Summary

Economic data for the week included the Federal Reserve keeping interest rates unchanged, as expected. ISM manufacturing data improved, while the employment situation report for January came in far stronger than expected.

Equities fared well in the U.S. especially, with continued better-than-expected earnings. Bonds gained as long-term yields fell back. Commodities overall declined, led by a lower risk premium in crude oil prices.

Economic Notes

(0) The January **FOMC** meeting was unsurprising in the lack of policy action, with the Fed funds level kept at 5.25-5.50%. Rather, markets have been seeking any change in tone that points to near-term potential policy reversal and rate cuts. After Q4 market sentiment tied closely to hopes for cuts 'soon,' anything less has been a disappointment.

Interestingly, while Fed Chair Powell's press conference was noted as being a bit dovish, with tightening bias removed from the official statement, the notable quote was that a rate cut in March "is probably not the most likely case." This was a catalyst for the immediate negative market reaction. (The CBS 60 Minutes episode featuring Powell that aired Sunday night also alluded to a 'mid-year' timeline for starting cuts, and that the Fed wouldn't necessarily need to see 2% inflation before cutting.) It was also noted that the March meeting will see a more in-depth discussion on the balance sheet process. This most likely relates to the current status of QT, and the pace of bond run-off from the Fed's books. Powell mentioned that if the labor market weakened unexpectedly, that would affect the speed of rate cuts; however, if inflation stayed persistent, the timeline for cuts would be lengthened. This again reiterates the 'better balance' in current policy choices and input data.

(+/0) The **ISM manufacturing index** for January rose points to 49.1, beating the median forecast of 47.2, but remaining in contraction for now 15 straight months. New orders and production both rose, back into 50+ expansionary territory; on the other hand, employment fell a fraction of a point deeper into contraction. Prices paid rose 8 points back into expansion, while supplier deliveries rose by 2 points to 49, just below the neutral level. The report data was positive in the sense that manufacturing has stopped deteriorating, but is still slowing, albeit at a level just below the level of neutral. Survey responses alluded to some concerns over economic slowing, notably with some signs of softer demand. Coming quarters should provide more clarity on the path—will they remain in the doldrums or recover upward?

(+) **Construction spending** for December rose 0.9%, matching the prior month's gain following several earlier month revisions, and exceeded the 0.5% median forecast. Private residential construction and public non-residential spending each increased by over a percent to lead the overall index, while public residential spending fell by nearly -3%. With construction costs falling by nearly a percent during the month, 'real' spending rose nearly 2%—a positive for economic growth calculations.

(0) The **S&P Case-Shiller** 20-city home price index for November rose 0.2%, below the median forecast of 0.5%. By city, 14 of the 20 saw gains, led by Las Vegas and Cleveland, at 1%, while declines were close to a percent in Seattle and San Francisco. Year-over-year, the pace of the index ticked up from 4.9% to 5.4%.

(+) The **FHFA House Price Index** for November rose 0.3%, a tenth stronger than forecast. For the month, the Mountain region saw a gain of 0.7% on the upside, while New England prices declined by -0.2%. Year-over-year, the price growth in the series also reaccelerated by 0.3% to 6.6%. Despite higher financing rates, low home price supply has kept price growth buoyant. The agency's dataset shows the strength of housing prices over the past cycle (7.5% since Jan. 2012, or roughly 5% on a 'real' basis based on annualized inflation during that stretch). This has far surpassed longer-term growth (4.4% since Jan. 1991, or 2% on an annualized 'real' basis).

(+) The Conference Board's **index of consumer confidence** for January rose by 6.8 points to 114.8, matching expectations, and the strongest reading in two years. While future expectations rose a few points, the index was primarily driven by assessments of present conditions, up 14 points. The labor differential, which measures the difficulty in finding employment versus jobs being 'hard to get,' improved again by several points. Anecdotally, respondents continued to see lower chances of recession, although they still appeared high on an absolute basis at 66%.

(+) The **JOLTs** government job openings report for December showed a rise of 101k to 9.026 mil., above the expected decline to 8.750 mil. Openings rose in professional/business services (239k), education/health services (73k), and manufacturing (48k); declines were most dramatic in leisure/hospitality (-131k) and trade/transports/utilities (-67k). The job openings rate was unchanged at 5.4%, while the hiring rate rose a tenth to 3.6%. On the departure side, the quits and layoff rates were unchanged at 2.2% and 1.0%, respectively. Job openings have fallen by over 2 mil. over the past year, mostly in the first half of 2023, but showing steady stabilization since at a high level. (By contrast, pre-pandemic JOLTs were in the 7-8 mil. range.) The number of unemployed persons per job opening, on a seasonally-adjusted basis, remained steady at 0.7, just above the all-time low of 0.5 in late 2022. By contrast, this is well below the levels of 4.0-6.5 levels seen in the 2008 and 2020 recessions.

(-) **Initial jobless claims** for the Jan. 27 ending week rose by 9k to 224k, in contrast to an expected decline to 212k. Continuing claims for the Jan. 20 week rose by a dramatic 70k to 1.898 mil., surpassing the 1.839 mil. median forecast. It's possible severe weather in some segments of the country may have triggered the spike in claims over that period.

