Cornerstone
ASSET MANAGEMENT GROUP, LLC

Economic Indicators | May 2023| By Kim W. Suchy

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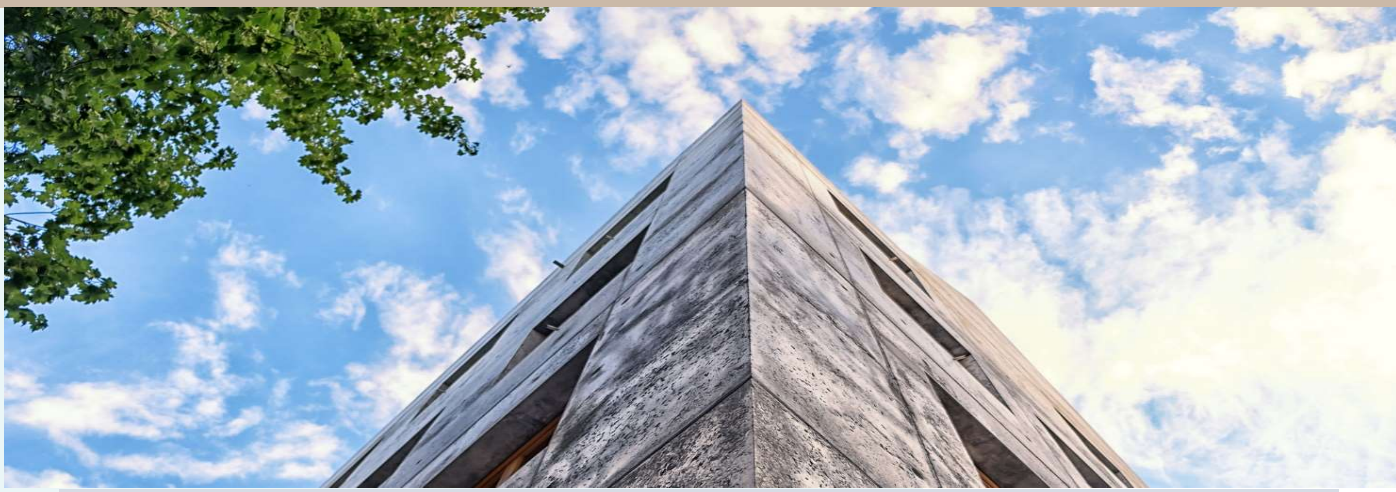


The themes of the letters we write to you often address the headwinds and tailwinds that are apparent in the investment arena. I wish we could report a nice tailwind, but today, we face a rather significant headwind, the U.S. debt ceiling.

Over the past year, the economy has been remarkably resilient to the 500bps hike in the fed funds rate, although it did trigger a temporary financial crisis with the failure of three banks two months ago. That crisis looks to have been mitigated by the Fed as it has not turned into an economy-wide credit contagion and/or recession. In fact, it may have helped the Fed with some heavy lifting as this helped slow the economy and squelch stubborn inflation. At the time of this writing, it is expected that the Fed will hike in early May and pause as it takes a wait and see on the lagged impacts of both the rate hikes on economic growth and inflation.

Assuming this scenario transpires, one headwind disappears but the big one remains: it's the "X-Day" for the federal debt ceiling. This is the day that the government exhausts all its borrowing capacity from the Treasury. We were rapidly approaching that date but tax revenues in April have managed to push this date into mid-June. If there is no deal in Washington by that day, the US will be in technical default. Currently, the U.S. debt ceiling is $31.3T, yes Trillion.

We have seen potential defaults before in recent history, but Congress has managed to establish a resolution just before "X-Day" as they raised the legally allowed amount of debt while establishing spending cuts as a concession. Congress and presidents do this routinely, but when there is a Democratic president and a Republican-led House, the process becomes thorny.

This past week, the House passed a resolution to increase the debt limit by $1.5T in exchange for $5T in budget cuts over ten years. Apparently, the market liked this as the market rallied for two days on the back of this news. However, the Bill has not gone to the Senate where the bloodbath is about to begin. So, what is often the case under this situation is the equity markets gyrate, and the safe-haven becomes short term Treasuries. We have already seen yields on short Treasuries fall as the demand for safe paper begins to tick higher. This will continue until the government checkbook has nothing left and Congress reaches an agreement. At that time, markets will settle down and stabilize.

