Nolte Notes
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Like the Easter Bunny jumping around the yard, the markets have been hopping back and forth for much of the past few months. There are many reasons to be skittish, from the continuing conflict in Ukraine to a still uncertain withdrawal of liquidity by the Fed. Following the pandemic, the Fed was forceful and quick to flood the market with liquidity. Now that inflation is running well over their 2% target, they are measured and careful about pulling back on the surfeit of money floating around. In fact, many of the indicators of "financial stress" still show the markets very stress free. The inflation numbers last week were in line with expectations. However, the core rates (excluding food and energy) were lower than expected, giving rise to the thought that "peak inflation" is here and the rate will begin dropping in the months ahead. Retail sales were up last month, but unit sales were roughly flat, with higher prices making up the "gains". The coming week is relatively light, but earnings will get into full swing. There will (always!) be something to watch in the markets. Expect the unexpected in the weeks ahead.

The alternating excited and depressed markets have been a boon for traders, but not so much for long-term investors. Sentiment is getting very bearish, as evidenced by the Amer. Assoc. of Individual Investors (AAII) weekly data. The widest spread between bulls and bears since 2013, ahead of a seven-year run for stocks. Volume has been expanding on market declines, indicating investors are turning tail anytime there is a sniff of bad news. Interest rates drop a bit one day, and it charges stocks, especially the growth style. The daily market moves are relatively easy to determine a reason why, but that reason is exclusive to that day and does not carry forward to the next as investors focus on something new. When will the back-and-forth end and a new trend begin? The trillion-dollar question without (as of yet) an answer.

The inverted yield curve has not only re-inverted but has gotten relatively steep quickly over the past few weeks. So too, the difference between high yield bonds and treasuries has also declined from their recent peaks. Does that mean the recession call is off the table? Maybe. However, it will depend upon how aggressive the Fed is over the coming months and whether they stick to their inflation fighting mantra or revert to making sure the equity markets stay elevated. One component of the bond model is commodity prices, which remain near all-time highs and have been up over 40% on a year over year basis for more than a year. If we are indeed close to "peak inflation", keep an eye on commodity prices to lend some additional credence to that claim. Hard to see inflation rolling over soon.

Year to date, there is at least a nine-percentage point difference between growth and value, whether looking at large, mid or small stocks. The divergence is a big change from the past few years, when growth was king of the market. Familiar names like Apple, Microsoft and Nvidia have all declined this year, while rather uncommon names like Abbvie, Duke Energy and pick an energy stock have all seen gains year to date. Investors have not given up on the familiar and embraced the "unusual", but if the trends continue through the summer months, those smaller gains in the big cap names may come under pressure as investors lock in "any kind" of gain. The defensive nature of the market is not unusual given the turmoil of the past six months in stocks in general. Volatility is up, worries abound, so investors are looking at companies and sectors that can still do well no matter the outlook. If inflation continues to be one of those worries, look for commodity companies to continue their run higher as well.

Earnings season will be interesting as companies discuss employment, input costs and whether they can pass them along to their consumers. Inflation and the Fed are likely to be key themes well into the summer. Will interest rates ever come back down again? If the Fed can not contain or rein in inflation, look for higher still interest rates this year.