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Market Commentary Q2 2024

The economic momentum we witnessed in the first quarter of 2024 continued into the second, with yet another positive period for equity markets. Initially, investors aggressively dialed back expectations for central bank rate cuts, as U.S. overheating worries had taken root towards the end of the first quarter. But as the quarter progressed the worst of these worries abated, and the soft-landing hopes were revived.

The S&P 500 gained approximately 4% in the second quarter, forging new all-time highs.[1] So far, year-to-date the index is now up ~15%.[1]

Leading US Indices (Total Return)	4Q'22	1Q'23	2Q'23	3Q'23	4Q'23	1Q'24	2Q'24 (sorted)	TTM
S&P/Citigroup Growth	1.4%	9.6%	10.6%	-2.6%	10.1%	12.8%	9.6%	32.5%
Nasdaq	-0.8%	17.0%	13.1%	-3.9%	13.8%	9.3%	8.5%	29.6%
S&P 100 Mega-Cap	5.6%	10.1%	11.1%	-2.8%	11.7%	11.2%	7.1%	29.4%
S&P 500 Total Return	**7.6%**	**7.5%**	**8.7%**	**-3.3%**	**11.7%**	**10.6%**	**4.3%**	**24.6%**
S&P/Citigroup Value	13.6%	5.2%	6.6%	-4.1%	13.6%	8.1%	-2.1%	15.3%
S&P 600 Small-Cap	9.2%	2.6%	3.4%	-4.9%	15.1%	2.5%	-3.1%	8.7%
Russell 2000	6.2%	2.7%	5.2%	-5.1%	14.0%	5.2%	-3.3%	10.1%
S&P 400 Mid-Cap	10.8%	3.8%	4.9%	-4.2%	11.7%	10.0%	-3.4%	13.6%

Strategas Securities, LLC – 07/02/2024

The second quarter was an unusual quarter for equities in that correlations collapsed; the big got bigger and the small got smaller. This was one of the best first halves of the year for large caps and yet one of the worst first halves for small caps. This extreme bifurcation has made it very difficult for investors to keep up with the S&P 500. At this point, even within the large cap space, only ~26% of S&P 500 stocks are beating the index YTD, which is extremely low by historical standards.[1]

Companies exposed to artificial intelligence continued to outperform other areas of the market, and a strong earnings season for U.S. technology companies meant global growth stocks were once again the top performing asset class. Those stocks continued to show resilience, driven by innovation and strong earnings reports. In contrast, sectors sensitive to interest rates, such as financials and utilities, faced challenges. As you'll see below, six of the eleven sectors in the index declined in the quarter.

S&P 500 Sectors (Total Return)	4Q'22	1Q'23	2Q'23	3Q'23	4Q'23	1Q'24	2Q'24 (sorted)	TTM
Technology	4.7%	21.8%	17.2%	-5.6%	17.2%	12.7%	13.8%	41.8%
Communication Services	-1.4%	20.5%	13.1%	3.1%	11.0%	15.8%	9.4%	44.9%
Utilities	8.6%	-3.2%	-2.5%	-9.2%	8.6%	4.6%	4.7%	7.8%
S&P 500 Total Return	**7.6%**	**7.5%**	**8.7%**	**-3.3%**	**11.7%**	**10.6%**	**4.3%**	**24.6%**
Staples	12.7%	0.8%	0.5%	-6.0%	5.5%	7.5%	1.4%	8.2%
Discretionary	-10.2%	16.1%	14.6%	-4.8%	12.4%	5.0%	0.6%	13.1%
Health Care	12.8%	-4.3%	3.0%	-2.7%	6.4%	8.8%	-1.0%	11.7%
Real Estate	3.8%	1.9%	1.8%	-8.9%	18.8%	-0.5%	-1.9%	5.6%
Financials	13.6%	-5.6%	5.3%	-1.1%	14.0%	12.5%	-2.0%	24.2%
Energy	22.8%	-4.7%	-0.9%	12.2%	-6.9%	13.7%	-2.4%	15.9%
Industrials	19.2%	3.5%	6.5%	-5.2%	13.1%	11.0%	-2.9%	15.5%
Materials	15.0%	4.3%	3.3%	-4.8%	9.7%	8.9%	-4.5%	8.7%

