Monday November 6, 2023

SUMMARY-

I. *Stocks post best week of the year after a broad-based rally.*

II. *Declining bond yields among biggest stock catalysts.*

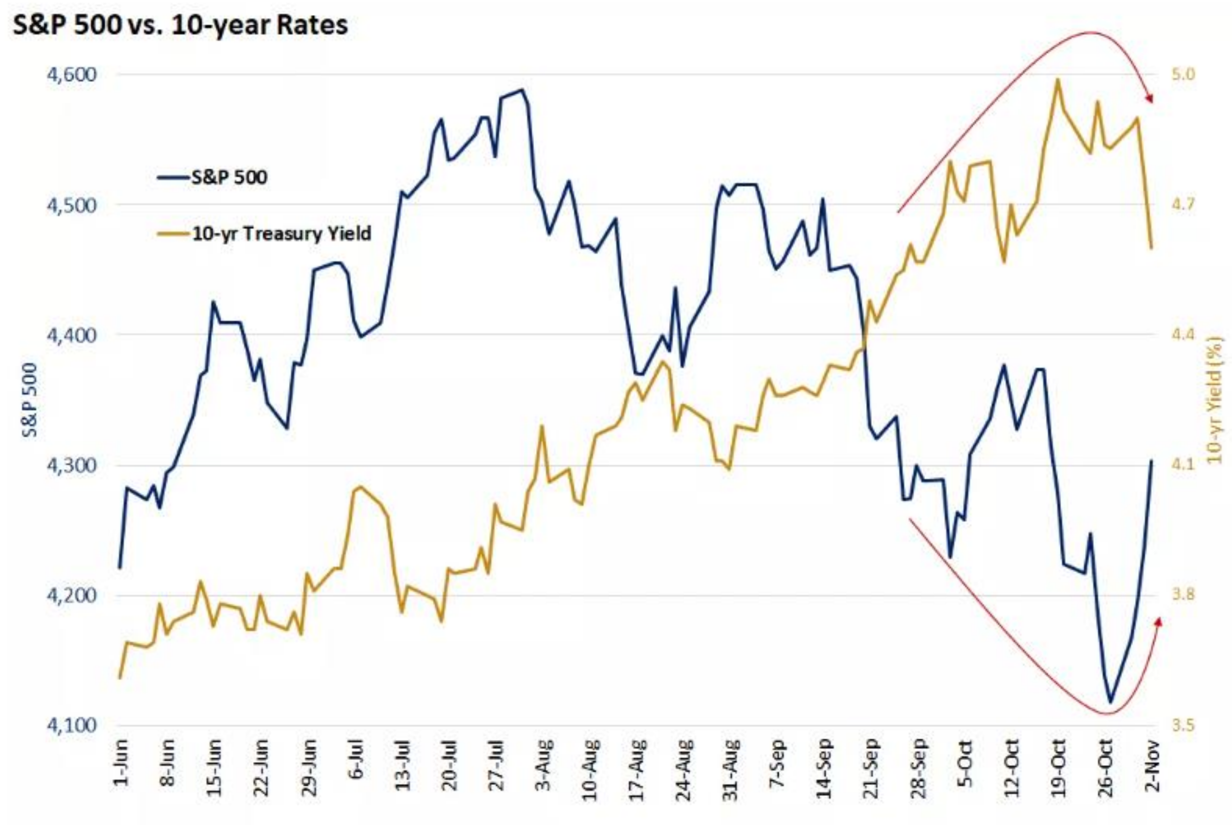
III. *Seasonally strong period for equities could propel rally.*

IV. *Markets mostly ignore global turmoil and focus on Fed.*

Good morning:

