Weekly Market Flash

Economy Slows, Businesses Grow

July 5, 2024

We received a few more data points this week validating the increasingly consensus view that the economy is slowing – gently, perhaps, but still slowing. On Wednesday the Institute of Supply Managers (ISM) Services index showed an unexpected slip into contraction territory, coming in at 48.8 versus economists' expectations of 52.5 (a figure of 50 or more represents expansion, while below 50 signifies contraction), That same day the ADP Employment Survey was a tad below the consensus forecast, at 150,000 versus 163,000. The GDPNow estimate published by the Atlanta Fed, an estimate for real GDP growth, has been falling steadily over the past two weeks and now sits at 1.5 percent, with a softening outlook for consumer spending the key influencing factor. Finally, today's jobs report from the Bureau of Labor Statistics showed unemployment ticking up slightly to 4.1 percent – not a big month-to-month change but 0.5 percent higher than the 3.6 percent level one year ago. And while June payroll gains of 202,000 came in a bit higher than expected, downward revisions to April and May amounted to a 111,000 reduction in job gains for those months.

Comms and Tech Front and Center

Attention now shifts to the corporate sector, with the second quarter earnings season getting underway next week. Here is where estimates are not being revised down; the projected earnings per share growth rate for S&P 500 companies stands at 8.7 percent, not far from previous estimates. Top line sales are expected to grow by around five percent. Operating profit margins are looking healthy, if the analysts covering the companies are to be believed.

Perhaps unsurprisingly, information technology and communications services companies are at the forefront of the growth projections. Analysts expect to see revenue growth of 9.3 percent and earnings per share of 15.7 percent for the tech sector, with growth rates of 7.3 percent / 18.7 percent respectively in the communications services sector. Large dollops of capital expenditure on AI-related projects continue apace (although there have been some questions recently in the financial press about the extent to which all the new AI capacity is finding its way into the broader economy in a practical sense.

As always, observers will be paying close attention to forward guidance as management teams report, with "macro uncertainty" having been an often-heard phrase in the recently-concluded first quarter season. And given the ceaseless pace of geopolitical developments at home and around the world, we expect that mentions of "political uncertainty" will be increasing as the weeks go by.

July Is the Kindest Month

For investors wondering what these various trends may mean for market performance, there is perhaps some solace in the historic market trends for the month of July. A recent analysis by Goldman Sachs noted that the first 15 days of July have been the best two-week trading period of the year going back to 1928 (we would remind our readers that time series averages do not give any degree of certainty for what might happen in any given year). That same analysis also offered up the cheery observation that the S&P 500 has been positive for the past nine Julys, and the Nasdaq's record in this regard stretches to 16 years). Money that has been sitting on the sidelines for the first half of the year often moves in the early days of the second half, explaining in part this favorable seasonal trend.

We shall see. It would be nice to have some favorable tailwinds for at least a few weeks, because we will have a full plate of macro news, earnings reports and geopolitical tectonics to deal with soon enough.

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