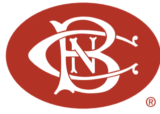

Wealth Management

QUARTERLY PERSPECTIVE
SUMMER 2024

2024 Mid-Year Review

In January's 2023 year-end review I noted the resiliency of the U.S. economy and how well markets had fared in spite of high interest rates, lingering inflation and two significant global conflicts. That resiliency continued through the first half of 2024. Many expected markets to do well this year based on the Federal Reserve starting a rate cutting cycle, even as soon as March, and then continuing throughout the year. But here we are halfway through the year with no rate cuts due to stubborn inflation, and few if any cuts on the horizon, yet markets are up strongly. In addition, the economy continues to push ahead, albeit at a slowing pace, while a strong jobs market holds unemployment around 4%. Of concern, however, is that while markets had a good first half when looking at broad indices, the underlying concentration of where those returns have come from is worth noting. The frenzy over artificial intelligence (AI) has driven many large cap technology stocks to new highs while other areas of the market have lagged significantly, and in some cases are negative year-to-date. This type of top-heaviness can undermine market stability until we start to see broader participation from other sectors.

Inflation continues to dominate economic headlines after a surprising move higher through the early part of the year. Most thought inflation's trajectory was set late in 2023 with consistently lower readings that would lead to a handful of interest rate cuts in this year. But those cuts have been shelved following higher readings on prices that have only recently begun to slow again. This has Federal Reserve officials taking a data dependent wait and see approach, one which they're afforded by continued low unemployment. They will likely want to see a few more months of slowing inflation before they're comfortable cutting rates. For now, the earliest potential cut would be in September, but could easily be moved closer to year end if inflation isn't on an established path toward 2%.

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Brian is a member of CNB Wealth Management's Investment Committee, where he is responsible for providing the research and analysis necessary to oversee the firm's investment portfolios. Additionally, Brian coordinates the firm's due diligence process, which monitors and evaluates all existing and prospective investment managers.

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Index Returns as of 6/30/2024	Q2 2024	YTD 6/30/2024
S&P 500	4.28%	15.29%
Russell 1000 Growth	8.83%	20.70%
Russell 1000 Value	-2.17%	6.62%
Russell 2000 Value	-3.64%	-0.85%
Dow Jones US Real Estate	-1.73%	-2.87%
MSCI EAFE (net)	-0.42%	5.34%
MSCI Emerging Markets (net)	5.00%	7.49%
Bloomberg US Aggregate Bond	0.07%	-0.71%
Bloomberg Global Treasury ex. US	-3.07%	-6.76%
Bloomberg High Yield Bond	1.09%	2.58%

Figure 1 - Source: Morningstar

Market Review

The S&P 500 Index was up 15.3% year-to-date through June 30th, led by growth stocks, especially those associated with the previously mentioned AI craze. The second quarter was a prime example of the market's recent bifurcation, with large growth/tech, as measured by the NASDAQ Composite, up 8.5%, while mid & small cap firms, large cap value and real estate were all down for the quarter. To be fair, those large growth names have also been the primary driver of earnings growth with the top seven S&P 500 stocks growing year-over-year earnings by 40% while the remaining 493 firms on average have had tepid earnings growth over the last year.

International equity returns for the first half were relatively modest, up 5.8% as measured by the MSCI

(continued on page 2)

Figure 2 - Source: J.P. Morgan Asset Management

EAFE Index. Part of the story has been the continued drag on returns by a strong U.S. Dollar, as the same index measured in local currency terms, was up 11.5%. With the European Central Bank embarking on its rate cut cycle ahead of the Fed, this strength is not likely to dissipate any time soon, potentially reinforcing the near-term outlook for U.S. stocks over international. Overall, however, much more favorable valuations in international stocks may lead to a longer-term resurgence.

Bonds have continued to struggle as yields have drifted higher in a sea of uncertainty around rate cuts, inflation and deficit spending by the U.S. government. The Bloomberg U.S. Aggregate Bond Index is down 0.71% this year, a much different scenario than was anticipated at the start of 2024. At that point interest rate cuts seemed imminent and fixed income investors expected some price appreciation along with collecting income that has been hard to come by over the last decade. When looking at the last few years, it has been an especially tough road for bonds, with an annualized 3-year return of -3.02%. The Fed's eventual transition to rate cuts will be a welcome event for conservative investors.

2024 – Act II

As we look to the second half of the year, it is likely that a few key topics will determine the direction of markets. One will be the trajectory of inflation. Should it continue on its most recent path with small but consistent downticks month-to-month, there is a strong potential for one or two rate cuts by year end, followed by a string of cuts in 2025. The housing market and the shelter component of inflation will be central to this story, as it has been the primary driver of still elevated prices. It is anticipated to begin easing through year-end and should it do so we're likely to see inflation move lower.

The second key will be corporate earnings. With the S&P 500 Index up roughly 30% in the last 18 months, its valuation as measured by its forward price-to-earnings ratio is now approximately 21x. That is expensive by historical standards, and earnings growth will be needed to substantiate that multiple and eventually bring it back down. Additionally, earnings growth will need to start coming from a more diversified set of sectors. Areas outside of large growth and tech will need to pull their weight in order to provide stability to the rally in order for it to continue.

The third key will be consumer spending, which is closely linked to unemployment and the jobs market. Low unemployment has helped drive consumer spending over the last few years, along with a spenddown of COVID relief funds. This has led to consistent GDP growth, but should unemployment begin to rise, consumer spending would likely slow and turn into a significant drag on the economy and earnings. The silver lining is that this may also entice the Fed to move more aggressively on interest rates, but overall would be a negative for the economy and the soft-landing scenario.

Conclusion

Not listed above is the presidential election. Historically, elections have very little effect on market outcomes over intermediate to long-term periods and serious investors are cautioned not to make short-term emotional decisions based on the potential outcome of an election. However, it is very likely that the contentious nature of this election will cause short-term volatility in the market. Even now, we have uncertainty around who the democratic nominee may be following the recent debate. Regardless of who controls the Presidency or Congress, financial markets and the economy have successfully adapted to the various political environments and performed well. We urge investors to focus on their financial plans and have patience as the long-term accumulation and compounding of their investment earnings work for them.

If you have any specific questions, please feel free to reach out to your advisor team here at CNB Wealth Management.

Data as of 6/30/2024. Not intended to be construed as tailored fiduciary advice. Investments are not FDIC insured, not bank deposits, not obligations of, or guaranteed by Canandaigua National Bank & Trust or any of its affiliates. Investments are subject to investment risks, including possible loss of principal amount invested. Past performance is not indicative of future investment results. Before making any investment decision, please consult your legal, tax or financial advisor. Investments and services may be offered through affiliate companies.