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ARGUS ECONOMIC COMMENTARY

April 22, 2024

Strong First Quarter but Market Technicals send Red Flags

Following its best first quarter in five years, the S&P 500 is down in April. The trading week of 4/8-4/12/24 was the worst since March 2023, when the stock market was trying to decide if it was going to replicate a poor 2022 or embark on a new rally phase (fortunately, the latter won out). As of mid-month, the S&P 500 was down 1.8%.

Although poet T.S. Elliot named it the "cruelest month," April is actually positive for stocks in most years. Since 1980, the S&P 500 has been positive 67% of the time. More significantly, the average April gain on the index over that time span is 1.70%, which is the second best of any month in the year. November is the best.

The problem with this particular April, as in earlier periods of stock weakness, has been the rising trend in interest rates. Data from March released in April includes the nonfarm payrolls report and CPI and PPI inflation; all were regarded as running "too hot" for comfort. Those data points pushed yields higher. Over the course of April, the two-year Treasury yield rose from 4.72% to begin the month to 4.93%, and the 10-year rose to 4.56% from 4.33%.

The strong jobs and inflation data also caused the market to recalibrate the timing of any rate cuts by the Federal Reserve. Volatility has definitely increased, with the VIX closing on 4/12/24 at its highest level since October 2023.

Environment: First-Quarter 2024

The U.S. stock market extended fourth-quarter 2023 momentum into 1Q24, with broad index and sector strength. After a sharp November-December 2023 surge as both interest rates and energy prices declined, the S&P 500 advanced 10.2% on a capital-appreciation basis in 1Q24 (10.6% on a total-return basis with dividends). From 4,193 at the end of October 2023, the S&P 500 rose by more than 25% to 5,254 at the end of 1Q24. While cheering the advance, investors also grew concerned that FOMO (fear of missing out) was driving 5% average monthly gains over that span.

The Fed held rates steady at its March 19-20, 2024, meeting, as it has done at every FOMC meeting since July 2023. Following the March meeting, the Fed appeared to ignore the back-sliding in February CPI inflation, as it remained on its path to cutting rates – just as it repeatedly ignored better-than-anticipated inflation readings during its rate-hiking campaign of the past two years.

The annual change in the core PCE price index was 2.8% in February, level with 2.8% in January, while the annual change in the all-items PCE was 2.5% in February, up from 2.4% in January. All-items and core PCE inflation have been range-bound in recent months, as progress on inflation has slowed.

The Fed started to hike rates two years ago based on the perception that pricing pressures were mainly tied to the supply-chain crisis and could be quickly subdued. Stubbornly high costs for shelter and other service components have underscored that inflation is about far more than the supply chain. The February PCE inflation readings, however, were a reminder that prices can creep higher in any area. In the February all-items PCE price index, prices for goods (up 0.5%) rose faster than prices for services (up 0.3%). Interest rates worked down in the final two months of 2023 as inflation eased, energy prices plunged, and the bond market rallied in anticipation of as many as six rate cuts in 2024.

The 10-year Treasury yield ended December 2023 at 3.88%, its lowest level since July. The five-year yield was 3.84% at December-end, and the two-year Treasury yield

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ended 2023 at 4.23%. During the first quarter of 2024, however, investors confronted stubborn inflation, impacted by rising food and energy costs, and dialed back expectations for Fed rate cuts in 2024. From 3.9% at the beginning of 2024, the 10-year Treasury yield worked up to 4.36% as of the 1Q24 close. The two-year Treasury yield was 4.72% as of 1Q24-end, and has maintained its 30-40 basis point (bps) premium to the 10-year yield.

After showing signs of moderation for most of 2023, the jobs economy strengthened at year-end 2023 and into the first quarter of 2024. Nonfarm payrolls for February 2024 increased by 275,000, meaningfully above the consensus call of 200K and the Argus forecast of 185K. The trailing three-month average of 265,000 new payroll jobs through February was above the 12-month average of 230,000. Unemployment ticked up to 3.9% for February, after holding at 3.7% from November 2023 to January 2024. While that may not seem like much of a change, 3.9% is the highest level since January 2022. Average hourly earnings in February 2023 increased 4.3% year-over-year. The slight increase in the average workweek and rising hourly wages means that individual paychecks are growing faster than inflation, as they have been for about a year.

