Market Movement Highlights

A 10,000 foot mid-year view of the US economy and the financial markets continues to point to momentum for both. Second quarter's GDP growth rate registered a surprising +2.8%, double that of the first quarter, while the stock market delivered additional upside performance marking a +15% return on the first half year. On the back of overall trends pointing to continuing growth, fixed income markets remained flat to modestly negative.

Peering under the hood, if Q1 was best described as "a tide lifting all boats", quite the opposite occurred in Q2. Once again the technology and communications sectors led by the "Mag Seven" wrestled back their market leadership to deliver outsized gains of +14% and +9% respectively, driving the major equity indices higher.

Following suit, the international markets, both developed and emerging, delivered +5.7% and +7.7% respectively, lending additional credence to the bullish view for stock markets worldwide.

A Few Observations

- **Performance Bifurcation and Top Heavy Concentration.** As the curtain fell on the first half year, some 60% of S&P 500's gains were attributable to the "Mag Seven", which on average accounted for some +30% of the index's overall market cap. This imbalance contributed to large cap stocks handily outperforming small cappers +15.3% vs +1.7% and growth stocks outpacing their value brethren +20.7% vs +6.7%. Behind the scene, these performance gaps are largely justified by their comparative growth in earnings.

- **Inflation Seems to be Easing as FED Signals 2024 Rate Cut(s).** With the most recent announcements that the PCE and CPI inflation measures remain in line with the forecast, relatively contained and trending down, speculation has once again emerged that the FED is likely to begin easing rates by at least 25bps as early as September. Recognizing that several economic measures are softening (wages, labor, unemployment rising to +4.1%, durable goods production slowing and spending marginally softer), Chairman Powell recognizes that a soft landing is currently in play. To avert anything worse, he is signaling that inflation need not hit its 2% target before rate cuts commence.

Looking Forward

Overall we remain positive on the outlook for both the stock and bond markets for the balance of 2024. Notwithstanding, just as was the case in the first half, returns are likely to be accompanied by shifts in stock market leadership, and elevated volatility due to both US politics and geopolitical risk.

- **Election Year Uncertainty.** According to analyses from Morgan Stanley, Morningstar and Ibbotson Associates from 1928 to 2023, the *average* return for the S&P 500 index in presidential election years was +11.0%. Could this year be different? What we all know at least in the moment is that in just a matter of a couple of news cycles, President Biden has bowed out of the campaign, VP Harris has seized the torch, and the former President narrowly escaped an assassination attempt. All this while two wars rage on! One might conclude this time around could be markedly different. It's near certain that forward market performance will almost solely be determined by the events leading up to and including who wins the "Harris vs Trump Trade" in November.

- **Outlook for Earnings Growth Remains Strong.** Bank of America's Global Research forecasts US earnings growth for 2024 and 2025 to be +10.3% and +14.3% respectively, while global growth tracks only modestly behind. Further, the outlook for global equity performance remains enhanced by increasing share buybacks, rising global investments in Artificial Intelligence (AI) and the likelihood that the FED will soon announce its first rate cuts.

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- **Rotation from Mega to Small Cap Stocks as Rate Cuts Loom.** At this writing, the Russell 2000 small cap index registered +10% for the month of July. Should rate cuts materialize soon, small cappers, which had most recently languished under the weight of debt and higher borrowing costs, could be the first group poised to benefit. Keep an eye peeled for that!

Closing Thoughts

- **Risks of Capital Expenditures in AI.** What appears to be playing out, at least "in the moment", regarding artificial intelligence is whether the hype surrounding it is real and whether the massive investments made to date are premature relative to immediate return? To this point we offer the following anecdotal evidence:

From Sundar Pichai, CEO of Google. This after Google's stock sinks (5%), due in part to their significant AI spending:

"The risk of underinvesting (in AI) is dramatically greater than the risk of overinvesting for us here, even in scenarios where if it turns out that we are overinvesting... We obsess around every dollar we put in."

From Mark Zuckerberg, CEO of Meta (Facebook):

"Yes there is a meaningful chance that a lot of the companies are overbuilding now… But on the flip side, I actually think all the companies are making a rational decision, because the downside of being behind is that you're out of position for the most important technology in the coming 10, 15 years…"

Our view is that the AI hyper-scalers, the likes of Google, Meta and Microsoft, can afford extra and perhaps even a few wasted billions in AI related capital expenditures, without material harm to their bottom lines. The risk of falling behind the evolutionary AI curve would be fatal to their existence.

- **Opportunities Do Abound.** AI hype or not, again we recite that investors are best served by intelligent, common sense diversification from the most speculative of investment to the most boring with much of the balance struck in the middle. We offer the final table below as proof of this thesis.

Please feel free to reach out to us if you have any questions.

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"Magnificent Seven" vs "Fab Four" Stocks: Who had it better?

Selective Stocks and S&P 500 Index as of 7/24/2024	Forward P/E ratio 7/24/24	P/E ratio 7/24/24	12/31/21 ~ YTD 24 Total Returns	YTD Return 7/24/24	2023 Return	2022 Return
Microsoft	32.3	37.1	30.3%	14.5%	58%	-28%
Apple	33.1	34.0	25.5%	13.8%	49%	-26%
NVidia	41.7	66.9	291.0%	130.7%	239%	-50%
Amazon	39.6	50.7	7.7%	19.01%	81%	-50%
Facebook	22.8	26.5	38.2%	30.60%	194%	-64%
Google	23.0	25.0	19.4%	23.87%	58%	-39%
Tesla	86.6	60.5	-38.7%	-13.28%	102%	-65%
"Magnificent 7" Stocks Equal Weighted	**39.9**	**43.0**	**53%**	**31%**	**105%**	**-45%**
Berkshire Hathaway	**22.0**	**12.8**	43.7%	21.35%	15%	3%
JPMorgan	**12.2**	**11.6**	42.2%	24.80%	31%	-13%
Exxon Mobil	**13.0**	**14.1**	105.8%	17.05%	-6%	87%
Caterpillar	**15.6**	**15.2**	72.5%	15.05%	26%	19%
"Fab Four" Stocks Equal Weighted	**15.7**	**13.4**	**66%**	**20%**	**16%**	**24%**
S&P 500 Index	**21.2**	**27.0**	**19%**	**15.0%**	**26%**	**-18%**

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