Monday September 25, 2023

SUMMARY-

I. *The Fed delivers a hawkish pause.*

II. *Projected 2024 rate cuts were lessened.*

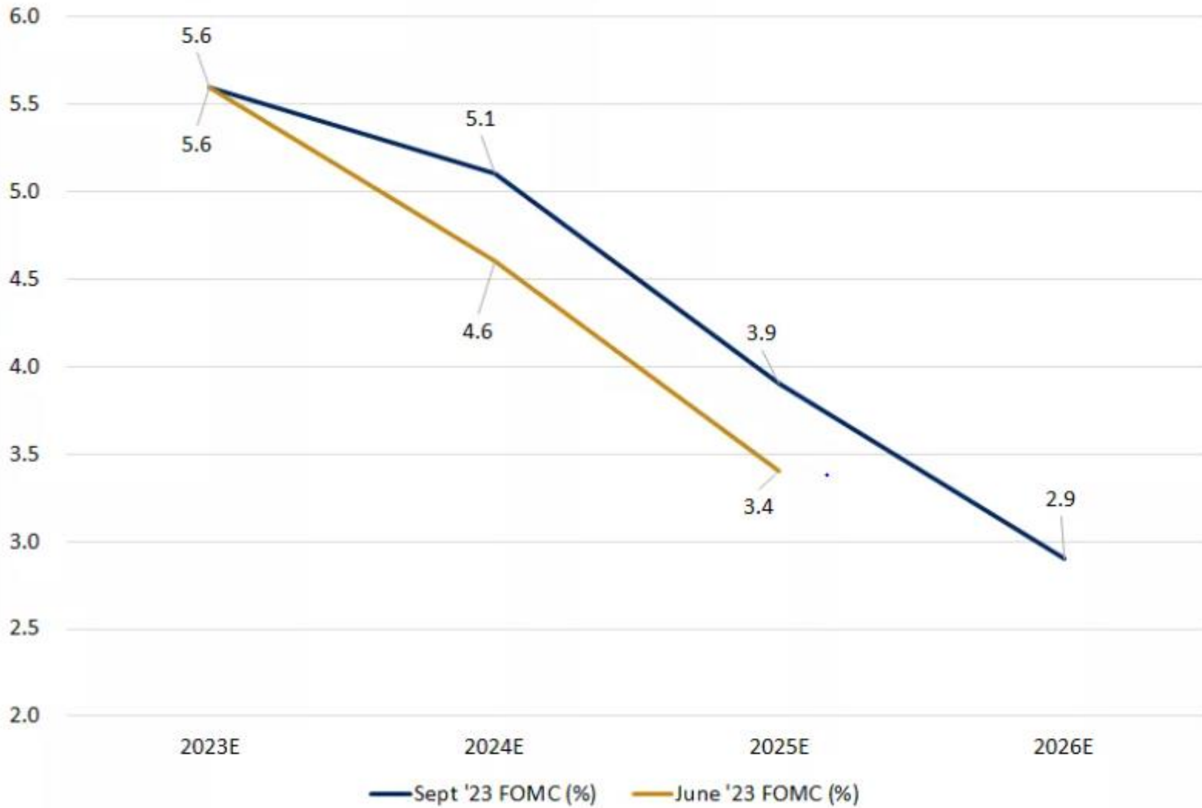
III. *Stocks and bonds sell off in response.*

IV. *Broader equity markets have growing value appeal.*

Good morning:

Last week's pivotal market event was the Fed's September FOMC meeting at which Chairman Powell maintained his hawkish rhetoric sending stocks lower in response. As expected, the Fed left interest rates unchanged, but accompanied the decision with a message that was clear: The Fed plans to continue to keep rates elevated until inflation moves more decidedly towards their 2.0% target. In fact, they clearly left open the possibility of another rate hike at their next meeting in November. The Fed's new set of projections also reduced the number of potential rate cuts in 2024 from a total of 1.0% to 0.5%, implying that rates may very well stay higher for longer.

However, the Fed's "Dot Plot" still projects significant rate declines in 2025-2026. This assumes that inflation has been tamed and returning short-term rates to lower levels will not reignite higher prices.

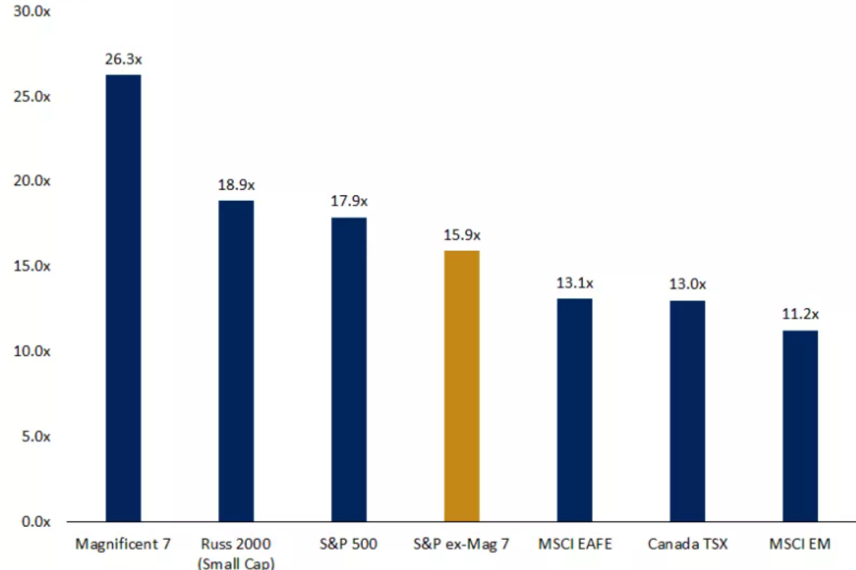


Source: FOMC, September 2023.

Markets were quick to react as both stocks and bonds sold off. Both 2-year and 10-year treasury bond yields reached new highs for this rate hiking cycle, although the yield curve still remains steeply inverted. Equity averages declined across the board, led in their retreat by the NASDAQ that fell 3.6% by week's end. Stocks are starting the last week of both the month and the third quarter today on firmer footing as bargain hunting may be bringing some buyers into many parts of the market that have seen price declines in recent weeks.

On the near-term horizon, investors will have a steady diet of updated labor statistics, inflation data, and consumer sentiment readings to go with the start of Q3 earnings season. Together, these reports will likely reveal whether inflation's trajectory is heading down to the Fed's target rate on its own, or if more hikes are required. We will also be watching these developments closely to determine how to best position our clients' portfolios for the coming months and years.

In the remaining quarter of 2023, as well as into 2024, we believe there could be a continued broadening out of U.S. equity sector performance. The largest seven mega-cap technology companies in the U.S. (often called the Magnificent 7) have generated much of the year's market gains and have been responsible for the majority of the move higher in several major averages. However, the current valuations of many other equity averages are far less expensive and may therefore continue to attract newfound interest.



We consider it far more prudent and sensible to invest in higher quality companies, particularly those that pay dividends, with sound long-term business fundamentals that trade at lower valuations than chasing the current hot sector that may be overvalued and experience far greater risk and volatility. Of course, diversification cannot protect against loss, but it often can reduce the overall degree of fluctuations in a balanced portfolio.

Have a great week!

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