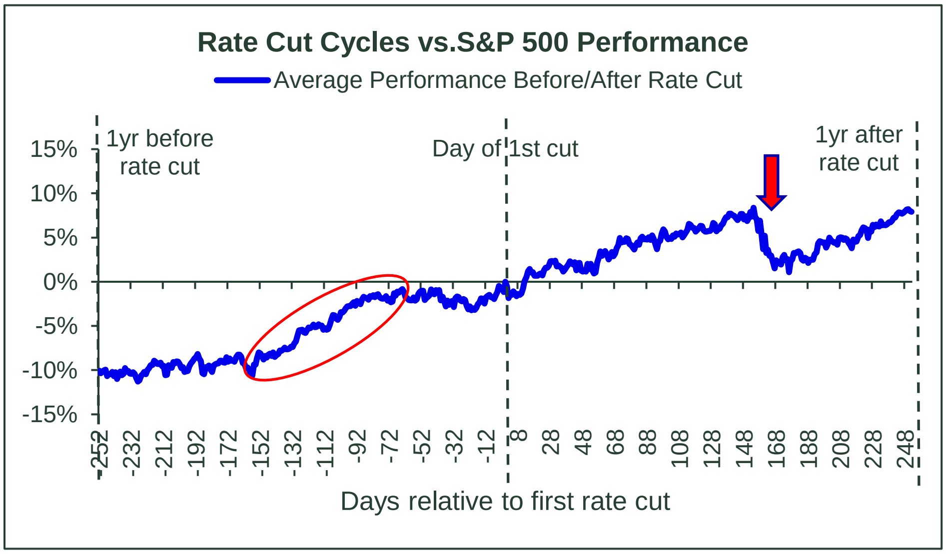
January 11, 2024
Commentary

Weekly Market Update

Insight of the Week

S&P 500 Performance Around First Rate Cut

As we enter into the new year, the expectations around rate cuts is one of the most important topic in the minds of investors. As of January 9th 2024, according to the CME Fed Watch Tool, a tracker for probabilities of Fed's target interest rate, investors expect the Federal Reserve to cut rates as soon as March 2024.



Source: FactSet, SSGA. Daily data from January 4,1988 until January 10,2024. Rate cut cycles of 1989,1995,1998,2001,2007 and 2019 are considered in the analysis.

As market participants are expecting a rate cut cycle to begin this year, we looked at the performance of the S&P 500 during past rate cut cycles starting from 1989 until 2019 (six samples). As shown in the above chart, the S&P 500 gradually rises as the first rate cut approaches. On average, equities seem to fluctuate sideways the 3 or so months prior to the first rate cut. This is the period we are entering now as markets are pricing in a rate cut in March. The bulk of the equity rally seems to happen 3-6 months prior to the first cut, which is the period we just passed and where we also experienced a healthy rally. Despite having an average 8% return 12 months after the first cut, the path isn't necessarily smooth and can experience sizable pullbacks as the market observes how the lower rates spur the economy.

We believe that in 2024 uncertainty will continue to persist, with sub-trend growth projected across the world's economies and the path to a soft landing appearing viable yet sensitive. To learn more about our outlook on markets please read our 2024 Global Market Outlook.

Sources: State Street Global Advisors, FactSet, S&P.

Equities

Then and Now – Equity Markets in 2023 and Thus Far in 2024

The macro environment during 2023 can be described by “different speeds, same direction” as our Chief Economist coined. Over the year, we saw disinflation emerge across the globe and although the trend took hold at varying speeds, this phenomenon was widespread. We believe 2024 will be a year of easing monetary policy, and similar to 2023, it will take hold at different speeds, but be in the same direction.

The macroeconomically volatile environment of 2023 led to equity market performance that could be characterized by two words: Narrow Leadership. In a year when the S&P 500 was up 26%, 87% of this performance came from three sectors: Communication Services, Consumer Discretionary, and Information Technology, as investors favored the Magnificent 7.

