Weekly Market Perspectives

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Fed Pushes Back on Rapid Rate Cut Expectations Given Strong Economic Conditions

The S&P 500 Index and NASDAQ Composite each rose more than +1.0% last week, shaking off Wednesday's selloff following the Federal Open Market Committee's policy announcement. However, the Russell 2000 Index posted its fifth weekly decline out of the past six, as small-cap stocks failed to gain traction in January following improved performance in late 2023. Big Tech again led markets higher last week, driven by generally well-received earnings reports from Amazon and Meta Platforms. As a result, Consumer Discretionary (+3.8%) led markets higher, with Communication Services (+1.6%) and Information Technology (+0.8%) also positive on the week.

Despite a hotter-than-expected January jobs report on Friday, which sent government bond yields higher on the day, U.S. Treasury prices were mostly firmer on the week, with the yield curve flattening. The U.S. Dollar Index was stronger on the week and Gold (+1.8%) notched its best week since early December. West Texas Intermediate (WTI) crude settled lower by nearly 8.0% last week, more than giving back the prior week's gains. Continued headline risk associated with Middle East tensions remains the go-to excuse for recent oil volatility.

What did investors learn from last week's economic releases and profit reports?

Importantly, last week was one of the busiest in terms of economic releases and key profit reports of the young year. So, what did investors learn?

- Based on current economic conditions, the Federal Reserve is very unlikely to cut interest rates in March. In fact, Fed Chair Jerome Powell said as much on Wednesday in his press conference following the FOMC leaving the fed funds target rate unchanged at 5.25% - 5.50% for the fourth consecutive meeting. The target rate remains at its highest level in nearly twenty-three years.
- One reason why the Fed isn't in a rush to cut interest rates lies in the continued strength of the labor market. Job creation in the U.S. continues to smash through most economists' estimates. And while Mr. Powell said in his press conference following last week's policy decision that the Fed is not necessarily looking for a slide in employment to inform their rate cut decisions, existing labor strength certainly doesn't require the committee to act with urgency on rate cuts.
- Big Tech remains the profit engine of America. With five of the Magnificent Seven reporting fourth quarter results last week, the S&P 500's Q4'23 EPS growth rate jumped to +1.6% year-over-year from negative year-over-year growth the week before.
- The bull market keeps charging higher. The S&P 500 again made new highs last week, finishing within striking distance of 5,000. Based on *Bespoke Investment Group* measures, the current bull market, which began just before the release of ChatGPT in November 2022, is up over +38%. As *Bespoke* affectionately dubs the "AI Bull," the current bull market may still have some upside based on history. According to *Bespoke* data, the average bull market sees the S&P 500 gain +114% on average, with a median gain of +76%, going back to 1929. Notably,

bear markets tend to sprint toward their bottoms, while bull markets tend to run for distance toward their tops.

Economic conditions remain strong

In terms of the economy, it's hard to imagine conditions any better. The U.S. economy added a stunning +353,000 nonfarm payrolls in January, well ahead of the +177,000 jobs *FactSet* estimates suggested before Friday's release. The unemployment rate held steady at 3.7% and came in below forecasts of 3.8%. Importantly, job growth was widespread across industries last month, indicating labor conditions remain broad-based and healthy at the start of 2024. Wage growth (a measure of labor inflation) was also stronger than expected, doubling economists' forecasts. In a further upside surprise, December and November job gains were boosted markedly higher. Notably, job gains in the final month of 2023 were revised higher by a whopping +216,000 jobs. Add in the stronger-than-expected 9.02 million open jobs in December, combined with strengthening consumer confidence in January, and it's hard not to stand in awe of the strength and resiliency across the U.S. job market and among consumers.

In other items of interest on the economic front last week, January ISM manufacturing, while remaining in contraction, came in above estimates, with new orders expanding for the second time in twenty months. And if one thought the +3.3% growth rate in the final quarter of 2023 was strong, the first quarter of 2024 is tracking even hotter. The Atlanta Federal Reserve's GDPNow forecast for the first quarter currently stands at +4.2%, indicating growth in the economy is accelerating at the start of the year.

Following last week's Federal Reserve meeting, we anticipate the committee will remain patient when it comes to monetary policy and will likely keep its fed funds target rate at current levels through at least the first quarter. But the latest policy statement, as well as Mr. Powell himself, indicated rates are likely restrictive enough to bring down inflation to target with more time and that there is room to ease policy should economic conditions soften. That said, the Fed again pushed back on market expectations for rapid rate cuts last week. Importantly, Powell and company maintained its steady line of "data dependency" as being the main driver of when it would be appropriate to ease policy. In a *60 Minutes* Interview on Sunday, the Fed Chair reiterated it is unlikely the committee will have enough confidence by March that inflation is trending to 2%. **As a result, a majority of investors now believe the first rate cut won't come until May.**

On the earnings front, five of the world's most influential companies, with a combined market value of roughly $10 trillion, reported fourth quarter results last week. Meta Platforms and Amazon generally wowed investors, sending their stock prices higher on the week. Investors liked what they heard from Meta on its commitment to increase investment in AI and begin paying a quarterly dividend. Strong holiday sales and continued strength in cloud computing helped Amazon shares climb higher after its results. However, market reactions to reports from Apple, Microsoft, and Alphabet were mixed, with results and outlooks doing little to change the overall narrative around Big Tech. **Bottom line: Last week's earnings reports from key constituents in the Magnificent Seven offered very few catalysts to motivate investors to step away from these large and influential market leaders.** Yet, varying stock reactions to each company's report last week may indicate the group could become less homogenous over time. Though we see profit opportunities broadening for more of the remaining 493 companies in the S&P 500 this year, the continued outsized earnings potential in just a handful of companies may mean market leadership could remain narrow until profit conditions improve for the rest of the market.

