Weekly Market Insights

November 18, 2024

A State of Confusion

Financial Markets

Equity markets have been in a state of confusion these past two weeks. Markets rallied strongly after Donald Trump's decisive victory but experienced a decline of equal magnitude just one week later.

	Total Return (%)		
Index	**Prior Week**	**Year-to-Date**	**1-Year**
S&P 500	-2.05	24.56	32.22
S&P 500 Equal Weighted	-1.68	16.27	26.85
Dow Jones Industrial Average	-1.24	17.11	26.59
NASDAQ Composite	-3.13	25.20	33.39

The markets fell over a fear of higher interest rates, which has been the principal mover of U.S. markets for some time now. Short-term interest rates tend to act as a thermometer for the economy, and last week, we saw stronger-than-expected retail sales data, an upside surprise to the Producer Price Index (PPI), and a Consumer Price Index (CPI) reading still stubbornly above the Fed's 2% inflation target. To compound the matter, on Thursday, Federal Reserve Chairman Powell told investors that the Fed could afford to be more cautious in determining whether to cut rates in December.

Fixed-income markets also fell in price as interest rates moved higher. This is a reminder to readers that one of the fascinating things about markets is they're often the first to show the fears and elations of a population. In the case of the last two weeks, markets may have overreacted.

Economics

It is challenging to discuss the economy's future because there is considerable confusion coming from the president-elect's camp. Even so, the United States economy appears to be in very good shape—the best in the developed world. Regarding the economy's future, an obvious point of discussion is tariffs. Mr. Trump has said he will impose tariffs, some high and some not so high. Although nothing is certain, companies in the U.S. and abroad are taking action to protect themselves. Tariffs will likely have an inflationary impact on the global economy. When most Americans think of imposing tariffs, they automatically think of China. That is an error. Certainly, tariffs on China will be the most significant, but our trading partners and allies will also be facing increased tariffs.

Aside from tariffs, China remains the most interesting country globally. Of course, China has many documented economic problems. Not long ago, the country's leadership held a weeklong meeting to conclude how to solve those problems. Well, they did, and they didn't. They had the meeting, but they didn't solve the problem. Their solution was to issue a tremendous amount of debt, and while these actions will benefit some in the short run, the underlying problem remains unsolved.

