D|A|DAVIDSON WEALTH MANAGEMENT

The Weekly Market Update – 2/20/24: Inflation Uptick Likely Extends Fed Pause

Major Indices (Price Returns)	Close	Last Week	Quarter-to-Date	Year-to-Date	Trailing 12-Months	All-Time High	% to High
S&P 500	5,005.57	-0.42%	4.94%	4.94%	22.79%	5,029.73	0.5%
Dow Jones Industrial Average	38,627.99	-0.11%	2.49%	2.49%	13.32%	38,797.38	0.4%
NASDAQ Composite	15,775.65	-1.34%	5.09%	5.09%	36.18%	16,057.44	1.8%
Russell 2000	2,032.74	1.13%	0.28%	0.28%	5.22%	2,442.74	20.2%
MSCI EAFE (USD)	2,257.21	1.44%	0.94%	0.94%	7.46%	2,398.71	6.3%
MSCI Emerging Markets (USD)	1,016.23	2.08%	-0.73%	-0.73%	-1.48%	1,444.93	42.2%
Bloomberg Commodity Index	96.25	-0.72%	-2.43%	-2.43%	-13.91%	237.95	147.2%
Barclays U.S. Aggregate Bond	89.56	-0.59%	-2.33%	-2.33%	-2.12%	112.07	25.1%

Source: FactSet

The consumer price index (CPI) month-to-month (M/M) increase in January could lead to higher interest rates. According to the U.S. Bureau of Labor Statistics (BLS), the January CPI (a popular measure of consumer inflation) increased +0.3% M/M from December, and the core CPI (excludes food and energy prices) M/M increase was +0.4% (+4.8% annualized). Both numbers were higher than expected and indicated rising services prices including medical services, transportation, shelter, and recreation. The year-over-year (Y/Y) data reflected ongoing annual improvement, but Y/Y CPI of +3.1% and Y/Y core CPI of +3.9% were higher than expected. The M/M increase in core CPI was the highest in eight months (since May 2023) and could alter investor perception about the direction of near-term interest rates. As of 2/16/24, the U.S. 2-year Treasury yield (used as a proxy for short-term interest rates) was 4.64%, compared to 4.22% as of 1/31/24. The U.S. Federal Reserve Bank (Fed) uses its overnight bank lending fed funds interest rate target to restrict (higher fed funds targets) credit conditions and limit inflation. Since July 2023, the fed funds target range has been 5.25% to 5.50%, but the Fed maintains that continued progress on inflation could lead to a lower, more neutral, rate target. Market expectations settled on May 2024 or June 2024 as the likely dates for the first Fed interest rate cut (the next three 2024 Fed policy meetings end on 3/20, 5/1, and 6/12). We believe the increase in 2-year Treasury yields in February reflects a new investor view that the first Fed rate cut will come in June, not May, and that the total number of Fed rate cuts in 2024 could be lower than previously expected (the possibility of 0.75% of rate cuts, compared to 1.50% of cuts contemplated a month ago).

Economic “soft landing” remains in play but both retail sales and housing starts missed expectations. Largely due to stronger-than-expected consumer spending, the U.S. economy grew +2.5% in 2023 (gross domestic product, GDP; the value of goods and services produced, reported by the Bureau of Economic Analysis, or BEA). This was well above expectations early in 2023 as many feared a decline in GDP, or recession, would develop. Even a “soft landing,” which we define as GDP growth below +1%, did not materialize. Entering 2024, a low-growth soft landing remains possible, in our view, but labor market strength in December and January validated bullish investors looking for another year of above-trend GDP growth. BLS data showed that nonfarm payrolls in Dec ’23 (+333 thousand, K) and Jan. ’24 (+353K) were the strongest in 12 months. But January retail sales (reported by the Census Bureau) declined -0.8% M/M, and previously released December data was revised lower. In addition, January housing starts (Census Bureau) were lower than expected as the January annual rate decreased -14.8% from December. While one month does not make a trend, it appears that GDP growth could slow from late 2023 levels. At this point, a 2024 slower-growth soft landing appears more likely than recession, which can create a supportive equity market environment. But last week, the widely followed, large-company S&P 500 equity index dropped -0.4%, following five consecutive weeks of gains.

It’s a 4-day trading week after Monday’s Presidents’ Day holiday, and the fourth quarter (4Q23) earnings season is winding down. With nearly 80% of earnings results now reported, S&P 500 4Q23 revenue and earnings are trending +3.9% and +1.2%, respectively. Both are moderately above FactSet consensus (Wall Street analysts) and estimates are fairly positive for the remaining 20% of companies. Focus will now turn to 2024 expectations, where FactSet consensus reflects expectations for +11% full-year growth. 1Q24 expected earnings growth is +4.5% and has trended lower in recent weeks.

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Please refer to page 2 of this report for detailed disclosure information.

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