Blackshield Capital

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WEEKLY INSIGHTS

Fundamental factors indicate higher risk in the stock market

Dynamics of key assets

Top charts of the week:

- divergence in equity performance
- it becomes more difficult for people to find a new job
- deterioration in EPS forecasts for Q1 2024

Have a question for the team? CONTACT US

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One of **the most important tasks of an investment firm is** to respond in a timely manner to the challenges of the economy and market conditions. While many risks of a geopolitical and financial nature cannot be predicted, it is worth staying informed to understand what is happening in a meaningful way.

Interest rates, the real estate market, employment and unemployment, inflation and corporate profits are just a few of the variety of factors affecting asset and security pricing.

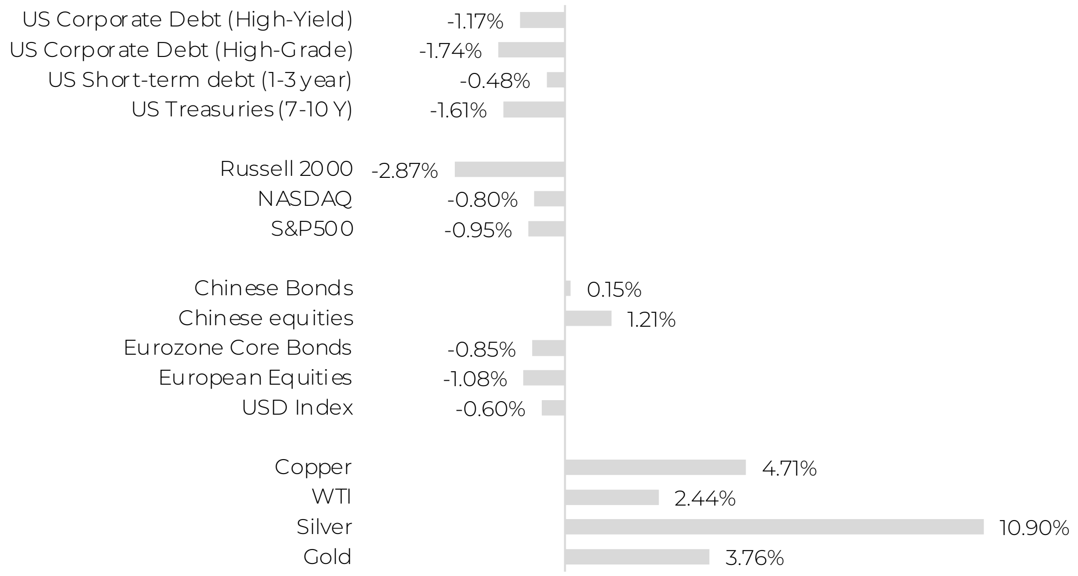
Our goal is to provide a deeper and clearer understanding of what is happening in the markets with an emphasis on illustrations, charts and visuals.

Weekly Insights will provide a more detailed look at industry specifics, delve into the nuances of price mechanics, and provide a more detailed understanding of our strategic vision offered in our quarterly strategic reports.

