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Market Update

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As a follow up to our brief market update published on August 5, 2024, I wanted to provide some more color on the recent volatility to hit the markets.

The sell-off across global financial markets that began on July 16, 2024 and accelerated over the last 3 trading days as of August 6, 2024, per FS Insight, has resulted in:

- S&P 500 has declined by -6.68%
- Nasdaq by -8.22%
- S&P 500 Equal Weighted Index -5.81%

In this time, the market's so-called fear-index, the VIX, had an intra-day high on 8/5/24 that has not been seen since the Spring of 2020 during the early days of the Pandemic. The primary cause of this volatility can be boiled down to one leading factor, a Growth Scare, which is occurring right now for the following reasons: [1]

- Continued contraction in the manufacturing sector
- Rising unemployment rate, which now sits at 4.3%
- Disappointing corporate earnings reports
- Political uncertainty with a close Presidential race
- Geopolitical tensions, including escalating tensions in the Middle East and the Japanese Carry Trade

At the expense of an over-used cliché, we must keep our emotions in check and take a step back. Markets were previously priced for perfection, especially in the technology and AI sectors, leading to an overcrowded trade.

The recent economic data has been soft in some places but not across the board:

- Not all sectors have been affected. For instance, the services sector showed expansion in July, indicating continued consumer spending (source: Bloomberg).
- Certain sectors like Utilities, Consumer Staples, Health Care, and high-quality dividend companies performed well, and in some cases had positive returns even on down days. [2]

[1] *The 7's Report*

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[2] *The 7's Report*

For the first time in years, fixed income is proving to be a valuable non-correlating asset class. As we have noted here in the past, we believe the market was seriously overlooking opportunities in long duration, high quality fixed income. Due to over-elevated real interest rates on some parts of the Treasury Market, there has been the opportunity to lock in higher yields and provide for a higher total return through capital appreciation as yields begin to fall.

- The 10-Year Treasury Rate dropped from 4.48% on July 1, 2024, to 3.76% as of yesterday, 8/5/24, a decline of 0.72 basis points or 16%. [3]

In the near-term, there are several indicators that are signaling a level of capitulation, especially, the VIX, and my favorite indicator, the CNN Fear/Greed Index: https://www.cnn.com/markets/fear-and-greed

It's worth noting, August is seasonally a tough month, especially after such a strong start to the year. The good news is, per Bloomberg, when the first 7 months of the year are up over 10%, and August has a negative return, there is still an 83% chance the markets will be even higher at year-end.

Finally, we must not forget the elephant in the room, the Federal Reserve. Right now, markets have priced in a total of 1.25% in rate cuts by year end! This includes a .50% cut by the Fed in September while the probability of .75% September rate cut has been increasing. That is a significant change and one that should not be ignored. In fact, the inversion on treasury yields, which is when short term rates are higher than long term rates, has largely disappeared over the last month. This is an important signal of lower rates to come and should benefit small and mid-sized companies that rely heavily on borrowing. [4]

There is much more going on that we simply can't cover in this update but if you have any questions or concerns about how your portfolio is positioned for both risk and opportunity, please feel free to reach out to me or any member of our team to schedule a review.

Thank you for your time and attention to this update.

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Regards,
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https://youtu.be/URCkH5TQpa4?si=TzpkZdtKEvQnWDio

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