Convergence Commentary

January 2024 Market Recap

Quick Hits:

- The S&P 500 reaches an all-time high.
- Quarterly GDP surprises to the upside.
- The market is anxious about the timing of rate cuts.
- Retail sales streak continues.

Market-Moving Highlights

The S&P 500 reached an all time high on Friday, January 19th, above its prior high of 4796.56 set on January 3rd, 2022. The slowdown in inflation, in addition to higher-than-expected growth, has created a positive environment for the equities. The market is currently entering a new stage, as the focus has shifted from rate hikes to rate cuts. This can be quite a choppy environment, as there is uncertainty whether the central bank could cut too late, causing a recession, or too early, causing inflation to re-emerge.

Two reports showcased the strength of the US economy in January. The Q4 2023 GDP expanded by an annualized 3.3%, much better than forecasts of 2%. Additionally, the US consumer keeps beating expectations, with retail sales rising by 0.6% month-over-month in December, higher than the 0.4% forecast. This strength is an encouraging sign for the US economy and lowers the chances of a recession in the near-term.

Inflation came in slightly hotter than expected with CPI at 3.4% year-over-year and 0.3% monthly. The expectations were for 3.1% and 0.1%. The higher inflation came from energy prices going down less than expected, as tensions rose in the Middle East with Houthi rebels attacking cargo ships. Core inflation came in on par at 3.9%. The Fed Chair Jerome Powell held a speech on January 31st, and he mentioned that the data is coming in good, and inflation is going down. However, there is uncertainty about the timing of the first rate cut, mostly due to higher-than-expected growth and a strong consumer. Therefore, a rate cut in March is unlikely.

January was a hot earnings month with big banks reporting mid-month and tech behemoths Microsoft, Apple, and Advanced Micro Devices reporting at the end of the month. Big banks have fared well, showing that they are in a good position to benefit from potential financial easing, while the big tech companies showed strong earnings growth, driven by enthusiasm in the sector. However, overall results were not as impressive so far as they were in the last couple of reporting quarters, with only 66% beating sales estimates by an average of 1.3%. While this might not seem like a bad number, it is important to remember that companies estimate conservatively in order to please shareholders. However, companies benefited from margin expansion as they improved efficiency, with 79% beating earnings by an average of 6%.

Index Performance

Index	1 Month	YTD	1 Year	5 Year
S&P 500	1.68%	1.68%	20.82%	14.80%
Nasdaq Composite	1.04%	1.04%	31.99%	16.80%
Russell 2000	-3.89%	-3.89%	2.40%	6.80%
MSCI ACWI ex US	-0.98%	-0.98%	6.42%	5.83%
Bloomberg US Aggregate Bond	-0.27%	-0.27%	2.10%	0.83%

The last day of the month caused the major US indexes to tumble around 2% after the Fed meeting on January 31st. Regardless, after an ecstatic end of the year in December, it is good to see a solid January. The labor market remained strong, while quarterly GDP growth surprised to the upside. Treasury rates initially nudged higher but ended the month flat, with investors weighing the risks of accelerating economy reigniting inflation. While in January the S&P 500 reached a new all-time high, it was mostly the growthier names of the so called "Magnificent Seven" that outperformed, while the broader market was down slightly. Small cap stocks of the Russell 2000 index were down -3.89% for the month; however, it is important to remember that in December the index was up 14%. On the international side, Japanese and Indian equities continue their strong performance while Chinese equities struggled, amidst the factors at play that were laid out in our December commentary. The broader developed and emerging markets were down slightly for the month of January.

S&P 500 Sector Highlights & Commentary

Best-Performing Sectors		Worst-Performing Sectors	
Communication Services	4.43%	Real Estate	-4.82%
Financials	3.09%	Consumer Discretionary	-4.41%
Health Care	2.93%	Materials	-3.89%

With growth showing major momentum, jobs not showing signs of weakness, and inflation still sliding, cyclical sectors remain the most sough-after. The appetite for entertainment has aided the communication services sector, with companies such as Netflix surprising to the positive. Big banks have had their earnings season mid-January and have delivered, with hopes of financial easing from the Federal Reserve aiding the performance. Health care benefited, as an increase in health care workers and innovation in medical devices provided a boost. On the worst-performing front, real estate has had quite a run in the last three months (up 20%), with hopes of pent-up demand reigniting the sector. Perhaps some consolidation is behind the underperformance. The consumer discretionary sector has a large weighting in Tesla (14%), which suffered a 25% drop due to a poor quarter. Materials suffered from a stronger dollar in the month of January.

What to Watch in February

Click here to read our reference guide for economic indicators.

02/01 – Manufacturing PMI
The ISM Manufacturing PMI improved slightly from 46.7 to 47.4 in December. It is still the 14th consecutive month of contraction for the sector. The forecast for the January reading calls for 47.6.

02/02 – Non-Farm Payrolls, Unemployment Rate
The US economy added 216,000 jobs in December, higher than the expectations of 170,000. Employment trended up in government, leisure and hospitality, health care, social assistance, and construction. Meanwhile, transportation and warehousing lost jobs. The Unemployment Rate held steady at 3.7% in December and is expected to continue to do so in January.