Dynamics of key assets

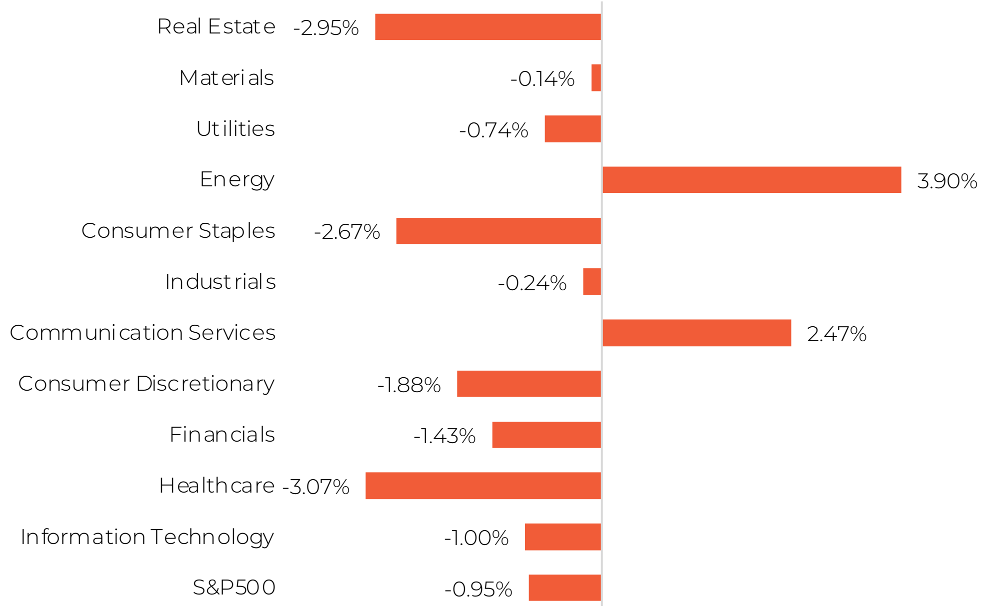
In recent weeks, we have seen a dominant rise in commodity prices, which continue to outperform all other asset classes.
At the same time, the US equity and bond markets continue to decline amid ambiguity in interest rate cuts.

Dynamics by key assets for the week



- Despite Friday's positive performance on the US stock market, both the stock and bond markets closed in negatively for the week, based on the general background of the possibility of a rapid reduction in monetary restraint in the coming quarters.
- Gold, as the main defensive asset, continues to grow on the back of new investment inflows, while silver is growing in value due to its relative cheapness to its counterpart, gold.
- Among other metals, copper is rising amid robust demand, while platinum group metals closed the week in a slight positive territory.

S&P500 index dynamics for the week

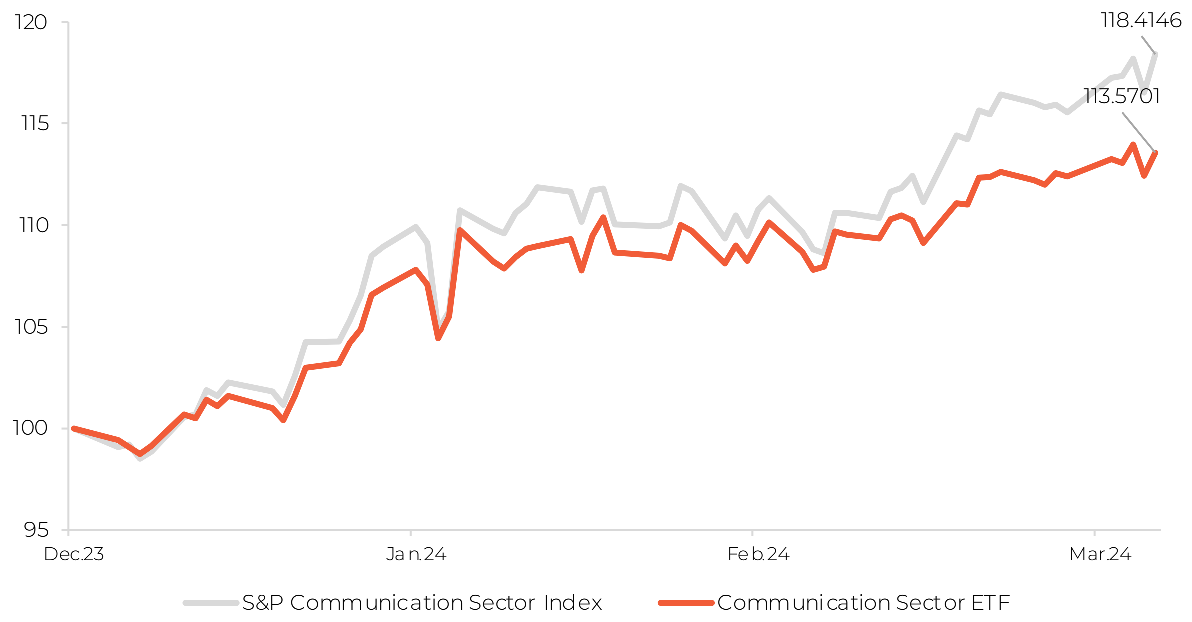


- Considering sectoral breakdown, most of the S&P 500 industries have declined in their quotations over the past week. The main declines were recorded in the Healthcare, Real Estate and Consumer Staples sectors.
- In contrast, Energy and Communication Services sectors were the only growing industries over the past week.
- At the moment, we notice a bigger difference in performance between such risk-factor categories as defensive and risk, large and small capitalization, or with a higher or lower free cash flow generation.

