Monday, August 19, 2024

SUMMARY-

I. Market rebound posts best week for stocks in 2024.

II. Inflation data continues to ease, supporting rate cuts.

III. Fears of imminent recession now appear overblown.

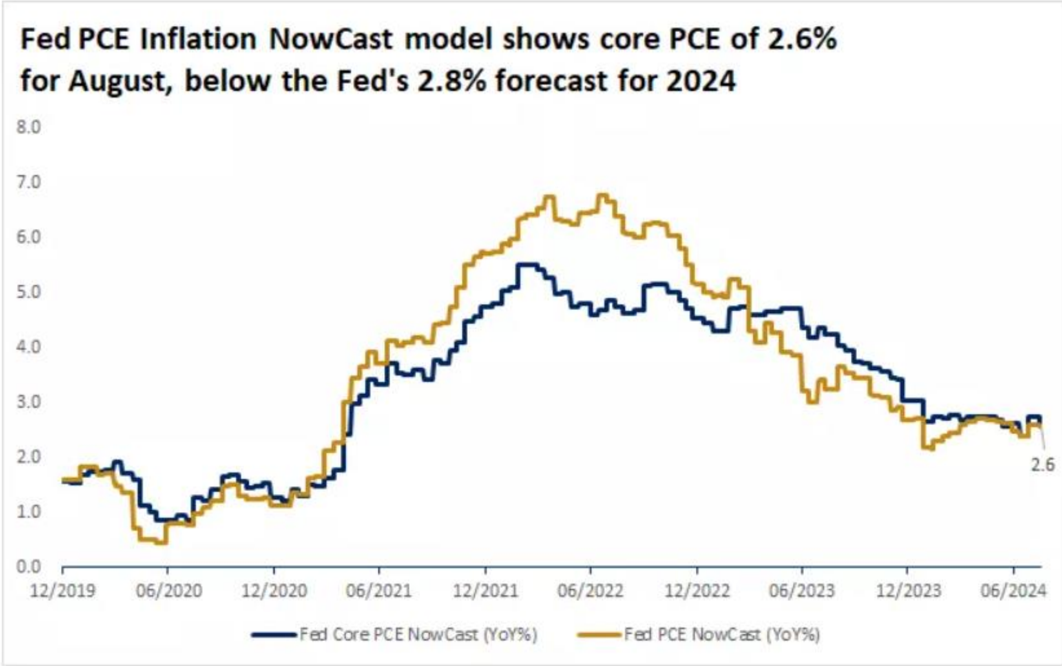
IV. Volatility could continue as numerous uncertainties remain.

Good morning:

After the sharp pullback to start this month, the equity rebound accelerated last week thanks to softer inflation figures and resilient economic data. Leading major stock averages was the NASDAQ that added 5.3%, while the S&P 500 gained 3.9% and the Dow added 2.9% making it the best week of the year for equities. Since the market's August 5th lows, the S&P 500 is up over 6.5%, and the tech-heavy NASDAQ is up over 8.0%. The confirmation of inflation's continued easing was a major contributor to the ongoing equity comeback.

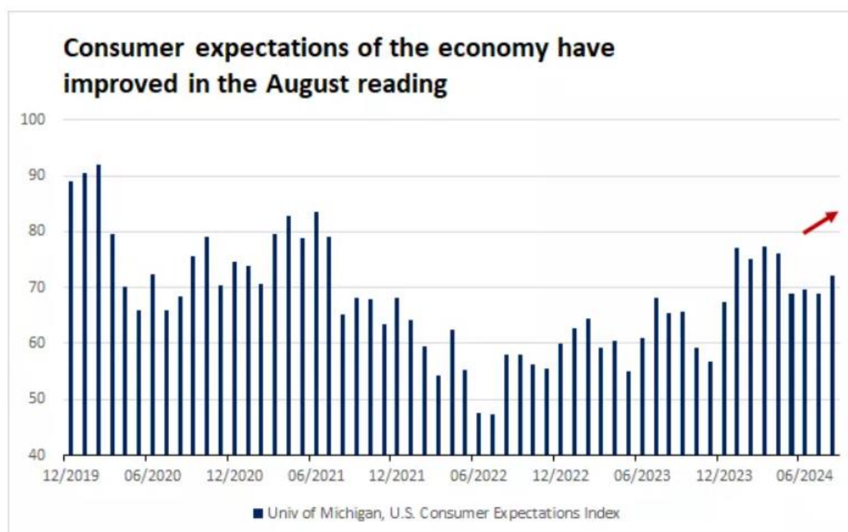
Both PPI and CPI inflation came in below expectations for July, with headline CPI inflation now at its lowest level of the year. Headline PPI inflation came in at 2.2% annually, below forecasts of 2.3%, while headline CPI inflation came in at 2.9%, also below expectations of 3.0%. Prices declined across several categories, including food items (cereals, bakery), apparel, new and used vehicles,

and even airline fares. However, inflation remained elevated in the areas of shelter and rent, as well as motor vehicle insurance. While the shelter components of CPI have been slow to move lower, there is a chance they will continue to play some catch-up with the softer real-time data in the months ahead. Similarly, as we are sure you noticed, pricing on property and casualty insurance has moved sharply higher over the past year but is not likely to continue rising at this pace. As this data moves us another step closer to the Fed's 2.0% target for PCE (personal consumption expenditure) inflation, their current "NowCast" model sees PCE falling to 2.6% in July and is tracking ahead of their year-end forecast.



