July 15, 2024

Last week officially marked the halfway point of 2024, and the beginning of summer activities for many families, which our team hopes you enjoy. Following a strong first quarter, the market continued to advance as most domestic indices hit fresh all-time highs during the second quarter. The S&P 500 crossed 5500 for the first time ever and added 4.3%, lifting its year-to-date return to approximately 15%. However, market breadth (i.e., underlying stock participation) weakened, with much of last quarter's gains attributable to just a few mega cap names. This deteriorating breadth, which is illustrated on page 9 of your report, has resulted in returns for most investors less than those of the very concentrated indices.

For instance, the five largest stocks in the S&P 500 have accounted for nearly 60% of the broad index's YTD return, with the top 20 accounting for over 75%. Meanwhile, the equally weighted S&P 500 decreased by 3.1% last quarter which means the average S&P 500 stock declined. Furthermore, out of the 11 major sectors only four posted a gain, with the AI-focused technology and communications sectors being the only ones to outpace the S&P 500 index. Note that utilities were not far behind due to AI-fueled energy demand growth.[1]

One index still beneath its all-time high is the Russell 2000, as small caps have lagged the overall market since peaking in 2021. The 950+ day streak without a new high is one of its longest ever. In the second quarter, the Russell 2000 declined by 3.6%, making it barely positive for the year.

Between political uncertainty and a slight appreciation of the US Dollar, there were enough headwinds to make international equities a mixed bag in the second quarter. Developed markets struggled to gain footing, with the MSCI EAFE Index falling 1.4%. However, emerging market equities were a bright spot, with the MSCI Emerging Markets index up 4.4% thanks to a rebound in China.[1]

The Bloomberg US Aggregate Index, a broad measure of the US bond market, were basically flat with a slight increase of 0.1%. Yield curve inversion continued during the quarter, as short-term debt instruments maintained higher yields than long-term debt instruments. The yield on the 10-year US Treasury note closed the second quarter at 4.40%, up from 4.20% at the end of the first quarter, while the three-month Treasury bill yields stayed nearly flat at 5.36% to end the second quarter. [2]

With the current economic backdrop, the Global Investment Committee remains underweight equities and overweight to fixed income. In equities, we recommend cyclical and secular-growth equities with quality balance sheets. We remain market-weight to international developed and emerging market equities. We remain overweight fixed income assets, as a higher-for-longer rate regime creates opportunities to achieve better risk-adjusted returns in current coupons, with the potential for capital gains if rates fade over the course of the next 12 months. Furthermore, we advocate that investors maintain a neutral-duration stance, as intermediate- to long-term bonds may help to fortify multi-asset portfolios across a range of potential outcomes.

Lastly, on the labor market front, the June payrolls report proved to be stronger-than-expected, with 206,000 jobs added in the month vs. economists' consensus of 190,000. Despite beating June payroll estimates, the labor market has shown signs of relative weakness as growing unemployment claims and lower-than anticipated payroll numbers are being reported. The Morgan Stanley & Co. Economics team believes that there will be three 25-bp cuts this year, commencing in September 2024, with an additional four 25-bp cuts through mid-2025. Weaker employment numbers, slowing wage growth, and decelerating inflation are being monitored closely by the Fed as it tries to deliver a "soft landing" for the economy.

As always, please reach out to anyone on our team if you have any questions, and we hope you enjoy your summer!

Best Regards,

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Sources:

[1]*Dorsey Wright market commentary*
[2]*Morgan Stanley Q2 204 client market commentary letter*

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