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Investment Institute

Market Commentary

Weekly perspective on current market sentiment **October 9, 2024**

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Last week's S&P 500 Index: +0.2%

Moving in the right direction, for now

Key takeaways

- As we see more Federal Reserve rate cuts and we move through the early months of next year, economic growth is likely to pick up.
- The moderate-growth, moderate-inflation environment we expect has typically been good for stocks.

The United States is now at somewhat of an economic crossroads where inflation and economic growth are slowing down and the Federal Reserve (Fed) has just started on what we expect to be a series of rate cuts that will last well into next year. The next couple of quarters are likely to show slower gross domestic product growth than has been the case so far this year. Given that, we have argued that the economy is late-cycle rather than in the early stages (early cycle) of an expansion as some other market pundits have suggested.

Late cycle, in our view, usually translates into churning, range-bound markets that exhibit a good degree of volatility. Just as we have seen in the bond market where prices appeared overly optimistic (yields were too low) a few short weeks ago, we see the equity market as richly priced for this moment in time and susceptible to downside from current levels. During the later stages of an economic cycle, it is usually a good idea to stick with higher-quality stocks and bonds. That is a key reason why we favor large-cap domestic equities over international equities and over mid and small caps.

A goal this year for our Strategy group has been to exercise patience and use pullbacks to add to equity positions in favored sectors such as Energy (most favorable), Industrials, Materials, Communication Services, and Financials. Corrections in stocks have been few and far between in 2024, but the brief downdraft in the S&P 500 (SPX) that occurred in early August in the wake of the weak July labor report allowed us the opportunity to adjust portfolio guidance. We prefer to move funds from short-term fixed income (our "parking spot") into stocks. We boosted our overweight to large caps and brought our small-cap position up to neutral after carrying an underweight position there for over two years.

Our analysis suggests that as we see more Fed rate cuts and we move through the early months of next year, economic growth is likely to pick up here at home. We think there is also some chance that developed international economies will see somewhat better performance in the second half of next year. The jury is still out, however, on emerging-market equities as China continues to try to stimulate growth as we remain unfavorable this equity class. Remember, around 41% of SPX revenues come from outside the U.S.

We see better growth next year pushing interest rates, and inflation, somewhat higher by year-end. A moderate-growth, moderate-inflation environment has typically been good for stocks. Our year-end target range midpoint for the SPX remains 6,000. Should uncertainty over the pace of Fed rate cuts or other geopolitical tensions result in downside volatility in stocks in the coming months, we want to consider that an opportunity to further increase exposure to equities in anticipation of better performance as we move through 2025.

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