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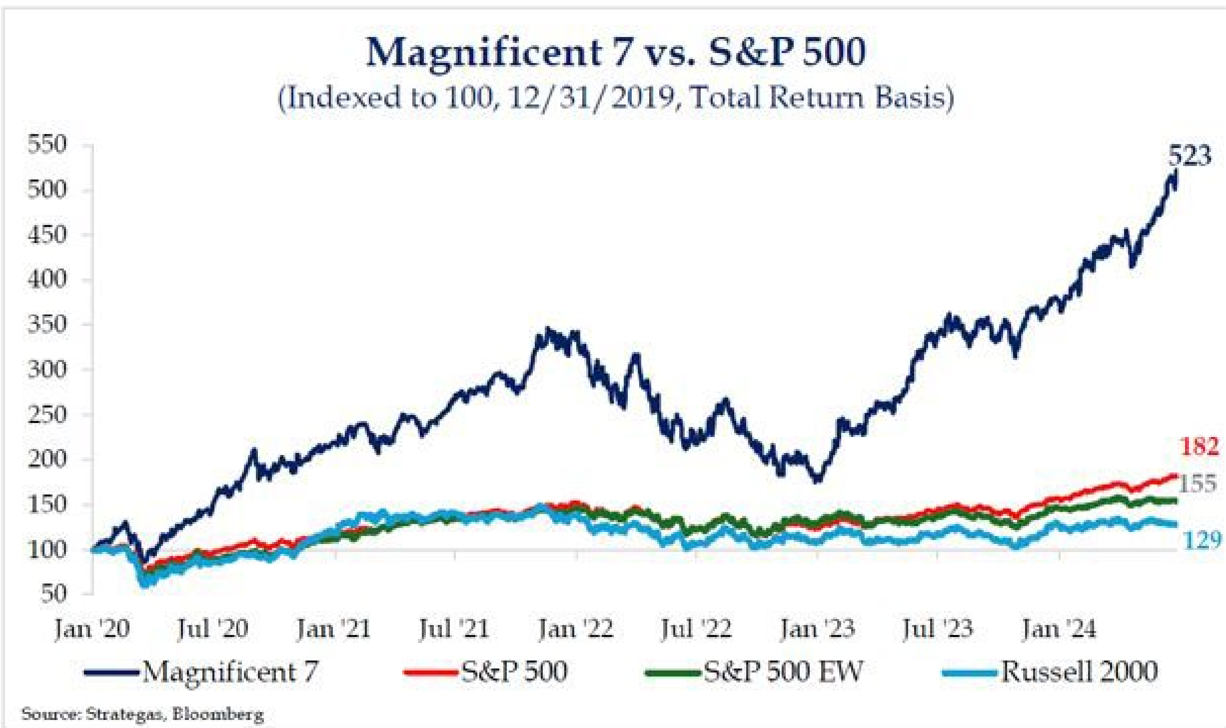
The average stock within the S&P 500 is up about 4% this year, while the broad index is up almost 15%.[1] That is the largest underperformance since at least 1990.[1] Meanwhile, the group of large technology companies known as the "Magnificent Seven" are responsible for almost 60% of the index's total return this year![1]



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As previously mentioned, the largest domestic stocks are doing well while everything else is relatively disappointing or an outright dud. Looking at the chart below, you'll see the impact of the 10 largest weights on the S&P 500 return, which sits at 77% through 6/30. We'd refrain from using this as an analysis on market breadth, but rather how influential the largest players within the S&P 500 have become (the top 10 weights are at 37% today).[2]

Annual S&P 500 Contribution of 10 Largest Weights During Positive Performance Years

Year	Top 10 as % of Total	S&P 500 % Perf.
2007	78.7%	3.5%
2024	**77.2%**	**14.5%**
2023	68.4%	24.2%
2020	58.9%	16.3%
1999	54.5%	19.5%
2021	45.0%	26.9%
1998	36.8%	26.7%
1996	33.9%	20.3%
2017	33.3%	19.4%
2019	32.8%	28.9%
1991	28.6%	26.3%
2006	27.6%	13.6%
2016	26.6%	9.5%
2003	23.6%	26.4%
1995	22.3%	34.1%
2014	22.2%	11.4%
2004	21.1%	9.0%
2005	20.5%	3.0%
2010	19.6%	12.8%
2012	19.2%	13.4%
1997	19.1%	31.0%
2013	17.6%	29.6%
2009	15.5%	23.5%
1992	14.9%	4.5%
1993	12.2%	7.1%

