Weekly Investment Insights

April 8, 2024

Key Takeaways:

- Homebuilder sentiment climbs on expectations for sales.
- Fed keeps rates steady, increases inflation forecast.
- Leading indicators increase for first time in two years.
- Global equities suffer led by U.S. losses.
- 10YR Treasury touches highest level of 2024.
- Commodities rally led by crude oil and gold prices.

Weekly Economic Recap –

Job Market Remains Strong

Manufacturing as measured by the ISM Manufacturing Index entered expansion territory (level above 50) in March and rose to the highest level since September 2022. The strength was led by production, inventories and prices paid. The prices paid component rose to the highest level since July 2022.

Job openings as reported by the JOLTS report showed that job openings rose modestly in February. The quits rate (those leaving jobs voluntarily) remained unchanged.

Activity in the services sector (ISM Services Index) slowed in March but remains in expansion territory (a level above 50). The weakness was led by the prices paid, backlog of orders and delivery times components.

The U.S. economy added 303K jobs in March, much more than the consensus estimate (i.e., 214K). It was the best month of job creation since May 2023 and follows net upward revisions of 22K jobs for the prior two months. The jobs added were led by healthcare, construction and leisure/hospitality. A gain of nearly half a million jobs in the household survey also pushed the unemployment rate lower (to 3.8%).

Average hourly earnings grew 4.1% YoY in March which is well above the trailing 20 year average we have experienced leading up to the pandemic (2.4% YoY). However, the pace of annual growth has slowed from prior months (4.3% in February and 4.4% in January).

Weekly Market Recap –

Global Equities Under Pressure on Mixed Rate Cut Signals

Equities: The MSCI AC World Index posted its worst one week performance since the first week of 2024. A pick up in economic activity in the U.S. and strong jobs report have investors pushing the odds of the first rate cut out. All major U.S. averages were lower for the week. The small-cap Russell 2000 fell the most and by the most since the beginning of 2024. The Dow Jones Industrial Average posted its worst weekly performance in 2024.

Fixed Income: The Bloomberg Barclays Aggregate Index fell for the first time in three weeks as Treasury yields rose sharply amid mixed signals from Fed officials around the future of rate cuts. During the week, the 10YR Treasury reached its highest level of 2024 (4.43%) before pulling back slightly. Floating rate instruments and leverage loans were the only areas of fixed income markets higher for the week.

Commodities/FX: The Bloomberg Commodity Index posted its best weekly return since June 2023. Crude oil prices were higher for the second straight week as tensions continue to intensify in the Middle East, causing investors to question the globaly supply outlook. Gold prices jumped to record highs as investors flock to the safe-haven on rate cut uncertainty.

Manufacturing Slightly Enters Expansion Territory

Footnotes: Data is as of March 2024.
Source: Bloomberg Finance LP, Verdence Capital Advisors.

Megan Horneman | Chief Investment Officer
mhorneman@verdence.com
Past performance is not indicative of future returns.

Key Takeaways:

- Four years since economic expansion started.
- GDP still strong; expansion intact…for now.
- Interest rate are not as tight as past cycles.
- Labor market makes the Fed's job difficult.
- Mixed economic data but risks remain.

Four Year Anniversary of Economic Expansion – Where are We?

In April 2020, the U.S. economy exited a short but painful recession due to the COVID lockdown. After four years, the question is where are we in the economic cycle? When can the Fed cut rates? In the table below we looked at past expansions and compared the end of those cycles to where we are now.[1] Major economic data is showing the Fed a conficting story as activity has accelerated and data remains stronger than at the end of past cycles when rate cuts are necessary to support growth. Some examples include,

- **GDP:** The U.S. economy grew 3.4% in 4Q23, much stronger than what growth looks like at the end of a cycle. On average, GDP grows less than 1% at the end of the cycle and justifies rate cuts. However, GDP is expected to grow above the historical average seen at the end of a cycle through 2024.
- **Interest rates accommodative:** The real Fed funds rate tends to be higher at the end of the cycle as the Fed raises rates to tame inflation. Currently, it is relatively low in a historical context which may warrant the Fed to be on hold for longer.
- **Labor market strong**: The current unemployment rate is lower than at the end of 8 of the 11 cycles observed. This challenges the view that rate cuts are on the horizon.
- **Leading indicators weak**: The Leading Indicator Index remains substantially weaker than the end or even during past cycles. This suggests the economy may not be as strong as other data points suggest.

The Bottom Line:

We think the economy is late cycle, despite the recent resumption in growth. While investors want rate cuts, a strong labor market and Fed funds rate that is not too restrictive suggests the Fed may be on hold until 2H24. Leading indicators are the one major data point that suggest a much weaker economy than other indicators suggest.

1. All data periods observed from 1945 to present. Only 1949 to present is shown as several economic data points were not available prior to 1949. Current is the most recent as of April 8, 2024.

Footnotes: Data is as of April 5, 2024.
Source: Bloomberg Finance LP, Verdence Capital Advisors.

Megan Horneman | Chief Investment Officer
mhorneman@verdence.com

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Megan Horneman | Chief Investment Officer
mhorneman@verdence.com