ROAN CAPITAL PARTNERS
- JOHNSON CITY, TN -

Market Update

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This week in the markets...

This week has been a reality check for a stock market that has moved forward all year in spite of growing concerns about a list of significant issues. At the time of this writing the Dow and S&P have retreated about 3% over the last week and the Nasdaq has pulled-back 4%. These numbers are hardly earth-shattering given the extended growth that we've enjoyed so far this year, and still a long way from a real correction (-10% or more) but the velocity of the last weeks trading is not something that we can wave away flippantly. It also feels more concerning because it's the first real pull-back of the year. We'll quickly try to outline the current economic/global financial issues and close with an opinion and some reassurance.

The biggest concern for the market this week has been about the state of the economy, particularly the job market and the state of the American consumer. In his Wednesday statement, Fed Chairman Powell warned that the US job market was exhibiting some weakness (Goldman, 2024) Powell's warning was reinforced Friday mornings job numbers as only 114,000 jobs were added in July and the unemployment rate grew to 4.3%, the highest since October of 2021 (Cox, 2024). Compounding the concerns are mentions in earnings reports from companies in the last weeks that US consumers have pulled back from restaurants and retailers (Goldman, 2024).

Obviously, the economic changes and concerns are generated by the Fed's tightening policies enacted to defeat inflation. Markets have expected the Fed to shift policy and begin to lower the Fed Funds Rate in September since mid-year, and Chair Powell all but confirmed a policy shift in his Wednesday remarks. However, the markets are now looking for reassurance that the Fed hasn't waited too long and that the economy may now move into recession (Goldman, 2024). The report from the Eurozone that inflation was rising in Europe also generated worries for equities around the world with the euro area annual inflation reading in July back up to 2.6% from 2.5% in June (Cignari, 2024). Remember that the European Central Bank began to reduce interest rates in June, and since then the rates of inflation have fluctuated between 2.6% and 2.5% on a monthly basis. The question now is, will global higher inflation affect the Fed's ability to pivot to a stimulative path in time? At least the question that the markets are fretting about, will the Fed pivot (finally) in September?

	08/05/2023	1/1/2024	08/05/2024	12 MO ROR	YTD ROR
DOW	35,281.0086	37,566.22	39,737	16.47%	5.43%
S&P 500	4,513.7599	4,745.20	5,347	26.78%	12.09%
NASDAQ	13,973.0135	14,873.70	16,776	34.91%	11.76%

U.S. Treasury Bond Yields

US1MO	5.29%
US3MO	5.08
US6MO	4.73
US1Y	4.20
US3Y	3.60
US5Y	3.53
US10Y	3.73
US30Y	4.06

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Many people, including some here at our firm, believe that the US market is waiting for a pivot and that inflation is still a concern, however, there's one other issue (at least on the financial front) that may not be as common knowledge. Thursday night the Japanese stock market pulled by nearly 6% in one trading day and really began the sell-off that ran around the rest of the world as markets opened (He, 2024). The market rout was a reaction to a pivot in Japanese monetary policy (opposite of the one hoped for in the US), as the Bank of Japan (BOJ) moved to tighten policy to the highest levels since 2008 in an effort to tame inflation:

"The BOJ made a hawkish shift after its surprising 15 (basis point) rate hike," said Ken Cheung, director of foreign exchange strategy at Mizuho Securities. "Importantly, the BOJ flagged the inflation upside risks ... and left the door open for further rate hikes. " (He, 2024)

The policy shift also affected currency markets as the Yen gained ground against the dollar pushing the Yen down 0.3% to 148.9 yen/dollar. The reality that the BOJ may continue to move to fight inflation may create more volatility that affects global markets.

Bruce Kirk, chief Japan equity strategist at Goldman Sachs explained that the (Japanese market) rally over the past two years was powered by three factors, namely, yen weakness benefiting blue-chip exporters and banks, expectations of monetary policy normalization, and corporate governance reform. Kirk said that the Japanese market rally had reached a "transitional phase". Kirk said. "We don't think the [rally] story is broken, but the narrative is definitely evolving, and that's likely to be accompanied by the continued volatility and this quite aggressive sector rotation that we're seeing. The rules of the game have [now] definitely changed, particularly around rates and FX (currency exchange rates)," Kirk said, adding investors are now reassessing sector positioning in the market (Jie, 2024).

What does this mean for me?

I mentioned last week that August will likely give us some opportunity to see the volatility that we've missed so far this year. My guess is that we will continue to see volatility as we get nearer the Fed decision and the US election. Usually, elections don't carry the weight of dramatic economic change regardless of candidate or party, however, this cycle we expect some changes if Trump wins that will change the paradigm for economies and markets. We will begin account reviews and rebalances next week and you will see trades reflecting some strategy changes executed. I think that the damage done in the last couple of days will likely be somewhat relieved by continued tech earnings and other AI related companies reporting next week, and it is our opinion that corporate stock buy-back campaigns reignite as earnings fade. This week has been a tough one, but as I said we're still a long way from a correction and the weekend will likely serve to cool passions.

I didn't cover elections or geopolitics in the letter. We'll likely have more to talk about next week on those fronts, so look for another letter mid-week.

Sources:

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