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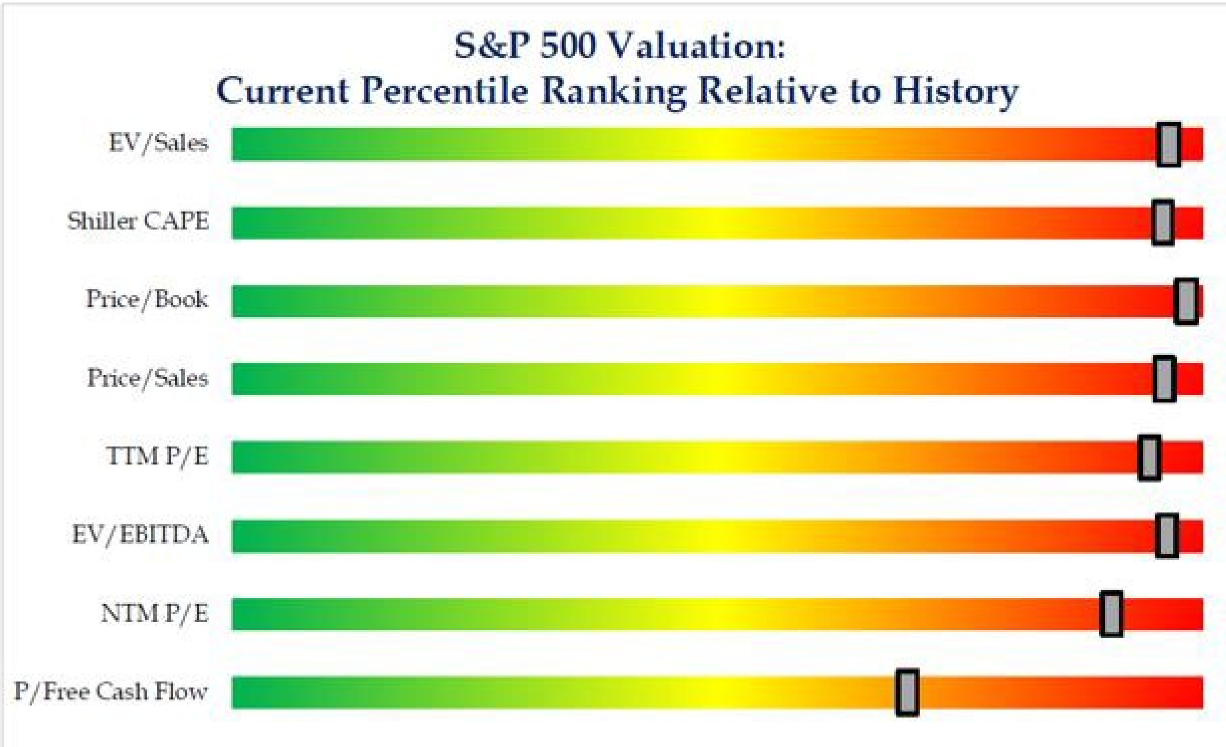
Turning to valuations, do they matter anymore? This inexorable climb in the market, with few interruptions and mild volatility, has led to increasing consensus among investors that valuations really don't matter any longer, especially given some of the unique characteristics of the largest stocks in the S&P 500. These companies could be considered in some cases to be quasi-monopolies; their large cash balances allow them to actually benefit from higher rates, and they generate almost shocking amounts of cash flow. Their only potential weakness, some might concede, may come from the regulatory winds that come from Washington. As the heatmap below indicates, there is really no way in which one can claim that the market as a whole is cheap based on historical standards. Still, there are times, like 2022, when great companies can become bad stocks. We do not believe the laws of financial physics have been repealed. The significant decline in private equity exits is some testament to the fact that there are limits.



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At the same time, the Bloomberg U.S. Aggregate Bond Index showed a tepid -0.71% return, though the leveraged loan and high yield bond markets generated respectable returns of 4.4% and 2.6%, respectively.[1] Equity investors have never lost their conviction that the Federal Reserve ("Fed") would cut interest rates this year and have been counting on a Fed pivot should the economy or markets falter. On the other hand, bond investors remain concerned by inflation and large U.S. Treasury financings. For May, the underlying U.S. inflation data showed further signs of cooling as the Fed's preferred gauge, the core personal consumption expenditure (PCE) price index, posted a 2.6% annual increase.[1] Although corporate profits and labor markets remain resilient, pockets of weakness are emerging in the U.S. economy. As a result, by the end of June, the equity markets began showing signs of fatigue. Hence, investors are banking on the Fed to subdue demand without triggering a recession and are counting on at least one rate cut in 2024.

Fixed income markets were influenced by central bank policies, with yields rising in anticipation of interest rate hikes. Government bonds faced selling pressure, while corporate bonds offered higher yields to investors seeking returns.

