Weekly Market Perspectives

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Stocks End A Nine-Week Winning Streak To Start The New Year

Following nine straight weeks of gains and a solid end to 2023, stocks opened 2024 modestly lower. Both the S&P 500 Index (-1.5%) and NASDAQ Composite (-3.7%) retreated in the abbreviated holiday week, while the Dow Jones Industrials Average declined 0.6%. That said, major U.S. stock averages are coming off an incredible 2023, having erased the declines seen in 2022. Inflation declining substantially throughout 2023, as well as building expectations for easier monetary policy this year, helped fuel a late-year rally. Notably, the S&P 500 advanced over +24.0% last year, while the NASDAQ roared higher by over +43.0%. The strong rally posted in the final weeks of last year also helped lift the Dow by nearly +14.0% in 2023 on a price-alone basis, while the Russell 2000 Index rose by over +15.0%. **Bottom line: Stocks entered 2024 overbought based on some measures after nine straight weeks of gains, which helped lift the S&P 500 higher by over +11.0% in the final quarter of 2023.**

At the end of 2023, 75% of S&P 500 stocks were trading at least one standard deviation above their 50-day moving average. As *Bespoke Investment Group* recently noted, the S&P 500 ended last year with 32 straight trading days in which the Index closed in an overbought condition. Such streaks are rare across history, and according to *Bespoke*, the Index has seen only four other streaks that have gone longer, going back to 1952. Combined with improving investor sentiment readings in late 2023 and end-of-year positioning that, to some extent, appeared to be driven by a *fear of missing out* mentality, stocks were likely overdue for a little weakness at the start of the new year.

Last week's modest stock declines came from areas where investors would intuitively suspect they would come from — last year's winners. Information Technology lost 4.0% in the opening week of the new year after an eye-popping +54.0% gain last year. In addition, Consumer Discretionary lost 3.5% last week after soaring higher by roughly +41.0% in 2023. Conversely, Health Care rose over +2.0% on the week and after essentially ending 2023 flat on a price-alone basis. Add in weekly gains from Utilities (+1.8%), Energy (+1.1%), and Financials (+0.3%), and it's not hard to see that investors seemed interested in starting the new year by rotating out of last year's winners and into some of last year's laggards. However, there are fifty-one more weeks in the new year, and as we pointed out in our 2024 Outlook reports, the direction of interest rates, as well as the degree of earnings strength, will likely play key roles in shaping sector performance this year.

Fed cautions policy path is dependent on how the economy performs

On the macroeconomic front last week, ISM manufacturing remained in contraction in December, while ISM services came in weaker than expected. On the services side, the headline reading in December hit its lowest level since May, though services activity remained in expansion. Also helping weigh on market sentiment was last week's release of the December FOMC meeting minutes, which proved less dovish than investors had hoped for. The minutes noted that officials see the fed funds rate likely near the peak, with most seeing baseline projections for a lower policy rate this year as appropriate. However, the Fed cautioned that the policy path is dependent on how the economy performs, and a high degree of uncertainty remains present. And since financial conditions have eased since the summer, it could be more difficult for the committee to reach its 2.0% inflation goal**.** **Bottom line: Although the FOMC minutes didn't offer any surprises, officials also didn't provide support for the market's expectations of six 25-basis point cuts in the fed funds rate for 2024 prior to the minutes' release.** As such, market odds of aggressive rate cuts for this year have been dialed back somewhat. However, the majority of market participants still see the first fed funds rate cut coming in March, with almost all of the market believing the policy rate will be lower by May. The Federal Reserve will hold its first policy meeting of 2024 later this month, and the committee is widely expected to hold the fed funds target range unchanged at 5.25% - 5.50%.

Job trends show evidence of "slowing but firm conditions"

Importantly, labor conditions in the U.S. remained firm at the end of 2023, but trends are undoubtedly slowing. December nonfarm payrolls grew by a healthy +216,000, and ahead of the +160,000 pace expected. The unemployment rate held steady at 3.7% last month. On the surface, job growth remains solid. However, below the surface, trends are downshifting. The prior two months of job gains were again revised lower, taking the three-month moving average down to its lowest reading since January 2021. Ten of the last eleven months have seen job gains revised lower. In December, the household survey showed a 638,000 decline in the number of employed (possibly due to seasonality factors), with the participation rate and prime-age employment-to-population ratio falling — essentially erasing most of the gains made in each of these areas last year. However, a modest uptick in average hourly earnings last month was somewhat offset by lower hours worked. Combined with a still healthy December ADP private payrolls report and a November JOLTS report that came in largely as expected, job trends are showing continued evidence of "slowing but firm conditions." And while that's exactly what the Federal Reserve wants to see to help tame inflation, labor conditions can change quickly. Yet, the latest batch of employment data last week continues to point to a solid labor environment, which we believe should help support economic and corporate profit growth in the coming months.