The week ahead

As the week gets started, some technical aspects of the U.S. stock market look favorable and could keep trading activity biased to the upside this year if fundamental conditions continue to cooperate. The S&P 500 appears to be in an upward trend that suggests the broad-based stock average is finally climbing out of its roughly two-year patch of going nowhere. In addition, breadth, measured by the S&P 500's advance or decline line, is breaking out to new highs in combination with the price of the Index climbing to new highs. In our view, these technical conditions add longer-term support for the bulls, who can already point to strong economic fundamentals and the growing potential for easier financial conditions in the quarters ahead. However, we believe near-term trading conditions point to a rally that is beginning to look extended in the absence of additional positive fundamental catalysts. The S&P 500 has been in a multi-month melt-up that has seen the

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major average trade one standard deviation above its 50-day moving average for the better part of the last three months. In addition, major performance participation across the S&P 500 remains rather narrow, and the equal-weighted version of the Index, along with small-cap stocks, has yet to test prior highs. **Bottom line: Over the intermediate term, we see stocks reacting favorably to incoming economic and corporate data that points to a soft-landing scenario and that keeps labor conditions on firm footing and consumers spending.** Nevertheless, a period of consolidation across the major averages or a potential period of near-term selling pressure is probably overdue at this point. Such a development could be healthy in the long term and help recalibrate expectations. Importantly, outside of the handful of stocks that have thus far done the heavy lifting to bring the S&P 500 to its current state, there is growing room for others to help lift broader averages higher over time and if fundamentals remain on track.

The economic calendar is fairly thin this week, with the January ISM Non-Manufacturing Index the key report to watch. Also, following last week's FOMC meeting, several Fed members will provide their individual assessments of policy this week, which should add color to the evolving Fed narrative. Finally, the corporate earnings calendar remains heavy this week, with 104 S&P 500 companies reporting fourth quarter results over the next five days.

Stock Market Recap

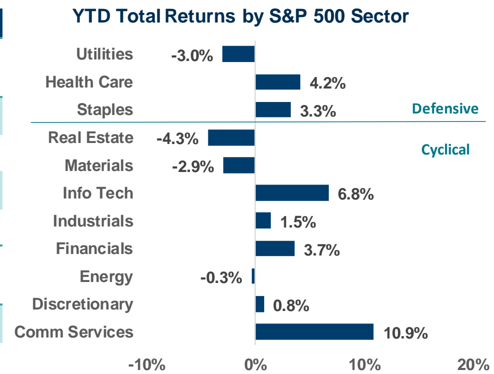
Benchmark	Total Returns			LTM PE		Yield %	
	Weekly	MTD	YTD	Current	5-Year Median	Current	5-Year Median
S&P 500 Index: 4,959	1.4%	2.3%	4.1%	24.5	21.4	1.4	1.6
Dow Jones Industrial Average: 38,654	1.4%	1.3%	2.6%	23.0	19.7	1.9	2.1
Russell 2000 Index: 4,878	-0.8%	0.8%	-3.1%	42.8	35.5	1.4	1.3
NASDAQ Composite: 15,629	1.1%	3.1%	4.1%	41.1	34.0	0.7	0.8
Best Performing Sector (weekly): Consumer Discretionary	3.8%	4.5%	0.8%	30.6	30.9	0.8	0.9
Worst Performing Sector (weekly): Energy	-0.9%	0.1%	-0.3%	10.0	11.6	3.7	3.9

Source: Factset. Data as of 02/02/2024

Bond/Commodity/Currency Recap

Benchmark	Total Returns		
	Weekly	MTD	YTD
Bloomberg U.S. Universal	0.6%	-0.3%	-0.6%
West Texas Intermediate (WTI) Oil: $72.27	-7.9%	-4.7%	0.5%
Spot Gold: $2,039.75	1.0%	0.0%	-1.1%
U.S. Dollar Index: 103.92	0.5%	0.6%	2.6%
Government Bond Yields	Yield Chg		
	Weekly	MTD	YTD
2-year U.S. Treasury Yield: 4.37%	3 bps chg	14 bps chg	12 bps chg
10-year U.S. Treasury Yield: 4.03%	-12 bps chg	8 bps chg	14 bps chg

Source: Factset. Data as of 02/02/2024. bps = basis points



Source: S&P Global, Factset. Data as of 02/02/2024

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There are risks associated with **fixed-income** investments, including credit risk, interest rate risk, and prepayment and extension risk. In general, bond prices rise when interest rates fall and vice versa. This effect is usually more pronounced for longer term securities.

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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 **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 **Russell 2000 Index** measures the performance of the small-cap segment of the US equity universe. The Russell 2000 is constructed to provide a comprehensive and unbiased small-cap barometer and is completely reconstituted annually to ensure larger stocks do not distort the performance and characteristics of the true small-cap opportunity set. The Russell 2000 includes the smallest 2000 securities in the Russell 3000.

The **GDPNow** forecasting model provides a "nowcast" of the official GDP estimate prior to its release by estimating GDP growth using a methodology similar to the one used by the U.S. Bureau of Economic Analysis. GDPNow is not an official forecast of the Atlanta Fed. It is best viewed as a running estimate of real GDP growth based on available economic data for the current measured quarter. There are no subjective adjustments made to GDPNow—the estimate is based solely on the mathematical results of the model.

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.

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