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Weekly Trader's Outlook

Stocks Set for Weekly Losses as Weak Guidance in Software/Cloud Drive Profit-Taking

May 31, 2024 Nathan Peterson

Stocks are on track to close out the month on a down note as soft guidance out of several software/cloud names (CRM, MDB, S, etc.) dampen tech sentiment.

The Week That Was:

If you read last week's blog, you might recall that my outlook for this week was "slightly bearish," driven by the weekly bearish engulfing candle on the SPX from last Thursday (May 23rd). At the time of this writing the SPX is down ~1.7% on the week, so that outlook turned out to be accurate. While this morning's PCE data essentially conveyed "more of the same" regarding this year's sticky inflation data, I feel there were two more important developments investors/traders should be paying attention to: weak demand in Treasury auctions and weak guidance in software/enterprise cloud companies. The poor demand in this week's bond auctions (more on this in the "Economic Data, Rates & the Fed" section below) suggests to me that upcoming auctions may need to be added to trader's radars (click **here** for a tentative auction schedule). Recent weak guidance out of software/cloud players such as Salesforce, MongoDB, Sentinel One, Workday, etc. put me in the cautious camp regarding the technology sector. There's no question that the AI infrastructure buildout theme has been robust, and has benefitted companies such as Nvidia, Microsoft, Super Micro, Oracle, etc., but the expectations around the

demand and monetization of AI are sky high, which could leave tech stocks vulnerable for disappointment, at least on a near-term basis. Technology stocks have contributed significantly to S&P earnings growth and performance, so if an expectation "reset" occurs around AI, this could dampen recent bullish sentiment. I'll reiterate what I stated last week, "While the bulls may be enjoying the 2024 rally in stocks to fresh record highs, I think it's prudent to take a step back and respect the fact that the S&P 500 is up nearly 7% in five weeks, currently trading at a forward P/E of nearly 21 (well above the 10-year forward P/E of 17.7 per FactSet), and the outlook on inflation and Federal Reserve monetary policy is anything but certain."

Outlook for Next Week:

At the time of this writing (1:50 p.m. EDT), tech stocks are getting hit ($COMPX – 1.15%) and perhaps a bit of a relief rally is being seen in the Dow Jones Industrial Average ($DJI +0.50%). Today's follow-through selling pressure in tech is primarily being driven by post-earnings sell-offs in DELL, MDB, S and profit taking in the semiconductor space ($SOX - $2.7%). While Nvidia has likely been the biggest sentiment driver in stocks this year, I think investors are becoming more aware that not every player in the AI space stands to benefit like they have been. This could suggest that a valuation reset is underway within the tech space. More specifically, investors may seek to take some exposure out of tech and rotate into other underperforming areas of the market. I'm not calling a top on the AI trade, but I believe the recent weakness out of the software-cloud space is significant enough to see additional downside in technology overall. Additionally, as I mentioned in the "Technical Take" section below, June is not a good month from a seasonality perspective over the past 20 years. Yes, we are approaching the Apple Worldwide Developers Conference the following week (June 10th-14th), but for next week I'm still leaning bearish. Therefore, my forecast for next week is once again "slightly bearish." What could challenge this outlook? Technically, the SPX is approaching potential support at the 50-day SMA and the DJI is near potential support around 37,750, so if support holds up

this could bring in some technical buying. Also, next Friday we'll get the monthly jobs report which *could* be a bullish catalyst if the headline number comes in below estimates and/or average hourly earnings come in soft.

Other Potential Market-moving Catalysts:

Economic:

- Monday (June 3): Construction Spending, ISM Manufacturing Index, S&P Global US Manufacturing PMI - Final
- Tuesday (June 4): Factory Orders, JOLTS – Job Openings
- Wednesday (June 5): ADP Employment Change, EIA Crude Oil Inventories, ISM Non-Manufacturing Index, MBA Mortgage Applications Index, S&P Global US Services PMI
- Thursday (June 6): Continuing Claims, EIA Natural Gas Inventories, Initial Jobless Claims, Productivity-Revised, Trade Balance, Unit Labor Costs-Revised
- Friday (June 7): Average Workweek, Average Hourly Earnings, Consumer Credit, Nonfarm Payrolls, Nonfarm Private Payrolls, Unemployment Rate, Wholesale Inventories

Earnings:

- Monday (June 3): Science Applications International Corp. (SAIC), Gitlab Inc. (GTLB)

- Tuesday (June 4): Ferguson PLC (FERG), Core & Main Inc. (CNM), Bath & Body Works Inc. (BBWI), CrowdStrike Holdings (CRWD), Hewlett Packard Enterprises Co. (HPE), Guidewire Software Inc. (GWRE), PVH Corp. (PVH)

- Wednesday (June 5): Dollar Tree Inc. (DLTR), Brown-Forman Corp. (BF/B), Campbell Soup Co. (CPB), Thor Industries (THO), Lululemon Athletica Inc. (LULU), Five Below Inc. (FIVE), Smartsheet Inc. (SMAR)

- Thursday (June 6): JM Smucker Co. (SJM), Nio Inc. (NIO), Samsara Inc. (IOT), DocuSign Inc. (DOCU), Vail Resorts Inc. (MTN), Braze Inc. (BRZE)

Economic Data, Rates & the Fed:

It was an average week regarding the number of economic data points released, which was highlighted by the monthly PCE data and a second estimate to Q1 GDP. In short, the inflation data essentially came out in line with expectations, though the data likely still lacks the level or consistency that would satisfy the Fed's objective on prices. Regarding GDP, the second estimate came in below estimates, primarily driven by downward revisions to consumer spending and private inventory investment.