Given changing expectations for Fed rate cuts this year and a still healthy labor market, bond yields jumped on the week. Both 2-year and 10-year U.S. Treasury yields moved higher last week, reversing the downward trend seen in late 2023 and weighing on stock sentiment. Interestingly, the higher correlation between stock and bond prices over the previous several quarters could be approaching the tail end of its run, particularly if inflation continues to trend lower this year. Certainly, the recent positive correlation between stock and bond prices (i.e., each moving in a similar direction) has acted to disrupt diversified portfolios and weigh on the benefits of using each in an investment strategy. Unfortunately, markets remain very in tune with rate expectations at the moment. Until government bond yields find a stable equilibrium point, changes in rates should be expected to influence stock prices over the short term. That said, we expect more dispersion in how stocks and bonds perform in the quarters ahead, which should help reestablish the benefits of using each inside a well-diversified portfolio. Notably, the income that can be produced by extending the duration on a portfolio of high-quality bonds today should not be ignored, particularly if rates are headed lower in 2024.

Outside of stocks and bonds, the U.S. Dollar Index notched its best week since July, Gold lost roughly 1.0% on the week, and West Texas Intermediate (WTI) crude settled higher by +2.6%.

The week ahead

After such a strong finish for stocks in 2023, investors are likely entering a *show-me-type* market environment at the start of the new year, following aggressive rate cut expectations and elevated stock valuations. This means the upcoming Q4'23 earnings season and incoming economic data should play key roles in directing stock prices over the coming weeks. Notably, we believe a period of consolidation for major stock averages or even a modest pullback in stock prices after such a strong rally should not deter investors from remaining mostly positive on the outlook for 2024. It's worth mentioning that the S&P 500 trades at roughly 19x this year's expected full-year earnings of approximately $244 per share. While that's not terribly expensive if such dollar earnings are realized this year, it's not exactly cheap either. Based on *FactSet* estimates, earnings growth in 2024 is expected to be driven by Healthcare, Information Technology, Communication Services, and Consumer Discretionary. Outside of Healthcare, continued price gains in the other three sectors may be contingent on not only stocks in these sectors matching profit expectations, but *surpassing* analyst forecasts. While this feat is certainly not out of the realm of possibility (reminder: the AI theme hasn't gone away just because the calendar shifted to a new year), the bar is pretty high for last year's winners to continue their leadership role in 2024.

But as we noted in our 2024 Outlook reports in mid-December, a largely balanced portfolio that recognizes potential opportunities in last year's laggards (e.g., divided payers, small-caps, and companies with recurring revenue) could be areas that have greater potential in a more normalized environment. **Bottom line: As rate and inflation pressures subside over the year, investors should be prepared to evaluate investments more on the merits of their fundamentals and underlying growth potential as opposed to simple shifts in underlying macro conditions.** Given that stock prices have moved aggressively on rate, policy, and economic shifts over the last handful of years, this new dynamic, or return to the basics, could take some adjustment for investors.

This week will bring important updates on inflation, with the December Consumer Price Index hitting on Thursday and the December Producer Price Index coming in on Friday. Interestingly, core CPI is expected to come in at +3.8% year-over-year, marking the first time the price measure has come in at a sub +4.0% level since August 2021. On a headline basis, consumer inflation is expected to tick slightly higher as gasoline prices edged upward last month. Nevertheless, we don't expect this week's inflation data to have a material impact on Fed policy or change the overall macroeconomic backdrop, which, from our perspective, remains on solid footing at the start of the new year. Finally, on Friday, the Q4'23 earnings season kicks off with a bang. Key reports from several big banks, including JPMorgan Chase and Bank of America, as well as Delta Airlines and UnitedHealth Group, will provide early looks into corporate earnings trends during the final quarter of 2023.

