2024 Midyear Outlook

What a start to the year it has been! The equity market surprised to the upside, with the S&P 500, Dow Jones Industrial Average, and Nasdaq indices all hitting record highs in 2024.

The S&P 500 is +15.08% and the Nasdaq is +20.02% year-to-date (as of 6/25/2024). This is an amazing return on the heels of a strong 2023, and many analysts are just now catching up to this bullish trend!

Will the momentum continue?

We think so. We expect volatility over the short-term, but believe we are in a long-term, secular bull market, and the stock market should continue to move in a positive direction despite potential short-term volatility.

In this commentary, we will recap what has happened year-to-date and what we expect for the remainder of the year.

April showers brought May flowers, and then some....

The adage, "sell in May and go away" did not ring true in 2024, as many stocks (e.g., Apple, Microsoft, Google, and Broadcom) set new highs in May, and then again in June. This can be attributed to better-than-expected Q1 earnings, and favorable economic data.

So, why do we expect short-term volatility? We believe parts of the equity market are approaching overbought conditions. This normally leads to an increase in volatility and potentially a correction in stock prices. Stock prices eventually realign with their intrinsic value, and then go on to set new highs if they continue to grow earnings.

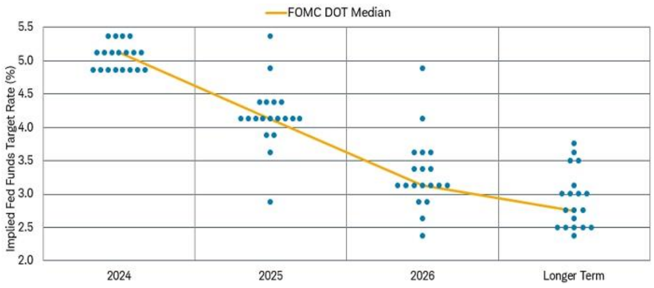
As we predicted in our Q1 market outlook, we saw the S&P 500 decline 5% in April and then eventually set new highs in May. This is a normal and healthy process for the stock market.

Historically, the S&P 500 pulls back 5% roughly 3 times per year, and 10%about every 16 months, when examining the index's historical performance from 1942[1].

Our medium- and long-term view is bullish, so we view short-term pullbacks as a buying opportunity for high-quality companies.

But what about inflation and interest rates?

Members of the Federal Open Market Committee (FOMC) published their anonymous forecasts in a "dot plot" at their June meeting, suggesting there may be only one quarter-point interest rate cut by the end of 2024. The dots in the chart below represent each member's interest rate projection for a given year.



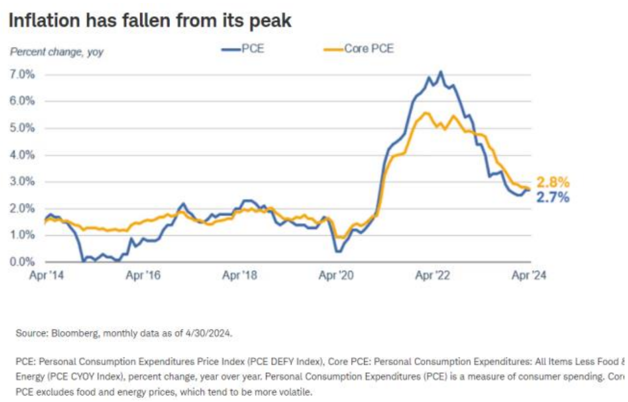
As of this week, the market participants are expecting the first rate cut in September, with a 64% probability[2].

[1] Bloomberg, 4/29/1942 – 3/28/2024

[2] CME FedWatch Tool 6/26/24

What will prompt the Federal Reserve to finally cut rates? Federal Reserve Chair Jerome Powell continues to state the FOMC wants full confidence that inflation is trending sustainably lower prior to cutting interest rates. That likely means several months of disinflationary data.

While inflation rates have gradually decreased, they are decreasing at a slower rate than expected, which is causing the FOMC to be very patient and deliberate with their monetary policy.

