CROSSMARK GLOBAL INVESTMENTS

May 13, 2024 | Issue 4.20

Doll's Deliberations

Weekly Investment Commentary

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Summary:

Equities advanced last week (S&P 500 +1.89%) for the third week in a row. The S&P 500 is less than 1% away from its all-time high. Earnings season is almost complete, with another week of mostly good news. Best sectors were utilities (+4.13%), financials (+3.12%), and materials (+2.60%); underperformers included consumer discretionary (+0.18%), energy (+1.42%), and technology (+1.46%).

Key takeaways:

1. The Q1 Fed's Senior Loan Officer Opinion Survey (SLOOS) indicated a continued tightening of lending standards for C&I loans.
2. Economic activity is very bifurcated. Middle/high-income consumers are sanguine, but low-income confidence is recessionary. Small-business confidence is recessionary. These observations are probably not consistent with a soft landing.
3. Looking into details of the monthly employment report: Temporary jobs are falling, manufacturing jobs have been flat for roughly a year, and even information jobs are moving lower.
4. Initial unemployment claims rose from 209,000 to 231,000. Following last week's somewhat soft monthly payroll report, some questions about economic slowdown need to be asked.
5. We continue to see 10-year yields trending sideways in a broad trading range bound by the inflation data on the upside (5.0% yield high of October 2023) and the employment data on the downside (3.8% yield low of December 2023).
6. With over 80% of S&P 500 companies reporting earnings, 59% of companies are exceeding revenue estimates, and 77% are exceeding EPS estimates.
7. In Q1, first quarter net income growth for the Magnificent 7 was 49% and -9% for the S&P 500 ex the Mag 7. Similar results are expected for Q2 (+26% vs. -1%). Beyond that, estimates are similar for both sets.
8. Double-digit earnings growth for both this year and next certainly suggests expectations are high. We are dubious. (We note that U.S. earnings growth has not achieved two years of double-digit growth except when climbing out of a recession.)
9. The S&P GSCI commodity index has returned 8% year-to-date. Despite weak Chinese demand, accelerating global growth and improving investor sentiment are the contributing factors.
10. Some hoped the so-called great generational wealth transfer would be a panacea for millennials, and the economy more broadly. The reality is that inheritances are very highly concentrated, and for many people, primarily residential real estate.

EQUITY MARKETS (INDEX TOTAL RETURN) (%)	LAST WEEK	YEAR-TO-DATE
DJIA	2.20	5.48
S&P 500	1.89	10.03
NASDAQ	1.17	9.12
RUSSELL 1000	1.69	9.42
RUSSELL 1000 GROWTH	1.61	11.30
RUSSELL 1000 VALUE	2.16	7.59
RUSSELL 2000	1.89	2.75

S&P EQUITY SECTORS (INDEX TOTAL RETURN) (%)	LAST WEEK	YEAR-TO-DATE
COMMUNICATION SERVICES	2.02	19.28
CONSUMER DISCRETIONARY	0.18	2.92
CONSUMER STAPLES	2.35	9.63
ENERGY	1.42	13.13
FINANCIALS	3.12	11.72
HEALTHCARE	1.99	5.76
INDUSTRIALS	2.35	10.71
INFORMATION TECHNOLOGY	1.46	11.78
MATERIALS	2.60	7.70
REAL ESTATE	2.07	-4.93
UTILITIES	4.13	13.51

Is the U.S. weakening as the rest of the world improves?

The global economic expansion is slowly improving, led by the resilience of the still-strong U.S. economy, an improving trade backdrop, and the ongoing positive performance of global corporate profits. This is sustaining a virtuous cycle of solid employment demand, income gains, and consumption in most of the developed world. Overall developed market inflation is not on track to return to 2%, and monetary conditions are not particularly restrictive. A rotation in relative equity market performance is gradually emerging and should gain momentum as the run in U.S. mega-cap stocks gives way to better performance in other sectors and select non-U.S. markets. There will eventually be growing divergences in developed market central bank policies, which will impact relative foreign exchange and equity market trends. While the case for U.S. policy rate cuts is not compelling, the weak-link economies will likely need easier monetary conditions over the course of the next year. Meanwhile, the BoJ is on a very independent trajectory—albeit this time, it will be gradually lifting its policy rate rather than pursuing even greater open-ended monetary accommodation as the country exits its deflationary trap.

The overall backdrop for markets remains unchanged, in that risk assets tend to rally whenever government bond yields are flat to lower, as has been the case again recently. Non-U.S. equities have slightly outpaced the recent rebound in U.S. equity prices. Stocks would not have rebounded so strongly from the recent pullback and credit spreads would not have been so narrow if the global economic expansion really needed lower policy rates.

The resilience in global equity markets continues due to the strength of corporate profits. An economic roadblock will eventually develop (most likely via restrictive monetary conditions), thereby bringing an end to the cycle. However, as is becoming increasingly apparent, the current level of policy rates and bond yields is still accommodative and not yet too high.

The bull case for equities rests on continued solid earnings growth, a belief that inflation is contained, and the longer term AI secular growth theme. The bears counter that inflation is sticky, the Fed is unlikely to ease anytime soon, low-end consumers are beginning to struggle, earnings estimates are too high, and stocks are expensive.

INTERNATIONAL EQUITY MARKETS (INDEX NET RETURN) (%)	LAST WEEK	YEAR-TO-DATE
MSCI ACWI	1.40	7.89
MSCI ACWI EX U.S.	0.93	5.22
MSCI EAFE	1.15	5.64
MSCI EM	0.21	4.65

FIXED INCOME MARKETS (INDEX TOTAL RETURN) (%)	LAST WEEK	YEAR-TO-DATE
BLOOMBERG U.S. AGGREGATE BOND	0.32	-1.74
BLOOMBERG U.S. CORP HIGH YIELD	0.04	1.51
BLOOMBERG U.S. GOV/ CREDIT	0.28	-1.70
BLOOMBERG U.S. T-BILL 1-3 MONTH	0.06	1.90

ALTERNATIVES (INDEX TOTAL RETURN) (%)	LAST WEEK	YEAR-TO-DATE
REAL ESTATE (FTSE NAREIT)	2.12	-4.84
COMMODITIES (DJ)	1.53	6.25
GLOBAL LISTED PRIVATE EQUITY (RED ROCKS)	1.16	5.06
CURRENCIES (DB CURRENCY FUTURE HARVEST)	0.74	7.77

Conclusion:

The global economy is slowly improving, led by the still-strong U.S. Periods of a calm bond market will continue to promote risk-on phases as the global corporate earnings backdrop remains supportive. The glacial rotation from the U.S. to select non-U.S. equity markets is expected to persist, as positive absolute corporate earnings trends will progress into positive relative earnings performance.

Data from Bloomberg, as of 5/10/2024.