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WEEKLY MARKET RECAP | November 27, 2023

Week in Review

Equity Markets:

The major indices rose for the fourth week in a row. The S&P 500 finished the holiday-shortened week up 1.02%. The equity market broadened out last week with all market capitalization and styles finishing the week in the green. The Russell 1000 Growth slightly outperformed its Value counterparty by 0.02% with a weekly return of 1.06%. Year-to-date, the divergence in performance continues. Large Cap Growth is up 36.7% while Large Cap Value is up a meager 4.8%[1].

As third-quarter earnings season is coming to a close, 96% of S&P 500 companies have reported. 82% have beaten earnings expectations while 61% have exceeded revenue estimates[2]. Earnings growth for the quarter is expected to be 7.1%, which will mark the first quarter out of the last three to see positive earnings growth. Reports have come in much stronger than expected, the 82% earnings beat rate is well above the 66.5% long-term average and the previous four-quarter average of 73.6%[2].

Fixed Income Markets:

The shortened week saw low trading volume with the majority of the yield curve only making minor moves. The 10-year Treasury yield increased 0.03% to 4.47% from the prior week's close of 4.44%. The 2-year Treasury saw a 0.04% increase to 4.92%. After seeing a quick steepening of the yield curve last month, the inversion spread has stabilized in the 0.4-.5% range so far this month. Currently, the 2's/10's spread stands at -0.45%.

The action in the market may have been light, but the release from the most recent Federal Reserve's policy meeting moved the futures market. The meeting minutes showed that most Fed officials remain in the restrictive camp and gave no indications for rate cuts in the near future. Policymakers remain committed to keeping rates in restrictive territory until inflation data confirms its move back to the 2% target. Following a positive CPI report, Fed Fund's Futures had moved up the first rate cut to May, instead of the previously assumed June. After the minutes were released, the futures market had priced in a 39% probability of a rate cut as early as May, below the 46% probability from the week prior[3].

Economic:

The Conference Board's Leading Economic Index fell 0.8% in October, which marks 19 straight months of deteriorating readings. Falling consumer expectations for business conditions and tighter credit conditions were among the detractors of the index. The final University of Michigan Consumer Sentiment Index was revised higher to 61.3, up sharply from the preliminary reading of 60.4 a few weeks ago. Existing home sales fell 14.6% year-over-year in October. Higher rates have continued to put pressure on the housing market, and economists are expecting 2023 to be the worst year for existing home sales since 2011[4]. Initial unemployment claims surprisingly fell 24,000 to a seasonally adjusted 209,000. Despite the surprise drop, the most recent report remains close to the year-to-date highs.

Looking Ahead

Equity Markets:

We remain in a seasonally strong period for the markets and the positive third-quarter earnings season provides support for the market through the end of the year. Investors should also be prepared for bouts of volatility as we have seen the VIX, which is an indicator of expected short-term volatility, falling almost 40% from a month ago. As a contrarian indicator, this could lead to heightened volatility towards the end of the year.

So far this year, earnings have been far better than expected as corporations have continued to maintain their historically strong margins. In the third quarter, profit margins for the S&P 500 increased slightly to 12.1%[5]. This is a key factor we will be watching closely as move into next year. Revenue growth for the third quarter currently stands at 1.5% for the S&P 500[2]. Companies have been able to pass along some of the input price increases to consumers and as some underlying inflationary pressures have improved (freight costs, labor cost cutting, etc) they have been able to maintain healthy margins. A breakdown in profit margin could signal future earnings weakness.

Fixed Income Market

Over the past three months, the fixed-income market has experienced its fair share of volatility. On August 30th the 10-year Treasury yield stood at 4.09% only to experience a swift sell-off that saw its yield reach 5% intraday on October 19th, which surpassed the previous cycle high in 2022. Since the high just over a month ago, yields have steadily moved lower to where we sit today, 4.40-4.5%.

We believe the action in the fixed-income markets over the last few months are quick overreaction to positive/negative headline noise. The 10-year yield is likely to roam the mid-4 % range through the rest of the year, but we do believe bouts of short-term volatility could push rates higher or lower and investors should be prepared for this if it does arrive. Our long-term positive outlook on the bond market remains intact. Bond investors have the opportunity to receive yields that were hard to come by during the previous cycle without reaching down the credit quality ladder or extending further out on the maturity calendar. Current levels present an attractive total-return profile and the added benefit of a potential negative correlation to the equity market if a deterioration in the economic environment does occur.

Economic:

Following a shortened holiday week and few economic reports, this week will be a busy one. New home sales and the S&P/Case-Shiller Home Price Index will get the week started on Monday and Tuesday. On Wednesday, the second estimate for third-quarter GDP will be released. On Thursday, the Fed's preferred inflation gauge, the Personal Consumption Expenditure Price Index (PCE) will be released. The PCE report will be closely watched as investors will be looking for further improvement on the inflation front to support a potential pivot in Fed policy.

***** See Important Disclosures on following page*

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Sources:

1)JP Morgan
https://am.jpmorgan.com/content/dam/jpm-am-aem/americas/us/en/insights/market-insights/wmr/weekly_market_recap.pdf

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5) FactSet Research, Inc.
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