Market analysis | November 18, 2024

At a glance

Equities gave up some of their post-election gains as attention turns to likely policies of the majority Republican government. U.S. economic data remains resilient, while growth in China softens.

Number of the week

0.4%

Increase in October retail sales month over month, with autos accounting for the bulk of the growth.

Term of the week

NFIB – The National Federation of Independent Business is the largest political advocacy organization in the U.S. that represents small and independent businesses.

Consumer Discretionary, Financials and Energy are up between 6.0% and 9.0% in November while the Healthcare sector has retreated 3.5%, all which are projected to be impacted by expected policies of the new Trump administration.

Terry Sandven, *Portfolio Manager, Chief Equity Strategist, U.S. Bank*

Global economy

Quick take: Control of the U.S. House of Representatives remained with the Republicans securing a sweep of Congress and the Presidency. U.S. economic data indicates elevated but moderating inflation with still solid consumer spending. Data from China indicates still challenging economic activity.
Our view: Growth in the United States and India remains exceptional while other major economies, including China, Europe, Japan and the UK, demonstrate modest but positive economic expansion despite elevated interest rates. Slowing growth and inflation trends are likely to persist well into 2025 due to lagged effects of high borrowing costs.

- **As final ballots are tallied, the Republicans retained control of the House, securing a sweep win.** With 218 seats in the House of Representatives, Republicans retain narrow control, with 5 seats yet to be determined, while holding a 53 to 47 seat advantage in the Senate. By retaining the House, Republicans hold control of the legislative agenda.
- **U.S. inflation remains stubborn as October consumer prices rose 2.6%, increasing from the 2.4% pace in September.** The core measure, which excludes volatile food and energy components, rose 3.3% year-over-year, the same as last month. Still elevated shelter costs, a hurricane related jump in used car prices, rising motor insurance costs and higher airfares contributed to the rise.
- **Consumer spending remains resilient with October retail sales up 0.4% month over month** and September's sales revised to a 0.8% gain from the 0.4% advance estimate. Autos accounted for the bulk of growth in October. Other notable gainers included appliance retailers, restaurants, and building supply stores. Large declines occurred in home furnishings, sporting goods, and miscellaneous stores.
- **NFIB Small Business Optimism Index rose by 2.2 points in October to 93.7, the highest since early 2022.** However, this was the 34th consecutive month below the 50-year average of 98. Small businesses still face economic adversity from soft sales, unfilled job openings and ongoing inflationary pressures.
- **China's October retail sales is up 4.8% year over year, improving from 3.2% last month.** Household appliances saw a big jump amidst the government trade-in program. Building materials fell as housing prices continued their decline, slipping 5.9% year-over-year. Industrial production growth slowed, slipping 0.1% from September to 5.3% year over year, hurt by slowing in passenger cars and smartphones.

Equity markets

Quick take: U.S. equities trended modestly lower last week in the aftermath of the U.S. elections and as the third quarter release period draws to a close.
Our view: The fundamental backdrop remains supportive of a risk-on bias. Inflation is falling, interest rate cuts are in motion, and earnings are trending higher, bolstering sentiment and provide valuation support. Near-term, price volatility is likely to be more the norm versus exception as new administration policies begin to emerge, valuations are elevated, holiday selling season looms, and geopolitical tensions remain.

- **Year-to-date performance remains superb and broad-based; November performance is more differentiated.** The S&P 500 ended last week up 23.1% year-to-date, with all 11 sectors in positive territory. For November, as of Friday's close, performance is less sanguine. The S&P 500 is up 2.9%, with six of 11 sectors posting gains. Most noteworthy, Consumer Discretionary, Financials and Energy are up between 6.0% and 9.0% in November while the Healthcare sector has retreated 3.5%, all which are projected to be impacted by expected policies of the new Trump administration.
- **The third quarter reporting period is drawing to a close with results trending modestly above expectations.** As of Friday's close, with 92% of companies having released results, sales are up 5.0% versus expectations heading into the quarter for sales to advance 4.4%; earnings are up 6.8% versus expectations for growth of 3.9%. Company guidance for 2025 is elusive following third quarter releases; forward guidance is likely to be more prevalent post-election following fourth quarter results beginning in mid-January.
- **Big box retailers and AI bellwether, NVIDIA, are among companies projected to impact sentiment this week following quarterly releases.** Lowes, Walmart, Target, network security company Palo Alto Networks, and AI-bellwether NVIDIA are slated to release results this week. The big box retailers should provide further insight into consumer spending trends among discretionary items and home furnishings, as well as an early read on expectations for the holiday selling period.
- **Consensus expectations are for S&P 500 earnings for 2024 and 2025 of roughly $240 and $273,** respectively, according to Bloomberg, FactSet and S&P Cap IQ. At present, the S&P 500 trades at 24.4 times 2024 estimates and 21.4 times 2025 estimates, both at the high side of its historical average.

Bond markets

Quick take: Choppy trading in Treasury markets continued last week as 10-year Treasury yields rose to their highest levels since July. Riskier high yield corporate and municipal bonds continue to perform well relative to higher-quality bonds with help from strong investor demand that has insulated both markets from swings in Treasury yields in recent months.

