Tuesday, February 20, 2024

SUMMARY-

I. January inflation data surprises by ticking higher.

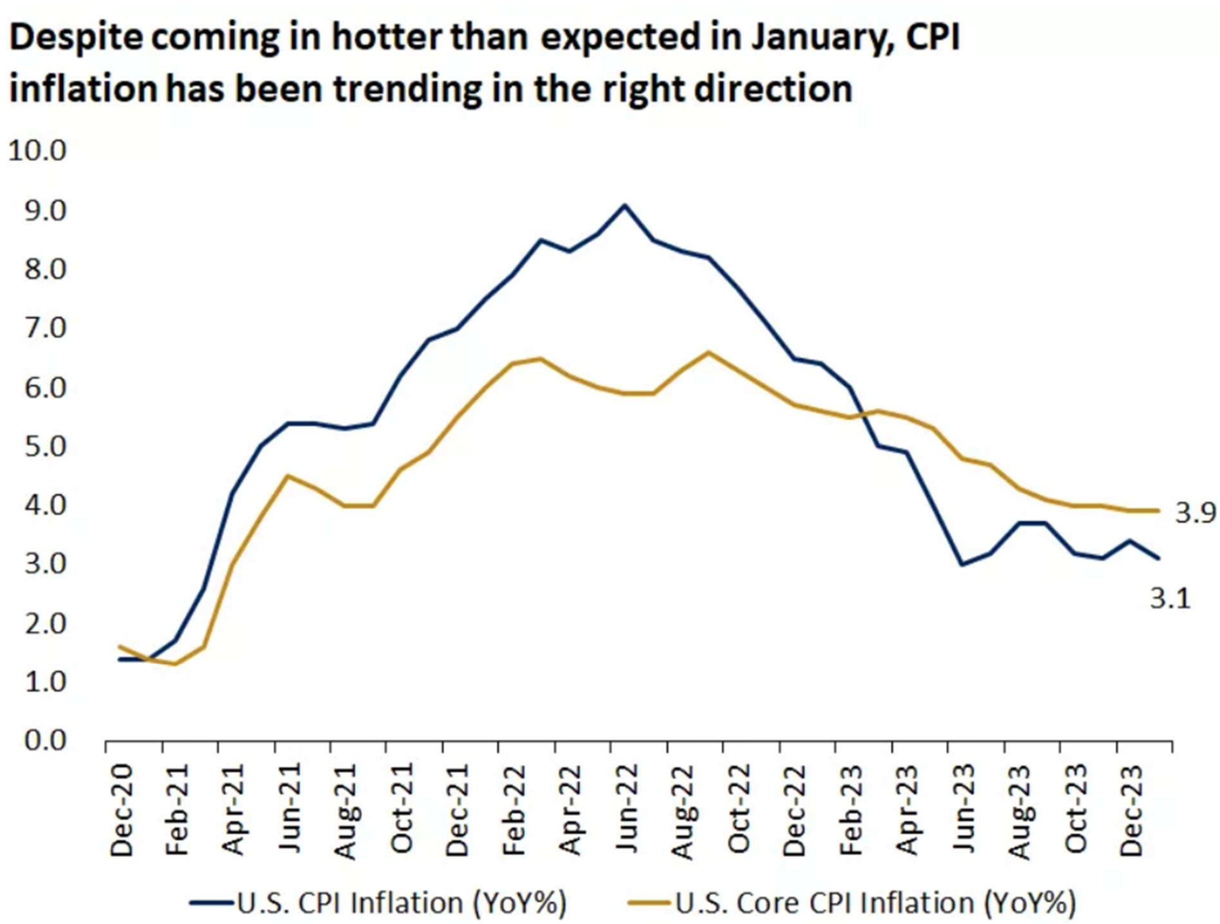
II. Leading NASDAQ tech stocks pull back while others gain.

III. Housing and shelter inflation remains sticky but data lags.

IV. Additional economic and Fed notes this week could set tone.

Good morning:

