March was another good month for equity markets. The S&P 500 rose 3.2 percent for the month with Mid Caps and Small Caps performing even better. The Russell Midcap gained 4.3 percent and the Russell 2000 gained 3.6 percent. International markets also trended higher with the MSCI world ex-US gaining 3.4 percent and MSCI Emerging Markets gaining 2.2 percent. Fixed income was also positive for the month, with the US Aggregate Bond Index gaining 0.9 percent.

In fact, the whole first quarter was quite pleasant for equity investors by just about any standard. As Lisa Shalett, our Chief Investor Officer, noted in this Month's On the Markets, "the first quarter was a fruitful one for equity investors. Not only did the S&P 500 Index rise more than 10% to an all-time high, but Japan also experienced double-digit returns while several emerging markets strengthened as well."

On a more concerning note, however, she writes that "virtually all the US market-cap-weighted benchmark's gains have come from multiple expansion, and investors are pricing in major profit margin improvement amid cooling growth." In other words, the market gains appear meretricious – earnings have not grown fast enough to justify valuations and seem unlikely to do so for the rest of this year. As a consequence, Our Global Investment Committee recommends that investors shy away from US mega-caps and focus on "valuation support and achievability of earnings forecasts." This does not mean our team is bearish on stocks in general. In fact, we agree with Richard Bernstein , who wrote in late February, that "the range of underappreciated investment opportunities seems historically broad and historically attractive. Given the last time similar opportunities arose was after the Tech Bubble, which was 24 years ago, we don't think we are exaggerating when we describe this as a once in a generation opportunity." Our worries about mega-cap tech do not extend broadly to all stocks across the globe and across the capitalization spectrum. Over longer time horizons, we are quite bullish on the majority of stocks by count if not by cap. Like Richard Bernstein, we especially favor capital-starved industries aligned with a theme of re-industrialization. We see globalization waning, populism and nationalism waxing, in a macro environment where the world moves toward a more bi-polar status quo with less overall US economic influence.

As you already know, our team does worry that in the short run the US equity market might have priced in more rate cuts than are likely to materialize this year; that might cause some volatility this spring and summer. The bond market, on the other hand, seems to be priced with less confidence in forthcoming rates cuts. Steve Edwards, Senior Investment Strategist, summed up the first quarter for fixed income markets quite well in this month's Fixed Income Insights , writing "In the first quarter, investors repriced their expectations for the Fed's potential cuts, based on revived inflation pressures and more robust growth data. As of late December, investors anticipated 6.3 25-bp cuts in 2024, which would have brought the federal funds rate band to between 3.50% and 3.75% from 5.25%. Subsequently, investors have reduced their expectations on the incoming data flow, trimming expectations to just 2.7 cuts in 2024."

Despite the adjustments to expectations so far, 2.7 cuts may still be too many. Recent data continues to support our cautious stance. The labor market remains strong, and, in our opinions, inflation is likely to remain above the Fed's target of 2 percent for the foreseeable future. Energy prices are rising. We continue to be concerned that short term risk lurks in a potential Fed disappointment this year. As Diego Anzoategui, one of Morgan Stanley's Economists writes ,

”although the median fed funds forecast from the Fed’s Summary of Economic Projections in March remained at 4.6 percent, inferring three cuts for 2024, the Fed included upward revisions to its forecasts for 2025, 2026 and longer term.“ Stated more directly: the Fed is also concerned that rates are likely to remain higher for longer. Chairman Powell ”also seems to be in that camp too, as he stated in the FOMC press conference was that his ‘instinct is rates will not go back to the very low’ pre-pandemic levels.“

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