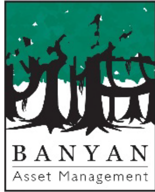


# "History Rhymes"

## Market Commentary – March 2024

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**The second estimate of Gross Domestic Product (GDP) shows that the output of goods and services produced by labor and property located in the U.S. grew at an annual rate of 3.2% in the fourth quarter of 2023.** This is lower than the advance estimate of 3.3% and the 2023 Q3 reading of 4.9%. Inflation has been relatively under control over the past eight months, although it remains a bit elevated. The Consumer Price Index (CPI), which measures inflation in consumer prices, peaked at 9.0% in June 2022 and hit 3.1% in June 2023. Since then, CPI has bounced between 3.1% and 3.7%, measuring 3.1% in January 2024. The Producer Price Index (PPI), which measures inflation in producer prices, peaked at 11.1% in June 2022 and hit 0.3% in June 2023. Since then, PPI has hovered between 0.3% and 1.9%, measuring 0.9% in January 2024. Meanwhile, unemployment came in at only 3.7% in January 2024, having been below 4.0% since January 2022. The Federal Reserve seeks to "achieve maximum employment and inflation at a rate of 2 percent over the longer run". While unemployment readings have been consistently low over the past eight months, inflation needs to cool a tad to meet the Fed's objectives.

**With the benchmark federal funds rate at a target range of 5.25% to 5.5%, futures markets now see the Federal Open Market Committee (FOMC) waiting until July to implement its first 0.25% cut.** One month ago, the first cut was expected by May, so market participants are expecting the Fed to delay the start of the cutting cycle. Futures markets still believe the Fed will slash the rate by 1.75% in the next cycle, which implies a new range of 3.5% to 3.75%. Meanwhile, the Fed's balance sheet had $7.582 trillion in assets on February 21, down $95 billion from $7.677 trillion in assets on January 24 (in-line with the Fed's commitment of $95 billion per month). The next FOMC announcement on monetary policy is scheduled for March 20.

**Technical factors of the market are bullish (more demand than supply), while fundamentals are fairly priced – therefore, we are mildly bullish on the market.** The Standard & Poor's forecast for S&P 500 operating earnings per share (EPS) through December 31, 2024 is $240.18, which implies a price-to-earnings (P/E) ratio of 21.2 with the S&P 500 at 5,096. The earnings yield (E/P) of 4.71% represents fair value relative to the 10-year U.S. Treasury note yield of 4.25%. The yield spread is 0.46%. Seven of the nine largest companies in the S&P 500 make up $13.3 trillion of the $44.9 trillion index market capitalization with a weighted P/E of 31.3. If 29.7% of the index has a P/E of 31.3, then 70.3% of the index has a P/E of 17.0 for the overall P/E to be 21.2. A P/E of 17.0 is an E/P of 5.89%, which is fairly priced compared to the 10-year Treasury note yield of 4.25% (a yield spread of 1.64%).

**The S&P 500 defied signs of technical weakness at the end of January to power ahead in February, driven by the popularity of mega-cap technology and growth stocks.** The S&P 500 pierced 5,000 for the first time, closing at an all-time high of 5,096 on February 29. Recall that the index corrected by 10% between July and October 2023, only to rally more than 23% off the October low. Stocks are ripe for a correction, although momentum right now points higher. A pullback to the January 2022 high near 4,800 would be logical, while the 200-day moving average is a more painful 11% away at 4,523. The longer stocks go without a correction, the steeper the eventual correction may be.

**In the spirit of Mark Twain's famous quote that "history doesn't repeat itself, but it often rhymes", the current mania in mega-cap technology stocks, and growth stocks in general, rhymes with the late-1990s tech stock bubble.** The financial press hypes the future of "A.I." (artificial intelligence). Financial TV channels constantly show charts touting the exponential growth of the "Magnificent Seven". Bitcoin has scarfed up more than $1 trillion of capital as the digital currency hits all-time highs. Investors, both amateur and professional, fear missing out and are pressured to jump on the bandwagon. It would be prudent to recall that the Nasdaq 100 peaked on March 27, 2000 and plummeted 83% by October 7, 2002. In other words, $1 million turned into $170,000. That is what it sounds like when a financial bubble pops.