

January 8, 2024 – Investment Commentary

Market Commentary

The Fed's recent revelation that it was targeting three rate cuts totaling 75 bps in 2024 sent the equity and fixed income markets surging in December. Both the NASDAQ and the Dow Jones Industrial Indices set all-time highs during the month. On 12/28/23, the S&P 500 Index closed within 14 points of its all-time high. The Bloomberg U.S. Aggregate Bond Index rose by 8.53% on a total return basis in November and December combined. That said, investors would be well served to watch the data closely. Inflation remains well above the Fed's stated target of 2.0%, and investors are pricing in significantly larger interest rate cuts than the Fed is forecasting. We expect the general themes of central bank policy, inflation, and the threat of a meaningful economic slowdown to remain front and center in investors' minds as we enter the first half of 2024.

Last week, the labor market data supported the case for a resilient economy, including strong US December non-farm payrolls and average hourly earnings year-on-year +4.1% actual vs +3.9% expected. These metrics likely lower the chances of the Fed lowering rates anytime soon. If accurate, that could put upward pressure on interest rates out of the curve, and downward pressure on P/E ratios. The Fed cutting rates may risk more economic activity and may derail or delay the Fed achieving its 2% inflation target. The unemployment rate has recorded 25 months of below 4% unemployment, the longest streak in over 50 years creating, another reason not to cut. All major US equity indices closed lower last week, with the S&P500 -1.5%, tech heavy Nasdaq -3.2% and small cap Russell 2000 down 3.7%, week-over-week. While in the fixed income markets 2 year US government bonds closed Friday +17bps/4.40% yield and the 10 year closed +17bps at 4.05% yield.

Portfolio Considerations

A current market narrative is a rotation into laggards following the strong outperformance of mega-cap growth stocks last year, with encouraging signs that equity market breadth is improving across market capitalizations, value stocks, and non-US markets. The market is convinced of a soft landing in 2024 just as it was convinced of a recession in 2023. The big risks to equities include but are not limited to the usual suspects of profit margins, earnings growth, valuations and potentially rates not declining as fast as many investors believe. We look forward to hearing the guidance from the banking sector later this week as earnings season kicks off again.

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