagnation weighs on the British economy. Every major economy has suffered from the effects of the coronavirus pandemic, but the **United Kingdom has had it worse than most of its peers**. Inflation hit a 40-year high of 9.1% in May—the highest among G-7 economies. Furthermore, it is forecast to climb above 11% later this year.

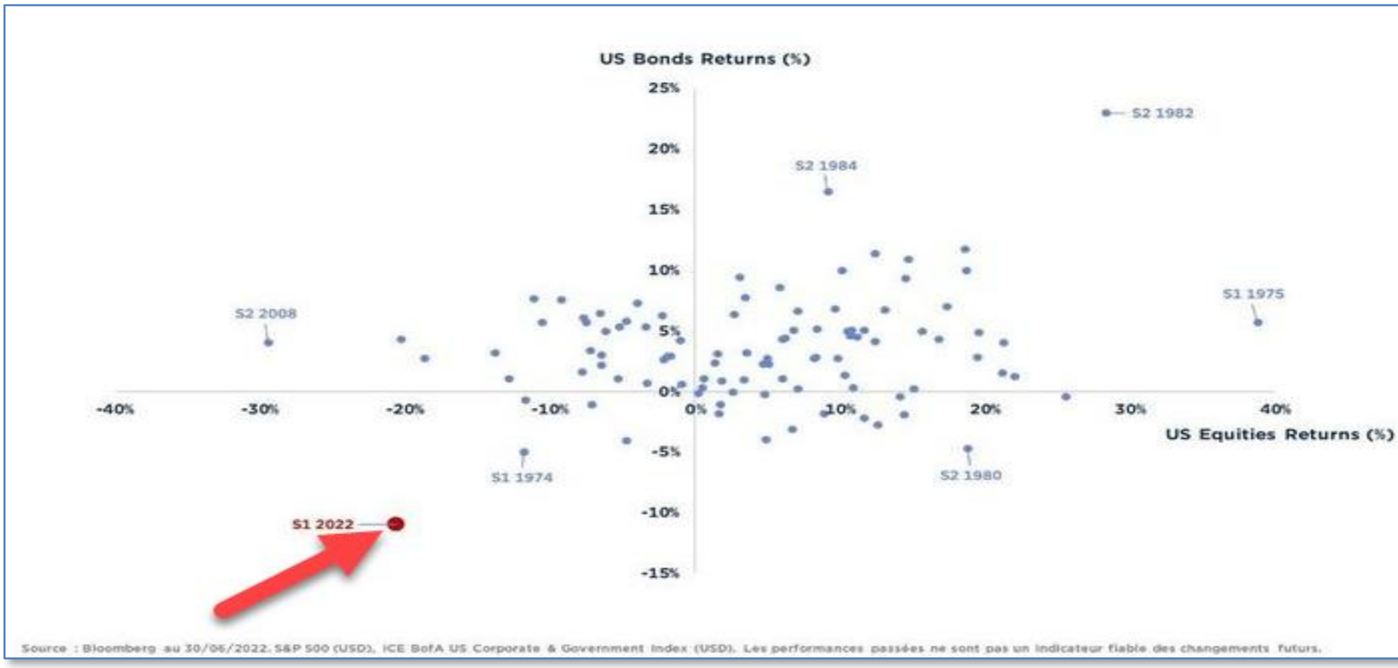
On Europe's mainland, **the French government has unveiled a 20 billion euro ($20.3 billion USD) package of measures meant to help struggling households cope with rising food and energy prices.** The government's move comes as annual inflation reached a record 8.6% for the 19 countries using the euro, propelled by a huge increase in food and energy costs. In France, annual inflation is estimated to be 6.5%, among the lowest in the Eurozone. **The measures include increasing pensions, raising welfare payments, caps on rent increases, and pay raises for civil servants (all themselves inflationary).**

Germany is no longer exporting more than what it imports from other countries, highlighting the strains that the nation and other European economies are facing from surging energy and food prices. **For the first time in 30 years Germany posted its first monthly trade deficit.** Germany posted a foreign trade deficit of 1 billion euros ($1.03 billion USD) in May as import prices surged. This marks a significant moment for the German economy, which had reported trade surpluses every month since 1991. "Germany's vaunted trade surplus is gone," Carl Weinberg, chief economist at High Frequency Economics, said in a note, adding that "higher prices for imports of energy, food and materials are goosing up the import bill."

In Asia, **the United States and China held talks this week to discuss the huge challenges facing the global economy and rising speculation that some Trump-era tariffs could be cut to ease inflation and boost growth.** US Treasury Secretary Janet Yellen and China's Vice Premier Liu He — Beijing's top economic official — had a "substantive conversation" on a call, according to a statement by the US Treasury. The talks, which were initiated by the United States, were described as "candid" and came amid reports the Biden administration may lift some tariffs on Chinese goods as soon as this week. The Chinese readout noted that the exchange was "constructive" and "pragmatic." It added that the two sides discussed "views on the macroeconomic situation and the stability of the global industrial chain and supply chain." Both sides agreed that the global economy is facing severe challenges and placed "great significance" on better policy coordination between China and the United States.

Japan's household spending posted a surprise drop in May, falling for a third consecutive month. Government data showed Japan's spending slipped 0.5% in May from a year earlier. **The consensus forecast was for a 2.1% increase.** Policymakers have been worried about growing pressure on households which are facing surging prices of food and other daily essentials as well as higher costs of utilities such as electricity. Japan's economy is projected to rebound on stronger consumption in the second quarter following contraction in January-March, however higher prices for energy and raw materials are clouding the economic outlook.

Finally: **With the worst first half for the stock market in 60 years now in the books, many want to know - just how unusual was it? In the graphic below, private bank and investment house Edmond de Rothschild showed not only equities had a difficult first half, but the other side of the investment barbell – bonds - did poorly as well. At Deutsche Bank, using a proxy index for the 10-year U.S. Treasury, research strategist Jim Reid showed it was actually the worst first half since 1788 for the stocks and bonds combo! And Michael Every at Rabobank summed it all up stating, "if you bought stocks in H1, you lost; if bonds, you lost; if commodities, you were doing great until recently; if crypto you lost; if the US dollar, you were fine" but lost purchasing power to inflation. (Chart from Edmond de Rothschild)**



(**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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