REGIONS ASSET MANAGEMENT

WEEKLY MARKET COMMENTARY

What We're Watching

MARKET UPDATES

January 7, 2022: Recorded Leadership Discussion Featuring: Regions Chief Economist, Chief Investment Officer and Chief Market Strategist.

January 21, 2022: Join the upcoming live Regions Market Update.

KEY OBSERVATIONS

Stocks: Sell-Off Stateside As Fed Minutes Strike A More 'Hawkish' Tone; Growth Significantly Lags Value On The Week. The minutes from the Federal Open Market Committee's December meeting were released last Wednesday and the market interpreted them to be even more 'hawkish' than the most 'hawkish' of expectations, spurring a 1.9% sell-off in the S&P 500 and an even more dramatic 3% decline in the small-cap Russell 2000 index on the day. All told, the S&P 500 and Russell 2000 each ended the week with a 1.8% and 2.9% drop, respectively. Value outpaced growth across the market cap spectrum on the week, but dispersion was particularly pronounced within small-cap stocks as the Russell 2000 Value index was flat on the week while the Russell 2000 Growth index fell 5.8%. Indices tied to international markets fared relatively better on the week as the MSCI ACWI ex U.S. index fell 0.3% and the MSCI Emerging Markets (EM) index declined 0.5%. Broad-based strength out of Europe was attention grabbing as individual country indices tied to France, Germany, Italy, Spain, and the U.K. each ended the week higher by at least 1%. Within emerging markets, weakness was widespread with Brazil, China, and Russia noticeably weak, while India was a standout performer to the upside.

Bonds: FOMC Talking Tough, But Will They Ultimately Follow Through? The big story so far in '22 has been the rapid rise in long-term interest rates as the 10-year U.S. Treasury yield, specifically, ended last week at 1.77%, or 25 basis points higher than where it started the year. After the minutes from the FOMC's December meeting were released last Wednesday, expectations built that the Committee could potentially hike the fed funds rate by a quarter-point up to four times in the coming year which contributed to the upward pressure on long-term yields. Yields on corporate bonds rose alongside Treasury yields over the balance of last week, but credit spreads only widened modestly, a sign of continued robust investor risk appetite. The credit spread over the U.S. Treasury curve for the Bloomberg U.S. High Yield index ended the week at 298 basis points, or 15 basis points higher, while the yield-to-worst (YTW) on the index finished the week at 4.60% or 39 basis points higher.

WHAT WE'RE WATCHING

- Consumer Price Index (CPI) for December is released Wednesday and is expected to rise 0.4% month over month after jumping 0.8% in November versus October. Core CPI, which excludes volatile food and energy prices, is expected to have risen another 0.5% in December after a 0.5% jump in November relative to October.
- Producer Price Index (PPI) for December is slated for release Thursday and is expected to show a 0.4% month over month rise after jumping 0.8% in November versus October. Core PPI, which excludes food and energy, is expected to have risen 0.5% in December after a 0.7% month over month jump in November.
- The University of Michigan Consumer Sentiment Index for January is released Friday and is expected to fall to 70.2 from 70.6 in December.

	Price/Yield	Total Return (%)					
	1/7/2022	1 Week	1 Month	Year to Date	1 Year	3 Years	5 Years
Dow Jones Industrial Average	36231.66	-0.25	1.52	-0.25	18.90	18.02	15.20
S&P 500	4677.03	-1.83	-0.09	-1.83	24.71	24.57	17.62
NASDAQ	14935.90	-4.52	-4.74	-4.52	15.04	30.97	23.18
Russell 2000 Index	2179.81	-2.91	-3.17	-2.91	4.99	17.21	11.19
MSCI World ex US	2349.33	0.03	1.33	-0.33	10.30	13.73	9.70
MSCI EM	1226.10	-0.27	-0.53	-0.47	-4.98	10.68	9.68
BbgBarc US Aggregate	1.98	-1.53	-1.61	-1.53	-2.23	4.19	3.21
BbgBarc Global Aggregate	1.45	-1.17	-1.42	-1.17	-5.39	3.02	3.12
BbgBarc US Corporate	2.55	-1.93	-2.11	-1.93	-1.55	6.80	4.78
BbgBarc 10-Year Muni	1.17	-0.72	-0.59	-0.72	0.24	4.32	3.98
BbgBarc High Yield	4.60	-0.94	-0.31	-0.94	4.11	7.78	5.89