(+) The employment situation release for January was considered a 'blow out' report, with **nonfarm payrolls** rising by 353k, almost twice the 185k expected, coupled with 126k of upward revisions for the two prior months of Nov. and Dec. By segment, gains were most significant in professional/business services (74k), health care (70k), retail (45k), government (36k), social assistance (30k), and manufacturing (23k). Declines were seen in mining/oil and gas extraction (-5k). Job breadth by industry generally improved, which is a positive from an economic standpoint.

The **unemployment rate** was unchanged at a rounded 3.7%, contrary to expectations for a tenth higher. The U-6 underemployment rate, though, ticked up a tenth to 7.2%. The household survey incorporated updated population estimates, which resulted in an employment gain of 239k, but again is a reminder of the fragility and wide standard error in these initial estimates. **Average hourly wages** rose 0.6%, twice the rate of the expected consensus 0.3%. For the trailing 12 months, wages are up 4.5%, up two-tenths from the prior month's pace, and continuing to show wage pressures. At the same time, Jan. is obviously a key time of year for salary adjustments, which explains a bit of the gap. **Average weekly hours** fell by -0.2 to 34.1, under expectations for no change, which appeared to be weather-related.

Earlier in the week, the preliminary **nonfarm productivity** measure for Q4 came in at an annualized increase of 3.2%, exceeding the 2.5% expected, but down from the 4.9% prior quarter. The year-over-year rate ticked up nearly a half percent to 2.7%. **Unit labor costs** rose at an annualized pace of 0.5% for Q4, above the -1.1% of the prior period, but fell short of the 1.2% expected. Over the past 12 months, costs rose 2.3%, a half-percent faster pace than the prior quarter.

Market Notes

Period ending 2/2/2024	1 Week %	YTD %
DJIA	1.43	2.65
S&P 500	1.41	4.06
NASDAQ	1.13	4.14
Russell 2000	-0.77	-3.12
MSCI-EAFE	0.02	-0.54
MSCI-EM	0.32	-3.43
Bloomberg U.S. Aggregate	0.65	-0.66

U.S. Treasury Yields	3 Mo.	2 Yr.	5 Yr.	10 Yr.	30 Yr.
12/31/2023	5.40	4.23	3.84	3.88	4.03
1/26/2024	5.44	4.34	4.04	4.15	4.38
2/2/2024	5.43	4.36	3.99	4.03	4.22

U.S. stocks were mixed until Wednesday, when the FOMC statement and post-meeting press conference alluded to lower chances of a March rate cut—contrary to market hopes for a sooner-than-later ease. Faster easing has been the growing narrative this year, despite continued strong economic data (and especially considering very strong labor data on Fri.).

All-in-all, large caps again experienced a positive week, again led by a narrow band of growth stocks during the busiest earnings week of the quarter. By sector, consumer discretionary and communications stocks led with strong weekly gains, while energy lagged, as the only declining group. Real estate also fell back a fraction of a percent, despite declines in long-term yields. In a high-volume earnings week, tech companies in focus showed mixed results, with Microsoft little changed despite optimism in the AI and cloud space, and Alphabet suffering weaker advertising sales growth. Interestingly, in addition to decent earnings results Meta began a dividend program, not necessarily a common feature in the tech space, leading to a 20% gain on the week. Amazon gains of 8% led the consumer discretionary sector.

Foreign stocks were mixed, with gains in Japan based on strong earnings were offset by minor declines in Europe and the U.K. The Bank of England kept interest rates steady, but alluded to eventual cuts, in line with other key central banks. Emerging markets also declined as Chinese markets fell more than -5%, with subdued economic data, led by manufacturing PMI remaining in contraction, although improving from the prior month. Real estate market data remained negative, as a Hong Kong court ordered Evergrande be liquidated, with debt estimates high enough to be of financial stability concern.

In fixed income, government and investment-grade corporate bonds saw gains, outperforming high yield and bank loans, which were little changed. Foreign emerging market bonds gained along with risk assets. Long-term Treasury yields fell sharply last week, some of which may have been related to New York Community Bank earnings news. This pointed to some continued stress in regional bank commercial loan portfolios, albeit quite idiosyncratic from bank to bank.

Commodities fell across the board, with the exception of precious metals, which saw minor gains, led by declines in energy. Crude oil prices fell over -7% last week to $72/barrel, due to word from Qatar about a possible Israel-Gaza ceasefire agreement—which would remove a significant potential source of geopolitical risk.

Have a good week.

Ryan M. Long, CFA
Director of Investments
FocusPoint Solutions, Inc.

Sources: FocusPoint Solutions, American Association for Individual Investors (AAII), Associated Press, Barclays Capital, Bloomberg, Citigroup, Deutsche Bank, FactSet, Financial Times, First Trust, Goldman Sachs, Invesco, JPMorgan Asset Management, Marketfield Asset Management, Morgan Stanley, MSCI, Morningstar, Northern Trust, PIMCO, Standard & Poor's, StockCharts.com, The Conference Board, Thomson Reuters, T. Rowe Price, Univ. of Michigan, U.S. Bureau of Economic Analysis, U.S. Federal Reserve, Wall Street Journal, The Washington Post. Index performance is shown as total return, which includes dividends. Performance for the MSCI-EAFE and MSCI-EM indexes is quoted in U.S. Dollar investor terms.

Notes key: (+) positive/encouraging development, (0) neutral/inconclusive/no net effect, (-) negative/discouraging development.