US Yields	4Q'22	1Q'23	2Q'23	3Q'23	4Q'23	1Q'24	Q/Q Chg (bps)	Y/Y Chg (bps)
Fed Funds Target Rate	5.0	5.3	5.5	5.5	5.5	5.5	0	25
3-Month T-Bill	4.9	5.4	5.6	5.4	5.5	5.5	2	5
2-Year Note	4.1	4.9	5.0	4.3	4.6	4.7	9	-17
5-Year Note	3.6	4.1	4.6	3.8	4.2	4.3	12	21
10-Year Bond	3.5	3.8	4.6	3.9	4.2	4.4	16	55
30-Year Bond	3.7	3.9	4.7	4.0	4.3	4.5	19	69

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After an initial pick-up in April, U.S. economic data softened over the quarter and has generally been coming in below consensus since early May. Despite this, the Fed struck a hawkish tone at its June conference with all but one cut being removed from the 2024 projections. That said, soft U.S. consumer data meant that investors were slightly more hopeful for policy easing, and rates markets continue to point to two cuts by the end of the year. This more sanguine investor view meant that, despite the changes to Fed projections, Treasury yields ended the quarter where they started, and US Treasuries were the only major sovereign market to deliver positive returns with gains of 0.1% over the quarter.

Municipal bonds remain attractive, with strong issuer fundamentals (healthy credit ratings and high levels of cash) and solid supply/demand.

Just as there was bifurcation within U.S. equities in the quarter, there was also bifurcation in global markets. Overall, emerging markets gained relative to developed markets, however there were several emerging regions at the very top and several at the very bottom.

Several developed markets declined in the quarter (Japan, Canada, Germany, France, Italy, etc.). There was significant bifurcation across emerging markets this quarter with several emerging regions at the very top and several at the very bottom of the country leaderboard.

Moves by the Chinese authorities to support the real estate sector provided a boost to Chinese equity markets. This development, combined with strong performance from the artificial intelligence-exposed Taiwanese stock market, helped Asian equities deliver strong returns over the quarter. The weight of Asian markets in the broader emerging market universe also meant that, despite lackluster returns in Latin America, emerging market equities outperformed their developed market counterparts to deliver quarterly returns of 5.1%.[1]

International Indices (Price Chg)	4Q'22	1Q'23	2Q'23	3Q'23	4Q'23	1Q'24	2Q'24 (sorted)	TTM
Sensex (India)	5.9%	-3.0%	9.7%	1.7%	9.7%	2.0%	7.3%	22.1%
Hang Seng (Hong Kong)	14.9%	3.1%	-7.3%	-5.9%	-4.3%	-3.0%	7.1%	-6.3%
MSCI AC World	**7.0%**	**6.5%**	**6.0%**	**-2.9%**	**9.0%**	**9.0%**	**2.9%**	**18.8%**
FTSE 100 (UK)	8.1%	2.4%	-1.3%	1.0%	1.6%	2.8%	2.7%	8.4%
Swiss Market Index	4.5%	3.5%	1.6%	-2.8%	1.6%	5.3%	2.2%	6.3%
OMX Stockholm 30 (Sweden)	11.7%	8.8%	3.9%	-6.7%	11.2%	5.1%	2.0%	11.2%
Kospi (South Korea)	3.8%	10.8%	3.5%	-3.9%	7.7%	3.4%	1.9%	9.1%
MSCI EAFE	**8.4%**	**6.7%**	**3.2%**	**-1.9%**	**4.6%**	**9.1%**	**0.0%**	**12.0%**
IBEX 35 (Spain)	11.7%	12.2%	3.9%	-1.7%	7.1%	9.6%	-1.2%	14.1%
S&P/TSX (Canada)	5.1%	3.7%	0.3%	-3.0%	7.3%	5.8%	-1.3%	8.5%
All Ordinaries (Australia)	8.1%	2.1%	0.4%	-2.1%	8.0%	4.1%	-1.7%	8.3%
Nikkei 225 (Japan)	0.6%	7.5%	18.4%	-4.0%	5.0%	20.6%	-1.9%	19.3%
Bovespa (Brazil)	-0.3%	-7.2%	15.9%	-1.3%	15.1%	-4.5%	-3.3%	4.9%
DAX (Germany)	14.9%	11.9%	0.3%	-4.7%	8.9%	10.0%	-3.9%	9.6%
Shenzhen SE A Shares (China)	3.3%	7.6%	-3.6%	-6.8%	-3.8%	-4.9%	-7.4%	-21.1%
Bolsa (Mexico)	8.6%	11.2%	-0.7%	-5.0%	12.8%	0.0%	-8.6%	-2.0%
CAC 40 (France)	12.3%	13.1%	1.1%	-3.6%	5.7%	8.8%	-8.9%	1.1%

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Commodities experienced varied movements, with oil prices showing volatility amidst supply chain disruptions and geopolitical uncertainties. Precious metals saw mixed performance, with gold benefitting from safe-haven demand while industrial metals fluctuated due to global economic growth concerns.