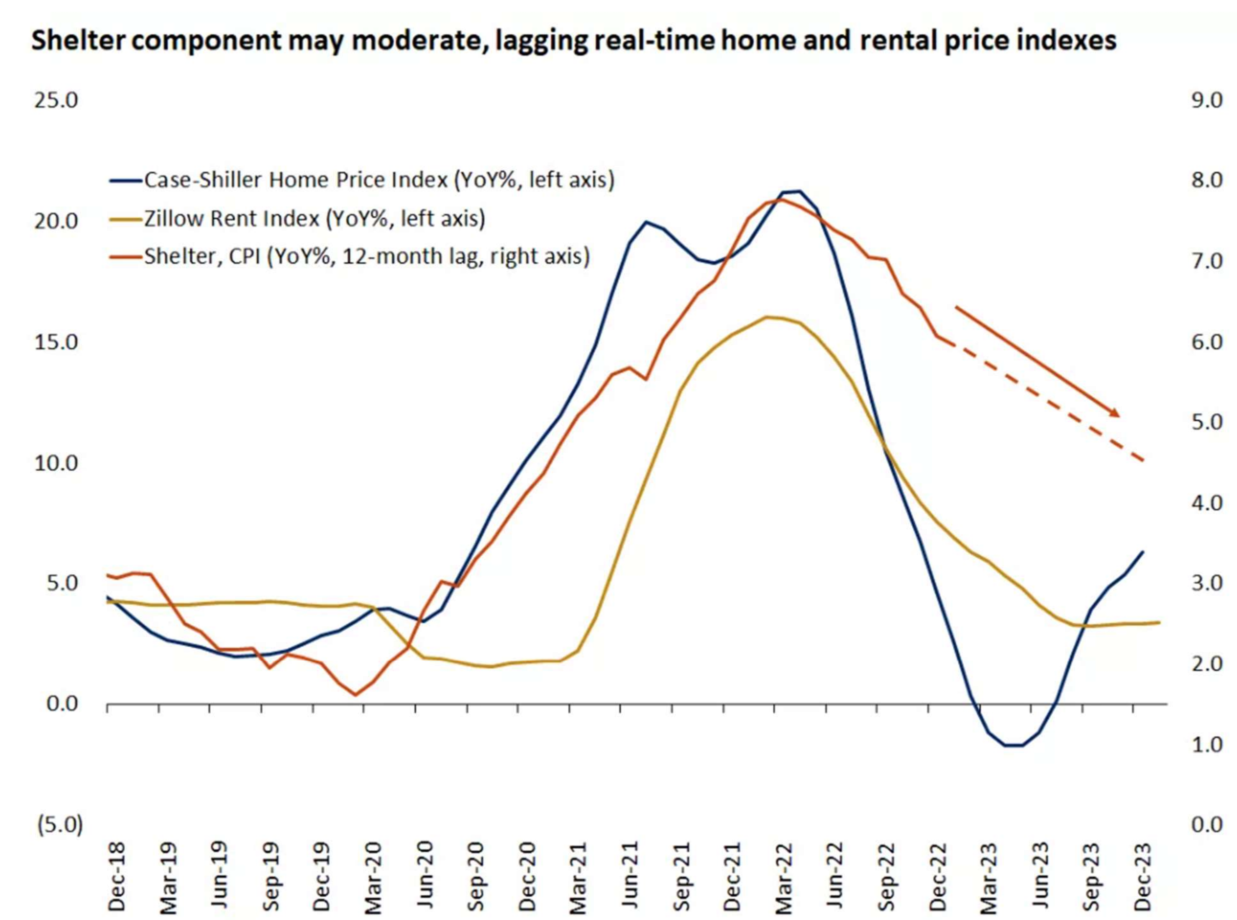
As we cautioned in our last *Monday Outlook*, markets were likely to take their cues last week from several key inflation reports for January, and after the recent runup, investors should be prepared for heightened volatility. First among these reports was the Consumer Price Index (CPI) data for January which came in at 3.1% year over year, above the 2.9% expectation, but still lower than December's 3.4% reading. Core inflation (which excludes food and energy prices) remained at 3.9%, also higher than the 3.7% expected rate. The realization that this will almost surely mean that the Fed will be on hold until the summer sent many stocks lower. Leading the selloff was some of the recent highflyers in the NASDAQ which gave back -1.31% on the week. The disappointment was tempered, however, since the overall trend for inflation is still clearly downward. The last mile in this effort to bring inflation down to the Fed's 2.0% target may still be achievable, just not likely in a straight line apparently.



Source: Bloomberg.

Similarly, the Produce Price Index (PPI) which measures the prices paid for goods and services at the wholesale level also came in hotter than expected. January's reading clocked in at 0.9% year over year versus a forecast of 0.6%. Core PPI was 2.0%, above the 1.6% expectation and December's 1.8% reading. However, PPI inflation has already fallen below the 2.0% target rate, down significantly from its highs of nearly 12% in 2022. Economists have noted that the Fed tends to put more weight on the CPI rate since it directly reflects prices paid by consumers and consumption accounts for nearly 2/3 of our GDP.

It is noteworthy to point out that within the CPI calculation, shelter and rent accounts for about 1/3 of the basket of prices tracked. This component is still quite high at 6.0% annually, again above expectations and not declining as fast as many other things. This is due to the tendency for both shelter and rent data to lag what is currently playing out in housing and rental markets across the country. Real-time data has some predicting these components will cool in the months ahead, enabling overall CPI to continue its descent and allowing the Fed to start their rate cuts, perhaps as early as June.



Source: FactSet.