Note, no one in Congress wants egg on their face should a default take place. Their constituencies would not welcome the cessation of programs or payments and with an election year around the corner, the result would be catastrophic. So, with history as a guide, we must put on our chinstraps and safety belts…the ride will be bumpy but in the end we will not default.

Here is your look at developments in the global marketplace.

POSITIVE DEVELOPMENTS

- Gold prices continue to surge as economic concerns, lower bond yields, a weaker U.S. dollar and a boost in buying this year by central banks has fueled the rally. Gold is up over 10% since late February, before the three dominant bank failures, and is up more than 25% since November. Other metals have rallied as well, i.e., the price of silver has surged nearly 30% in a month. *Note, the World Gold Council reports that China, Russia and Turkey have purchased a combined total of nearly 100 tons of gold over the last two months (period ending April 17th).*
- Builder sentiment in the market for newly-built homes rose in April for the 4th consecutive month, as the supply of existing homes for sale remains scarce. The National Association of Home Builders Index rose to 45 in April, a one-point gain. *Note, anything below 50 is considered negative but the recent print is the highest since September. The index stood at 77 in April 2022.*
- SP500 company earnings that have reported have come in almost 5% above analysts' estimates as of last week, according to Evercore. Barron's notes that while those that have topped their numbers are getting rewarded, those that miss aren't being punished too much. Companies that have announced earnings and sales that beat expectations have gained 2.3%, versus an average advance of 1% over the past 5 years. A double miss has resulted in a mere 1.8% drop, versus an average 2.9% decline. This could be a sign that investors have an optimistic view of the market down the road.
- US households are in good shape as the ratio of liabilities to net wealth has declined 50% since the 2008 financial crisis, and household leverage is currently at levels last seen in the early 1980s according to Haver Economics. If the unemployment rate rises, consumer spending will slow down, but the starting point for US households is very strong.
- New single-family home sales increased 9.6% in March. The median price of new homes sold was $450K in March, up 3.2% yoy. The average price of new homes sold was $562K, up 9.9% versus last year. The good news is that sales continued to recover last month, signaling that activity may have hit bottom back in mid-2022. Sales are on an upward trend and are now up 25.8% off the low in July of last year.
- Personal income rose 0.3% in March while personal consumption was unchanged in March. The best news in this report was that incomes rose 0.3% as private-sector wages & salaries led the way, and wage gains outstripped the pace of inflation for the 8th time in the last 9 months.

