

Inflation concerns fueled retreat

The stock market started the week on an upbeat note. Market participants had a rosy outlook for the future having latched onto the peak inflation, peak hawkishness, and soft-landing narratives.



Upside momentum quickly fell to the wayside after the August CPI report gave market participants a reality check. It renewed concerns about persistently high inflation, an aggressive Fed rate-hike path, and a potential hard landing that would undercut current earnings estimates.

The reaction from both the stock market and the bond market was brutal. This marks the fourth losing week out of the last five weeks for stocks and Tuesday's sell-off was the fifth-largest point loss for the S&P 500 in history. By the end of the week, the S&P 500 fell below the psychologically important 3,900 level.

The outsized reactions were due to market participants knowing hotter-than-expected inflation data likely meant

the Fed is going to stay on an aggressive rate-hike path. The Fed desperately wants to get inflation under control, and it has no interest in being the stock market's friend.

Following the CPI report, the fed funds futures market shifted noticeably. It priced out any expectation of a 50-basis point increase at the September 20-21 FOMC meeting. Instead, it now prices in a 100% probability of a rate hike of at least 75 basis points at the next meeting, according to the CME FedWatch Tool.

The 2-yr note yield, which is more sensitive to changes in the Fed funds rate, rose 28 basis points this week to 3.85%. The 10-yr note yield rose 13 basis points on the week to 3.45%.

Aside from the August CPI report, there was a slew of economic data to digest this week, including a better-than-feared August PPI report that did nothing to dissuade the sell-off. The August Retail Sales report, which didn't show a whole lot of vigor, was also in play for participants.

Adding fuel to the fire, several companies issued earnings warnings this week. FedEx being chief among them, which followed warnings earlier this week from Eastman Chemical, Nucor, and Arconic.

Following the warnings from the aforementioned materials companies, the S&P 500 materials sector was the biggest laggard on the week, closing down 6.7%.

The real estate and communication services sectors suffered the steepest losses after materials, closing down 6.5% and 6.4%, respectively.

Energy and health care were the “best” performing sectors this week, closing down 2.6% and 2.4%, respectively.

- Dow Jones Industrial Average: -4.1% for the week / -15.2% YTD
- S&P Midcap 400: -4.7% for the week / -16.3% YTD
- S&P 500: -4.8% for the week / -18.7% YTD
- Russell 2000: -4.5% for the week / -19.9% YTD
- Nasdaq Composite: -5.5% for the week / -26.8% YTD

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