Weekly Investment Insights

July 15, 2024

Key Takeaways:

- Consumers increase spending on credit cards.
- Headline inflation posts first monthly decline since May 2020.
- Powell cites risks to keeping rates too high for too long.
- Large-cap growth falls; investors flock to beaten down sectors.
- Yields fall as investors increase bets for Fed rate cuts.
- Commodities broadly fall, but gold prices firm.

Weekly Economic Recap –

Inflation Continues to Moderate While Consumer Confidence Slides

Consumer borrowing increased at the fastest pace in three months driven almost entirely by a surge in credit card borrowing, which increased at the fastest pace since February.

The NFIB Small-Business Optimism Index increased for the third straight month in June and to the highest level this year. Inflation remains the top issue for small businesses, as 21% of respondents cited it as their single most important problem. The number of firms planning to increase prices moved to a three-month high.

Inflation as tracked by the Consumer Price Index declined in June. It was the first time the headline reading declined since May 2020. Inflation also increased less than expected at the core level (excluding food and energy) (+0.1% vs. 0.2% est). Gasoline prices fell 3.8% for the month, helping offset modest increases in both food and shelter prices.

Producer prices increased more than expected in June as prices for services offset the second straight monthly decline in the price for goods.

Fed Chairman Powell provided his insight on the state of the economy on Capitol Hill last week. He cited progress on inflation and a cooling labor market from recent highs. He also noted, “reducing policy restraint too late or too little could weaken economic activity.”

Consumer confidence as tracked by the University of Michigan Consumer Sentiment Index fell in June to a year to date low. Confidence on current economic conditions dropped to the lowest level since December 2022.

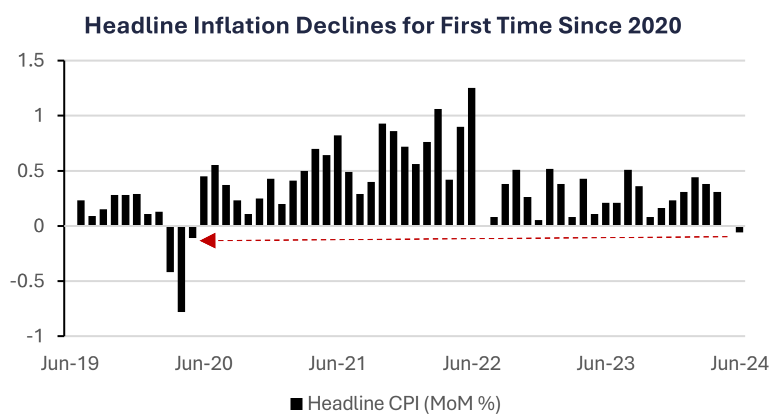
Weekly Market Recap –

Investors Flock to Beaten Down Areas of Markets; Large-Cap Growth Falls

Equities: The MSCI AC World Index was higher for the sixth consecutive week as headline U.S. inflation declined for the first time since May 2020. U.S. equities were broadly higher for the week, with outperformance coming from areas other than large-cap growth, which was the only area lower. Small-caps, as tracked by the Russell 2000, posted their best weekly return since November 2023.

Fixed Income: The Bloomberg Barclays Aggregate Index was higher for the second straight week as bond yields fell on expectations the Fed can start cutting rates as early as September. The yield on the 10YR Treasury ended the week below 4.20% for the first time since March. All sectors of fixed income markets were higher.

Commodities/FX: The Bloomberg Commodity Index was lower for the third time in four weeks. Gold prices moved back above the $2,400/oz. level and were higher for the third straight week as investors see Fed rate cuts in the future. Wheat prices moved lower amid persistent weather concerns.



Footnotes: Data is as of June 2024.
Source: FactSet Research Systems, Verdence Capital Advisors.

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Key Takeaways:

- 2Q24 S&P 500 earnings season kicks off with major banks.
- Earnings still concentrated in magnificent seven.
- Utilities are benefitting from AI.
- Guidance is important.
- Watching comments on economy.

2Q24 Earnings Season Preview

S&P 500 earnings for 2Q24 kicked off late last week with reports from major financial firms, giving investors their first look at how companies are withstanding the slowing economic backdrop. In aggregate, the S&P 500 is expected to report year-over-year earnings growth of ~9%, which would be the highest since 1Q22 (9.4%). It would also be the fourth consecutive quarter of year-over-year earnings growth. It is normal for analysts to reduce EPS estimates during a quarter to beat a lower bar. However, from March 31, 2024 – June 30, 2024, analysts only decreased their EPS estimate by ~0.5%, well below the 20-year average of ~4.0%.[1] In this weekly, we aim to provide an overview of what to expect from 2Q24 earnings season.