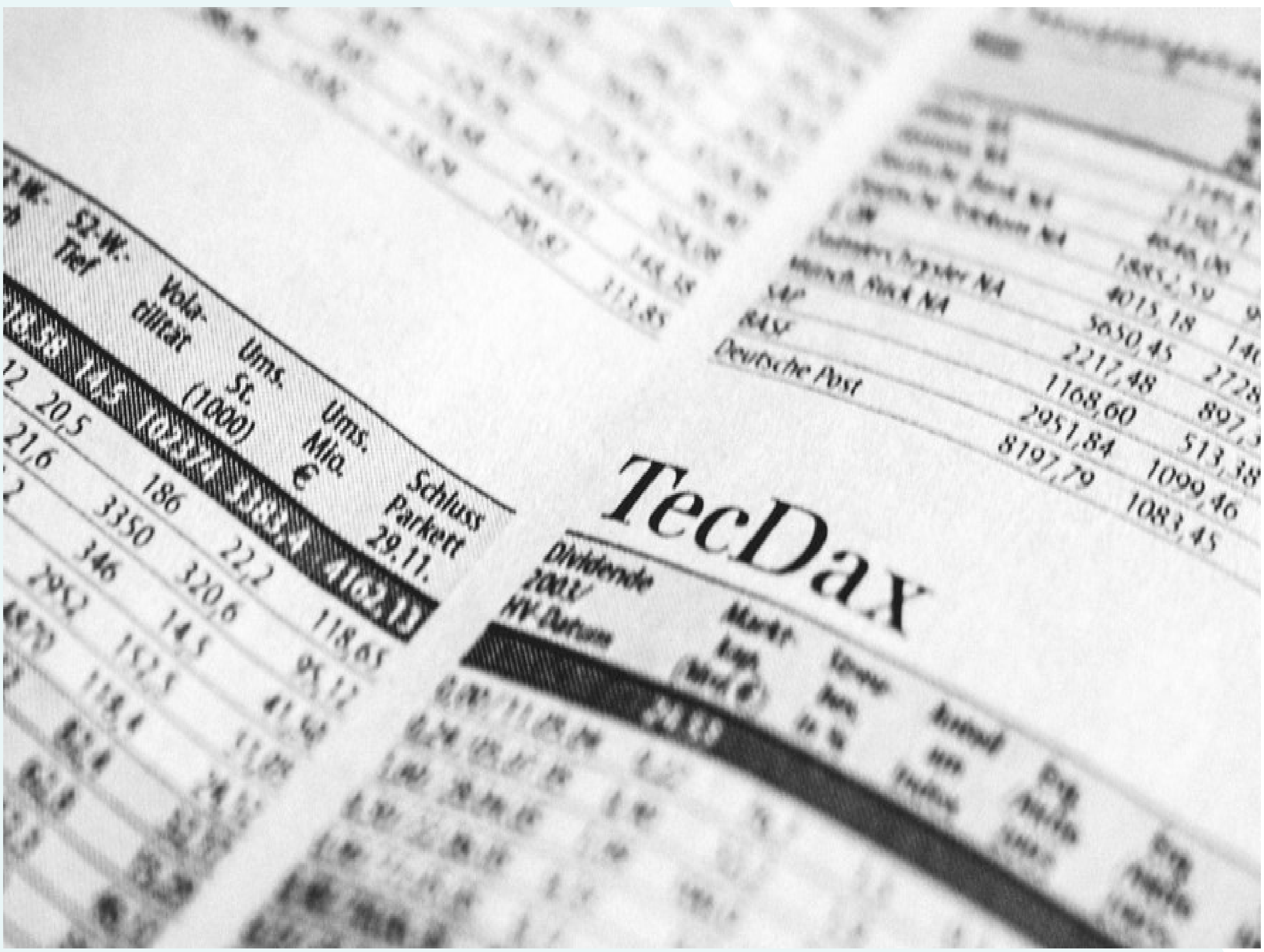
NEUTRAL DEVELOPMENTS

- Food inflation remains elevated, but it appears to be, finally, slowing. Food prices reflect food commodities, *but* retail food also has elements of energy, transportation, and labor costs in it, which remains stubbornly high. Shelter continues to be the single fastest growing component of inflation measures, but it has also been a source of optimism as new rent contracts are being signed at lower prices.
- The Bureau of Labor Statistics reports that US workers are starting to see pay gains run faster than inflation, amplifying their purchasing power and giving the Federal Reserve reason to raise interest rates again in May. Median weekly earnings of full-time wage and salary workers were 6.1% higher in Q1 compared to the same period a year earlier. Inflation during that time ran at 5.8%.
    - *With wage gains starting to run faster than inflation and amplifying their purchasing power, the Fed has a reason to keep rate increases on the radar.*
- Existing home sales moderated last month after surging in February. The outlook is a bit choppy as the housing market faces some headwinds. First, mortgage rates that are currently in the 7% neighborhood and assuming a 20% down payment, the rise in mortgage rates since March 2022 amounts to a 22% increase in monthly payments on a new 30-year mortgage for the median existing home (source: First Trust). While financing costs remain a significant hurdle, the good news for prospective buyers is that median prices fell on a year-over-year basis in March and are down 12.7% from their peak in mid-2022, which should help future sales.

NEGATIVE DEVELOPMENTS

- Retail sales fell for a 2nd consecutive mo. in March, as shoppers pulled back on buying big-ticket items. The value of overall sales declined 1%, with vehicles, furniture and appliances seeing the biggest drops, according to the Commerce Department. The Dept. also reported that spending on credit and debit cards last month rose at the slowest pace in 2 yrs.

- Bank deposits have been leaving banks and flowing into money market mutual funds which currently offer higher yields than bank accounts. The outflows have accelerated in the wake of the recent bank collapses. While higher interest rates have been the primary cause of US deposit outflows, that could still be destabilizing for banks with soft balance sheets, or at least reduce their willingness to lend. Further, even if the outflows do not hurt banks, they are still contributing to tighter financial conditions. This is something the Fed is monitoring closely as this indirectly helps their tightening strategies and may lead to a Fed “pause.”



