MARKET REVIEW & OUTLOOK

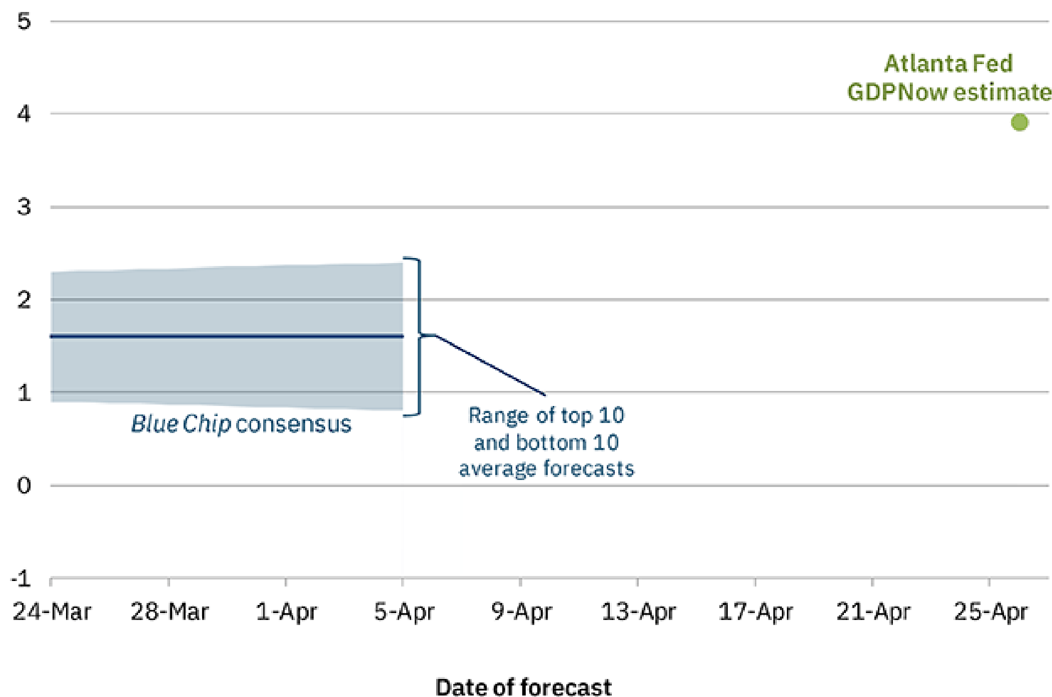
APRIL 2024

KEY TAKEAWAYS

- The equity markets started the month near record highs, up 5 consecutive months. All good things eventually come to an end and that was the case for the rally.
- The U.S. 10-year Treasury Yields had 3 large daily jumps and ended around the 4.70% mark.
- Crude oil managed to stay above $80 for the month, but not by much.

The U.S. Economy

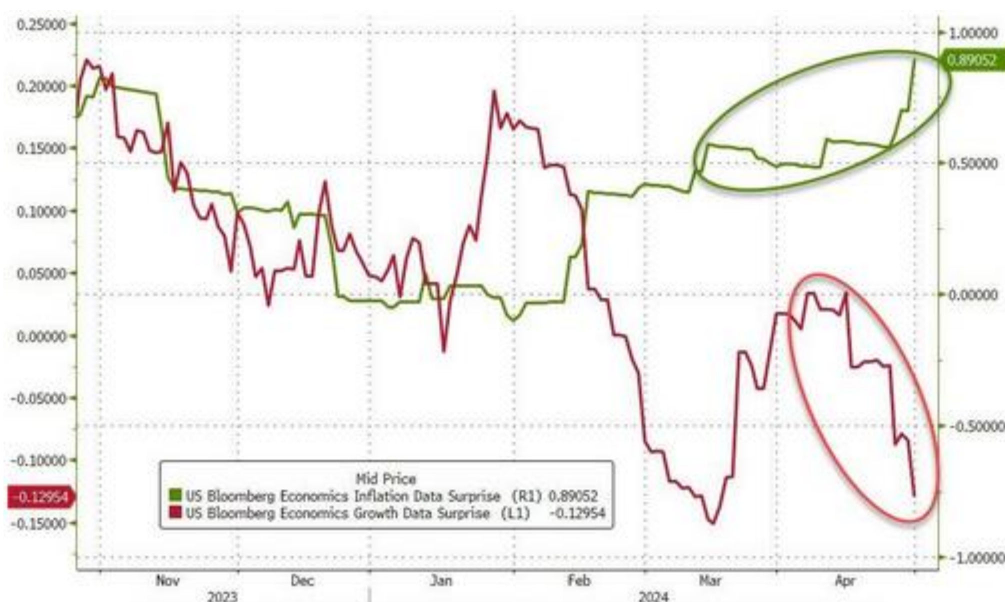
The initial look at 1st quarter GDP came in much weaker than expected at 1.6%, missing expectations of 2.5%. The core PCE, the imbedded inflation measure, jumped from last quarter's 2.0% to 3.7%, beating expectations of 3.4%. Looking to the 2nd quarter, estimates for GDP from GDPNow are almost 4% and the Blue-Chip consensus forecast is near 1.5%, as shown in the chart below. Economic activity weakened, and the PCE deflator strengthened well north of the sweet spot of "2%" inflation. While only one quarter, weaker growth and stronger inflation puts the Fed in a bind. Cut to support the economy and inflation likely soars, raise rates to fight inflation and the economy likely gets even weaker. Is the Fed now at the hold and hope phase?!?!