Our view: Investors can improve current income generation through a variety of bonds with solid fundamentals including high yield bonds, bank loans, structured credit, and non-agency mortgages. Incremental allocations spread across riskier bond categories help limit the impact of price swings in any individual bond type while income on the broader fixed income portfolio accumulates over time.

- **Investors remain unsure whether the Fed will deliver an additional rate cut in December.** While the Fed voted unanimously to reduce policy rates by 0.25% at their last meeting on November 7, officials expressed a wide variety of expectations for policy going forward. Fed Chairman Jerome Powell said, "The economy is not sending any signals that we need to be in a hurry to lower rates." In contrast, Chicago Fed president Austan Goolsbee said, "As long as we keep making progress toward the 2% inflation goal, over the next 12 to 18 months rates will be a lot lower than where they are now." While the pace of cuts is debated, flexibility was a common theme across officials' remarks as the Fed balances its inflation and employment mandates. Interest rates reflect expectations the Fed will likely deliver 3 additional 0.25% rate cuts by year-end 2025.
- **Strong corporate and municipal bond demand kept prices relatively stable despite Treasury yield changes.** The incremental yields on high yield corporate bonds over Treasuries fell to their lowest levels since 2007 last week. The extra yields on high yield municipal bonds relative to Treasuries are also below historical norms. Investor demand for high yield bonds remains strong despite their elevated valuations, preventing meaningful price declines. While the broad exposure to Treasuries index lost 3.9% since Treasury yields bottomed (prices peaked) in mid-September, high yield corporate bond returns have been roughly flat. High yield municipal bonds lost just 0.3% without accounting for their tax-free income benefit over the same time frame. Even with elevated valuations, the extra income on high yield bonds can improve long-run portfolio return potential.

Real assets

Quick take: A broad pullback in equity prices extended to publicly traded real estate companies last week with prices falling 2.0%. The increase in 10-year Treasury yields from 3.6% in September to nearly 4.5% last week weighed on real estate investor sentiment given increasing funding costs.

Our view: Interest rate changes can cause near-term price swings in publicly traded real estate, but patient investors can benefit from meaningful income opportunities in the category over the medium-term.

- **Borrowing costs remain a headwind for real estate.** Riskier segments of publicly traded real estate struggled last week, such as office real estate companies, losing 6.6%. Elevated borrowing costs are burdensome for office real estate that already faces headwinds from rising vacancies hurting rental income. However, office makes up less than 5% of the publicly traded real estate market and the prospect of easier borrowing conditions ahead creates opportunity for improving activity across all types of real estate. Last week's Fed Senior Loan Office Opinion Survey (SLOOS) showed commercial real estate lending standards are still tightening, but to a lesser extent than prior surveys.
- **Oil and gas pipelines continue to lead within infrastructure investments.** Master Limited Partnerships (MLPs) in oil and gas pipelines returned 1.3% last week. Rising natural gas prices have been a tailwind, along with expectations for increased domestic energy production with confirmation last week that Republicans won a majority in Congress. Utilities, roughly 40% of the global infrastructure market, also delivered a slight gain of 0.1% last week. Utilities can benefit from weakness in riskier assets given they're traditionally viewed as a defensive investment for their income stability.
- **Commodity prices fell last week.** Both gold and oil prices fell nearly 5% last week. Rising interest rates can hurt gold demand given the investment doesn't generate income, but the pullback in gold prices is small in comparison to strong year-to-date price gains of nearly 30%. Oil prices fell following the International Energy Agency (IEA) warning of the potential for oil production to surpass demand by one million barrels per day in 2025. Opportunities in commodities hinge on a global economic expansion that fuels stronger demand.

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The Institute of Supply Management Manufacturing Index, also called the Purchasing Manager's Index, measures manufacturing activity based on a monthly survey, conducted by the Institute for Supply Management, of purchasing managers at more than 300 manufacturing firms. The New Orders Index is one of four indexes that make up the Institute of Supply Management Manufacturing Index, the others being Business Activity, Employment and Supplier Deliveries.

The **National Federation of Independent Business Small Business Optimism Index** is a composite of 10 seasonally adjusted components. It provides an indication of the health of small businesses in the U.S., which account for roughly 50% of the nation's private workforce.

Past performance is no guarantee of future results. All performance data, while obtained from sources deemed to be reliable, are not guaranteed for accuracy. Indexes shown are unmanaged and are not available for direct investment. The **S&P 500 Index** consists of 500 widely traded stocks that are considered to represent the performance of the U.S. stock market in general. The **Institute of Supply Management Manufacturing Index**, also called the Purchasing Manager's Index, measures manufacturing activity based on a monthly survey, conducted by the Institute for Supply Management, of purchasing managers at more than 300 manufacturing firms. The **Personal Consumption Expenditures (PCE) Price Index** is a measure of the prices that people living in the United States, or those buying on their behalf, pay for goods and services. It is known for capturing inflation (or deflation) across a wide range of consumer expenses and reflecting changes in consumer behavior. The **Conference Board** is a nonprofit research organization that distributes vital economic information to its peer-to-peer business members. The **S&P CoreLogic Case-Shiller Home Price Index** measures the value of single-family housing within the United States. The index is a composite of single-family home price indices for the nine U.S. Census divisions and is calculated monthly.

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