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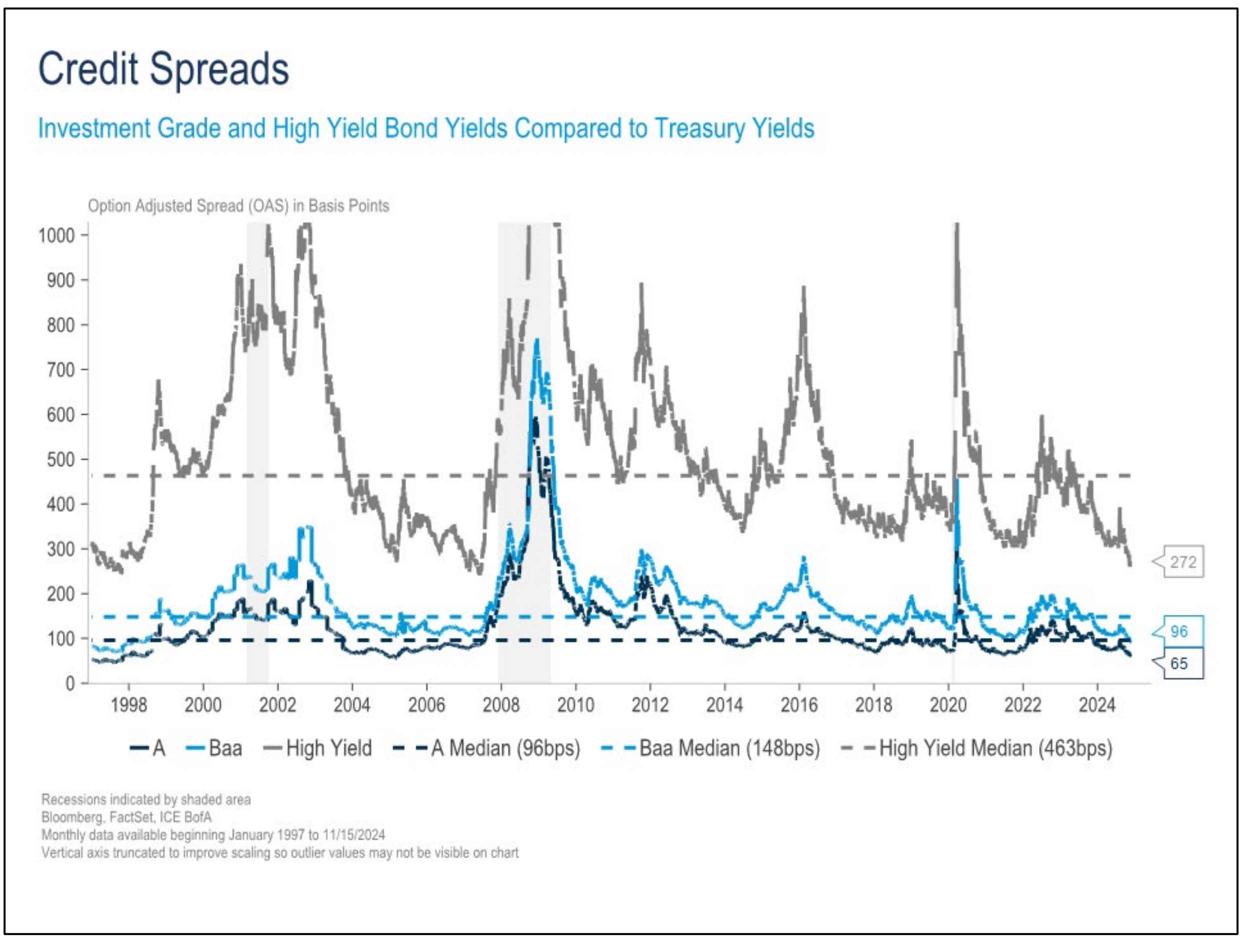
Credit Spreads Update

A few weeks ago, we introduced the topic of credit spreads—the additional yield investors gain for taking on credit risk. Spreads were tight a few weeks ago, and they've only tightened more since. Over the past three weeks, the spread between BBB-rated corporate bonds and comparable credit-risk-free Treasuries tightened by 6 basis points, while high yield spreads tightened by 17 basis points.

Credit spreads tend to fluctuate with changes economic conditions, narrowing during periods of economic growth and widening during periods of economic weakness and/or recession. The latest moves have been consistent with the former, with spreads grinding lower as U.S. economic indicators continue to point to a robust labor market, resilient consumption, and a growing economy. Over the last few weeks alone, both retail sales and consumer spending surprised to the upside, 2nd quarter GDP topped consensus estimates, the unemployment rate held at 4.1%, and unemployment claims fell to the lowest level since May of this year—a very strong economic backdrop to say the least.

