Summary

On a week shortened by the Good Friday holiday, economic data included the final U.S. GDP growth number for the 4th quarter being revised slightly higher. Recent monthly data included gains in durable goods orders, and mixed house price and home sales data, as well as mixed results in consumer confidence.

Equities fared positively around the world last week, with some economic improvements abroad and continued hopes for rate cuts mid-year. Bonds fared decently with a small decline in yields. Commodities saw gains, primarily in crude oil and gold.

Economic Notes

(+) The final estimate of fourth quarter 2023 **U.S. GDP growth** was revised up by 0.2% to 3.4%. This was driven by upward revisions in personal consumption by 0.3% to an annualized pace of 3.3%, non-residential fixed investment by 1.3% to 3.7%, and government spending by 0.4% to 4.6%. On the negative side, inventory and residential investment were revised down a bit. The core PCE price index was revised down slightly to a quarterly annualized pace of 2.0%, while the year-over-year rate was little changed at 3.2%. The GDP price index was unrevised at an annualized 1.6%. The improvement in inflation from peak levels is certainly notable in the report.

As Q4 revisions are interesting, it represents old news now as far as markets are concerned. The Atlanta Fed's GDPNow estimate for Q1 growth activity started high in January, at around 3.5-4.0%, but has steadily faded, to now 2.3% (although this is still above the long-term trend growth rate of around 2%). Growth continues to be led by positive contributions from consumer spending (1.8% of the 2.3%, or nearly 80% of the growth), non-residential and residential fixed investment, as well as government (each of the three being 0.5% of total). These contributors are offset by expected declines in net exports and inventories, which tend to be cyclical and somewhat mean-reverting from quarter to quarter. Based on these and other metrics, growth doesn't look as robust as last year, but not bad by any means. This has raised the odds by many for the continued 'soft landing.'

(0) **Personal income** rose by 0.3% in February, a tenth below expectations, decelerating from strong January gains which were likely related to year-end effects. Wage income rose 0.8%, likely related to the same delayed year-end impact, along with a nearly-2% rise in rental income. Overall, personal income is up nearly 5% on a year-over-year basis, no doubt led by worker wage increases, which were up 7%. **Personal spending** rose 0.8% for the month, well above the 0.5% increase expected, due to increases in services and durable goods, while non-durable goods barely budged. Over the past 12 months, spending was also up 5%. This divergence caused the personal saving rate to fall by a half-percent to 3.6%, the lowest point over a year. The **PCE price index** came in up 0.3% on both a headline and core basis, with headline being a tenth below expectations. Year-over-year, headline PCE remained up 2.5% with core up 2.8%—each little changed from last month's pace. This was aided by a -2% drop in energy prices during the year, related to slight deflation for goods generally, while services prices rose nearly 4% for the year. The inflation component is the one most closely-watched, being the Fed's preferred gauge. It remained higher than hoped (target being 2.0%), but not radically worse, either.

(+/0) **Durable goods orders** rose 1.4% in February, exceeding the median forecast of 1.0% and the dismal -6.9% decline of the prior month—which had included some downward revisions. With the month driven by large commercial aircraft (up 25%) and autos (1%), removing transportation lowered the increase to 0.5%. Core capital goods orders rose 0.7%, led by machinery up 2%, followed by metals, while computers/electronics/electrical equipment each fell over a percent. Core capital goods shipments declined by -0.4% on the month, below expectations of little change. Durable goods orders overall are up nearly 3% from a year ago, while excluding transportation trims that to just over a 1% increase.

(0) The **S&P Case-Shiller home price index** for January rose just over 0.1%, decelerating from last month and half the increase expected. For the month, 13 of the 20 cities saw gains, led by San Diego and Washington up 1% or more, while Denver and Phoenix prices fell a half-percent each. Year-over-year, the pace of increase nationally improved from 6.2% to 6.6%.