- Personal Consumption Expenditures Price Index (PCE): Headline was 0.3% (in line with expectations), year-over-year (YoY) change was 2.7% (in line with estimates and unchanged from the prior month). Core PCE headline was 0.2% (below the 0.3% expected) with the YoY Core PCE coming in at 2.8% (in line with estimates and unchanged from the prior month).

- Q1 GDP – Second Estimate: Q1 GDP was revised lower to just 1.3% from the initial (advanced) reading of 1.6%. This was driven by downward revisions to consumer spending on goods, with motor vehicles being the largest contributor.

> For reference, the current GDPNow estimate is 2.7%, down from a 3.5% estimate just last Friday (May 24th).

Another notable data point was this morning's Chicago PMI, which fell to its lowest level since the pandemic in May of 2020. The index came in at 35.4, which was well below the 40.8 economists had expected and down from 37.9 in April.

Bond yields are little changed on a week-over-week basis, but we did see a mid-week spike which was driven by some poorly received bond auctions. Yields on the 10-year closed at a four-week high on Wednesday following weak demand for two-year and five-year notes on Tuesday, followed up with soft demand for seven-year notes on Wednesday. Thursday's softer GDP figure, coupled with this morning's in-line PCE data helped yields ease as yields on the 10-year currently sit at 4.50% at the time of this writing.

Market hopes around the potential for Fed rate cuts remain subdued. While the Bloomberg probabilities around a September rate cut haven't changed that much since last Friday (currently 58% vs. 54% last Friday), there currently isn't enough evidence in the data to warrant a Fed rate cut. Earlier this week, Minnesota Federal Reserve President Neel Kashkari said that "many more months of positive inflation data" will be needed before he has confidence that it is appropriate to ease current monetary policy.

Technical Take:

S&P 500 Index (SPX - 36 to 5,199)

Last Friday I highlighted the weekly bearish engulfing candle on the SPX chart (shown below) and it appears that it was an accurate bearish indicator based on this week's price action. The index is roughly 20 points above its 50-day Simple Moving Average, which *could* provide some near-term support. However, leadership within the tech sector is beginning to show some cracks and seasonality is not great with June being in

the bottom quartile in terms of performance over the past 20 years. Additionally, while the 50-day SMA could provide near-term support, it hasn't demonstrated reliability as support if you look at what happened back in April. Therefore, I'm still in the bearish camp until it proves otherwise. *Near-term technical translation: bearish*

Source: ThinkorSwim trading platform

Past performance is no guarantee of future results.

Dow Jones Industrial Average Index ($DJI + 136 to 38,247)

I'm highlighting the $DJI this week because the index is down roughly 4.5% over the past six trading days and the Down Jones Transportation Average ($DJT) closed at a six-month low on Wednesday. Most of the money flow/attention has been going towards the technology space because of the enthusiasm around the AI secular growth story, but I think it's important to keep the perspective wholistic and keep an eye on all of the majors. Outside of tech, there's been a bit of a rollover in several other industries over the past two weeks such as industrials, health care, materials, and financials. Nothing is necessarily flashing a technical warning (except perhaps the sharp sell-off in

transports), but if you are bullish on stocks, you probably would like to see the $DJI stay above support around 37,750. *Near-term technical translation: slightly bearish*

Source: ThinkorSwim trading platform

Past performance is no guarantee of future results.

Market Breadth:

The Bloomberg chart below shows the current percentage of members within the S&P 500 (SPX), Nasdaq Composite (CCMP) and Russell 2000 (RTY) that are trading above their respective 200-day Simple Moving Averages. We've seen some continued degradation in breadth over the past couple weeks in the SPX, which is at the lowest levels since last December. Compared to last Friday, the SPX (white line) breadth moved down to 68.07% from 73.29%, the COMPX (blue line) ticked up ever so slightly to 45.09% from 44.84%, and the RUT (red line) inched up to 54.39% from 53.61%.

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 (94 today): Alcoa Corp. (**AA** + $1.40 to $45.33), Costco Wholesale Corp. (**COST** - $19.17 to $796.17), Cameco Corp. (**CCJ** + $0.30 to $55.07), Eli Lilly & Co. (**LLY** + $0.07 to $815.13), Nvidia Corp. (**NVDA** - $25.79 to $1,079.21), T-Mobile US Inc. (**TMUS** + $0.59 to $171.29), Universal Health Services Inc. (**UHS** + $0.61 to $186.51)

This Week's Notable 52-week Lows (77 today): Accenture PLC (**ACN** - $5.21 to $279.59), Dayforce Inc. (**DAY** - $0.78 to $49.61), Gilead Sciences Inc. (**GILD** - $0.73 to $63.34), MongoDB Inc. (**MDB** - $76.15 to $233.85), Paycom Software Inc. (**PAYC** - $4.49 to $43.49), Snowflake Inc. (**SNOW** - $1.43 to $198.98), Vail Resorts Inc. (**MTN** + $3.60 to $188.78)