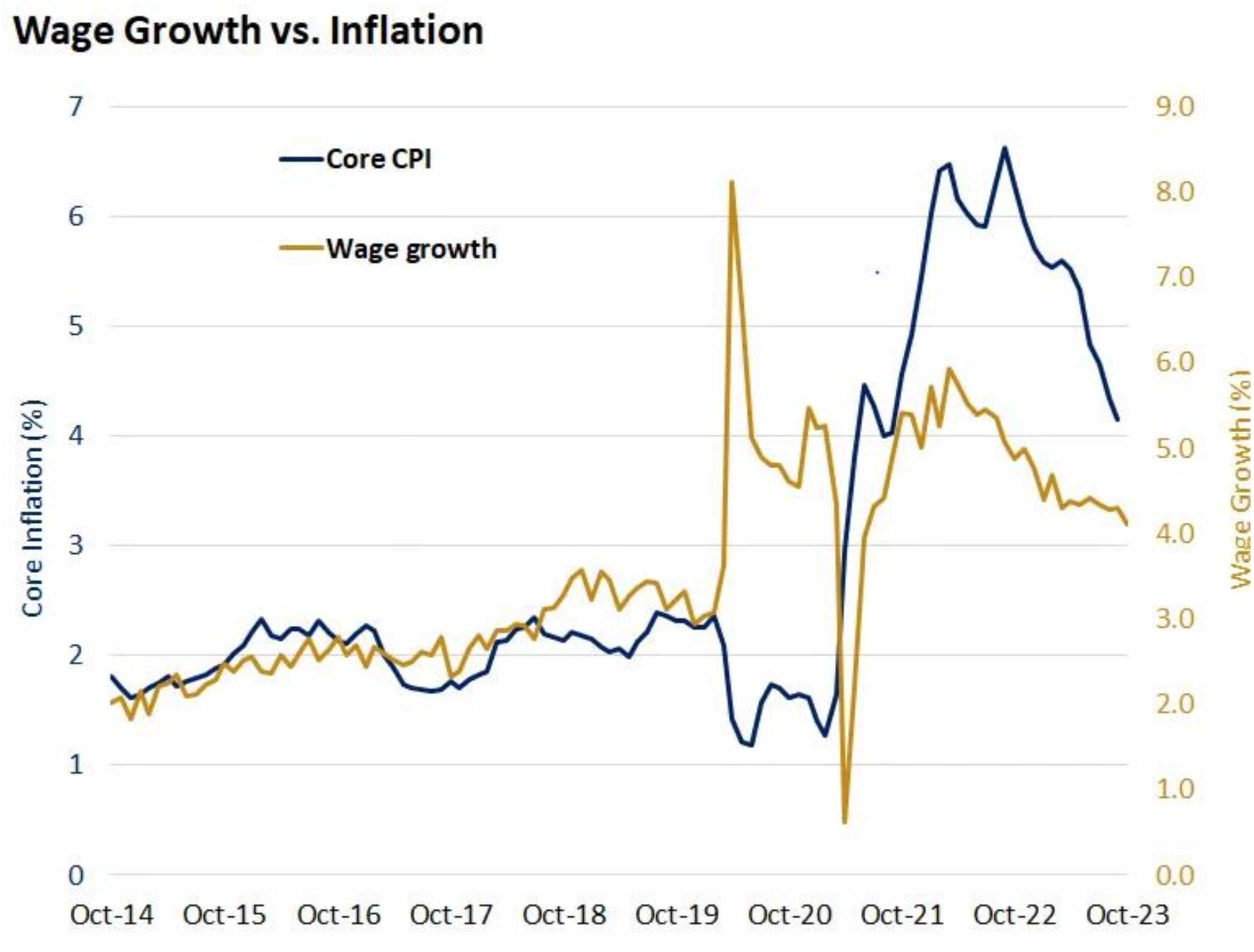
From the rather oversold condition that we mentioned in last Monday's Outlook, stocks staged a broad-based rally to post their best week of the year. Off correction level lows to start the week, major averages gained between 5 and nearly 7% creating new hope that equity returns may finally stage a wider sustainable rally into year end. We remain cautiously optimistic while realizing that it may take more than a single week to alleviate investors' deeper economic and earnings concerns.

Among last week's biggest equity catalysts was the rally in Treasury bonds. After brushing the 5% level on the all-important 10-year Treasury, its yield declined to below 4.6% by week's end. Part of this bond rally came after the Fed opted to remain on hold rather than hiking rates once again this year. Markets also welcomed their accompanying comments that suggested policy makers are not convinced that more rate hikes are preordained.



