Amplify ETFs

Market and
Economic **Update**

What Slowing U.S. Manufacturing and Growth Means

MARCH 2023

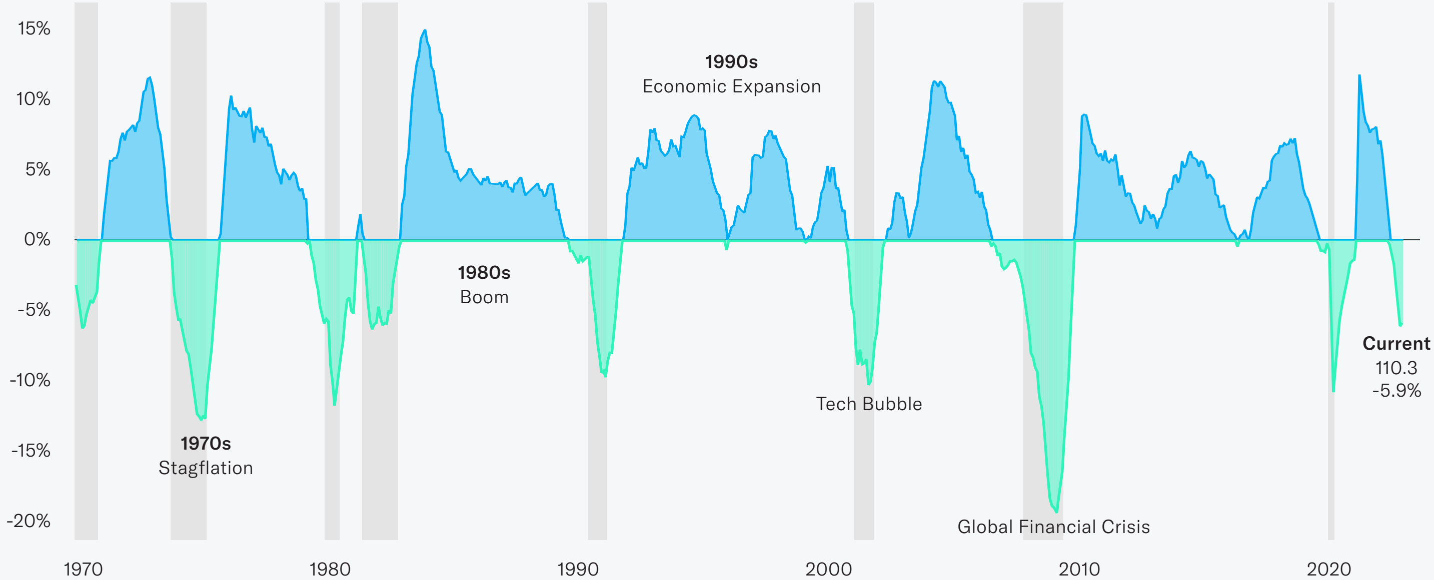
Stock market volatility has once again picked up as recent economic data have led markets to reverse course after a strong start to the year. While investors have grown accustomed to daily swings, it's still important to remember that stock market fluctuations are normal, expected and unavoidable. After all, it's the willingness and ability to withstand pullbacks in the short run that allows investors to be rewarded in the long run. During periods of uncertainty, understanding the underlying trends driving markets can help investors maintain perspective.

What dynamics are driving markets beneath the surface? First, there is no doubt that the economy has slowed in recent months. The accompanying chart shows that an index of leading economic indicators (LEIs) has contracted on a year-over-year basis. U.S. gross domestic product (GDP) data for Q4 was also revised down slightly to 2.7%, meaning that growth was still positive at the end of last year, but was weaker than originally believed. This was due to slower consumer spending and exports.

1. The economy has decelerated in recent months

LEADING ECONOMIC INDICATORS

Conference Board LEI year-over-year percent change / Recessions are shaded



Sources: Clearnomics, Conference Board, NBER, Refinitiv, January 1970 to January 2023

Meanwhile, inflation figures for January were unexpectedly hot with personal consumption expenditures (PCE) inflation - the measure that the Federal Reserve (Fed) favors - still far above the Fed's 2% target, stoking concerns that the central bank may need to raise rates more aggressively. They are now expected to push the fed funds rate to nearly 5.5% later this year.

Second, and perhaps more importantly, is the divergence between goods and services. Goods are tangible items that consumers and businesses need such as cars, food, gasoline, clothing, home appliances, and more. Services are everything else, such as eating at restaurants, rent, education, medical care, etc. One defining characteristic of the past few years is that the demand for goods skyrocketed during and after pandemic lockdowns, while services languished as consumers stayed home. This has reversed as life has returned to normal across the country, shifting spending back to services.