The industrial economy is still growing. For the first time in over a year, supply-chain executives in the manufacturing sector expressed cautious optimism. For March 2024, the ISM manufacturing PMI came in at 50.3%, up 2.5 percentage points from 47.8% recorded in February. ISM's manufacturing PMI had remained below 50% from September 2022 to February 2024, or for 16 months. After several years of adding workers as fast as they could, manufacturers are now engaging in targeted, rather than broad, layoffs. With companies doing more with less, output – measured by the production and employment indices – had a combined 7.7-percentage-point upward impact on the manufacturing PMI calculation. The ISM services PMI for March showed expansion in the services sector for a fourteenth consecutive month – important, given that the services economy is several time the size of the manufacturing economy. Signals from the consumer economy remain mixed. As reported in mid-March, retail sales rose 0.6% in February, up from a 1.1% decline for January. Retail sales ex-autos and gasoline were up 0.3%. Consumer sentiment and consumer confidence both closed year-end 2023 below peak levels reached near mid-year, and have been little changed in 2024 to date.

S&P 500 earnings for 4Q23 (reported from mid-January to mid-February) rose in high-single-digit percentages year-over-year, marking a second consecutive quarter of annual EPS growth as well as acceleration from low-single-digit growth for 3Q23. Around 80% of companies exceeded consensus expectations for 4Q23 EPS versus 70%-75% on average. The magnitude of the beat was at the high end of the 5%-8% historical range.

Fourth-quarter 2023, GDP grew at a 3.2% annual rate. Personal consumption expenditures (PCE) for 4Q23 increased 3.0% while non-residential fixed investment (a proxy for corporate capital spending) jumped 3.7%. Together, these two components make up about 83% of GDP. According to the BEA's preliminary estimate, GDP grew by 2.5% in 2023. GDP growth in 2023 signaled economic expansion at a solid pace, reflective of modest improvement in productivity and slow population growth.

In an unusual development, the S&P 500 finished 1Q24 a few ticks ahead of the Nasdaq Composite. For the S&P 500 to outpace the growth-heavy Nasdaq, as it did in 1Q24, many more sectors have to be rising – and they did in January through March 2024. For 1Q24, the best sector performance in the S&P 500 came from Communication Services, up 12.4%. Tied for second place in 1Q24 were Financial Services and Energy, both up 12.0%. Technology appreciated 10.0% in 1Q24, which put it just behind the market's 10.2% capital-appreciation gain and just ahead of the Industrial sector (up 9.9%). Healthcare logged 8.1% appreciation in 1Q24, as the medical profession continues its prolonged transition out of the post-pandemic phase. Three sectors – Consumer Staples, Materials, and Utilities – delivered 5%-7% capital appreciation in 1Q24. Consumer Discretionary, one of the better performers in 2023, was eleventh among 11 sectors in 1Q24. The Wall Street narrative is that inflation is in retreat, the economy is strong, and people are employed. Yet the average consumer is wallet-constrained after two years of inflation.

In broad terms, the 2023 gain in stocks was positive, but it was also too narrow. Three sectors – Communication Services, Technology, and Consumer Discretionary – accounted for all of the 2023 market advance. None of the other eight sectors beat the overall market for 2023. After a worrisome level of AI-driven sector concentration in 2023, much-better breadth in 1Q24 can help extend any gains into coming months and quarters, in our view.

Conclusion

After rising more or less steadily from the end of October 2023 to the end of March 2024, the S&P 500 stumbled through mid-April. On the way up to the end-of-March peak, the index engaged in a pattern of higher highs off higher lows, as investors repeatedly bought any dips. "Hot" jobs and inflation data sent rates higher and caused investors to rethink the timing and magnitude of any shift in Fed policy from restrictive to accommodative.

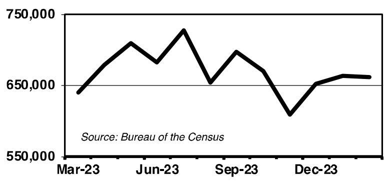
The S&P 500 closed on 4/12/24 sitting right atop its 50-day simple moving average (SMA). The index was last in that danger zone on 11/9/24, right before embarking on its five-month, 30% rally. Stocks rose on tax day (4/15/24) to provide some temporary relief.

Where the market goes from here will be influenced by external events, such as worsening strife between Israel and Iran. However, we continue to believe the market's main drivers will remain economic fundamentals, including earnings, economic growth, interest rates, and inflation.