Despite all the uncertainty surrounding election cycles, historically markets tend to move higher over the long-term regardless of the party occupying the White House or Congress. In fact, the vast majority of election years have been positive for the market, with a few notable exceptions. As usual, large scale economic events drive market performance, even during election years, but often not the elections themselves. As history suggests, presidential election years have been a good time to invest regardless of the candidates or the eventual winner.

The current state of interest rates and their impact on the consumer (who, in turn, drives the vast majority of overall economic activity) needs to be highlighted. Some of the most influential people in the world, (members of the Fed, who dictate all interest rates) got it wrong to start 2024 when they proclaimed three interest rate reductions in 2024. However, the experts who make their livelihood analyzing influential people in the world got it even more wrong when they called for six or seven interest rate reductions this year. So far, there have been a whopping zero interest rate cuts in 2024.

This discrepancy between projections and reality just further reinforces one of our core beliefs: guessing the short-term trajectory of anything is just that, a total guess. Higher interest rates than markets anticipated and the impact they have on consumers often only tell one side of the story. Yes, too many Americans carry credit card debt and are suffering from these higher rates, but a full one-third of households have no debt at all.[1]

Turning to housing, mortgage rates remain high, yet nearly half of all homes in the U.S. have no mortgage at all![1] Even though new mortgage rates are above 7%, on average, all mortgages are currently at 3.8%, a far cry from the more than 10% average rate and 17% new rate the baby boomers paid "back in the day."[3]

As we look back to the broader strength of the economy in past quarters, it's important to highlight that there's a large swath of consumers that are not impacted by or are actually benefiting from higher interest rates.

Consumers are still spending, which is helping drive the economy forward. Because we're in the season of summer holiday travel, we need look no further than record levels of Americans traveling abroad.

It's great that investors are earning more in their savings accounts and from bonds, but don't let these higher rates fool you; you are rewarded more over the long run for being an owner (stocks) than for being a lender (bonds), and cash underperforms 100% of the time over the long term.

Cash, bonds, alternatives and stocks can all serve a purpose in a well-diversified portfolio, but even those nearing or in retirement hopefully have a long time horizon ahead of them to justify the benefits of leaning more toward equity ownership. Household net worths being near all-time highs, on average, not only benefits overall economic activity but also reinforces the long-term benefits of broad ownership and the prosperity it slowly manifests.

The times we live in have always been and hopefully always will be exciting, but they're also fraught with things to worry about. Political concerns and market innovations to mesmerize are as old as politics and the markets themselves, but the benefit of tuning out this noise in prudent investment decision-making is just as timeless.

Broad diversification works beautifully over time, as you get to participate in the exciting names as they grow and grow but you're not beholden to them when they inevitably fade from glory. This concept is so important, because the names always change. There's always a different hot dot investment, and inevitably there's a change in who it is. Oftentimes, names will grow and come to dominate only to then disappear. Don't bet on who'll be the king of the jungle, just own the jungle.

As the second half of the year begins, investors are wondering whether something must give. Looking ahead, investors are closely monitoring economic indicators, corporate earnings, and central bank actions for clues on future market directions amidst ongoing uncertainties.

On the surface, it would seem as if the growth in the U.S. economy and in risk assets has been inexorable and without drama. But while some could claim that we are trying to make a certain set of circumstances more interesting than it really is, we believe there are slight changes in both the economy and the stock market that will lead to greater economic volatility and a dispersion in returns from risk assets over time.

A key question now facing investors is whether the improved inflation news will continue, allowing the Fed to start cutting rates in September, as markets now expect. At the same time, can the economy continue its moderate growth pace, or will a slowdown raise the risk of recession?

Avoid emotional, short-term decisions; focus on being a long-term investor. Contact your wealth advisor to ensure your portfolio aligns with your long-term investment goals and objectives.

To discuss this commentary further, please contact us at 914-825-8630.

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[1] Y-Charts – 07/02/2024
[2] Strategas Securities, LLC – 07/02/2024
[3] https://creativeplanning.com/insights/investment/q2-2024-market-commentary/ - 07/05/2024