THE MARKETS

The S&P 500 closed April on a high note as the House passed a bill which may avert a debt default. This, coupled with the sentiment that the Fed may be pausing its unprecedented rate hikes after the May meeting, have given a boost to the markets.

The S&P 500 closed the month up 3.5% while the Nasdaq posted a 2.5% gain. Small cap stocks, as measured by the Russell 2000, had a flat month. The cyclical-heavy Dow had a nice month posting a 4.25% return.

Energy, financials and consumer staples were the big winners last month while industrials, technology and materials were laggards.

Across the pond, European markets moved higher in lockstep with the U.S. Asian markets were mixed last month with China relatively flat, Japan posting a 3.5% gain and Hong Kong logging a -1.5% return.

U.S Index	Last Month (% return)	YTD (%)
S&P 500	3.5	8.6
Dow Jones	4.2	2.9
NASDAQ Comp	2.5	16.8
Russell 2000	-0.2	0.4

Source: https://tradingeconomics.com/stocks

NEWS YOU CAN USE

Hands down, Artificial Intelligence has been the dominant topic this year. Since ChatGPT's emergence, major tech companies have redirected their efforts towards their own AI projects in what is predicted to be a $718 billion global market by the end of 2030. Nonetheless, AI has sparked debate and there are currently few regulatory frameworks or guidelines in place. We anticipate that regulation will come in short order. One of the most significant controversial topics is the potential displacement of human labor. As companies seek to increase profit margins and reduce salary overheads, many jobs will inevitably become subject to AI takeover, which is significantly less costly in terms of computer power compared to human salaries, health care, and retirement benefits.

https://finance.yahoo.com/news/global-artificial-intelligence-market-size-165600472.html

https://www.salon.com/2021/03/12/astronomers-hope-to-use-a-quasar-as-a-flashlight-to-see-into-the-universes-dark-past/

The Tampa Bay Rays have set a new record for the longest home winning streak in the modern era of baseball by winning their first 14 home games of the season. The all-time record for the longest home winning streak, prior to the MLB, belongs to the 1880 Chicago White Stockings, who won 21 consecutive home games. The White Stockings finished the 1880 season with the NL championship with an impressive 67-17 record, or a .798 winning percentage. The team later underwent several name changes, including the Chicago Colts, Remnants, and Orphans, before settling on the nickname “Cubs” in 1907. The old name, Chicago White Stockings, was adopted by a minor league team on the south side of Chicago in 1900, which later turned major in the AL in 1901 and the team changed its name to the Chicago White Sox, for short.

https://www.espn.com/mlb/story/_/id/36284483/rays-set-modern-record-14th-straight-win-home-start-season

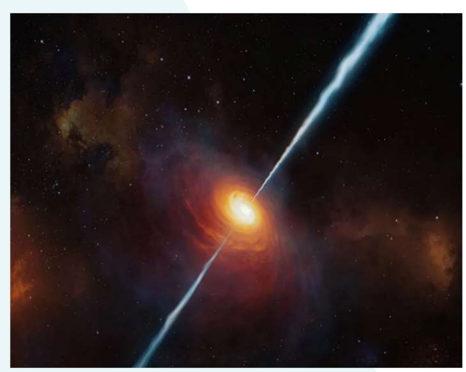
https://en.wikipedia.org/wiki/History_of_the_Chicago_Cubs

https://news.illinoisstate.edu/2016/05/alumni-invited-cubs-white-sox-games-july/

A 60-year-old mystery surrounding the cause of quasars, the Universe's most powerful objects, has been recently solved by astronomers. These objects are known for their exceptional brightness, and it has been discovered this month that their brilliance is a result of the collision between galaxies, which have black holes at their centers. During the collision, gas is driven towards the black holes, and before it is consumed, it releases vast amounts of energy in the form of radiation, leading to the quasar's brightness. Quasars are considered the most extreme phenomena in the Universe. In approximately 5 billion years, the Milky Way, our galaxy, is expected to collide with the Andromeda galaxy.

https://www.sciencedaily.com/releases/2023/04/230425205342.htm

https://scitechdaily.com/images/Quasar-Observed-in-Six-Separate-Light-Reflections-for-the-First-Time.jpg



As always, if I can be of additional guidance, please feel free to call me at 312.485.6847.

Best regards,

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