Donaldson
CAPITAL MANAGEMENT

The Outlook

DCM Weekly Market Brief

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Bad News is Good News Once Again

The S&P 500 nearly completed a round trip this week. After falling almost 3% by mid-week, a quick reversal ensued and the market closed down only .25% on the week. This turn around came as bad news in the form of weakening economic data quickly transformed into rising expectations for a Fed rate cut in October. Even with negative economic momentum building, the market sits on a solid structural foundation. It held strong at an important level of resistance and continues to make a series of higher lows in a roughly 10 month-long uptrend. The 200-day moving average is turned up and we are just about 2% below an all-time high. Yet, sentiment is far from stretched and a number of indicators actually show the market oversold. It remains a slow grind higher for the moment.

This week's important economic releases continued to show that the trade war is biting. The manufacturing sector contracted for a second straight month and at a faster rate. Even services are beginning to feel the impact of slower global economic activity. While the sector is still growing, its pace slowed dramatically and far more than expected over the last month. These two releases initially sent the market into a tailspin this week, but the realization soon swept over participants that the Fed would be much more likely to cut in October. Expectations for an October cut bounced from around 73% last week to almost 90% by week's end! In other words, the Fed put is back on. The market is far more comfortable with the prospects of a prolonged trade war knowing that the Fed stands with them and not against them. This is far different than the 4th quarter of 2018.

The consumer also continues to plug along. Employment numbers out today showed record low unemployment of 3.5% and job gains only slightly below expectations. Positive revisions to prior month job numbers were also a welcome development. So even against the backdrop of a contracting manufacturing sector and slowing services, consumers are still working at record rates. While we continue to see that further gains on the job front will be difficult from here, it's very comforting that employment has been so stable in such seemingly turbulent times.

In the equity market, pockets of cyclicality continue to reinforce a more positive outlook. Bellwethers like semiconductors and housing look as good as they have for some time. If there is one area of concern, it's that some of the FANG heavyweights aren't participating. NFLX has been abysmal for months, FB isn't carrying much weight, and AMZN is starting to weaken. It would be encouraging if participation could broaden out to some of these names in the coming weeks.

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S&P 500: Standard & Poor's (S&P) 500 Index. The S&P 500 Index is an unmanaged, capitalization-weighted index designed to measure the performance of the broad U.S. economy through changes in the aggregate market value of 500 stocks representing all major industries.