Top charts of the week – divergence in equity performance

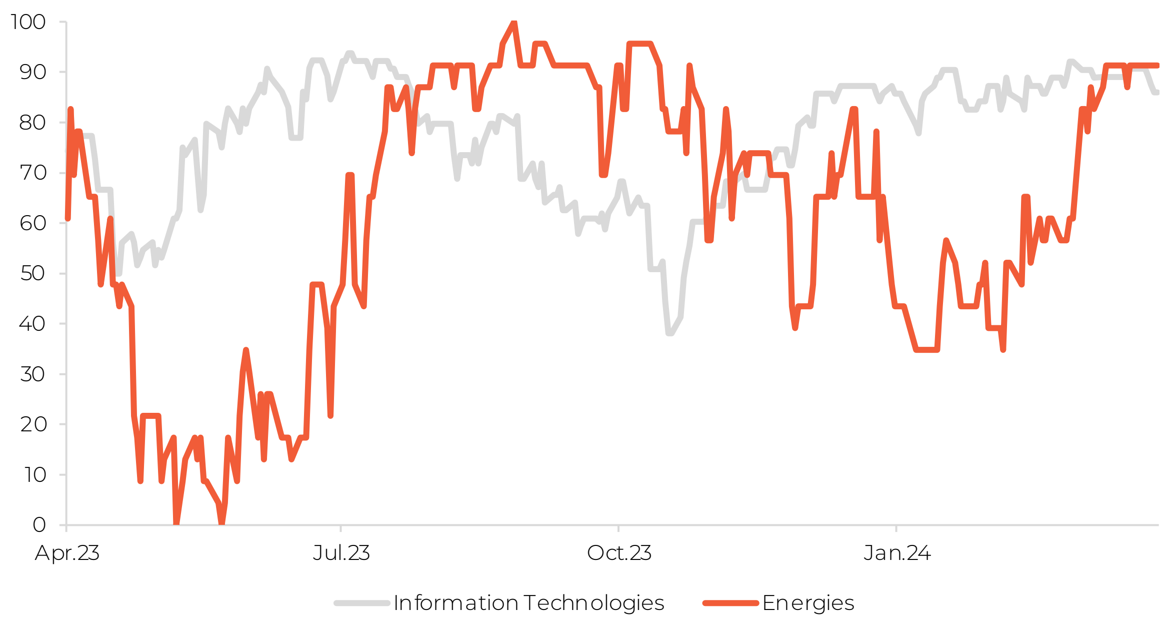
A temporary market correction requires a reassessment of both individual securities and the structure of stock indices. This is important primarily for understanding the main driving forces and early drivers of market dynamics.

Difference between index and sector ETF yields on communication services



- We have repeatedly drawn attention to the high market concentration of stock indices, but there is one interesting aspect worth noting. Currently, the difference between stock indices and ETFs, funds that allow trading these same indices, is growing significantly. The fact is that the methodology for calculating index ETFs sets a limit of 23-24% of the weight of one company in the index.
- Since indices are representative indicators, this leads to investors actually buying indices through ETFs, receiving much lower risks than the market actually provides (since the beginning of the year, ETFs on some indices have lagged behind the indices by 3-5%). If the methodology is modified, this will lead to an actual increase in market volatility.

