QUARTERLY ECONOMIC OUTLOOK | SECOND QUARTER 2023

Peeking at possible peaks.

By: James R. Solloway, CFA, Chief Market Strategist and Senior Portfolio Manager

SEI recently released its second-quarter Economic Outlook. Here is summary of our key perspectives.

- While professional forecasters have been making recession predictions for the U.S. economy since the first half of 2022, at present there are no signs currently suggesting that the economy is about to fall off a cliff.
- Unemployment rates in North America, Europe, and the U.K. remain exceptionally low, despite the slowing of overall economic growth. In the U.S., the U.K., and Canada, unemployment levels remain near all-time lows.
- The Conference Board's Composite Index of Leading Economic Indicators has been in sharp decline since April 2022, consistent with a recession. However, coincident indicators, which track the current health of the real economy, continue to advance.
- The yield curve, a predictor of past economic downturns, has been inverted since November 2022. Since an inversion has often occurred a year or less before a recession, it is understandable why economists have underestimated the economy's resiliency.
- The Organisation for Economic and Development's version of the Leading Economic Indicators suggests that the global economy is not firing on all cylinders. As of April, only three of the 18 countries represented are delivering better-than-average growth.
- The surprising resilience of the global economy reflects the long tail of the post-COVID recovery. It also explains the divergence of the services sector, which is keeping the global economy afloat, and manufacturing, which is in stagnation or decline.
- Although the banking panic has subsided, we worry about the impact on small businesses. Recent readings of lending conditions are already at levels consistent with previous recessions. While hiring plans of companies dependent on local banks are still reasonably strong, a further tightening of credit conditions could spark the recession many economists have been forecasting.
- China continues to struggle with a disappointing economic recovery. The equity market got off to a strong start in January on hopes that the end of COVID lockdowns would spark growth, only to turn lower during February and March. More recently, economic data have been coming in below consensus expectations, leading to additional declines in equity prices.
- Inflation has peaked, but remains high. We continue to think that inflation pressures will remain persistent in labor-intensive service industries, at least until some slack opens up in the labor markets and spending by households fades more dramatically.
- Sticky inflation and ongoing labor-market tightness have forced central banks to keep raising rates. Although the Federal Reserve left its benchmark federal-funds rate unchanged in June, it warned of two potential rate hikes by year-end.
- We continue to believe that inflation and interest rates will remain higher for longer. While U.S. inflation is decelerating, we doubt it will fall below 3% on a sustainable basis. Nonetheless, we think the end of the interest-rate hiking cycle is within sight.
- Japan's monetary policy remains expansionary. Our belief that a new central-bank head and finance minister would bring about change hasn't happened—yet. As a result, the yen has been quite weak against the dollar and other major currencies.
- The yen's depreciation has accelerated as traders short the currency. We believe this dynamic will add to inflationary pressures in Japan. If their monetary policy turns restrictive, the unwinding of these short positions could spur a rally in the yen.
- The U.S. stock market's advance this year has been highly concentrated, with 27% of the S&P 500's constituents outperforming the index itself. If this figure holds through year-end, it would mark the lowest level in the 50-year history of the dataset.
- Adding to the woes of active managers, seven stocks account for about three-quarters of the S&P 500's 16.9% year-to-date return, with the remaining 493 companies posting a cumulative year-to-date total return contribution of only 4.4%. A reversal in relative performance may not be far off.
- The rally in equities has surprised us, especially in recent months. But, while buoyant stock indexes have engendered increasing optimism among investors, it makes us more cautious. Investors with a tactical bent should take a contrary view of the rally.

A full-length paper is available if you wish to learn more about these timely topics.

© 2023 SEI

All data as of 6/30/2023 and in U.S. dollar terms unless otherwise noted.

Glossary

The S&P 500 Index is a market-weighted index that tracks the performance of the 500 largest publicly traded U.S. companies and is considered representative of the broad U.S. stock market.

Important information

SEI Investments Canada Company, a wholly owned subsidiary of SEI Investments Company, is the Manager of the SEI Funds in Canada.

The information contained herein is for general and educational information purposes only and is not intended to constitute legal, tax, accounting, securities, research or investment advice regarding the Funds or any security in particular, nor an opinion regarding the appropriateness of any investment. This commentary has been provided by SEI Investments Management Corporation (“SIMC”), a U.S. affiliate of SEI Investments Canada Company. SIMC is not registered in any capacity with any Canadian regulator, nor is the author, and the information contained herein is for general information purposes only and is not intended to constitute legal, tax, accounting, securities, or investment advice, nor an opinion regarding the appropriateness of any investment. You should not act or rely on the information contained herein without obtaining specific legal, tax, accounting and investment advice from qualified professionals. This information should not be construed as a recommendation to purchase or sell a security, derivative or futures contract. You should not act or rely on the information contained herein without obtaining specific legal, tax, accounting and investment advice from an investment professional. This material represents an assessment of the market environment at a specific point in time and is not intended to be a forecast of future events, or a guarantee of future results. There is no assurance as of the date of this material that the securities mentioned remain in or out of the SEI Funds.

Statements that are not factual in nature, including opinions, projections and estimates, assume certain economic conditions and industry developments and constitute only current opinions that are subject to change without notice. Nothing herein is intended to be a forecast of future events, or a guarantee of future results.

This material may contain "forward-looking information" ("FLI") as such term is defined under applicable Canadian securities laws. FLI is disclosure regarding possible events, conditions or results of operations that is based on assumptions about future economic conditions and courses of action. FLI is subject to a variety of risks, uncertainties and other factors that could cause actual results to differ materially from expectations as expressed or implied in this material. FLI reflects current expectations with respect to current events and is not a guarantee of future performance. Any FLI that may be included or incorporated by reference in this material is presented solely for the purpose of conveying current anticipated expectations and may not be appropriate for any other purposes.

There are risks involved with investing, including loss of principal. Diversification may not protect against market risk. There may be other holdings which are not discussed that may have additional specific risks. In addition to the normal risks associated with investing, international investments may involve risk of capital loss from unfavourable fluctuation in currency values, from differences in generally accepted accounting principles or from economic or political instability in other nations. Emerging markets involve heightened risks related to the same factors, in addition to those associated with their relatively small size and lesser liquidity. Bonds and bond funds will decrease in value as interest rates rise.

Information contained herein that is based on external sources is believed to be reliable, but is not guaranteed by SEI Investments Canada Company, and the information may be incomplete or may change without notice.

Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.