MARKET REVIEW & OUTLOOK

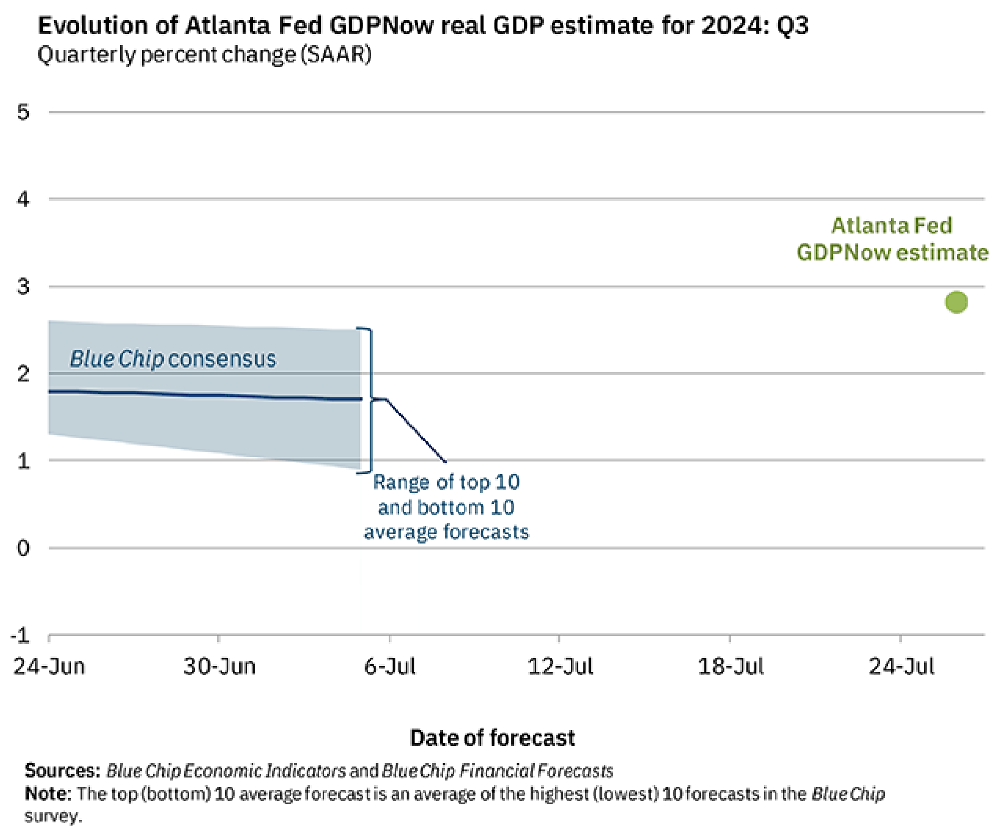
JULY 2024

KEY TAKEAWAYS

- The equity markets had a rocket fueled rally the first 2 weeks, with more record highs, but then hit some strong turbulence before a big rally the last day and a half.
- The U.S. 10-year Treasury Yields had a large jump the first day of the month and then had a steady decline, closing at the lows of the month, near the mid-March lows.
- Crude oil held above $80 most of the month before a swoon to around $75 ending with a rally on more geopolitical risks related to Israel and Iran/Iranian-proxies.

The U.S. Economy

The first look at 2nd quarter GDP was a barn burner at 2.8%, well above the 2.0% expectation. Core PCE, the imbedded inflation measure, fell to 2.9% down from 3.7% last quarter, but higher than the 2.7% expectation. The 3rd quarter estimates for GDP from GDPNow is currently a repeat of 2nd quarter at around 2.8% with the Blue-Chip consensus forecast just under 2%, as shown in the chart below. Economic activity strengthened, and the PCE deflator fell, but still held north of the sweet spot of "2%" inflation. So, growth is picking up and inflation is still working lower, seems to be just right. However, the Fed seems intent on cutting rates sooner or later.



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

Stocks and Bonds

The U.S. 10-year Treasury yield started with a jump of over 0.10% to start the month, near 4.5%, but that turned out to be a one hit wonder. Yields then steadily fell with some noise around 4.2%, but decisively broke that level to finish at the lows of the month. The Fed meeting ended today and was as predictable as could be without a rate cut. They may be thinking about rate cuts soon, which the bond market seemed to take as potentially meaning recession or that inflation will continue meaningfully lower. The market is now pricing in a full rate cut for September and maybe a couple of more before year end. The drop in yields provided a solid tailwind for High Quality fixed income, which as measured by the iShares US Aggregate Bond ETF jumped +2.35% for the month. The U.S. 10-year Treasury bond yield ended the month at 4.11%, down from June's close of 4.34%.

The Dow Jones Industrial Average jumped +4.41%, the S&P 500 rose +1.13%, and the small cap iShares Russell 2000 ETF soared +10.11%. The international markets traded like the U.S. markets. The MSCI EAFE iShares Core International Developed Markets ETF Index gained +3.32%, and the MSCI Emerging Markets iShares Core ETF Index increased +0.62%.