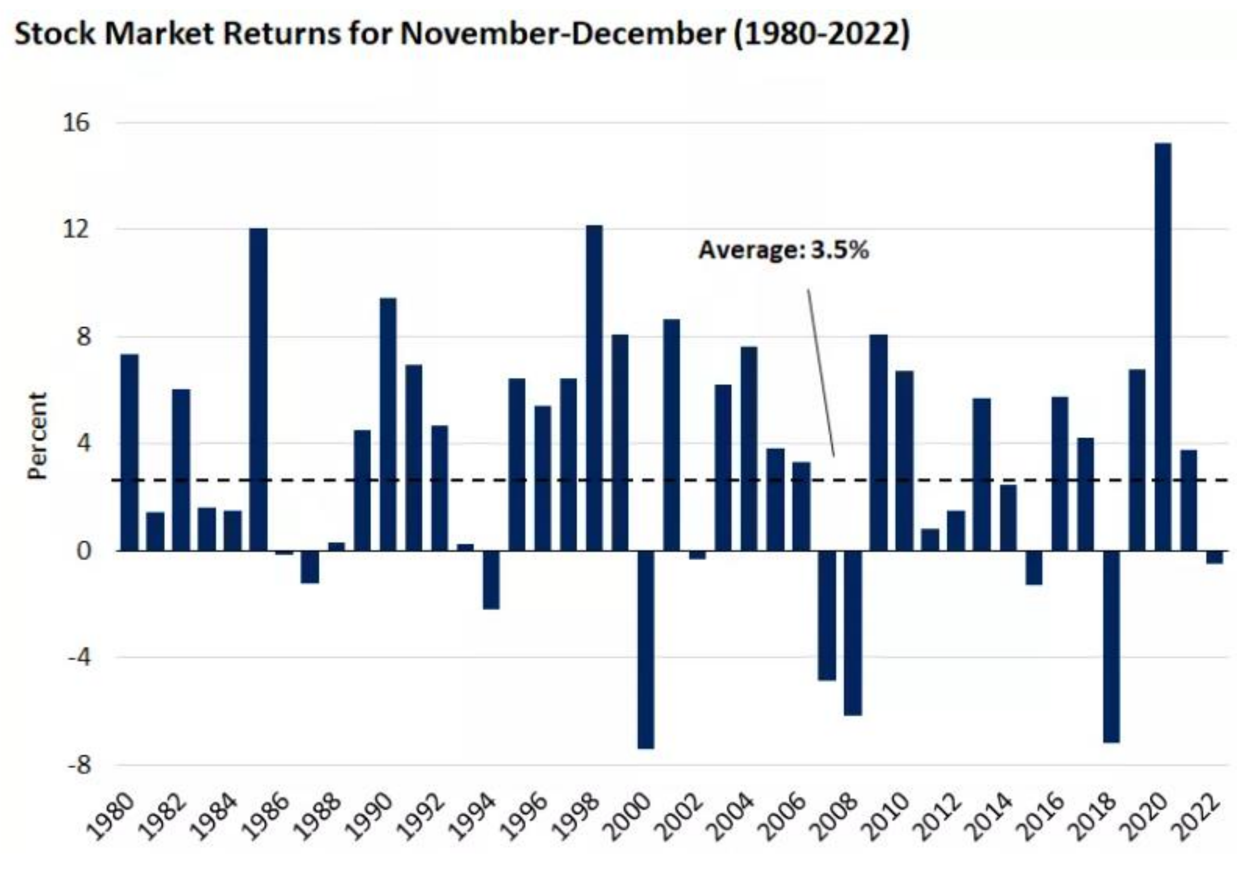
Source: FactSet. S&P 500 index and U.S. 10-year Treasury yield.

It seems clear that the higher borrowing costs orchestrated by the Fed this year have had a dampening effect on inflation, enabling the Fed to remain in pause mode. Inflation seems to be continuing on a declining path after a new labor report that could be interpreted as Goldilocks in its near-term effect. The October jobs report showed the economy added 150,000 jobs last month. It's positive to see that hiring gains continue, while at the same time it's clear that some softness is emerging in the labor market, as October's payroll gains were half that of September and down from the 216,000 average over the last six months. The coincident trends of ongoing job gains and moderating wage growth is the zone that the market will likely cheer as we advance, as that combination would be consistent with hopes for a soft landing in the economy. Again, moderating wage growth appears to have a direct impact on easing inflation levels.