Although we are less than 10 trading days into 2024, the sector rotation has been interesting to see. Year-to-date, the only 2023 leader that is still thriving in the new year is Communication Services, due to the performance of Meta and Alphabet. Consumer Discretionary and Information Technology have fallen behind. Interestingly, the sector with the best performance thus far YTD is Health Care. Healthcare’s underperformance in 2023, brought it’s LTM P/E ratio to 17.9 in December, lower than the S&P 500s P/E of 19.5, and far lower than S&P 500 Information Technology sector’s P/E of 26.7, making it quite attractive relative to peers.

Sector	Price Return	
	2023 (%)	2024 YTD (%)
Information Technology	59.45	-0.18
Communication Services	54.93	1.87
Consumer Discretionary	41.84	-0.91
Industrials	15.41	-1.35
Financials	12.83	0.44
Materials	10.22	-2.27
Real Estate	8.53	-1.10
Health Care	0.33	3.40
Consumer Staples	-2.38	0.86
Energy	-4.80	-2.67
Utilities	-10.20	1.73

Source: FactSet, S&P. Data as of 1/10/2024.

On the earnings front, things were bleak over 2023. Although Q4 earnings have not rolled in just yet, the S&P 500 is expected to report 2023 calendar year earnings growth of just 0.6%. For 2024, S&P 500 earnings growth estimates from analysts have decreased slightly over the last few months, but 11.5% growth is anticipated, most of which is expected in the fourth quarter of 2024.

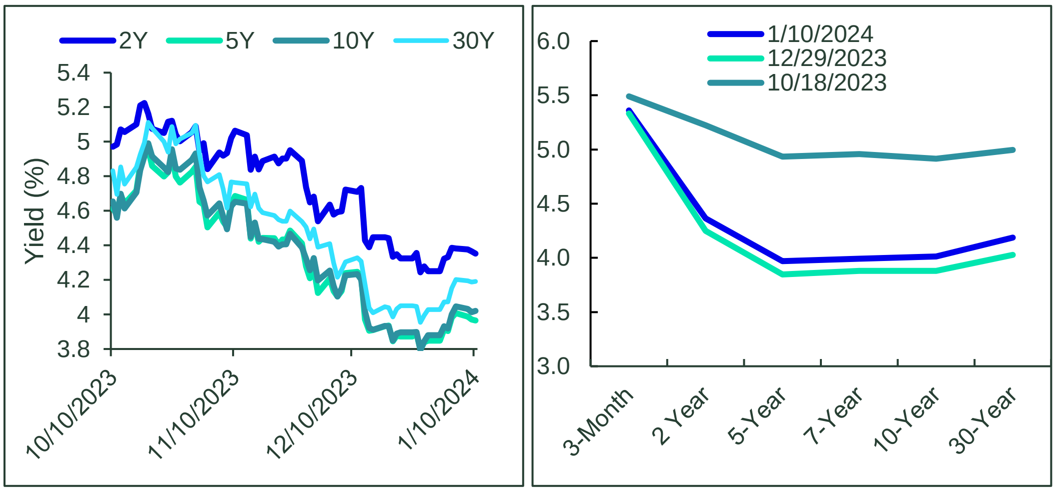
Earnings provide some optimism around equity market performance next year, however markets are likely to continue to be driven by monetary policy decisions. Healthcare’s performance YTD has shown the market may be interested in changing its preferences, which warrants caution around whether last year’s high performers can hold onto that strength. All in all, expect volatility as the Fed starts on their easing path, it is not a given that 2024 will be smooth sailing.

Source: State Street Global Advisors, FactSet. Data as of 1/10/2024 unless otherwise stated.

Fixed Income

Jittery Start to 2024

2023 ended with a bond market rally that saw 10 year yields fall below 4% and positive excess returns across all sectors. Ten year yields fell from their 16 year high of 5.0% in October 2023 to 3.88% as markets closed for the last day of 2023. Markets began to price in the first rate cut by the Federal Reserve as early as March 2024. But then January happened…



Source: Bloomberg LLP. Data as of 1/10/2024.

Yields increased to 4.03% amidst a slew of positive labor market data. Initial jobless claims for December 30, 2023 came in at 202k (versus estimates of 216k), continued claims for the prior week, December 23. 2023 decreased to 1,855k (versus estimates of 1,881k). The ADP employment changes for the last month came in at 164k (versus estimates of 125k), and change in nonfarm payrolls was recorded at 216k (versus estimates of 175k). The unemployment rate held steady at 3.7%, hourly earnings increased to 0.4% m/o/m and 4.1% y/o/y (slightly above estimates of 0.3% and 3.9% respectively). In response to resilient labor market data, markets pulled back expectations of a rate cut from 100% in March of 2024 to 60%.