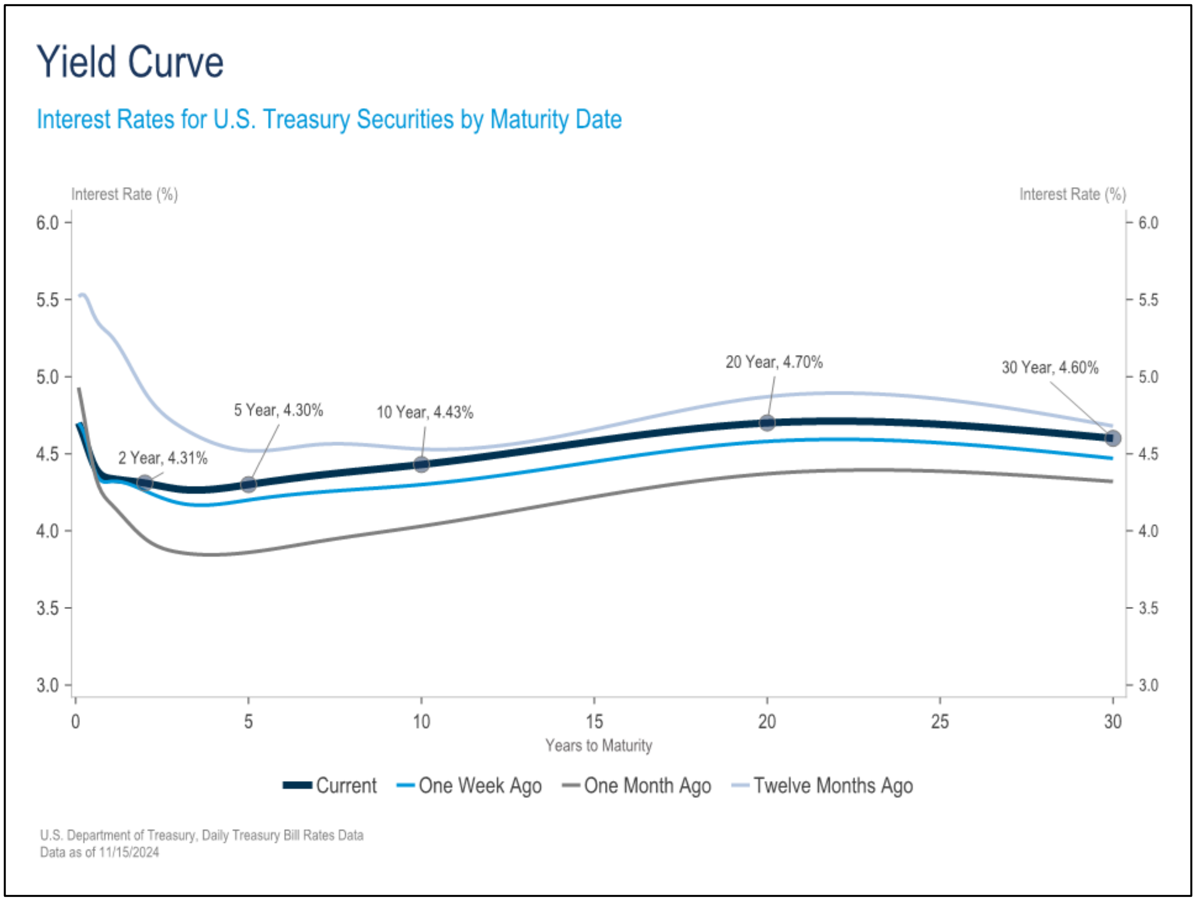
Readers may be left asking where spreads go from here? There's no debating that spreads are very tight. With little runway for further tightening, we can expect to see some degree of spread widening in the future. The questions are when and what will the catalysts be? Default rates are low, and the economic outlook remains strong. So, as it stands now, weakening fundamentals are unlikely to be the reason. Instead, technical factors may start to play a role, with waning demand causing spreads to drift higher. The crystal ball is always cloudy, but we will continue to keep readers abreast of what develops.



	Credit Ratings		
	S&P	**Moody's**	**Fitch**
Investment Grade	AAA	Aaa	AAA
	AA	Aa	AA
	A	A	A
	BBB	Baa	BBB
High Yield/Junk	BB	Ba	BB
	B	B	B
	CCC	Caa	CCC
	CC	Ca	CC
	C	C	C
	D	D	D

Conclusion

As we wrote earlier, discussing the economy's future with so much uncertainty surrounding the incoming president's cabinet selections is challenging. What has not changed is that the U.S. economy remains the strongest in the developed world. With political and economic difficulties, France and Germany continue to weigh down the European Union. Hopefully, next week we will have more information to work with and more insight to share.



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