

Doll's Deliberations[®]

Weekly Investment Commentary



Robert C. Doll, CFA
CEO/CIO

Summary:

Stocks advanced for the sixth consecutive week (S&P 500 +0.87%), the longest streak this calendar year. Rising stock prices came from strong earnings and increased support for a soft landing. Best sectors were utilities (+3.42%) and real estate (+3.02%); the only declining sectors were energy (-2.61%) and healthcare (-0.50%).

Key takeaways:

- Retail sales and initial unemployment claims data were both better than expected, continuing a stretch of positive economic surprises despite hurricanes and Boeing layoffs.
- Given the recent robust economic data, the Atlanta Fed's GDPNow model has raised Q3 real GDP estimates from 3.2 to 3.4%.
- Consumer sentiment as measured by the University of Michigan deteriorated in October, breaking a three-month improvement streak. This is explained in part by consumer's short-term inflationary expectations increase.
- There is an increased risk that the Fed declared mission accomplished prematurely in the inflation fight, as shown by the increase in 10-year Treasury yields from 3.63% to 4.10% in less than a month. By cutting interest rates despite strong economic growth, the Fed now risks overstimulating demand and reviving inflation.
- Copper is a bellwether for the global economy, given its industrial usage, while gold is perceived as a safe-haven asset with inflation-hedging properties. Therefore, the ratio of copper over gold often carries important signals for the global economy. That ratio is falling, which signals potential trouble for the global industrial cycle.
- Financials, banks in particular, are among the earliest companies to report earnings. Generally speaking, big banks have reported positive surprises, with investment banking results especially strong.
- At current levels, markets seem to be pricing in a soft landing, where disinflation continues without a significant rise in unemployment. Any surprises are likely to fall short rather than exceed current lofty expectations.
- Stocks seem not worried about the economy or rising bond yields. Evidence is the strong relative performance of industrials and financials, the weak relative performance of healthcare and staples, and the outperformance of consumer discretionary relative to consumer staples.
- All sentiment readings are more than one standard deviation above the long-term average, which has been a short-term negative signal for stocks in recent years.
- China is attempting to stimulate a highly indebted country (that is rapidly aging) out of a collapsed property bubble. As the U.S. discovered post the great financial crisis, consumers and businesses take time to rebuild their balance sheets and start borrowing again. China is likely in for a long period of stagnation and could become like Japan.

EQUITY MARKETS (INDEX TOTAL RETURN %)	LAST WEEK	YEAR-TO-DATE
DJIA	0.98	16.55
S&P 500	0.87	24.33
NASDAQ	0.80	23.87
RUSSELL 1000	0.52	23.09
RUSSELL 1000 GROWTH	0.73	27.03
RUSSELL 1000 VALUE	1.13	19.00
RUSSELL 2000	2.08	13.74

S&P EQUITY SECTORS (INDEX TOTAL RETURN %)	LAST WEEK	YEAR-TO-DATE
COMMUNICATION SERVICES	0.35	29.42
CONSUMER DISCRETIONARY	1.22	13.23
CONSUMER STAPLES	0.72	18.03
ENERGY	-2.61	11.41
FINANCIALS	2.44	28.17
HEALTHCARE	-0.50	13.71
INDUSTRIALS	0.60	23.51
INFORMATION TECHNOLOGY	0.81	33.98
MATERIALS	1.94	15.95
REAL ESTATE	3.02	14.50
UTILITIES	3.42	32.54

The high-risk, momentum-driven bull market continues

After slowing for several months, macro conditions have improved relative to expectations this fall as the S&P 500 has resumed its steady upward march. Despite the improving tenor of the incoming data, we remain comfortable (although a bit less so) with our significant economic slowdown view. We are pushing back against the soft-landing consensus because we think the savings tailwind is nearly exhausted, meaning households' ability to maintain their consumption pace will turn on compensation growth, and we expect it will cool as the labor market continues to soften before rate cuts can boost activity.