	Price/Yield						
	1/7/2022	1 Week Ago	1 Month Ago	12/31/2020	1 Year Ago	3 Years Ago	5 Years Ago
SOFR (yield)	0.05	0.05	0.05	0.05	0.10	2.41	N/A
30 Year Mortgage (average rate)	3.44	3.27	3.25	2.88	2.88	4.51	4.15
2 Year Treasury (yield)	0.87	0.73	0.69	0.73	0.14	2.52	1.21
10 Year Treasury (yield)	1.77	1.51	1.48	1.51	1.07	2.68	2.35
30 Year Treasury (yield)	2.11	1.90	1.80	1.90	1.84	2.98	2.95
WTI Crude (closing price)	78.90	75.33	71.94	75.33	50.63	48.27	53.98
Brent Crude (closing price)	81.84	77.24	75.54	77.24	53.70	57.10	55.90
Gold (NYM $/oz)	1797.00	1827.50	1782.60	1827.50	1912.30	1286.80	1171.90

Source: FactSet

WHAT HAPPENED LAST WEEK?

Stocks: Sell-Off Stateside As Fed Minutes Strike A More 'Hawkish' Tone; Growth Significantly Lags Value On The Week.

The minutes from the Federal Open Market Committee's December meeting were released last Wednesday and the market interpreted them to be even more 'hawkish' than the most 'hawkish' of expectations, spurring a 1.9% sell-off in the S&P 500 and an even more dramatic 3% decline in the small-cap Russell 2000 index on the day. All told, the S&P 500 and Russell 2000 each ended the week with a 1.8% and 2.9% drop, respectively. Value outpaced growth across the market cap spectrum on the week, but dispersion was particularly pronounced within small-cap stocks as the Russell 2000 Value index was flat on the week while the Russell 2000 Growth index fell 5.8%. Indices tied to international markets fared relatively better on the week as the MSCI ACWI ex U.S. index fell 0.3% and the MSCI Emerging Markets (EM) index declined 0.5%. Broad-based strength out of Europe was attention grabbing as individual country indices tied to France, Germany, Italy, Spain, and the U.K. each ended the week higher by at least 1%. Within emerging markets, weakness was widespread with Brazil, China, and Russia noticeably weak, while India was a standout performer to the upside.

• Notably, while there was a downward bias to equity prices last week, volatility failed to spike markedly higher, the CBOE Volatility Index, or VIX, rising to just 20 at its peak, evidence of minimal demand for hedges against additional equity market weakness. During the Omicron induced pullback in the S&P 500 in late November/early December, the VIX spiked to above 30, so last week's rise in volatility barely showed up as a blip on the VIX chart in comparison.

• This week marks the unofficial start to quarterly reporting season as bellwether companies in the financial services sector, specifically, Blackrock, Wells Fargo, J.P. Morgan Chase, and Citigroup are slated to kick things off on Friday. The analyst community projects that the S&P 500 will generate $52.40 in earnings per share (EPS) for the 4th quarter, implying a 26.2% jump over the 4th quarter of 2020. For comparison purposes, in the 3rd quarter of '21, over 81% of companies topped the analyst estimate for earnings per share, while over 75% bested the consensus estimate for sales. Investor focus this quarter will likely remain fixed on profit margins as companies have done an outstanding job over prior quarters of converting sales into profits, despite a persistent rise in input costs, specifically commodities, shipping, and labor. Should reports point toward sustained earnings momentum into the new year, analysts will likely grow more confident in the S&P 500's ability to achieve the current consensus estimate of $226.15 in EPS for the full year, and may be emboldened to hike estimates, thus avoiding a scenario in which forward earnings are revised lower, souring investor sentiment in the process.