Percentage of companies in sectoral indices above the 200-day average

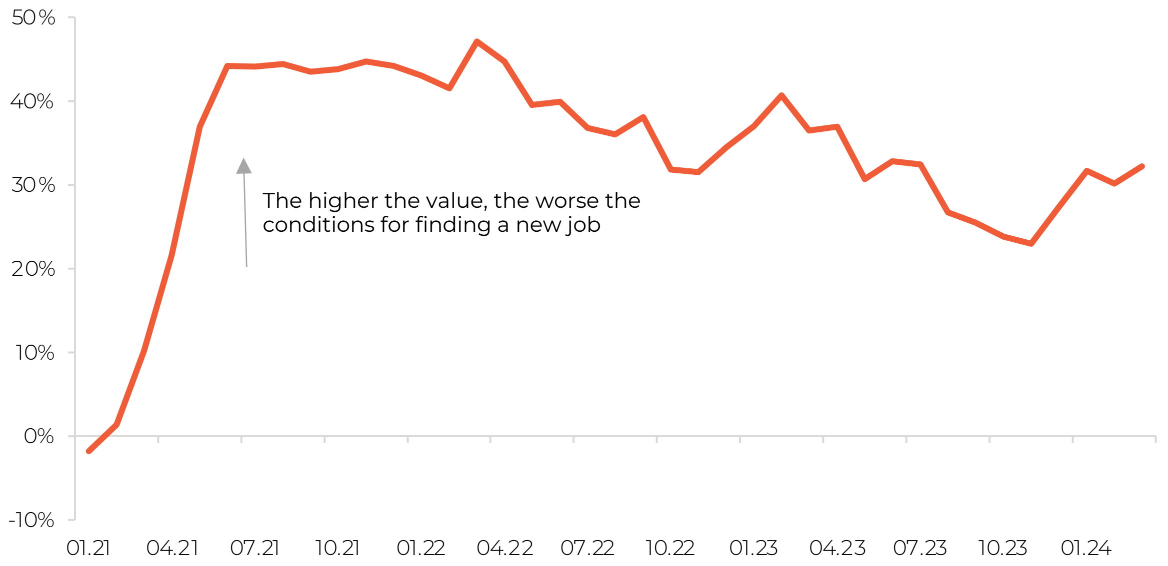


- A slight market correction amid a reassessment of expectations for the pace of interest rate cuts led to sectoral divergences in the S&P 500 index.
- So, in order to better understand what is happening within the stock indices, we calculated the number of companies that are above the 200-day average in each sector. It was interesting to note that IT-sector temporarily lost its leadership to the Energy sector.
- The comparison of shorter-term 2-month indicators is even more representative: 100% vs. 58%. This indicates the short-term interest of market participants in Energy sector, which may develop.

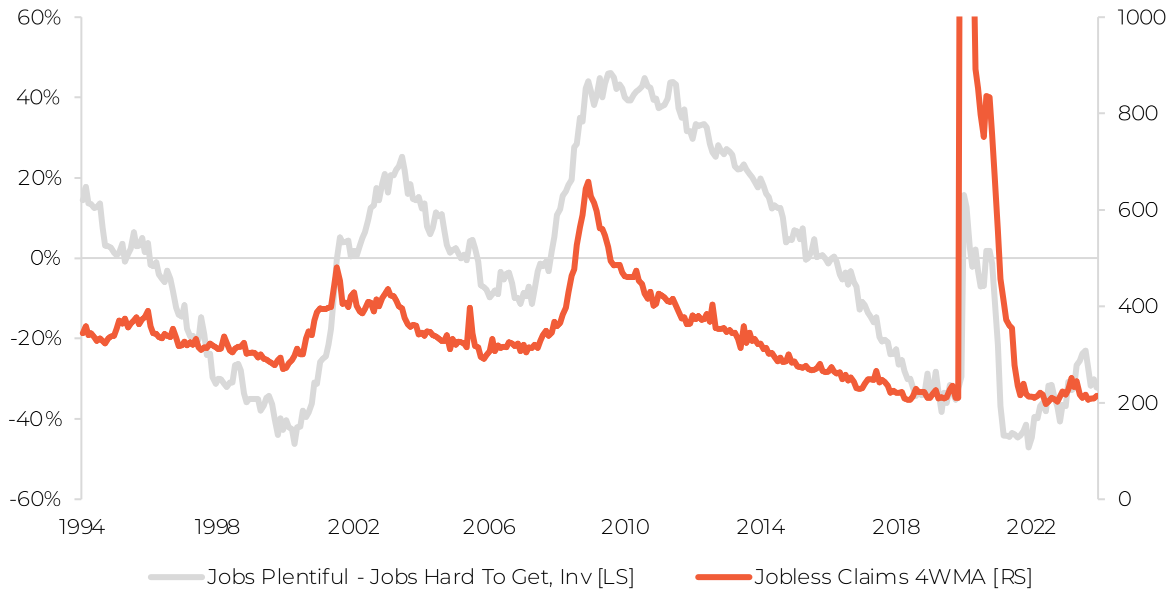
Top charts of the week – it is difficult to find a new job