Although the labor markets continue to show resilience, it is important to remember that labor data is a lagging indicator. There are clear signs of a slowdown within the economy. Manufacturing activity remained in contractionary territory, and the services sector showed signs of softening. Consumer credit increased $23.75b in November vs expectations of +$9b. Higher debt and higher borrowing costs puts consumers at risk of pulling back spending in the coming months and decreasing aggregate demand. Additionally, the two month payroll net revisions actually subtracted 71k jobs from the non-farm payrolls.

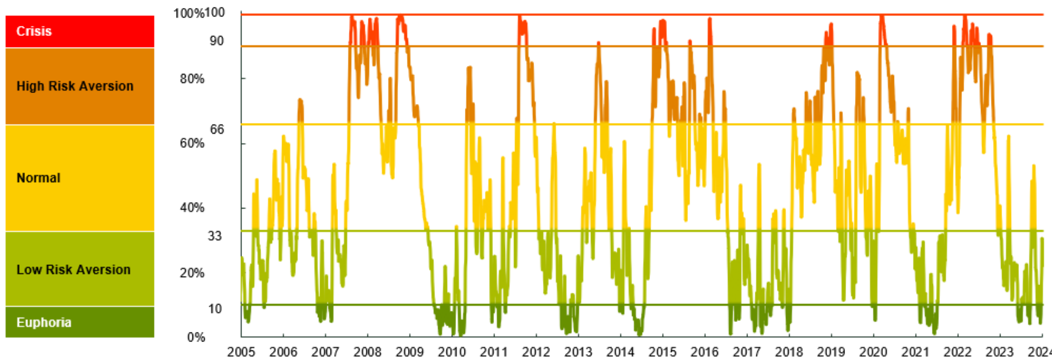
As we start the year, it is important to remember that rate cuts are a part of the foreseeable future, but the exact timing may be hard to predict with certainty. There are clear signs that the economy is softening, and the Federal Reserve will have to pivot as higher costs work their way through the system. Our base case continues to favor rates with a bias toward long duration and a curve steepener.

Source: State Street Global Advisors, Bloomberg

Market Regime Indicator

The Market Regime Indicator (MRI) represents a proprietary multi-asset class model designed to characterize risk appetites within the capital markets.

Days in the Low Risk Regime (since December 27): 11 days



As of December 13, 2023. The data displayed is not indicative of the past or future performance of any SSGA product. The portion of results through March 31, 2011 represents a back-test of the MRI model, which means that those results were achieved by means of the retroactive application of the model which was developed with the benefit of hindsight. Data displayed beyond this date is not backtested, but is still generated by the model referenced. All data shown above does not represent the results of actual trading, and in fact, actual results could differ substantially, and there is the potential for loss as well as profit. The Market Regime Indicator (MRI) is a quantitative framework that attempts to identify the current market risk environment based on forward - looking market indicators. We believe the factors used, equity implied volatility, currency pairs implied volatility and bond spreads, are good indicators of the current risk environment as they are responsive to real - time market impacts and in theory should include all current and forward views of those markets. These factors are combined to create a single measure and used to identify one of five risk regimes: Euphoria, Low Risk, Normal, High Risk, and Crisis. A slight calculation change was made as of June 28, 2019.

About State Street Global Advisors

For four decades, State Street Global Advisors has served the world's governments, institutions and financial advisors. With a rigorous, risk-aware approach built on research, analysis and market-tested experience, we build from a breadth of index and active strategies to create cost-effective solutions. And, as pioneers in index, ETF, and ESG investing, we are always inventing new ways to invest. As a result, we have become the world's fourth largest asset manager* with US $3.69 trillion† under our care.

*Pensions & Investments Research Center, as of 12/31/22.
†This figure is presented as of September 30, 2023 and includes approximately $58.13 billion USD of assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated. Please note all AUM is unaudited.