02/13 – CPI and Core CPI
The annual CPI went up from 3.1% to 3.4% in December as energy prices went down at a slower pace than expected. Core CPI declined from 4% to 3.9%.

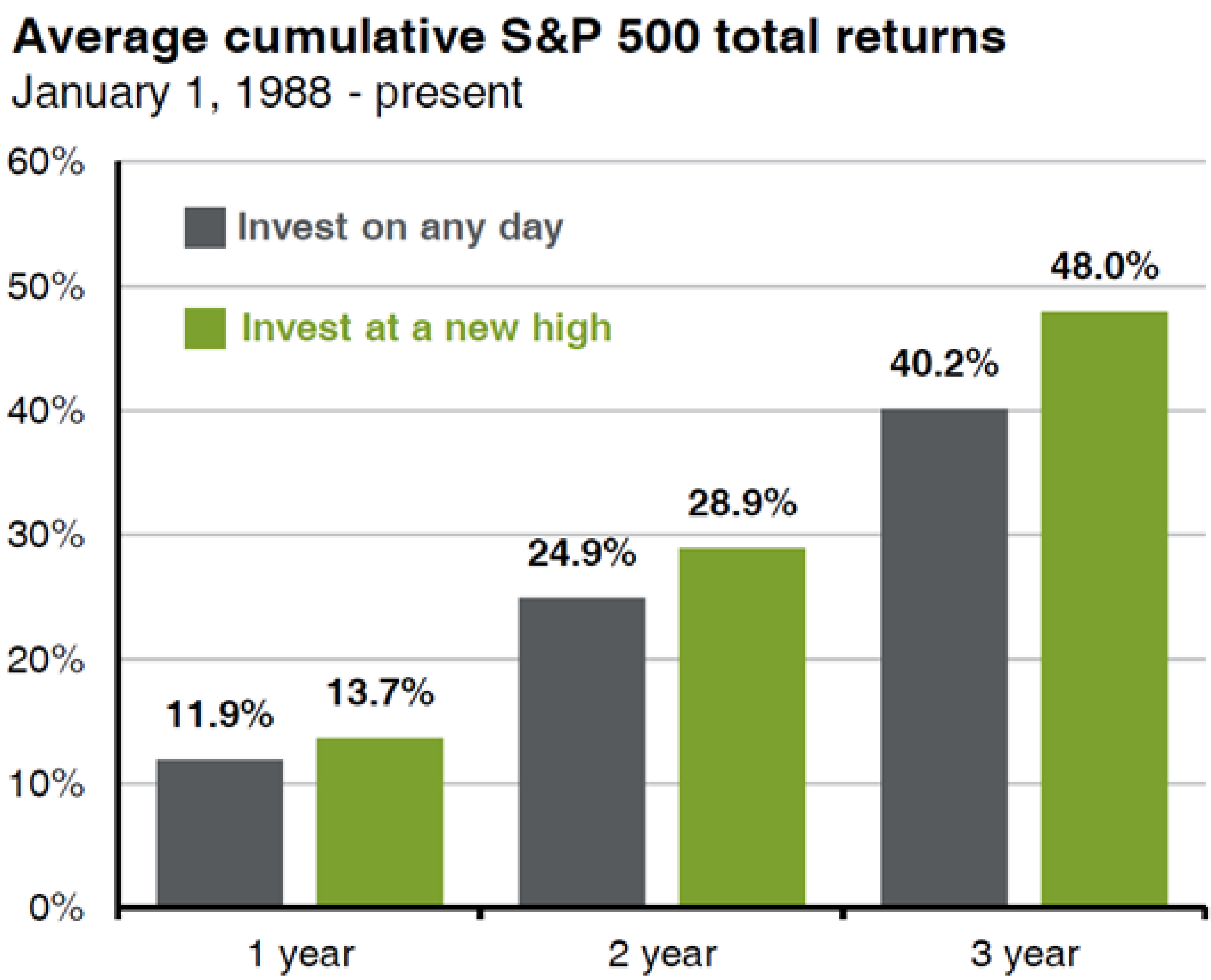
02/15 – Retail Sales
With the strong consumer being a large part of the reason why the US economy is beating expectations as of late, retail sales continue to be closely watched for any signs of deterioration of this strength.

02/16 – Michigan Consumer Sentiment Preliminary
The University of Michigan's consumer sentiment for the US soared from 69.7 to 78.8 in January 2024, which is the highest it's been since July 2021. Consumers gained confidence that inflation will become less of an issue, strengthening their income expectations.

02/21 – FOMC Minutes
The Federal Funds Rate remained unchanged in January with a fairly positive speech on the progress made while reiterating data dependency. However, after mentioning that the path ahead is uncertain, and a March rate cut is unlikely, the short-term market reaction was quite negative.

Market Wrap

With the S&P 500 closing at a new all-time high and a plethora of economic and earnings reports, January marked an eventful start to the year. The news of an all-time high can be a psychological factor, causing some investors to wait on the sidelines. The graph below shows what kind of returns buying at an all-time high would provide, versus buying at any day. The results show that investing at an all-time high would result in above average returns. While past returns do not guarantee future returns, it is a good reminder of how psychological bias can cause poor decision making.



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