SCHWAB: Weekly Trader's Outlook

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More volatility likely in the cards next week with Nvidia earnings on deck.

Stocks have remained buoyant this week, despite higher yields and hotter inflation data. Will Nvidia's earnings alter recent bullish sentiment?

The Week That Was:

If you read last week's blog, you might recall that my outlook for this week called for "Higher Volatility" and that's what we got. Yes, this week's hot inflationary data was the primary catalyst for the volatility (more on this week's economic data below), but the "melt-up" we've been seeing in stocks recently also played a role. Following Tuesday's hot CPI report, most of the majors dropped 2.0% on an intraday basis (the RUT was down double that) and the VIX spiked to a three-month high. Stocks subsequently recovered and are roughly flat week-over-week. While expectations have been downwardly adjusted regarding how accommodative the Fed will be, the bullish thesis still seems to be that the U.S. economy is stronger than expected, which will translate into higher corporate earnings, and by extension higher stock prices. Also potentially contributing to earnings growth is the AI secular growth story, which is being validated by strong earnings reports from the technology sector. The bears would likely point to high valuation, economic uncertainty (stubborn inflation and an over-extended consumer), and the potential for a recession which is being underappreciated by investors. The cross currents are what makes a market, and as is usually the case, we'll need more time & data points to see how things play out.

Outlook for Next Week:

The biggest potential catalyst for markets next Wednesday is Nvidia's quarterly earnings report, slated to be released after the bell on Wednesday (February 21st). I'm concerned this event could be a catalyst for profit taking in technology (especially in the AI and chip space), regardless of what they report, given how much tech has run this year. I'm also a little concerned about the recent lift in bond yields we've seen, even though stocks have been able to take it in stride, at least so far. On the other hand, I'm encouraged by the relative strength in the RUT (more in the Technical Take section below) and how this suggests a broadening of the rally in stocks, which is bullish. The strength in the Russell in addition to the anticipation of NVDA earnings on Wednesday leads me to believe we could have a bullish bias in the first half of the week and a volatile, and potentially bearish, back half of the week. Therefore, my outlook for next week is "Slightly Bullish" for the first half of the week and "Slightly Bearish" for the second half of the week. What could challenge my forecast? Nvidia reports a stellar quarter on Wednesday, moves higher post earnings and fuels additional FOMO in the technology space.

Next Week's Potential Market-moving Catalysts:

Economic:

- Wednesday (Feb. 21): EIA Crude Oil Inventories, Federal Open Market Committee (FOMC) Minutes, MBA Mortgage Applications Index

- Thursday (Feb. 22): Continuing Claims, EIA Natural Gas Inventories, Existing Home Sales, Initial Jobless Claims, S&P Global Services PMI, S&P Global US Manufacturing PMI (Preliminary)

Earnings:

- Monday (Feb. 19): Masonite International (DOOR), Transocean (RIG)
- Tuesday (Feb. 20): Walmart (WMT), Home Depot (HD), Medtronic (MDT), Palo Alto Networks (PANW), Public Storage (PSA), Realty Income (O)
- Wednesday (Feb. 21): Analog Devices (ADI), Verisk Analytics (VRSK), Exelon (EXC), Nvidia (NVDA), Synopsys (SNPS), Rivian Automotive (RIVN)
- Thursday (Feb. 22): Pioneer Natural Resources (PXD), Keurig Dr. Pepper (KDP), Cheniere Energy (LNG), Moderna (MRNA), Intuit (INTU), Booking Holdings (BKNG), MercadoLibre (MELI)
- Friday (Feb. 23): Warner Bros Discovery (WBD), AerCap Holdings (AER)

Economic Data, Rates & the Fed:

Inflation data took center stage this week and the results were hotter-than-expected:

- **Consumer Price Index (CPI):** Headline month-over-month (MoM) was +0.3% (above the +0.2% est) and core MoM came in at +0.4% (above the +0.2% est); Headline year-over-year (YoY) was + 3.1%, down from 3.4% in December but above the 2.9% expected while core YoY was +3.9%, unchanged from December but above the 3.7% expected. The MoM super core CPI, which excludes shelter and energy services increased 0.8% (highest since April 2022) following a 0.3% rise in December while the super core YoY was up to 4.4%, up from 3.9% in December.
- **Producer Price Index (PPI):** Headline month-over-month (MoM) was +0.3% (above +0.1% est, largest increase since August 2023) and core MoM came in at +0.6% (above the +0.1% est and the biggest jump since January 2023); Headline

year-over-year (YoY) was + 0.9%, down from 1.0% in December but above the 0.6% expected while core YoY was +2.6%, unchanged from December but above the 1.6% expected.

