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The Heartland Group at Morgan Stanley Investment Insights

Halloween, Earnings Season & Election, Trick or Treat, markets got spooked

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As October comes to a close, let's take a look back at the market's performance throughout the month. The S&P 500 closed at 5705.45, only slightly higher than its Oct 1st closing of 5708.75. The Nasdaq followed a similar trend, climbing from 17910.36 to 18095.15, marking a 1% increase.[1] However, what's truly intriguing is the path these indices took to reach these endpoints.

Both the S&P 500 and Nasdaq steadily gained throughout the month before experiencing significant drops on October 29th, just two days before Halloween.[1] These declines erased the majority of their hard-earned gains. So, what caused this sudden change in trajectory?

Throughout October, the market encountered several potential hurdles, and on each of the dates listed the Stock market had significant downward moves:

* On October 15th, CPI numbers were released, showing a 0.2% increase in September and an annualized rate of 2.4%, which was slightly higher than the anticipated 2.3%.[2]
* On October 23rd, the Federal Reserve's Beige Book revealed slower-than-expected economic growth.[3]
* On October 30th, GDP numbers were published, showing a growth rate of just 2.8%, disappointing some, again showing that growth may be moderating.[4]

Overall, the economy experienced mixed signals throughout October: employment and job numbers remained strong, unemployment data that came out showed a 4-week moving avg of 236,500 jobless claims, and that avg is trending lower.[5] Additionally, inflation proved to be persistent, and the upcoming election has introduced a degree of uncertainty.

In past newsletters, we have identified 5700 as a crucial level for the S&P 500,[6] and we expect this level to be tested, and likely to hold 5700 even with the election around the corner. However, we also anticipate a potential knee-jerk reaction in the days surrounding November 5th.

What should investors watch out for going forward? Equities remain in a bull market for now, so it's wise to keep an eye on current trends. Earnings season is underway, with 70% of the S&P 500 companies having reported their earnings so far. Of those, 75% have posted positive EPS surprises, although this figure is slightly lower than in previous quarters. Meanwhile, 17 companies have issued lower earnings guidance, while 18 have issued higher guidance - both figures are fairly typical, if slightly on the low side.[7]

Earnings overall appear to be in line with expectations, and companies are generally showing growth. With stock buybacks likely to continue, this should keep the market on an upward trajectory. However, investors should be

1 Dow Jones/ Reuters news and Thompson One
2 Consumer Price Index Summary - 2024 M09 Results (bls.gov)
3 Fed's Beige Book Shows Little Growth Across Most of US (msn.com)
4 Gross Domestic Product, Third Quarter 2024 (Advance Estimate) | U.S. Bureau of Economic Analysis (BEA)
5 Unemployment data (dol.gov)
6 Sept24_New_Newsletter_-_Heartland_Grp_vers1.pdf (morganstanley.com)
7 Factset Earnings Q3
8 10-Year Treasury Constant Maturity Minus 2-Year Treasury Constant Maturity (T10Y2Y) | FRED | St. Louis Fed (stlouisfed.org)
9 ICE BofA US High Yield Index Option-Adjusted Spread (BAMLH0A0HYM2) | FRED | St. Louis Fed (stlouisfed.org)
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mindful of any significant divergence from the norm, as it could indicate weakness in the market.

The bond market may offer a more valuable insight into the state of the economy. The 2yr vs 10 yr bond spreads are no longer inverted and have hovered between 10-20 bps this month, currently sitting at 12 bps.[8] The 10yr rate has risen from a low of 3.6% in mid-September to its current level of 4.3% - a significant jump, especially considering the Fed's recent easing cycle. This suggests that the bond market anticipates higher-than-expected inflation and interest rates.

Additionally, high yield spreads and consumer credit data could provide further clues about the economy's direction. High yield spreads are currently at a 30 year all-time low of 2.88%.[9] Typically, you would see this indicator spike high at the start of a recession, and since it is at an all-time low, this could indicate that either a recession is still far off, or the bond market is underestimating the risk associated with sub-investment-grade companies.

To gain more insights, it's worth examining consumer debt levels. The delinquency rate for credit cards has been steadily increasing since Q4 2021, currently sitting at 3.25%, above the 10-year average. However, it's important to note that this rate has remained historically lower than pre-2008 levels.[10] Keeping an eye on these consumer credit data points, will help inform us of the consumer's financial health and whether they are becoming overextended. Analyzing these factors alongside broader economic indicators can provide valuable insights into the market's overall strength and potential future trajectory. As always, maintaining awareness of these key indicators is essential for making informed investment decisions.

We recommend monitoring the 5700 price for the S&P 500, after last month action, it looks like it could be a good support level. But we suspect volatility leading up to and right after this presidential election. We are neutral-to-bullish on equities, unless the 5700-support level is broken and the bullish trend reverses. Expect modest market returns and volatility from now until year-end. You can continue to use cash reserves to add to investments if the volatility provides an entry point.

The greatest compliment one can give us is a referral to their friends and family.
As always, please call or email us with any questions or concerns about the management of your family's wealth.

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https://www.morganstanley.com/wealth-investmentsolutions/wmir-definitions
An investment cannot be made directly in a market index.

Technical analysis is the study of past price and volume trends of a security in an attempt to predict the security's future price and volume trends. Its limitations include but are not limited to: the lack of fundamental analysis of a security's financial condition, lack of analysis of macro-economic trend forecasts, the bias of the technician's view and the possibility that past participants were not entirely rational in their past purchases or sales of the security being analyzed. Investors using technical analysis should consider these limitations prior to making an investment decision.
The value of fixed income securities will fluctuate and, upon a sale, may be worth more or less than their original cost or maturity value. Bonds are subject to interest rate risk, call risk, reinvestment risk, liquidity risk, and credit risk of the issuer.

An investment in a money market fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. Although the Fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the fund.

Investors should carefully consider the investment objectives, risks, charges and expenses of a mutual fund before investing. The prospectus contains this and other information about the mutual fund. To obtain a prospectus, contact your Financial Advisor or visit the mutual fund company's website. Please read the prospectus carefully before investing.

Duration, the most commonly used measure of bond risk, quantifies the effect of changes in interest rates on the price of a bond or bond portfolio. The longer the duration, the more sensitive the bond or portfolio would be to changes in interest rates. Generally, if interest rates rise, bond prices fall and vice versa. Longer-term bonds carry a longer or higher duration than shorter-term bonds; as such they, they would be affected by changing interest rates for a greater period of time if interest rates were to increase. Consequently, the price of a long-term bond would drop significantly as compared to the price of a short-term bond.

The value of fixed income securities will fluctuate and, upon a sale, may be worth more or less than their original cost or maturity value. Bonds are subject to interest rate risk, call risk, reinvestment risk, liquidity risk, and credit risk of the issuer. High yield bonds are subject to additional risks such as increased risk of default and greater volatility because of the lower credit quality of the issues.

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