WELLS FARGO
Investment Institute

Market Commentary

Weekly perspective on current market sentiment — **June 7, 2023**

Scott Wren
Senior Global Market Strategist

Last week's S&P 500 Index: +1.8%

Narrow

Key takeaways

- Ideally, in a bull market, lots of stocks are participating and breadth is strong.
- That has not been the case in the current rally, as the advance in the S&P 500 has been quite narrow and most stocks are lagging.

Market prognosticators often talk about "breadth." Is a move in the market, up or down, supported by a broad swath of stocks or are just a handful (or a couple of handfuls) of individual company stocks pushing the S&P 500 Index (SPX) one way or the other? That is an important question. Participation from a large number of underlying stocks is typically a much more reliable indicator that the trend in place may very well continue, at least in the very near to intermediate term. But over the past three months or so, breadth has been narrow as the SPX has rallied. Only a limited number of mega-capitalization stocks, largely in the Information Technology and Communication Services sectors, have helped push the index up to levels not seen since mid-August of last year.

In the current case, from a trader's point of view, the lack of broader participation has built some expectations that the market upswing might not last. But those investors betting against stocks due to weak breadth have not had much to smile about in recent months, despite what we see as deteriorating fundamentals.

A quick look at the traditional SPX versus the S&P 500 equal-weighted index over the past few months tells the story. Recall that the SPX that is reported in the financial news each day is a capitalization-weighted index. That means the highest-valued companies (shares outstanding x price = market capitalization) have the most impact on the underlying movement of the index. The equal-weighted S&P 500 is just that: every stock carries the same weighting in the index.

Ideally, in a bull market, or one that is at least going up, the equal-weighted index is keeping pace with or even outperforming the traditional SPX. That means lots of stocks are participating and breadth is strong. That has not been the case in the more recent rally as the equal-weighted S&P 500 is up just 2.4% versus the 10.8% rise in the SPX since March 10 as of the time of this writing. That tells investors that the advance in the SPX has been quite narrow, and most stocks are lagging.

Further confirmation of a narrow market can be seen in the performance of the S&P 100 (OEX) versus the SPX. The OEX is the 100 largest-capitalization stocks within the SPX. Since the above-mentioned March 10 date, the OEX has traded 14.8% higher, leaving the performance of the SPX far in the rearview mirror (14.8% - 10.8% = 4% outperformance).

The lack of breadth in recent months only adds to our caution on the equity market and the reiteration of our recommendation not to chase this rally. We see economic headwinds building and expect a recession to begin at some point in the coming months. With the Federal Reserve likely to keep interest rates higher for longer and credit conditions tightening, a narrow market rally does not give us confidence that recent gains will hold.

Risk considerations

Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve. **Stock markets**, especially foreign markets, are volatile. Stock values may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors. Sector investing can be more volatile than investments that are broadly diversified over numerous sectors of the economy and will increase a portfolio's vulnerability to any single economic, political, or regulatory development affecting the sector. This can result in greater price volatility. Risks associated with the **Technology** sector include increased competition from domestic and international companies, unexpected changes in demand, regulatory actions, technical problems with key products, and the departure of key members of management. Technology and Internet-related stocks, especially smaller, less-seasoned companies, tend to be more volatile than the overall market. **Communication Services** companies are vulnerable to their products and services becoming outdated because of technological advancement and the innovation of competitors. Companies in the communication services sector may also be affected by rapid technology changes; pricing competition, large equipment upgrades, substantial capital requirements and government regulation and approval of products and services. In addition, companies within the industry may invest heavily in research and development which is not guaranteed to lead to successful implementation of the proposed product

Definitions

An index is unmanaged and not available for direct investment.

S&P 100 Index measures large cap company performance and consists of up of 100 major, blue chip companies across diverse industry groups. The primary criterion for index inclusion is the availability of individual stock options for each constituent.

S&P 500 Index is a market capitalization-weighted index composed of 500 widely held common stocks that is generally considered representative of the US stock market.

S&P 500 Equal-Weighted Index is designed to track the equally weighted performance of the 500 companies in the S&P 500.

General Disclosures

Global Investment Strategy (GIS) is a division of Wells Fargo Investment Institute, Inc. (WFII). WFII is a registered investment adviser and wholly owned subsidiary of Wells Fargo Bank, N.A., a bank affiliate of Wells Fargo & Company.

The information in this report was prepared by Global Investment Strategy. Opinions represent GIS' opinion as of the date of this report and are for general information purposes only and are not intended to predict or guarantee the future performance of any individual security, market sector or the markets generally. GIS does not undertake to advise you of any change in its opinions or the information contained in this report. Wells Fargo & Company affiliates may issue reports or have opinions that are inconsistent with, and reach different conclusions from, this report.

The information contained herein constitutes general information and is not directed to, designed for, or individually tailored to, any particular investor or potential investor. This report is not intended to be a client-specific suitability or best interest analysis or recommendation, an offer to participate in any investment, or a recommendation to buy, hold or sell securities. Do not use this report as the sole basis for investment decisions. Do not select an asset class or investment product based on performance alone. Consider all relevant information, including your existing portfolio, investment objectives, risk tolerance, liquidity needs and investment time horizon. The material contained herein has been prepared from sources and data we believe to be reliable but we make no guarantee to its accuracy or completeness.

Wells Fargo Advisors is registered with the U.S. Securities and Exchange Commission and the Financial Industry Regulatory Authority, but is not licensed or registered with any financial services regulatory authority outside of the U.S. Non-U.S. residents who maintain U.S.-based financial services account(s) with Wells Fargo Advisors may not be afforded certain protections conferred by legislation and regulations in their country of residence in respect of any investments, investment transactions or communications made with Wells Fargo Advisors.

Wells Fargo Advisors is a trade name used by Wells Fargo Clearing Services, LLC and Wells Fargo Advisors Financial Network, LLC, Members SIPC, separate registered broker-dealers and non-bank affiliates of Wells Fargo & Company. CAR-0623-00892