- **Major banks start with mixed results:** Analysts at FactSet expect the banking sub-industry to report a year-over-year earnings decline of ~10%. If this sub-industry were excluded from the financial sector, the sector would report year-over-year earnings growth of 14.8% vs. 4.3%, as-is. On Friday, July 12, 2024, several major banks, including JPMorgan, Wells Fargo, and Citigroup reported 2Q24 earnings, but results across the banks were mixed. Both JPMorgan and Citigroup reported better-than-expected results amid a surge in investment banking revenues. Wells Fargo, however, reported a sharp drop in net interest income, citing higher interest rates on funding costs.
- **Communication services to lead earnings growth:** The communication services sector is expected to report year-over-year earnings growth of 18.4%. Two of the magnificent 7 companies (i.e. Meta and Alphabet) are expected to contribute the most to earnings growth. In fact, if these companies were excluded from the sector, the sector's earnings would grow ~3.0% vs. 18.4%.
- **Nvidia driving information technology earnings:** The information technology sector is expected to report the third-highest year-over-year earnings growth of all eleven S&P 500 sectors. At the sub-industry level, semiconductors are expected to show year-over-year growth of ~51%. NVDA is expected to be the largest contributor to earnings growth. If the company were excluded, earnings would only grow 6.9% vs. 16.4%.
- **Utilities in the spotlight:** Utility stocks have benefitted from the AI craze given growing demand for energy from new data centers. After posting an impressive 1Q24 earnings season performance, the utilities sector witnessed the third-largest increase in price of all eleven sectors from March 31, 2024 – June 30, 2024. However, the sector has seen the second-largest percentage decrease in estimated earnings since March 31, 2024, suggesting the price movement from AI trends was potentially overdone.

The Bottom Line:

While earnings are still growing, we are concerned that estimates for the remainder of 2024 and 2025 remain too optimistic given the slowing economic backdrop. In this earnings season, we will look closely at clues to the health of the consumer since consumer spending makes up ~70% of GDP. In addition, are companies starting to see less flexibility with passing on higher costs to consumers? This may have a negative impact on margins. Lastly, has the view on hiring changed given the slowing economic backdrop?

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Global Equities Higher on Hopes for Central Bank Rate Cuts

U.S. Equities	Current	1WK	1MO	3MO	1YR	YTD
Dow Jones Industrial Average	40,001	1.60%	3.50%	5.80%	18.90%	7.20%
S&P 500	5,615	0.90%	3.70%	10.00%	27.40%	18.60%
Russell 1000 Growth	3,791	-0.40%	4.60%	13.40%	37.30%	24.70%
Russell 1000 Value	1,757	2.80%	2.40%	4.40%	14.50%	9.10%
Russell Midcap	3,331	3.40%	2.10%	3.70%	13.30%	7.90%
Russell 2000	2,148	6.00%	4.60%	7.60%	12.80%	6.80%
Nasdaq	18,398	0.30%	4.50%	14.00%	33.30%	23.00%

International Equities	Current	1WK	1MO	3MO	1YR	YTD
MSCI AC World (USD)	829	1.40%	3.50%	8.80%	22.40%	15.10%
MSCI EAFE (USD)	2,418	2.30%	2.00%	6.70%	15.30%	10.10%
MSCI Europe ex UK (USD)	2,716	2.30%	0.60%	7.60%	14.80%	10.00%
MSCI Japan (USD)	4,101	2.20%	4.20%	2.50%	17.90%	11.90%
MSCI UK (USD)	1,276	2.10%	1.80%	8.50%	16.20%	11.00%
MSCI EM (USD)	1,124	1.80%	5.70%	9.00%	14.60%	11.50%
MSCI Asia ex Japan (USD)	721	1.80%	5.40%	11.50%	15.40%	14.00%

Fixed Income	Current Yield	1WK	1MO	3MO	1YR	YTD
U.S. Aggregate	4.80%	0.80%	1.40%	3.40%	4.20%	0.80%
U.S. Govt/Credit	4.70%	0.80%	1.30%	3.30%	4.30%	0.80%
U.S. 10 Year Treasury	4.20%	0.90%	1.60%	3.80%	1.40%	-0.40%
U.S. TIPS (1-10YR)	4.40%	0.30%	1.30%	2.70%	4.80%	2.20%
U.S. High Yield	7.70%	0.80%	1.10%	3.30%	10.80%	3.70%
EM Bonds (USD)	7.00%	0.90%	1.30%	3.30%	9.40%	3.60%
Municipal Bonds	3.60%	0.50%	0.60%	1.30%	4.00%	0.20%

Commodities	Current	1WK	1MO	3MO	1YR	YTD
Bloomberg Commodity Index	238	-1.60%	-2.10%	-0.80%	2.90%	5.10%
Crude Oil (USD/bbl)	$82.10	-0.30%	3.60%	-3.40%	6.60%	10.40%
Gold ($/oz)	$2,411.40	2.40%	3.50%	1.30%	23.50%	17.10%
Copper	$459.90	-1.20%	1.60%	4.20%	16.40%	17.30%
Wheat	$550.80	-6.20%	-14.90%	-8.40%	-25.20%	-18.50%
U.S. Dollar	104	-0.80%	-1.30%	-1.90%	4.30%	2.80%
VIX Index	12.5	-0.20%	3.50%	-28.00%	-8.00%	0.10%

[1]: https://advantage.factset.com/hubfs/Website/Resources%20Section/Research%20Desk/Earnings%20Insight/EarningsInsight_071224.pdf

Footnotes: Data is as of July 12, 2024.

Source: Bloomberg Finance LP, Verdence Capital Advisors.

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Past performance is not indicative of future returns.

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