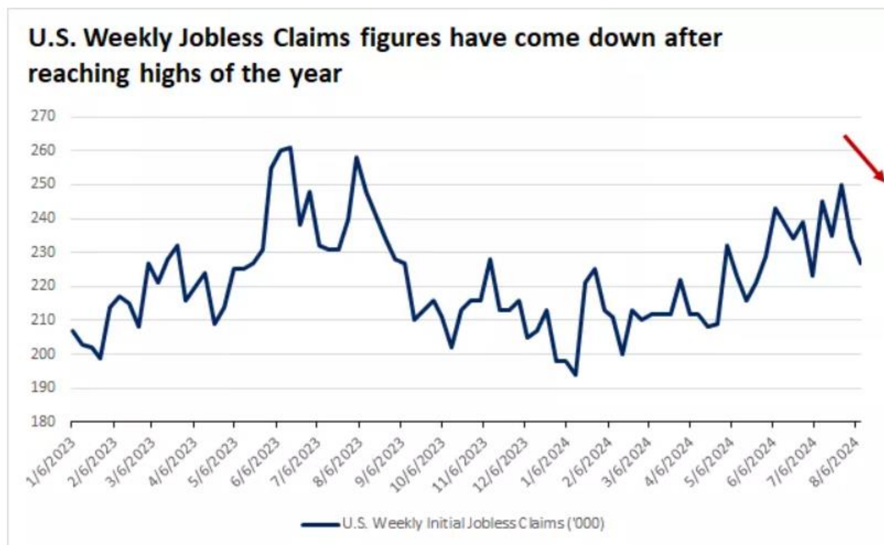
Source: Bloomberg

A major catalyst to this month's sharp selloff was the sudden fear of an impending recession after a weaker than expected jobs report for last month. However, since then, markets have seen a string of better economic data providing some optimism that while the economy may be cooling, a recession is not imminent. One of the most important of these datapoints was the retail-sales data released last week which pointed to a U.S. consumer that was still healthy and spending. The monthly retail-sales growth came in at 1%, well above the forecasts for 0.4% and last month's -0.2%. Spending was broad-based, with 11 of the 13 major categories showing positive gains, led by a strong recovery in auto sales. This data was accompanied later in the week by a strong University of Michigan consumer expectations figure, which came in at 72.1, versus forecasts of 68.5. Both sets of data point to a U.S. consumer that is still spending and remains relatively optimistic about the future.



Source: Bloomberg

In a bit of a contradiction to last month's weaker jobs data, the real-time weekly U.S. initial jobless claims data (tracking those that have filed for unemployment benefits) reported some good news. After peaking at 250,000 two weeks ago, jobless claims have steadily declined now to 227,000. With "stable prices" and "maximum employment" comprising the Federal Reserve's dual mandate, inflation and labor statistics will undoubtedly drive Fed policy as they embark on the much-anticipated rate easing cycle. Futures markets are nearly unanimous that the initial rate cut will come at the next FOMC meeting on September 18th. Some have suggested that a larger cut of 0.50% may be warranted, but after the recent better economic data, we expect the Fed to stay measured (and not signal any panic) with a 0.25% cut.



Source: Bloomberg

We are encouraged by the market's healthy rebound and felt the selloff was not fully justified. However, we remain cautiously optimistic as markets navigate through the coming months. We also expect that we could continue to experience episodes of heightened volatility (in both directions). As often cited, markets generally hate uncertainty, although a healthy market is one that "climbs a wall of worry."

The current laundry list of potential anxiety-inducing market factors includes:

- Economy's growth trajectory
- Inflation rate & Fed rate cuts
- Corporate earnings growth and guidance
- Domestic political developments – election year
- Geopolitical developments – Iran, Russia, China

In addition to some remaining earnings reports this week, attention will likely focus on the U.S. Federal Reserve's annual three-day economic policy symposium in Jackson Hole, Wyoming. Chairman Powell is scheduled to deliver his comments on Friday, August 23rd. In the past, the Fed has used this meeting to signal major policy changes which could serve to add clarity to market strategists trying to project interest rate and market conditions through year end. Once again, investors should be prepared for elevated market volatility and potential knee-jerk reactions to anything said by Jerome Powell in Jackson Hole.

Have a great week!

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