JULY 2023

MARKET UPDATE

Stocks continued to rise, continuing their late May momentum – at least in the US – with the S&P 500 returning 6.61% in June and putting year-to-date gains at 16.88%. From the 2022 lows, the S&P 500 has recovered nearly 25% but remains over 7% away from its all-time high in early 2022. While US large cap, mega cap in particular, sit on top of the year-to-date leaderboard, mid and small cap stocks surged in June, outpacing the S&P 500 for the month. Globally, developed and emerging international equities lagged through the month, though developed markets are still ahead of US mid and small caps on a year-to-date basis.

Following the Federal Reserve's June meeting, their tone shifted to be more hawkish than before. While they have long had a fairly hawkish stance in their fight against inflation, some recent language shifts appeared to begin to tone that down. Also, the market had been expecting a significant pivot in terms of policy and the Fed to be able to move into an easing stance and begin rate cuts later this year or early next. However, the Fed has made a seemingly concerted effort to change those expectations by alluding to multiple more rate hikes this year, and that they were a couple of years away from cutting rates. Despite the shift in language and tone, the market still believes better probabilities lie in rate cuts in the first half of next year.

While the market still expects rate cuts, the Fed's language did shift yields upward in the short-to-intermediate section of the yield curve. The upward shift in yields put pressure on bond prices, where the Bloomberg US Aggregate fell 0.36% in June, putting its year-to-date gains at 2.09%.

ADVISORS' PERSPECTIVE

The S&P 500 surged higher in June, maintaining and furthering the positive trends in equity markets throughout most of 2023 thus far. The glimmers of optimism that appeared earlier this year appear to have been sustained through the first half, despite a rocky end to the first quarter with bouts of banking concerns. Part of this may be due to hopes of productivity gains amid an artificial intelligence wave while improving economic data - although still mixed - has helped the equity market shrug off the Federal Reserve's increasingly hawkish messaging.

The recent rally in equity markets has pushed down short-term volatility expectations, which are down to half the levels seen in mid-March. However, the health of corporate balance sheets continues to be a concern. Although credit spreads have come down from their recent peaks in March and May, the recent ebbs and flows in investor sentiment continues to be worth keeping an eye on as changes in credit spreads have implications across capital markets. This is especially true as the Federal Reserve attempts to adjust the market's rate expectations.

Fears of a recession beginning in Q2/Q3 2023 are subsiding with the latest revisions to Q1 2023 data. Expectations for a substantial pullback in GDP have moved from Q2 to Q4 in the latest forecasts. As underlying economic data related to jobs has stayed strong and previously troubling data, such as consumer sentiment, has improved, we've seen equity markets maintain their strength through the first half of 2023. Concerning economic data persists, despite market growth. The threat of a recession looms but will either be delayed or soft given the current readings.

At a high level, the economic data continues to suggest that a recession is not imminent and that the economy remains resilient, even perhaps mildly improving. Certainly, risks remain across the economy, particularly with the background of a Federal Reserve with a more aggressive stance towards rate policy. Payrolls have improved in each of the last three months, along with other signs of consumer resilience in retail sales and personal income.

We remain cautiously optimistic and continue to use a quantitative investing approach. In times of uncertainty, it is more important than ever to follow the data and not make decisions based on emotions. Hilltops partnership with Helios relies on facts and data, which we use during our recalculations on a bi-weekly basis. Our models adjust appropriately to market conditions.

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