Source: FactSet. U.S. Core CPI and wage growth.

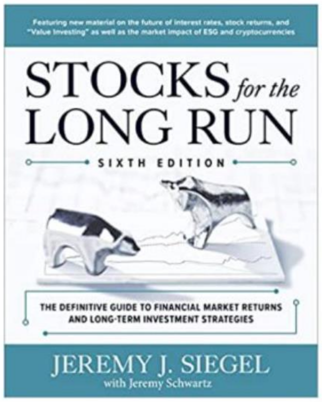
With the Fed all but announcing a conclusion to their tightening cycle, and inflation still in decline, the historically positive period of November-December may be poised to punctuate the end of 2023 with a continued rally to higher levels. After a sideways-to-somewhat-negative year for much of the stock market (apart from the Magnificent Seven tech stocks), a broad-base rally into year-end could catch a lot of investors with sidelined cash unprepared. If history is a guide, the calendar could be tilted in investors' favor, as stocks have typically enjoyed strong returns in the November-December time frame. Since 1980, the stock market has delivered a gain in the final two months of the year 79% of the time.

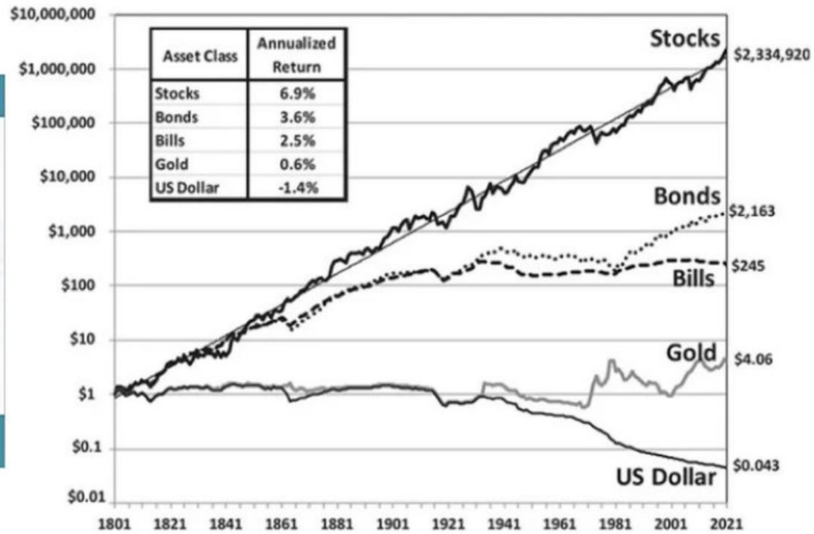


Source: Morningstar Direct

With a resilient consumer backed by a strong labor market, it is likely that forthcoming economic growth and earnings will remain intact for the near term. The often cited but less seldom seen "soft-landing" may be materializing. The Fed's own "Dot Plot" projection of future interest rate moves predicts no more hikes and 0.50% of cuts in 2024 after an extended pause at current levels. We will be watching closely for further lagging effects of Fed tightening while we monitor ongoing corporate earnings forecasts. If interest rates can manage to keep from resurging higher, we believe odds favor a strengthening stock market during this seasonably positive period for equities.

Perhaps surprisingly to some investors, the market has largely ignored much of the geopolitical turmoil unfolding after the October 7th Israel attacks, the subsequent response, and the saber-rattling rhetoric. The current assessment that an expanding Middle East war leading to a disruption in oil production is unlikely has led to a decline in petroleum prices in the past four weeks. While such exogenous events have taken a backseat to interest rates, the Fed, and corporate earnings results, it is important to remember we live in a volatile world and markets can react abruptly to unforeseen circumstances that may develop suddenly. Similarly, 2024 is an election year which could also result in enhanced market volatility as some investors attempt to handicap various political outcomes. The important thing to remember is the 220+ year history of asset class superiority of equities, despite regular corrections and bear markets.





Source: Stocks for the Long Run, Dr. Jeremy Siegel

An important key to success for all investors is not to let short-term events or market results alter their understanding of asset class performance over the long term. Patience is generally rewarded versus successful market timing which often proves elusive.

Have a great week!

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