Source : https://www.frbatlanta.org/cqer/research/gdpnow

Stocks and Bonds

The U.S. 10-year Treasury yield started the month with a big jump in yield, that was later followed up with two more big jumps. The continued reports of strengthening inflation and Fed talk of higher for longer, spooked the bond market. The Fed meets tomorrow where the market long ago removed any expectation of a rate cut. Rather, all eyes are on the tone of the Fed, hawkish or dovish, fighting inflation or supporting the economy. Further, there is speculation that the Fed will announce a wind-down of the Quantitative Tightening policy. As the chart below shows, inflation is surprising to the upside and the economy is surprising to the downside, not the combination the Fed was hoping for. The sharp rise in yields created a strong headwind for High Quality fixed income, which as measured by the iShares US Aggregate Bond ETF dropped -2.48% for the month. The U.S. 10-year Treasury bond yield ended the month at 4.69%, up significantly from March's close of 4.21%.



Source: Bloomberg

Source : https://www.zerohedge.com/markets/gold-flowers-amid-april-stagflation-showers-stocks-bonds-crypto-crushed

The Dow Jones Industrial Average dropped -5.00%, the S&P 500 fell -4.16%, and the small cap iShares Russell 2000 ETF dumped -7.09%. The international markets traded relatively better than the U.S. markets. The MSCI EAFE iShares Core International Developed Markets ETF Index declined -3.26%, and the MSCI Emerging Markets iShares Core ETF Index increased +0.10%.

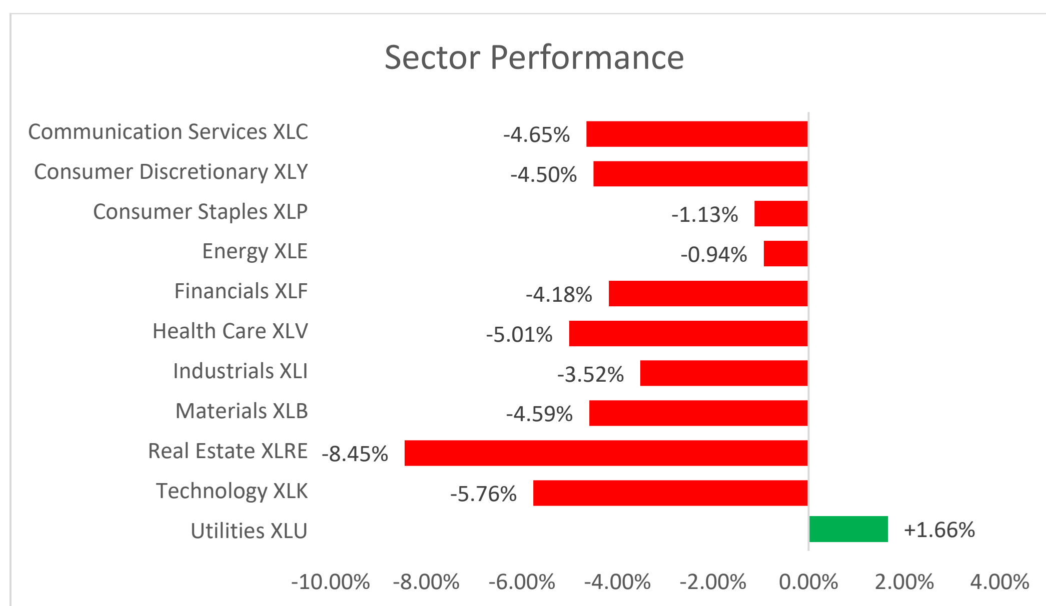
April's performance was generally red with only Utilities in the green.