- This morning's one-year inflation expectations from the University of Michigan Consumer Sentiment ticked up to 3.0% from 2.9% in the prior month (five-year inflation expectation was unchanged at 2.8%).

- Lastly, you might recall that the Prices Paid component from the ISM Manufacturing index rose to 52.90 in January from 45.20 in December.

While these data points do not necessarily mark a reversal in the decelerating trend in inflation that we've seen over the last year, it does suggest that the path down to the Fed's 2.0% annual inflation target may be more difficult to achieve than anticipated. If inflation data continues to remain stubborn in the coming months, the Fed will likely keep policy higher for longer, which suggests bond yields are likely to remain elevated (which could be relatively negative for stocks).

How healthy is the U.S. consumer? January's retail sales were weak (-0.8% vs. -0.2% expected) and December retail sales were revised lower (to +0.4% from +0.6%). The month-over-month drop in retail sales was the largest decline since March of 2023. January retail sales, excluding auto and gas, declined -0.5% versus expectations for a 0.2% increase. Again, this is only one data point, but the health of the consumer is important to monitor as it ties directly into GDP and corporate earnings.

Bond yields saw a lift this week, mostly driven by the inflation data mentioned above. On a week-over-week basis, yields on the 10-year Treasury yields (TNX) are currently up to a two-month high of 4.309% from 4.187% last Friday. Perhaps more sensitive to the recent economic data are two-year Treasury yields which are up to 4.671% from roughly 4.20% at the end of January.

Market expectations around Fed cuts continue to move down towards what the Fed has communicated rather than the other way around. Last December markets were expecting six rate cuts in 2024 and that expectation is now down to just three. The current Bloomberg probability for a Fed rate cut in March is now just 11%, down from last Friday's 19%, and May has dropped all the way down to 34% from 73% last Friday.

Technical Take:

S&P 500 Index (SPX - 2 to 5,027)

Yes, the S&P 500 index (SPX) is still in a bullish uptrend and the index is holding up relatively well given the inflation data and subsequent rise in yields this week. However, there are some signs that momentum is waning, which may suggest that some consolidation of recent gains is coming near-term. Will it happen next week? Impossible to know for sure but let's take a step back and remember that the SPX is up over 20% since late October, so some mean reversion shouldn't be a surprise when it hits. If we get a pullback, a logical area of support appears to be around 4,800 given the confluence of the following–4,800 was roughly the prior all-time high and represented a key resistance level late last year, the 50-day SMA is roughly 4,800, and the 23% Fibonacci Retracement level from the October level to recent highs is also roughly 4,800. *Near-term technical translation: slightly bearish.*

Source: ThinkorSwim trading platform

Past performance is no guarantee of future results.

Russell 2000 Index (RUT - 14 to 2,047)

