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Wealth & Investment Management

# Quarterly Economic Commentary

*July 2024*

## Market Returns

| | 12/31/2023 | 06/30/2024 | % Gain/Loss |
|---|---|---|---|
| Dow | 37,690 | 39,119 | 3.79%* |
| S&P 500 | 4,770 | 5,460 | 14.47%* |
| NASDAQ | 15,011 | 17,733 | 18.13%* |

**Total Return Including Dividends*

*By Jim Watts, KS Trust Senior Portfolio Manager*

While mostly positive, the second quarter saw a change in sector leadership for the equity markets. It seems reminiscent of 2023, as the S&P 500 and the NASDAQ made substantial gains, especially compared to the Dow. Technology leads the way, up 28.2%, followed by Communication Services, up 26.7%, with Energy coming in a distant third, up 10.9%. The bottom three sectors were Real Estate -2.4%, the only negative sector, Materials, up 4.0%, and Consumer Discretionary, up 5.7%. In the past 12 months, the indices have measured up this way: S&P 500 is up 26.7%, Dow is up 17.9%, and NASDAQ is up 31.5%.

Fixed income continued to be negative over the first half of 2024. The 10-year Treasury is down 2.0%, US Bonds are down 0.7%, and municipals are down 0.4%. The yield on the 10-year Treasury was 4.37%, with the two-year Treasury yield at 4.70%. The inversion continues but has narrowed during the first half of 2024. I expect as we move closer to a Fed rate cut, the inversion will continue to diminish.

The Fed continues to sit on the sidelines looking as they monitor improving inflation data, as they have done for seven straight meetings. The current thought process is that there may be two rate cuts this year, the first in September. However, I believe that there will only be one cut, starting in November, with a "wait and see" attitude before the second rate cut. I had a question asked of me last week regarding an article on Fox News concerning the possibility of a 30% drop in the equity market by year-end. My response was, first, there is too much money sitting in money market funds, thinking they have missed out on the AI / Technology bonanza over the past 18 months. Any significant pullback will bring immediate relief as those investors "jump in" to be a part of the next move up. Second, the economy, while slowing somewhat, is still very strong. Unemployment has moved up slightly, but still just 4.1%. Higher mortgage rates have taken some of the steam out of the housing market, but supply is still well below demand.

Here are my expectations for the equity markets over the remainder of the year. The second quarter held up better than I expected. I was looking for the market to take a breather during May, but it did not materialize. The Fed is holding the line on inflation, probably for the next several months. The result of the first of two presidential debates has caused some very serious concerns about the abilities and electability of President Biden. Any significant changes in the potential election process would give the equity markets a reason to experience additional volatility until there is clarity. I believe that progress on inflation, election process/outcome clarity, and status quo for the geopolitical concerns will keep the equity markets in a +/- 5% trading range until the fourth quarter while a floor is built and established. The fourth quarter will see the next real move higher for the equity markets.

Fixed income has already begun pricing in lower interest rates. Even short-term investments, such as money market funds, are beginning to see their rates reduced. Currently, we are "locking in" rates with longer maturities to provide a hedge against the upcoming rate cuts by the Fed. We have been employing this strategy since late 2023. However, that window is quickly closing as we get closer to the expected rate cuts.

Oil prices are up 16+% this year, increasing prices at the pump. The summer driving season is in full swing, and domestic travel is booming. I don't expect any relief until the fourth quarter of this year, if then. The SPRs (Strategic Petroleum Reserves) are extremely low, and demand is strong. This has benefited the energy sector, making it the third best-performing sector this year. We are slightly overweight in the energy sector this year and expect better than usual performance through the remainder of this year.

The geopolitical landscape has been very volatile, and escalation seems possible at any moment. This would add additional volatility to the broad markets, at least for the immediate concern. I think it is highly likely that expectation #5 (shown below) is a distinct possibility as our election process shows signs of uncertainty, creating yet another distraction for the American public.

At the mid-year point, here are my 10 expectations for 2024.

1) Interest rates will trend lower, but the Fed will be reluctant to lower rates until at least the second half of the year;
2) Bonds will perform better in 2024 than in 2023;

3) Oil prices will remain in the $75 - $95 range;
4) 2024 will continue to be very precarious geopolitically with no resolution in Israel or Ukraine;
5) China will make a proposed annexation of Taiwan;
6) Iran and N. Korea will continue to push the envelope militarily;
7) The US stock market will end the year with a high, single-digit or low, double-digit return;
8) The US will not go into a recession;
9) Gridlock will continue in domestic politics, but there will be no government shutdown;
10) And I will not make any predictions for the 2024 Presidential election!

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Our team's collective knowledge and experience forges our ability to serve our clients more extensively and develop a clear path. It allows us to address the increasingly complex challenges of today's landscape and provide comprehensive financial advice with a clear vision for the future.

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