Wealth Advisory Market Update

December 4, 2023

Market Update

Equities

In November, the S&P 500 index demonstrated robust performance, surging by 8.9% and marking its most impressive monthly gain since October of last year. This brings the year-to-date performance to 18.9%. This positive momentum is attributed to a substantial drop in bond yields and optimism regarding a soft landing.

Macroeconomic indicators reveal a slowdown as the U.S. consumer faces obstacles. The manufacturing sector has experienced contraction for thirteen consecutive months, suggesting stagflation as prices increased while orders and employment declined. Survey data in the manufacturing sector further predicts a challenging economic landing.

The equity market currently relies heavily on the performance of the "Magnificent Seven," with the current surge driven by multiple expansions rather than earnings growth. Anticipating an economic slowdown, we advocate for adhering to a disciplined approach by investing in defensive companies with strong balance sheets, inelastic demand, robust cash flow, and a history of resiliency during economic downturns.

Economic Indicators and Monetary Policy

Concerning signs continue to emerge, with consumers taking on more debt during Black Friday shopping. Buy-now-pay-later purchases surged by 47% from the previous year, and indications of financial strain include a rise in credit card delinquencies and a 27% increase in 401(k) hardship withdrawals since the beginning of the year.

The labor market adds to these concerns, as continuing jobless claims reach their highest level since November 2021. This, in turn, is exerting pressure on the housing market, with pending home sales reaching their lowest point since tracking began in 2001. Geopolitical risks remain elevated, with conflicts in the Middle East and Ukraine posing potential market shockwaves.

The Federal Open Market Committee (FOMC) did not meet in November, although numerous Fed speakers shared insights. Market forecasts predict a series of rate cuts, starting as early as March. Chairman Jerome Powell emphasized a data-driven decision-making approach while acknowledging the current inflation levels. His press conference maintained a dovish tone, expressing caution and suggesting the Fed has not yet overcome economic challenges.

Unlike the FOMC, we believe the economy is on shaky ground with a recession looming in the coming quarters. The consumer's precarious state, as mentioned, paints a troubling picture, and the Fed’s swift rate hiking portends a recession.

Strategy

In response to the economic slowdown and increasing recession risks, our strategy remains a defensive stance in equities, favoring large-cap companies with inelastic demand, pricing power, and historical resilience during recessions. In the fixed-income landscape, declining yields and rising prices lead us to extend duration in portfolios, particularly in seasoned Mortgage-Backed Securities (MBS) with attractive spreads and appealing risk-return profiles. Our main focus in fixed income is staying in high quality credits.

As we navigate this challenging environment, we appreciate your support and the opportunity to collaborate in achieving your financial goals.

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