Week in Review

Equity Markets:

Fueled by strong earnings results last week, the S&P 500 rallied 1.68%. Participation was spread equally in the large-cap space. The Russell 1000 Growth rose 1.65% while its value counterpart finished the week up 1.41%[1]. Small caps lagged with the Russell 2000 finishing down 0.77%, bringing its year-to-date return to -0.37%.

90% of S&P 500 companies have reported earnings. 77.5% have beaten earnings expectations and 63.8% have beaten revenue estimates[2]. Recent reports have been better than feared and pushed the earnings beat rate above the previous four-quarter average of 76.4% and well above the long-term average of 66.6%[2]. The expected earnings growth rate is 10% which is well above the 4.7% growth that was expected on January 1[2]. The recent string of earnings beats has pushed the expected growth back to the level that was expected a year ago.

Fixed Income Markets:

The bond market was relatively flat last week but we did see a notable deepening of the curve inversion. Long bonds experienced a slight rally with the 10-year Treasury yield closing the week at 4.26%, down 0.04% from the previous week's close of 4.30%. The 2-year Treasury sold off and closed the week at 4.67%. The 2's/10's spread finished the week at -0.41%.

The Federal Reserve released its meeting minutes from January. Policymakers still have concerns over the threat of inflation reemerging if they are too quick to loosen financial conditions. The market had previously anticipated the Fed to cut rates 6-7 times at the start of the year. Currently, the Fed fund's futures market is pricing in only three cuts for the year[3].

Economic:

Last week was light on the economic report front. The labor market remains strong as we saw initial unemployment claims fall to 201,000, marking a 5-week low. Lower mortgage rates helped existing home sales rise by 3.1% from a year ago.

Looking Ahead

Equity Markets:

The recent rally has been fueled by better-than-expected earnings results, and to a lesser extent, multiple expansion. Again, analysts underestimated the resilience of corporations and their ability to navigate an environment that was experiencing margin compression and slowing sales. The theme of pushing slowing growth further out on the calendar has continued also. Q1 2024 earnings have growth estimates at 5.4%, down from the 7.2% estimate at the beginning of the year. Full-year 2024 earnings growth has been revised down to 9.5% from 11.1% on January 1 and most notably Q4 2024 has experienced its first major decline in estimate to 13.9% from the original 18.2%[2].

The S&P 500 is currently trading at 21x forward four-quarter price to earnings. While this is not extreme, it is elevated and we believe investors should take note of it as they evaluate the current landscape. As long-term investors, we believe that earnings are the main driver of market returns. Rich multiples can remain intact for longer timeframes but it could also be accompanied by volatility. We believe the market has priced in a very optimistic outcome and it would be prudent for investors to evaluate their current allocations to ensure it still properly aligns with your long-term investment objectives.

Fixed Income Market

Two major economic reports, GDP and PCE, have the potential to exert significant influence on the bond market this week. The market has recently moved expectations closer in line with policymakers. This should lead to less volatility around these announcements. Our view remains positive on the fixed-income market. We believe the cycle high has already occurred and the odds of lower rates a year from now are greater than rates higher from where we currently stand. This presents investors an opportunity to capture 4% yields on high-quality bonds and the potential for the benefits of negative correlation if we were to see the economy slow significantly and cause stock market weakness.

Economic:

The headline report for this week will be the PCE release on Thursday. Being the Fed's preferred inflation gauge means the market has the potential for a strong reaction following the release. Current estimates have Core PCE, which excludes food and energy, to come in at 2.8% year-over-year and the headline reading at 2.4%[4]. Other notable reports this week include the Consumer Confidence Index, the second estimate of fourth-quarter GDP, ISM Manufacturing PMI, and the University of Michigan Consumer Sentiment Index.

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

Sources:

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

2) LSEG I/B/E/S
https://lipperalpha.refinitiv.com/wp-content/uploads/2024/02/TRPR_82221_736.pdf

3)CME Group
https://www.cmegroup.com/markets/interest-rates/cme-fedwatch-tool.html

4) Market Watch
https://www.marketwatch.com/economy-politics/calendar