(0) The **FHFA home price index** on the other hand declined -0.1% in January, in contrast to expectations of a 0.1% rise, representing the first monthly decline since the summer of 2022. By region, West North Central (ND south to MO) rose over a percent, while the South Atlantic (DE south to FL) fell by a half-percent. The national year-over-year rate of change decelerated from 6.7% to 6.3%, with a nearly 9% rise in East North Central (Great Lakes region) leading the way. This points to perhaps some tempering in strong home price gains of the past several years.

(-) **New home sales** in February fell by -0.3% in February to a seasonally-adjusted annualized rate of 662k, relative to expectations calling for a rise of 2.3%, following a few months of gains. By region, the South led with a 13k rise in sales, while the Northeast was in last place with a -17k decline. No doubt, tight inventories continue to keep a lid on sales activity, as much as continued-high mortgage rate levels. Months' supply ticked up a tenth to 8.4, right where it was a year ago, despite a drop to as low as 7.1 last year. Sales are up 6% over the last 12 months, while the median new home price came in at $400,500, down -8% from last year, and down over -20% from the peak in 2022. This price decline is a bit misleading, though, as it's less due to demand than it is smaller home sizes to accommodate buyer finances burdened by higher mortgage rates.

(+) **Pending home sales** rose 1.6% in February, just over the median forecast of 1.5%, and showing a reversal of the sharp decline the prior month. By region, the Midwest saw gains of over 10%, while the West declined the most at -7%. Year-over-year, pending home sales remain down -2%. Upward movement here bodes well for upcoming existing home sales in the next few months.

(-) The Conference Board's **index of consumer confidence** in March fell by -0.1 of a point to 104.7, in contrast to an expected increase to 107.0. While assessments of the present situation improved by several points, expectations for the future fell by a nearly equivalent amount. The labor differential ticked up a bit, with more consumers noting that jobs were plentiful and fewer claiming they were 'hard to get.' Opinions of current business conditions were mixed, with more descriptions of 'good' and fewer as 'bad.' The perceived likelihood of a U.S. recession in the next year saw further declines, to 64%, the lowest level in nearly two years. Average inflation expectations for the next 12 months actually ticked up a bit to 5.3%.

(0/-) **Initial jobless claims** for the Mar. 23 ending week fell by -2k to 210k, below the median forecast calling for no change at 212k. Continuing claims for the Mar. 16 week rose by 24k to 1.819 mil., just above the 1.815 mil. level expected. Claims were mixed by state with no major pattern, other than a larger drop in MI.

Question of the Week

Where do we stand at the end of Q1?

From their lows in late Oct. of last year, U.S. stocks have run almost straight up (by nearly 30%). Earnings have also come in better than expected (with positive growth, rather than the originally-expected decline), but not nearly as fast as price growth—implying valuation expansion as the key driver. Foreign stocks have also fared better and would have shown even stronger results for domestic investors absent the strength of the U.S. dollar, which acts as a headwind. Japan is a notable example on the positive side, with a strong sentiment shift due to fiscal tailwinds in process and transition away from negative interest rate conditions. Conditions in Europe have also seemed to improve, from a recessionary-like trough.

Whenever stocks rise by as much as 10% in a quarter—historically, a year's worth of returns—a reset of expectations is probably warranted. This is a good time for the periodic reminder that, on average, stock markets have historically corrected by -10% roughly once every 1-2 years, with -5% pullbacks happening a few times a year on average. Deeper bear markets of -20% are less frequent, approximately every 5-7 years, synched more in line with changes in business cycles. Currently, investor sentiment does not appear strongly positive, at least compared to past periods when exuberance was a prelude to a final push into too-expensive territory. At the same time, some periods of higher valuation can solve themselves. As earnings represent the long-term driver of stock market returns historically, improvement toward stronger earnings growth (FactSet expects an optimistic 10-15% each in 2024 and 2025 for the S&P 500), could well sustain positive momentum. While large cap growth has garnered the most attention as of late, smaller companies broadly have remained priced at discounts. Real estate investment trusts, which tend to be driven by interest rate changes in the short-term, continue to be priced at discounted levels. Contrary to public perception, office properties only represent a small piece of the commonly-tracked indexes (like the FTSE), with attractive growth originating less from 'classic' segments like residential and malls, but from 'modern' sectors such as data centers and cell towers.