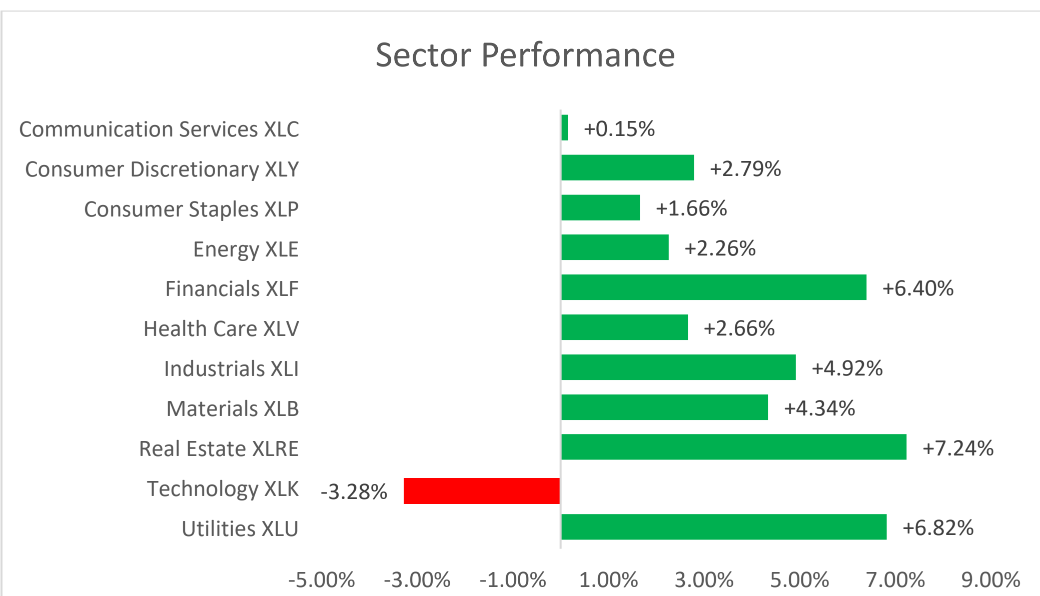
July's performance was generally green and very green, except for Technology.

The best performers were…

- Real Estate: +7.24%
- Utilities: +6.82%
- Financials +6.40%

The worst performers were…

- Technology: -3.28%
- Communication Services: +0.15%
- Consumer Staples: +1.66%



Source: https://www.morningstar.com

Oil Report

Crude Oil traded around $82.50 for the first 3 weeks and then slumped on concerns about China demand and dipped below $75 on July 30th. Then Israel killed high level Iranian-proxy leaders in Lebanon, Syria and Iran and the worries of a significant escalation spiked oil prices to finish the month. The saber rattling was coming from many sides and spooked the oil markets. Though there is some skepticism as to how hard the retaliation will be, as so far, the retaliation efforts have been rather meager. Oil supplies continue to be drawn down, though mostly offset by concerns the economy, globally, continues to slow. The current NYMEX WTI Crude Oil futures settled at $77.91 posting a loss of over 4% from the prior month's close of $81.54 a barrel. RBOB gasoline followed Crude for the month and declined over 2% vs. June's close. The markets were really concerned about hurricane season when one of the largest storms for a June occurred, but the storm front was very quiet in July. Though the heart of hurricane season is still in front of us, so we will have to keep an eye on the weather.

The Rest of the Data

The June ISM Manufacturing Index slipped to 48.5 from May's reading of 48.7, remaining below 50. The ISM Services Index reversed the May jump and slumped to 48.8 in June, from May's print of 53.8. Any reading below 50 generally indicates deteriorating conditions, whereas a reading above 50 generally indicates improving conditions. The prices paid component for Manufacturing dropped to normal and Services prices further eased off elevated levels. Consumer confidence increased to 100.3 in July, which compares to a downwardly revised 97.8 in June. The unemployment rate increased to 4.1%, while the economy added a solid 206,000 jobs in June, beating expectations of 190,000 jobs. The Consumer Price Index for All Urban Consumers (CPI-U) was down -0.1% in June, on a seasonally adjusted basis. Over the last 12 months, the All-Items Index rate decreased to +3.0% on a non-seasonally adjusted basis. The CPI ex Food and Energy again decreased to 3.3% over the last year. So, the story has changed a little; the economic data is showing signs of firming, and inflation, while still above the Fed target of 2%, has been showing signs of moderating. The market is starting to price in reductions of the current "restrictive" Fed policy, pricing in September rate cut, and increasing rate cut expectations, for 2024, with one or maybe two rates cut in November and December. The Fed is suggesting that the economy is ok, that employment doesn't need any more cooling and that inflation is showing signs of improving. We will continue to monitor economic activity along with inflation reports.

Summary

Have we moved into the Goldilocks scenario, with a soft landing? With Interest rates returning to "normal" and economic growth continuing? Does this set us up for a year end rally and happy times? It is hard to say, but the signs are starting to emerge. The sector performance showed that interest rate sensitive sectors did really well. Then there is the eye-popping rally in the US Small Cap markets, which are widely viewed as highly sensitive to the economic cycle. Maybe all of us cynics will be proven wrong, and the Fed will engineer a mid-cycle slowdown that results in another leg higher for the economy and the markets. The Tech sector was looking on the ropes as recently as the afterhours price action yesterday, on the back of Microsoft's earnings report, but like a cat with 9 lives; the Microsoft conference call set the markets on fire and Tech rallied over 4% by today's close.

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 interest rates, 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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