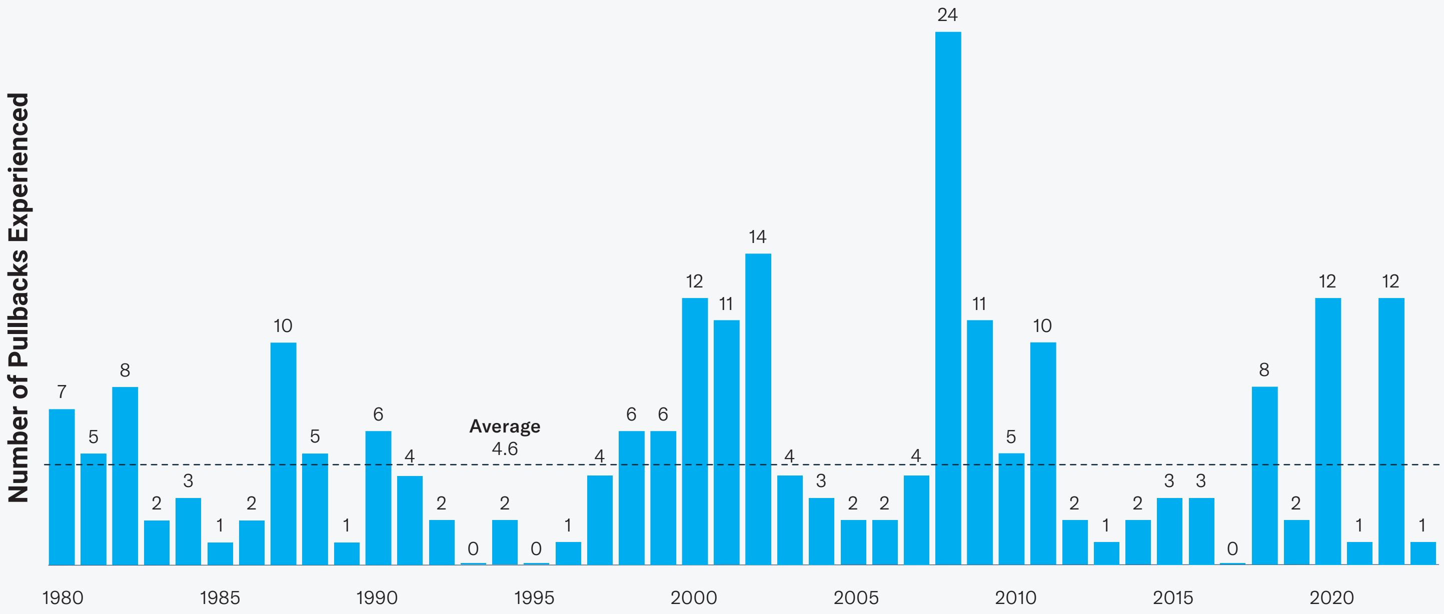
This, in turn, has resulted in a slowdown in manufacturing which can be seen across a variety of data. The manufacturing purchasing managers' index (PMI) - a measure of economic activity - has contracted while services PMI, on the other hand, are still expanding after a brief dip. This can also be seen in other data such as industrial production which has decelerated to a year-over-year growth rate of less than 1%.

This is occurring at a time when "reshoring" manufacturing back to the U.S. is part of the economic and political debate. One lesson of the past few years is that while global supply chains can be a boon when things are running smoothly, they can also be fragile when there are unforeseen economic shocks, whether related to the pandemic or Russia's invasion of Ukraine. Securing these supply chains through policies such as the CHIPS Act and individual business decisions will likely be a priority in both the public and private sectors over the next several years.

2. Despite recent swings, markets have been calmer in 2023

STOCK MARKET PULLBACKS

The number of 5% S&P 500 pullbacks experienced by investors each year



Sources: Clearnomics, Standard & Poor's, January 1, 1980 to March 6, 2023

So, what does this all mean? It's clear that the economy has slowed and that the differences between goods and services are driving both growth and inflation. However, not only is this widely expected with GDP anticipated to be flat in 2023, but there are always swings and uncertainty in the data. The fall in durable goods, for instance, is largely due to a decline in aircraft and parts orders after it surged the month before.

Inflation can vary significantly from month-to-month too, especially as rent and housing prices stabilize due to rising rates. Fed expectations have shifted higher in recent weeks, but they have also fluctuated wildly over the past year. While data is important, focusing too much on any individual datapoint can be problematic.

Investors should remember that markets have regained significant ground since last summer. Diversified portfolios are mostly in the black this year and the S&P 500 Index has only experienced one 5% pullback in 2023. Staying invested can be difficult amid all the negative market headlines but it's ultimately what allows investors to achieve their long-term goals.

Past performance is no guarantee of future results.

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