The best performers were…

- Utilities: +1.66%
- Energy: -0.94%
- Consumer Staples: -1.13%

The worst performers were…

- Real Estate: -8.45%
- Technology: -5.76%
- Healthcare: -5.01%



Source: https://www.morningstar.com

Oil Report

The oil market held above the $80 level for the entire month, though prices peaked early in the month. The combination of inventory builds on "waning" demand combined with the Iran-Israel tit for tat not yet escalating into WWIII seemed to take some steam out of crude oil prices. The question; is this the end of the big rally, and prices will continue to rollover or is this the pause that refreshes on a charge to $100. It is too early to tell, likely the evolution of geopolitics and the state of the economy will end up being the deciding factor. The current NYMEX WTI Crude Oil futures settled at $81.93 posting a loss of over 1% from the prior month's close of $83.12 a barrel. The RBOB gasoline traded up during the month, but a couple of large selloffs resulted in price ending essentially where it started down 0% vs. March's close. A big driver of inflation is energy prices and judging by the roughly $1 jump in pump prices, there seems to be some bubbling inflationary pressures in the energy space. And we are not even in the historically strong driving season which is almost upon us and usually drives up gas prices until July 4th.

The Rest of the Data

The March ISM Manufacturing Index jumped to 50.3 from February's reading of 47.8. The ISM Services Index decreased to 51.4 in March, from February's print of 52.6. The prices paid component for Services moved back toward neutral levels and Manufacturing prices firmed at neutral levels. Any reading above 50 generally indicates improving conditions. Consumer confidence dropped meaningfully to 97.0 in April, which compares to yet another downwardly revised figure of 103.1 in March. A report showed that the consumer confidence downward revisions have shaved off almost 15 points. The unemployment rate declined to 3.8%, while the economy added another strong 303,000 jobs in March, again beating expectations of 214,000 jobs. The Consumer Price Index for All Urban Consumers (CPI-U) again increased +0.4% in March, on a seasonally adjusted basis. Over the last 12 months, the All-Items Index rate increased to +3.5% on a non-seasonally adjusted basis. The CPI ex Food and Energy held at 3.8% over the last year. So, the narrative is changing a bit, the economic data is softening, and inflationary pressures are turning up, and moving higher than the Fed target of 2%. However, employment reports remain good/strong. The market has now backed off expectations for a June rate cut or even September, and rate cut expectations, for 2024, are down to 1, in December, from 6 at the start of 2024. The early signs of stagflation, i.e. slow growth, and robust inflation, leaves one to wonder if the Fed has to shift to hold and hope. The Fed seems to have really painted itself into a corner of two bads. We will continue to monitor economic activity along with inflation reports.

Summary

Well, the happy go lucky markets got a bucket of cold water in their face this month. The bond market is used to it as it has not been nearly as positive this year as equities had. However, the equity markets haven't had this type of experience since October, which was the springboard for the massive 5-month rally we experienced. The crosscurrents in the market continue to get bigger. Financial conditions continue to ease, inflationary pressures continue to build, and the economic reports have been weakening. Everyone is looking to the Fed to cut rates, but that seems a lot dicer today than just a couple of months ago. Does the Fed risk letting the inflation genie fully out of the bottle, i.e. the 1970's or risk economic weakness. The lesser long-term evil is probably to let the economy rebalance and try not to let inflation get completely out of control. However, that is not likely how it will go, society has, sadly, generally given up on long-term thinking and will be focused on the short-term pain and want it to stop. So, the odds are the Fed will huff and puff and fold like a straw house and cut rates. That seems almost certain to spark an inflationary fire, which at some level will be helpful to equities, but likely leads to much greater pain, i.e. big rate hikes, ala the early 1980's. Not necessarily the greatest news, but probably the path that the Fed ends up taking. Maybe Fed head Powell will surprise us this time, but I wouldn't hold my breath given his track record. 😊

As always, the markets can be emotional, so we retain our focus on what we can control, which is the amount of equity risk that is taken in a clients' portfolio in concert with the clients' risk tolerance and long-term goals. The markets will always face different "worries", today it is inflation/war vs. growth and growing debt, tomorrow it will be something else. We have built our asset allocation models with dynamic features and quarterly rebalancing, both in fixed income and equities.

If you have specific questions about your portfolio or financial situation, we are here to help. Long-term financial planning is designed to deal with uncertainty like those we discussed above. Our portfolio management process is to design a prudent allocation across many asset classes. Equities are for long-term growth and several vehicles that we utilize offer defensive mechanisms to mitigate equity market declines.

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