According to the latest US consumer sentiment survey by the Conference Board, one of the negative factors noted by respondents was the labor market, where it is becoming increasingly difficult to find a new job.

Dynamics of the difference between indices: Jobs Plentiful and Jobs Hard To Get



Dynamics of indices on the possibility of finding a new job and jobless claims



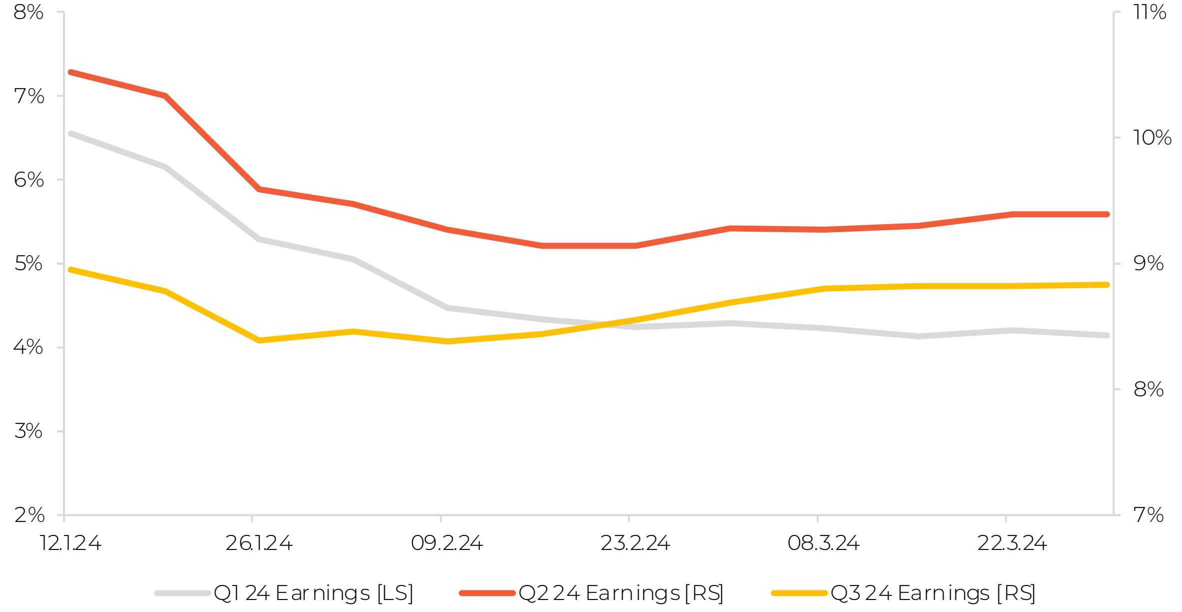
- The monthly survey by the Conference Board, which is aimed at assessing consumer sentiment, showed a slightly negative overall trend, which continues for the 3rd quarter in a row (since the beginning of the year, the index has decreased from 110.9 to 104.7 points). The reason for this decline was a drop in a number of consumer expectations indicators for the next 6 month(sentiment indicators about the future deteriorated from 76.3 to 73.8).
- As noted in the survey itself, the main negative factor behind the deterioration in expectations was the labor market, where respondents said it is increasingly difficult to find a new job. This dynamics further confirms the general trends in the labor market, which currently indicate fewer new job openings.

- For example, these observations have a high correlation with the dynamics of jobless claims in the economy, which, although currently at a low level, have been on the rise for the past 6-8 months. Particular attention should be paid to the dynamics of continuing jobless claims, which have increased by more than 100 thousand over the past year.
- As we noted earlier, the labor market can go through several stages: when there is a decline in new job openings and a real increase in layoffs. Historically, the first factor (a decline in hiring) precedes the second (an increase in layoffs). That is why we predict that in 2024 we should expect a larger increase in unemployment.