Stock Market Recap

Benchmark	Total Returns			LTM PE		Yield %	
	Weekly	MTD	YTD	Current	5-Year Median	Current	5-Year Median
S&P 500 Index: 4,697	-1.5%	-1.5%	-1.5%	23.2	21.2	1.5	1.6
Dow Jones Industrial Average: 37,466	-0.6%	-0.6%	-0.6%	22.2	19.6	1.9	2.1
Russell 2000 Index: 4,849	-3.7%	-3.7%	-3.7%	43.2	35.5	1.4	1.3
NASDAQ Composite: 14,524	-3.2%	-3.2%	-3.2%	38.3	33.9	0.7	0.8
Best Performing Sector (weekly): Health Care	2.1%	2.1%	2.1%	25.6	21.8	1.6	1.6
Worst Performing Sector (weekly): Info Tech	-4.0%	-4.0%	-4.0%	34.8	29.1	0.8	1.0

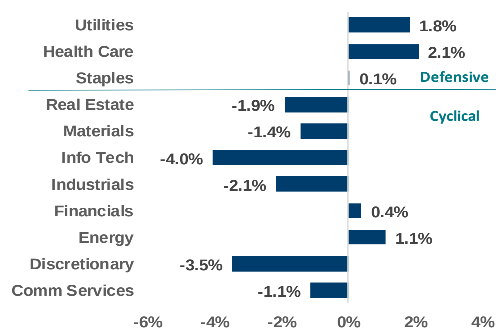
Source: Factset. Data as of 01/05/2024

Bond/Commodity/Currency Recap

Benchmark	Total Returns		
	Weekly	MTD	YTD
Bloomberg U.S. Universal	-1.2%	-1.2%	-1.2%
West Texas Intermediate (WTI) Oil: $73.76	2.6%	2.6%	2.6%
Spot Gold: $2,045.63	-0.8%	-0.8%	-0.8%
U.S. Dollar Index: 102.41	1.1%	1.1%	1.1%
Government Bond Yields	**Yield Chg**		
	Weekly	**MTD**	**YTD**
2-year U.S. Treasury Yield: 4.39%	14 bps chg	14 bps chg	14 bps chg
10-year U.S. Treasury Yield: 4.05%	16 bps chg	16 bps chg	16 bps chg

Source: Factset. Data as of 01/05/2024. bps = basis points

YTD Total Returns by S&P 500 Sector



Source: S&P Global, Factset. Data as of 01/05/2024

These figures are shown for illustrative purposes only and are not guaranteed. They do not reflect taxes or investment/product fees or expenses, which would reduce the figures shown here. An index is a statistical composite that is not managed. It is not possible to invest directly in an index. Past performance is not a guarantee of future results.

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Stock investments involve risk, including loss of principal. High-quality stocks may be appropriate for some investment strategies. Ensure that your investment objectives, time horizon and risk tolerance are aligned with investing in stocks, as they can lose value.

The fund's investments may not keep pace with **inflation**, which may result in losses.

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Past performance is not a guarantee of future results.

An index is a statistical composite that is not managed. It is not possible to invest directly in an index.

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The **Standard & Poor's 500 Index** (S&P 500® Index), an unmanaged index of common stocks, is frequently used as a general measure of market performance. The index reflects reinvestment of all distributions and changes in market prices but excludes brokerage commissions or other fees.

The **NASDAQ composite** index measures all NASDAQ domestic and international based common type stocks listed on the Nasdaq Stock Market.

The **Dow Jones Industrial Average** (DJIA) is an index containing stocks of 30 Large-Cap corporations in the United States. The index is owned and maintained by Dow Jones & Company.

The **US Dollar Index** (USDX) indicates the general international value of the USD. The USDX does this by averaging the exchange rates between the USD and major world currencies. This is computed by using rates supplied by approximately 500 banks.

The **Institute for Supply Management** (**ISM**) manufacturing index is a national manufacturing index based on a survey of purchasing executives at roughly 300 industrial companies. It is an index of the prevailing direction of economic trends in the manufacturing and service sectors.

The **ISM Services PMI** (formerly the Non-Manufacturing NMI) is compiled and issued by the Institute of Supply Management (ISM) based on survey data. The ISM services report contains the economic activity of more than 15 industries, measuring employment, prices, and inventory levels; above 50 indicating growth, while below 50 indicating contraction.

JOLTS report is a monthly survey of U.S. job vacancies, hiring, and job separations released by the Bureau of Labor Statistics of the U.S. Department of Labor.

The **ADP** National Employment Report is a monthly report of economic data that tracks nonfarm private employment in the U.S.

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