Bonds continue to adjust from the past 15-or-so years when interest rates were minimal, tied to extremely low starting yields (including Fed funds of effectively zero from 2008-2015). While 2022 was a historically-painful reset for bonds, again scaring off some investors to the asset class, conditions have gradually normalized. Now, more 'historically-normal' 4-6% yield levels provide a stronger base for forward-looking results, raising the odds of better diversification and return contribution in the context of an asset allocation portfolio. Bonds have also historically fared well upon the final phases of a Federal Reserve pause and ultimate cutting cycle, with the impact of duration providing a tailwind. A smaller yield change in a 10-year Treasury is required compared to that in a 2-year to have the same price impact. That less-understood feature is an important reminder of the reinvestment risk involved with staying too long in cash, having benefited from 5% yields being an enticing reward. In the post-GFC era, many central banks have been joined at the hip, but this normalization may positively affect foreign bond markets as well, with a wider country-by-country divergence potentially providing more unique return opportunities.

Overall, considering the excitement surrounding several mega-cap U.S. growth stocks, and their accompanying richer valuations, a wide variety of other portfolio assets show appeal looking forward.

Market Notes

Period ending 3/29/2024	**1 Week %**	**YTD %**
DJIA	0.84	6.14
S&P 500	0.40	10.56
NASDAQ	-0.29	9.31
Russell 2000	2.60	5.18
MSCI-EAFE	0.13	5.78
MSCI-EM	0.45	2.37
Bloomberg U.S. Aggregate	0.23	-0.78

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
3/22/2024	5.46	4.59	4.20	4.22	4.39
3/29/2024	5.46	4.59	4.21	4.20	4.34

U.S. stocks continued their run of positive weeks, with the S&P 500 again reaching record highs. However, breadth has improved, with outperformance from the equal-weight version of the index and small caps outperforming mega-caps. Value and more defensive parts of the market led, with the largest gains spread between utilities, energy, financials, and healthcare—all near or over 2%. Technology was one of only two sectors with negative returns for the week, down over a percent. Real estate saw gains of over 2% for the week as well.

There appeared to be some negative impact early in the week by Tuesday's collapse of the Francis Scott Key Bridge in Baltimore, due to the potential negative effects on one of the busiest U.S. ports (particularly for autos), and secondary potential upward impacts on near-term inflation.

Foreign stocks gained as well, with Europe, U.K., and emerging markets all outperforming the U.S., while Japan lagged. It was noted that the U.K. officially moved into recession in Q4, upon a growth contraction of -0.3%. conditions elsewhere, though, such as in Germany and Spain, have improved a bit. Sentiment has also ticked higher—in fact the European Commissions' confidence gauge is now the highest it's been in two years. Emerging markets saw gains across the board. The Japanese yen has continued to weaken (to the lowest levels in over 30 years, in fact), despite recent small interest rate hikes, which would normally provide some support. It appears a continued dovish stance on 'easy policy' is the culprit, implying markets don't believe conditions will tighten significantly further.

Bonds saw minor gains as interest rates ticked down just slightly across the curve, with U.S. Treasuries and corporate credit providing similar returns. Foreign bonds were held back a bit by a stronger dollar.

Commodities gained almost across the board last week, led by precious metals and energy, while industrial metals were little changed. Crude oil rose 3% last week to $83/barrel. Ukraine has been intensifying its drone strikes on Russian refinery facilities, which reduces crude oil demand a bit, a downward influence, but has a more meaningful impact on negatively impacting supply of distillates (jet fuel, diesel, etc.), driving those prices potentially higher. Weaker U.S. drilling activity has also raised inventory concerns. A little-followed area of the commodities world (being only 0.3% of the S&P GSCI index), cocoa, has seen a spot price rise of over 130% year-to-date due to extremely weak harvests and crop disease in key African growing nations Ghana and Ivory Coast, which has led to shortages. Ironically, reports of illegal mining (in response to now higher prices for gold) have negatively impacted key growing areas.

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, House.gov, 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.