• S&P 500 leadership leaned heavily in favor of cyclicals last week and away from secular growth, broadly speaking. The energy sector was the big winner on the week, rallying 10.6% as the price per barrel of West Texas Intermediate (WTI) crude oil rose 5%. The S&P 500 financial services sector took second place after rising 5.3% on the week amid a sharp jump in long-term Treasury yields. While financial services fared quite well, the real estate sector bore the brunt of the rise in interest rates and fell 4.9% on the week. The information technology sector fell 4.6% as it served as a source of funds for investors looking to shift allocations into shorter duration cyclical value shares, i.e., energy, financial services, and industrials. Health care was also noticeably weak as the sector fell 4.6%. Within the S&P 500's more defensive sectors, performance was mixed as utilities declined 1.6%, and consumer staples turned out a 0.3% positive return.

• Crude oil kicked off the year in rally mode as the price per barrel of West Texas Intermediate (WTI) crude oil rose 5% on the week and was knocking on the door of $80 mid-week, its highest close since early November. The energy sector of the S&P 500 ended 2021 with a 53.2% gain, and while we don't expect a return of that magnitude to be repeated in '22, the supply/demand imbalance for crude oil that pushed energy and related stocks higher in '21 will likely remain in place throughout 2022 and should be supportive of additional gains for the sector this year.

Bonds: FOMC Talking Tough, But Will They Ultimately Follow Through?

The big story so far in '22 has been the rapid rise in long-term interest rates as the 10-year U.S. Treasury yield, specifically, ended last week at 1.77%, or 25 basis points higher than where it started the year. After the minutes from the FOMC's December meeting were released last Wednesday, expectations built that the Committee could potentially hike the fed funds rate by a quarter-point up to four times in the coming year which contributed to the upward pressure on long-term yields. Yields on corporate bonds rose alongside Treasury yields over the balance of last week, but credit spreads only widened modestly, a sign of continued robust investor risk appetite. The credit spread over the U.S. Treasury curve for the Bloomberg U.S. High Yield index ended the week at 298 basis points, or 15 basis points higher, while the yield-to-worst (YTW) on the index finished the week at 4.60% or 39 basis points higher.

• While the FOMC meeting minutes were uncharacteristically 'hawkish,' the Committee may be attempting to talk tough and use forward guidance to get the bond market to do some of its work for it via higher interest rates. The FOMC is attempting to regain some lost credibility on the inflation fighting front, and the meeting minutes will likely go a long way toward achieving that goal. While we continue to expect inflation to run well above the FOMC's 2% target in 2022, we are seeing signs that supply chain bottlenecks are easing and that inventories are being replenished, which should put downward pressure on prices paid over coming quarters. However, rising wages, rents, and healthcare costs could offset much of the benefit received from falling goods prices. Fed funds futures imply that four quarter-point hikes to the fed funds rate are in the cards for 2022, with the first occurring in March. After the release of the FOMC's December meeting minutes, we, and the market, now expect March to be a 'live meeting,' with a rate hike on the table for discussion, but just how 'live' it ultimately proves to be could depend, at least in part, on the January and February nonfarm payrolls reports.

• The labor market continues to heal, evidenced by the December nonfarm payrolls report released last Friday which showed 199,000 jobs were created during the month, falling short of the consensus estimate of 400,000; however, payrolls for both October and November were revised higher by 141,000 in total. While the unemployment rate fell to 3.9% from 4.1% the prior month, an encouraging sign, the labor force participation rate remained steady at 61.9% month over month. There were nearly 11 million jobs open at month-end, and average hourly earnings rose 0.6% versus November, highlighting increasingly tight labor market conditions.

Source: Bloomberg, FactSet

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