Top charts of the week – deterioration in EPS forecasts for Q1 2024

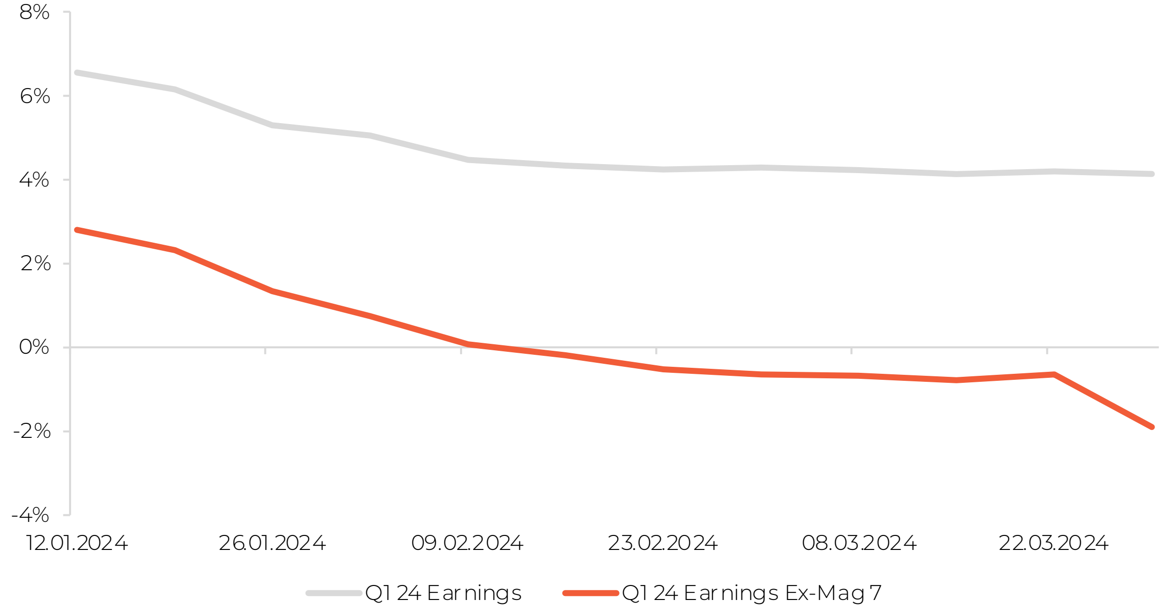
Before the start of quarterly reports, it is worth capturing the input data that will start the reporting season for US companies for Q1 2024. Currently, expectations for earnings growth for the S&P 500 have declined, especially without Magnificent 7.

Dynamics of revisions of quarterly EPS growth for 2024 of the S&P 500 index



- In general, given recent trends, the market does not make significant revisions to its forecasts for more than 2-3 quarters ahead. This is especially noticeable today, where EPS growth forecasts for Q1 2024 alone have undergone significant changes, decreasing from 6.6% at the beginning of the year to 4.1% at the end of March.
- However, during the reporting season, it will be important to understand whether the S&P 500 corporate earnings forecasts for the next quarters of 2024 will change, which are currently under greater threat given recent macroeconomic changes.
- To date, the forecasts for Q2 and Q3 2024 have remained almost unchanged, which seems disturbing.

Dynamics of EPS growth revisions for Q1 2024 S&P 500 with and without Magnificent 7



- Particular attention should be paid to the so-called Magnificent 7 group of companies, which is the main driver of growth not only in quotations but also in the overall EPS value across the S&P 500 index.
- Based on the latest data, S&P 500 corporate earnings excluding Magnificent 7 will decline by 1.9% in Q1 2024, which is a significant deterioration from the beginning of the year, which was +2.8% growth.
- This trend clearly has some negative signals that point to structural changes in the economy. Although the same dynamics were observed in the previous quarter, the widening gap between the S&P 500 and S&P 500 Ex-Mag 7 earnings growth is a factor of increasing stock market risks.

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