While the large-cap tech stocks took a breather last week, some of the stock market's lagging areas managed to post gains. Leading the gainers higher were several international equity averages, as well as the small caps in the Russell 2000 Index, each of which added 1 to more than 2% for the week. This is a healthy sign for the market to see a pause in some recent favorites while participation broadens out. We believe this trend may gain traction as the year unfolds.

As we start this holiday-shortened trading week, the market will again have a few key economic reports to add to the developing story of 2024. Initial jobless claims and existing home sales data will accompany the release of the minutes from January's FOMC Fed meeting. Many will try to glean additional insight as to exactly what the Fed may do and when from this new information. We are also still in earnings season, so any mega cap firm's results has the potential to cause a bullish or bearish reaction in the broader market if the stock was widely owned and well represented in large index funds.

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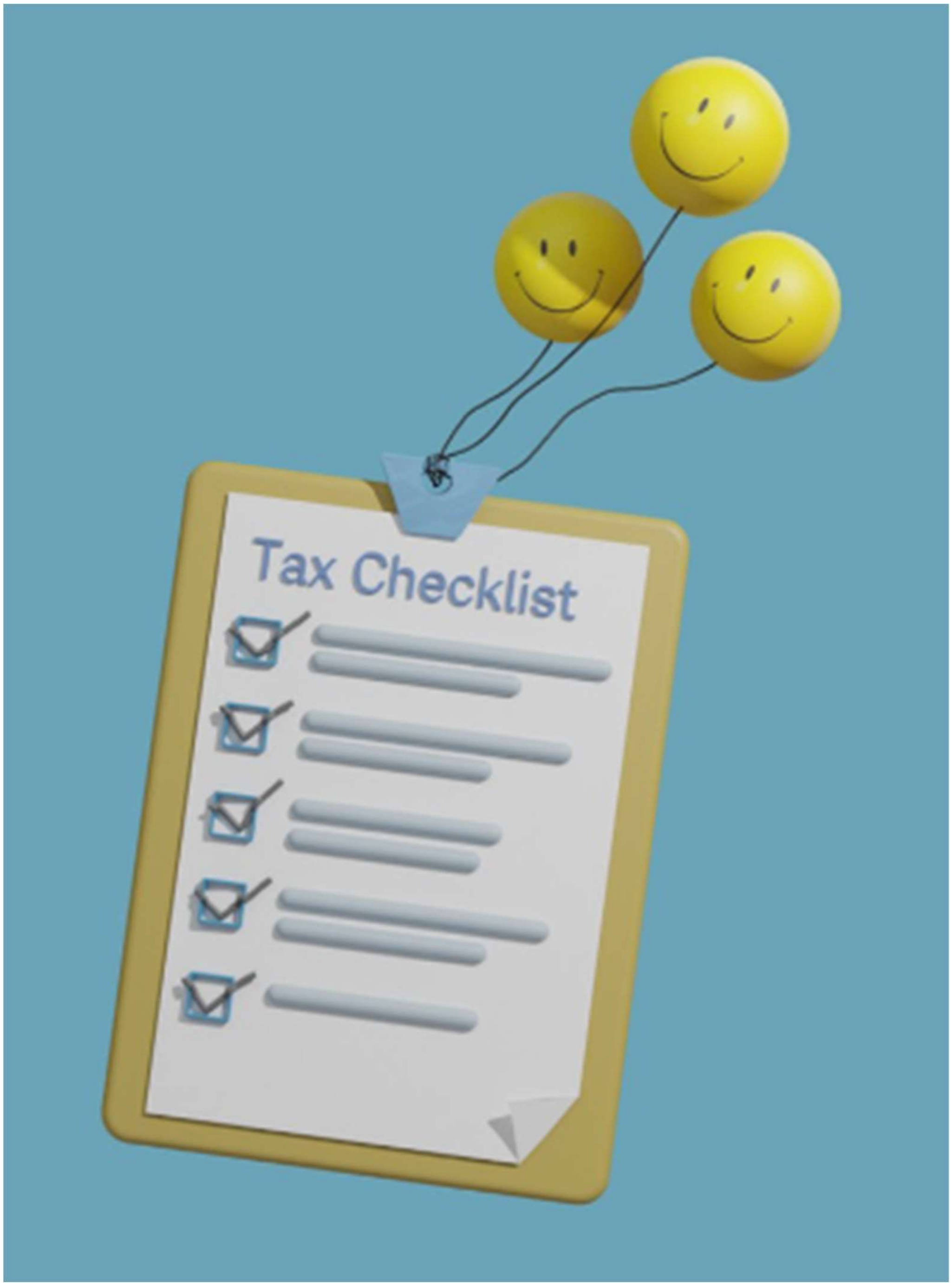

Have a great week!

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Investing in small cap stocks generally involves greater risks, and therefore, may not be appropriate for every investor.

Market return and statistical data obtained from: https://am.jpmorgan.com/blob-gim/1383452890099/83456/weekly_market_recap.pdf?segment=AMERICAS_US_ADV&locale=en_US

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