Small-business hiring intentions have slowed, temporary employment has been weakening, initial jobless claims have been edging higher, and slowing compensation growth usually leads to decelerating consumption, which leads to fewer payrolls, which leads to consumer and corporate belt tightening, layoffs, less consumption, etc.

Judging by analysts' projected 14% increase in 2025 S&P 500 earnings per share and the tight spreads on investment grade and high-yield bonds, financial markets appear to be counting on a soft landing. The same goes for investors' willingness to pay between 22- and 23-times earnings expectations. Valuation is a notoriously poor timing indicator, but historically pricey spreads and multiples testify to corporate bonds' and large-cap equities' vulnerability to adverse surprises. While growth is cooling from too hot, no one will be able to say for sure if the economy's ultimate near-term destination is soft landing or recession or no landing or bumpy landing.

There is always the chance that the risk-on phase might be cut short by some major geopolitical or possibly U.S. political development. The main and immediate conduit for current geopolitical threats to undermine the global economic expansion would be via a spike in energy prices. This has not happened despite a chaotic geopolitical backdrop; rather, oil and natural gas prices are at the low end of their ranges and are supportive of growth.

While protectionist actions in the late-2010s almost derailed the global economy, former President Trump pulled back before too much damage occurred, although it did produce a downcycle in global trade. It is premature to bet that a possible Trump victory next month would create an even larger global economic roadblock. If elected, Trump would threaten draconian trade actions, but probably more as a negotiating tactic rather than an intended policy direction. The eventual outcome may well be less than feared (and less than he currently claims he might enact).

Conclusion

Financial markets are betting on the soft-landing outcome. The combination of rich valuations and ambitious growth targets suggests that risk assets could decline even in the event of a soft landing.

Data from Bloomberg as of Oct. 18, 2024

Crossmark Global Investments Inc. (Crossmark) is an investment adviser registered with the Securities and Exchange Commission that provides discretionary investment management services to mutual funds, institutions, and individual clients. Investment advice can be provided only after the delivery of Crossmark's firm Brochure and Brochure Supplement Form ADV (Parts 2A and 2B) and Form CRS, and once a properly executed investment advisory agreement has been entered into by the client.

All investments are subject to risks, including the possible loss of principal. Past performance does not guarantee future results.

Information and recommendations contained in market commentaries and writings are of a general nature and are not intended to be construed as investment, tax, or legal advice. These materials reflect the opinion of Crossmark on the date of production and are subject to change at any time without notice. Where data is presented that was prepared by third parties, the source of the data will be cited, and we have determined these sources to be generally reliable. However, Crossmark does not warrant the accuracy of the information presented.

INTERNATIONAL EQUITY MARKETS (INDEX NET RETURN %)	LAST WEEK	YEAR-TO-DATE
MSCI ACWI	-0.07	18.74
MSCI ACWI EX U.S.	-1.06	11.28
MSCI EAFE	-0.78	9.87
MSCI EM	-2.10	13.33

FIXED INCOME MARKETS (INDEX TOTAL RETURN %)	LAST WEEK	YEAR-TO-DATE
BLOOMBERG U.S. AGGREGATE BOND	0.00	2.93
BLOOMBERG U.S. CORP HIGH YIELD	0.30	7.82
BLOOMBERG U.S. GOV/ CREDIT	0.06	2.91
BLOOMBERG U.S. T-BILL 1-3 MONTH	0.04	4.30

ALTERNATIVES (INDEX TOTAL RETURN %)	LAST WEEK	YEAR-TO-DATE
REAL ESTATE (FTSE NAREIT)	2.25	13.18
COMMODITIES (DJ)	-2.46	3.87
GLOBAL LISTED PRIVATE EQUITY (RED ROCKS)	2.02	20.09
CURRENCIES (DB CURRENCY FUTURE HARVEST)	0.74	10.46