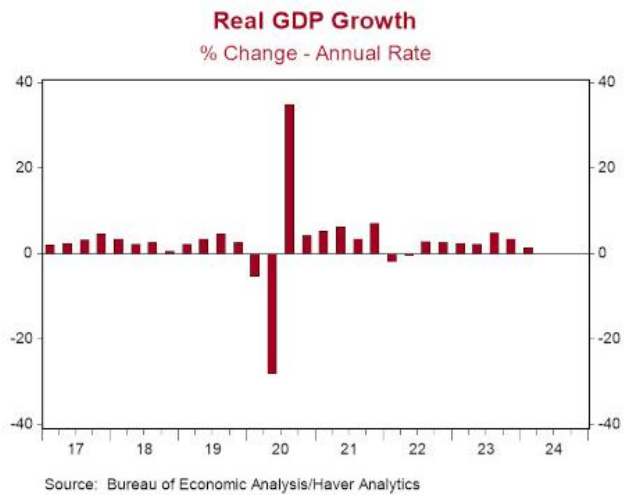


The Federal Reserve's target of 2% (annualized) for the core Personal Consumption Expenditure (PCE) Price Index has been difficult to achieve. All eyes will be on May's PCE data which will be released on Friday, June 28. If the inflation data is materially higher than expected, then we will likely experience volatility in the stock market. If the inflation data is lower than expected, then we could experience another rally in the stock market.

While many investors are eager for a flurry of interest rate cuts, we favor a gradual and planned course of interest rate cuts. Why? Cutting rates quickly would be a sign of significant deterioration (or "breaking") in the economy which could be more troubling than inflation running at 3% (annualized) vs. the Fed's 2% (annualized) target. Cutting rates prematurely could spur additional inflation.

Are we going into a recession?

While economic growth (as measured by Gross Domestic Product) has slowed over the last few quarters, this was expected given the higher interest rate environment over the last two years. The Federal Reserve's restrictive monetary policy is having its intended consequences on the economy.



Initial jobless claims are increasing, averaging ~240,000 in the last two weeks, compared to an average of ~210,000 in Q4 2023 and Q1 2024[3]. Unemployment rates have increased from 3.9% to 4.0%. Meanwhile, retail sales data came in worse than expected, rising only 0.1% in May (including sharp downward revisions to prior months) vs. a consensus expected increase of 0.3%[4]. There has also been a softening in the housing sector, with single-family and multi-family starts declining 5.5% in May[5]. There simply is not enough home supply to meet the demand… hence elevated home prices.

[3] First Trust Monday Morning Outlook 6/24/24

[4] First Trust Data Watch 6/18/24 – Bureau of Census

[5] First Trust Data Watch 6/20/24 - U.S. Census Bureau

So, what does all this mean for investors? A gradual slowing of the economy, along with a gradual decline in inflation could give the Federal Reserve the confidence to cut rates soon.

Where do we go from here?

Looking ahead, we expect the stock market to continue to perform well overall, with potential volatility over the short-term. Seasonality historically favors stocks throughout the summer, with September having the lowest average monthly returns in the S&P 500 since 1950.

As stated previously, we believe we are in a secular bull market underpinned by the next revolution in technology – Artificial Intelligence (AI). Admittedly, as investors, it is difficult to fully grasp the impact of AI on the economy and the stock market. We are in the early stages of AI, and we believe AI will be the catalyst for an enormous paradigm shift that will fundamentally transform the way we live and do business. Exciting times lie ahead, and we aim to stay at the forefront of this innovation.

Q2 earning season is just around the corner (July). We believe corporate earnings are the most important driver for the equity markets. Earnings continue to grow this year with an 8% growth rate in Q1, and earnings estimates continue to rise[6]. S&P 500 profit margins have remained stable, landing at 11.5% for Q1, despite sticky inflation and elevated interest rates[7].

Earnings season is always an exciting time for investors. Earnings reports let us know how companies performed over the prior quarter, and more importantly, what lies ahead – both opportunities and challenges. We expect the major themes for Q2 earnings reports will be AI-related capital expenditures and the strength of the consumer.

What about the election?

As we near the presidential election in November, it's important to note that historical data suggests economic and inflation trends, more so than election outcomes, tend to have a stronger, more consistent relationship with stock market returns.

Since 1926, stocks have continued higher, regardless of which party has been in the White House. In fact, the S&P 500 has averaged 11.6% in presidential election years since 1926[8].

If you are interested in more election-related and Washington D.C. insights, be on the lookout for our next quarterly webinar on October 24th with Scott Eckel, Legislative and Regulatory Affairs Managing Director at Charles Schwab.

As always, thank you for placing your trust in our team. It is a responsibility we do not take lightly. If you have any questions or if there is anything else we can be doing for you, please reach out to our team.

Wishing you and your family a happy Fourth of July!

- Evans May Wealth

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[6] Standard and Poor's, Sanctuary Wealth, June 2024
[7] Standard and Poor's, Sanctuary Wealth, June 2024
[8] Morningstar as of 12/31/23. Stock market represented by the S&P 500 Index from 1/1/70 to 12/31/23 and IA SBBI U.S. large cap stocks index from 1/1/26 to 1/1/70