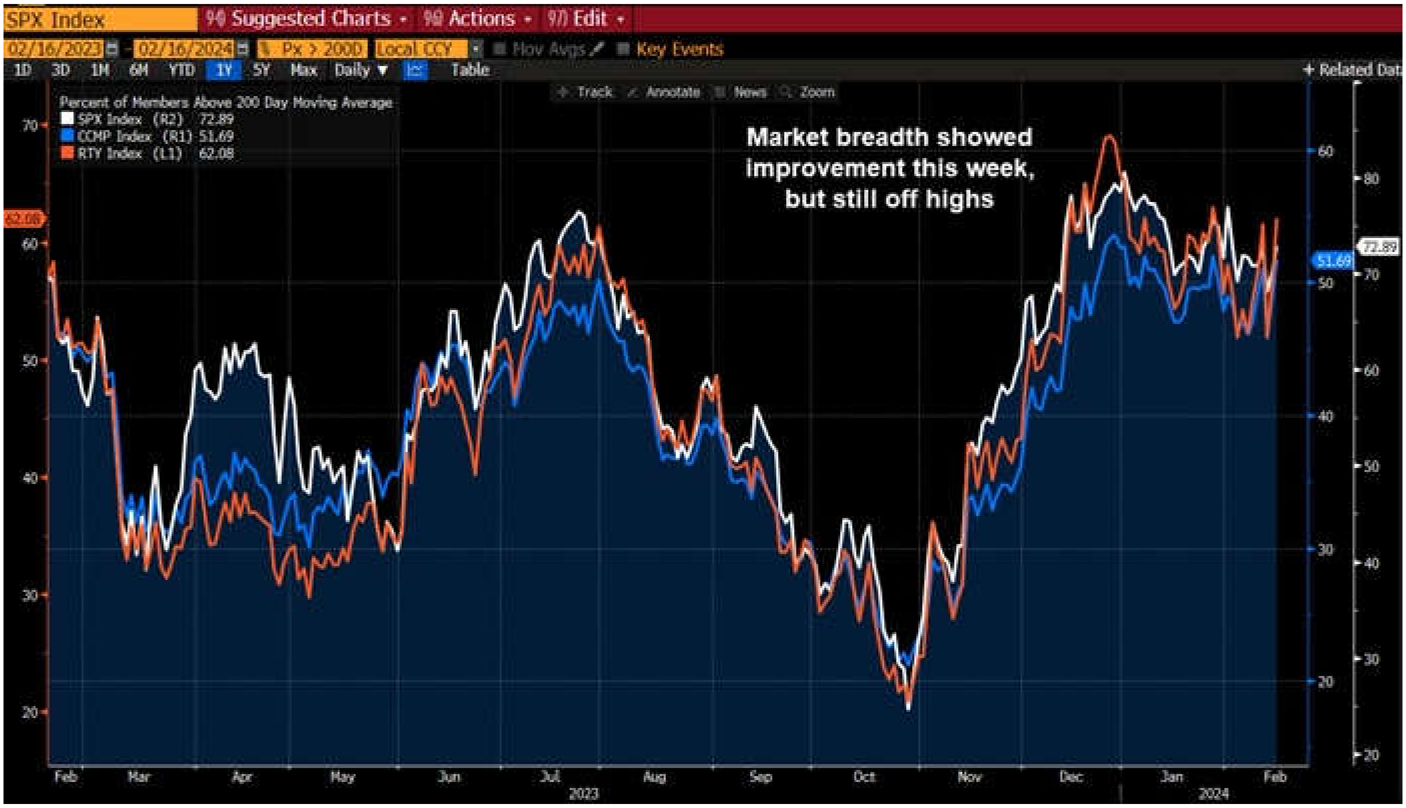
What stands out to me about the Russell 2,000 index (RUT) this week is the relative strength that it exhibited in the face of rising bond yields. Higher yields over the past two years have made this rate-sensitive index a relative underperformer among the majors, but it appears a shift in sentiment is underway. The five long green candles on the right-hand side of the chart below suggest money flow is finding its way into the RUT. If the index is able to breakout to fresh two-year highs next week (prior two-year high from December is 2,066), this could contribute to recent bullish momentum. *Near-term technical translation: bullish.*

Source: ThinkorSwim trading platform

Past performance is no guarantee of future results.

Market Breadth:

Although the majors are relatively flat on the week in terms of performance, we did witness improvement in market breadth. Below is a Bloomberg chart showing the current percentage of members of the S&P 500, Nasdaq Composite, and Russell 2000 that are trading above their respective 200-day Simple Moving Averages. Compared to last Friday, the SPX (white line) breadth moved up to 72.89% from 70.88%, the COMPX (blue line) is up to 51.69% from 46.88%, and the RUT (red line) showed the biggest improvement, moving up to 62.08% from 54.91%.



Source: Bloomberg L.P.

Market breadth attempts to capture individual stock participation within an overall index, which can help convey underlying strength or weakness of a move or trend. Typically, broader participation suggests healthy investor sentiment and supportive technicals. There are many data points to help convey market breadth, such as advancing vs. declining issues, percentage of stocks within an index that are above or below a longer-term moving average or new highs vs. new lows.

This Week's Notable 52-week Highs (207 today): Abbvie Inc (**ABBV** + $0.66 to $177.25), Abercrombie & Fitch Co. (**ANF** + $0.54 to $120.34), Cummins Inc. (**CMI** + $3.50 to $269.30), Dick's Sporting Goods Inc. (**DKS** - $0.73 to $169.45), JP Morgan Chase & Co. (**JPM** - $0.64 to $179.22), Super Micro Computer Inc. (**SMCI** - $110.10 to $893.90), Walt Disney Company (**DIS** - $0.23 to $112.22)

This Week's Notable 52-week Lows (40 today): Agco Corp. (**AGCO** - $0.03 to $110.55), Alnylam Pharmaceuticals Inc. (**ALNY** - $0.23 to $147.19), Biogen Inc. (**BIIB** -

$4.57 to $218.78), Herbalife Ltd. (**HLF** + $0.01 to $8.04), Medifast Inc. (**MED** + $0.06 to $51.52), Nu Skin Enterprises Inc. (**NUS** + $0.26 to $14.08), Transocean Inc. (**RIG** - $0.09 to $4.94)