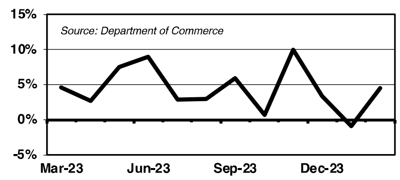
Jim Kelleher, CFA,
Director of Research

ECONOMIC TRADING CALENDAR

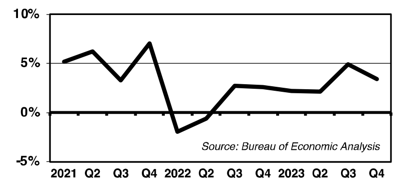
Release: **New Home Sales**
Date: 4/23/2024
Month: March
Previous Report: 662000
Argus Estimate: 672000
Street Estimate: NA



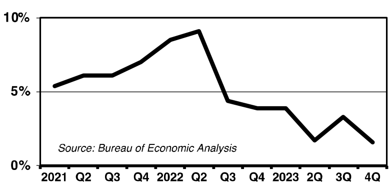
Release: **Durable Goods Orders**
Date: 4/24/2024
Month: March
Previous Report: 4.5%
Argus Estimate: 4.8%
Street Estimate: NA



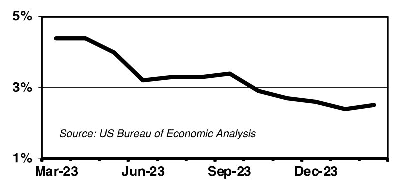
Release: **GDP Annualized QoQ**
Date: 4/25/2024
Month: 1Q
Previous Report: 3.4%
Argus Estimate: 2.4%
Street Estimate: NA



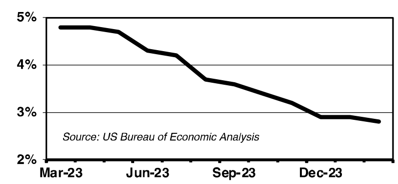
Release: **GDP Price Index**
Date: 4/25/2024
Month: 1Q
Previous Report: 1.6%
Argus Estimate: 2.8%
Street Estimate: NA



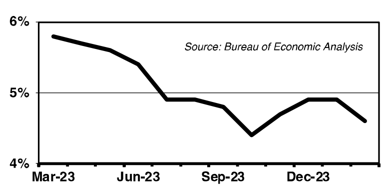
Release: **PCE Deflator**
Date: 4/26/2024
Month: March
Previous Report: 2.5%
Argus Estimate: 2.7%
Street Estimate: NA



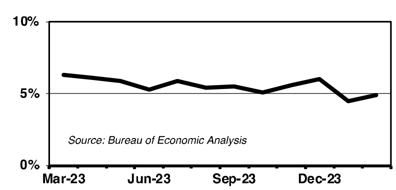
Release: **PCE Core Deflator**
Date: 4/26/2024
Month: March
Previous Report: 2.8%
Argus Estimate: 2.8%
Street Estimate: NA



Release: **Personal Income**
Date: 4/26/2024
Month: March
Previous Report: 4.6%
Argus Estimate: 4.7%
Street Estimate: NA



Release: **Personal Spending**
Date: 4/26/2024
Month: March
Previous Report: 4.9%
Argus Estimate: 5.0%
Street Estimate: NA



Previous Week's Releases and Next Week's Releases on next page.

ECONOMIC TRADING CALENDAR (CONT.)

Previous Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
15-Apr	Retail Sales	March	**2.1%**	1.3%	NA	**4.0%**
	Retail Sales ex-autos	March	**2.0%**	1.0%	NA	**4.3%**
	Business Inventories	February	**0.5%**	0.6%	NA	**1.0%**
16-Apr	Industrial Production	March	-0.2%	0.1%	NA	NA
	Capacity Utilization	March	78.3%	78.5%	78.5%	NA
	Housing Starts	March	1,521 K	1,350 K	NA	NA
18-Apr	Leading Index	March	0.1%	0.1%	NA	NA
	Existing Home Sales	March	4.38 Mln.	3.90 Mln.	NA	NA

Next Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
30-Apr	Consumer Confidence	April	104.7%	NA	NA	NA
1-May	ISM Manufacturing	April	50.3	NA	NA	NA
	ISM New Orders	April	51.4	NA	NA	NA
	Construction Spending	March	10.7%	NA	NA	NA
2-May	Trade Balance	March	-$68.9 Bil.	NA	NA	NA
	Factory Orders	March	1.0	NA	NA	NA
	Nonfarm Productivity	1Q	3.2%	NA	NA	NA
	Unit Labor Costs	1Q	0.4%	NA	NA	NA
3-May	Nonfarm Payrolls	April	303 K	NA	NA	NA
	Unemployment Rate	April	3.8%	NA	NA	NA
	Average Weekly Hours	April	34.4	NA	NA	NA
	Average Hourly Earnings	April	4.1%	NA	NA	NA
	ISM Services Index	April	51.4	NA	NA	NA

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