Ropes Wealth Heralds A Default Free Weekend & Strong Jobs Report

Payrolls once again blew through the consensus forecast, rising 339,000 as jobs were added in professional and business services, government, and healthcare. Add in a further 93,000 of upward revisions to prior months and the picture of an undeniably strong labor market is clear. One mitigating factor was the rise in the unemployment rate to 3.7%, above the expected 3.5% level, despite the labor force participation rate holding steady at 62.6%. This was the biggest one-month increase in unemployment since April 2020, reflecting 440,000 more people out of a job. On the wage inflation front, monthly wage growth was slightly lower than expected, rising at a 0.3% in May following a 0.4% increase in April. Year-over-year, wages are up 4.3%.

On balance this data is likely to keep rate increases on the agenda but may give wiggle room for a Fed "skip" in the month of June, or at least Wall Street thought so as stocks continued their positive streak with high hopes of a soft landing in the offing. It didn't hurt either that both the House and Senate were able to get their act together this week to pass the debt ceiling increase, which Biden signed into law today. As we previewed last week, the bill caps spending for the next two years with a modest cut to non-military spending and a modest expansion in defense spending. It includes conservative measures to claw back about $28 billion in unspent Covid relief funds, eliminate $1.4 billion in IRS funding and overhaul the permitting process for energy projects. As expected, both sides are claiming victory, though Democrats protected their biggest policy goals on clean energy, health, and infrastructure while Republicans achieved work requirements in anti-poverty programs, and approval of an Appalachian gas pipeline.

What does this all mean for the economy in the second half of the year? Will recession be averted? The answer is no, but before you panic, keep in mind that recessions come in different shapes and sizes, and this could be a milder one thanks to a resilient labor and housing market. That said, we should all be prepared as large swaths of economic data outside of labor are showing signs of a slowdown. Higher mortgage rates have hurt sales of new homes, CEO and consumer confidence measures are deteriorating, companies are delaying capital spending plans, and consumers have depleted much of their savings. The Federal Reserve has raised rates higher and more quickly than they have in decades, and the ongoing U.S. regional banking crisis has caused a widespread stiffening of lending standards that has demand for, and supply of, loans now close to 2008 levels.

It is possible that the Fed is nearing a pause in rate hikes and grappling with the ideas of living with some inflation to avoid the deep recession needed to get inflation near its target. But a pause in policy is a lot different than the Fed coming to the rescue of a faltering economy with rate cuts later this year, which is probably what is needed to support a sustainable and more broad-based rise in stock prices. Outside of some AI darlings, this market is rising on a very narrow breadth, and under the hood a lot of stocks remain downbeat, at least in the U.S. In fact, the market-capitalization weighted S&P 500 is beating its equal weighted counterpart by nearly 10 percentage points in 2023. That's the biggest margin of outperformance year to date on record, according to Dow Jones Market Data. With that, we are urging clients to carefully consider their market positioning and performance analysis, as only a handful of names are responsible for this year's rebound. A catalyst for a more wide-ranging rebound may rest only in a complete pause or pivot in the Fed's course, and that may not be forthcoming. These dynamics are less prevalent in overseas markets, though performance there is also strongest in the largest and most well capitalized international companies given recession and slowdown fears. As always, we remain steadfast in our goal to maintain some cash and liquidity for short-term needs, and a focus on quality with valuation discipline. We suspect there will be some volatility ahead as we get closer to the Fed's decision and the dynamics that follow. At that point, it may be interesting to consider some shifts and we are poised to take advantage on your behalf.

Thank you as always for your interest in our investment commentary. If you would like to speak personally with a member of our team at any time, please click **here.**

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