Vestor Capital
INVESTMENT & WEALTH MANAGEMENT

Economic and Investment Outlook

October 3, 2024

Equity Market Update

Equity indexes continue to perform well in 2024. The S&P 500 index has caught up with the technology-heavy NASDAQ composite index in the third quarter, and both are up 22% YTD. We are seeing more stocks participate in the market rally as investors are now embracing interest rate sensitive stocks as the market is pricing in more interest rate cuts over the next few years. Somewhat surprisingly, U.S. small-cap stocks continue to lag despite the fact they will likely see a bigger benefit from lower interest rates due to generally higher debt levels and more floating rate debt. Developed international indexes continue to lag their U.S. counterparts as the U.S. economy continues to outperform much of the rest of the developed world. Finally, the emerging market index performed very well in the third quarter and is now up 17% due in large part to a strong rebound in Chinese stocks spurred by recently announced economic stimulus measures.

Markets are celebrating the beginning of long-awaited interest rate cuts as inflation eases. We are surprised by the strong performance in the third quarter of stocks that continue to report weak results as investors place their wagers that lower interest rates will stimulate growth and improve earnings. We anxiously await third quarter earnings to get a clearer picture of how company leaders see the impact of recent interest rate cuts.

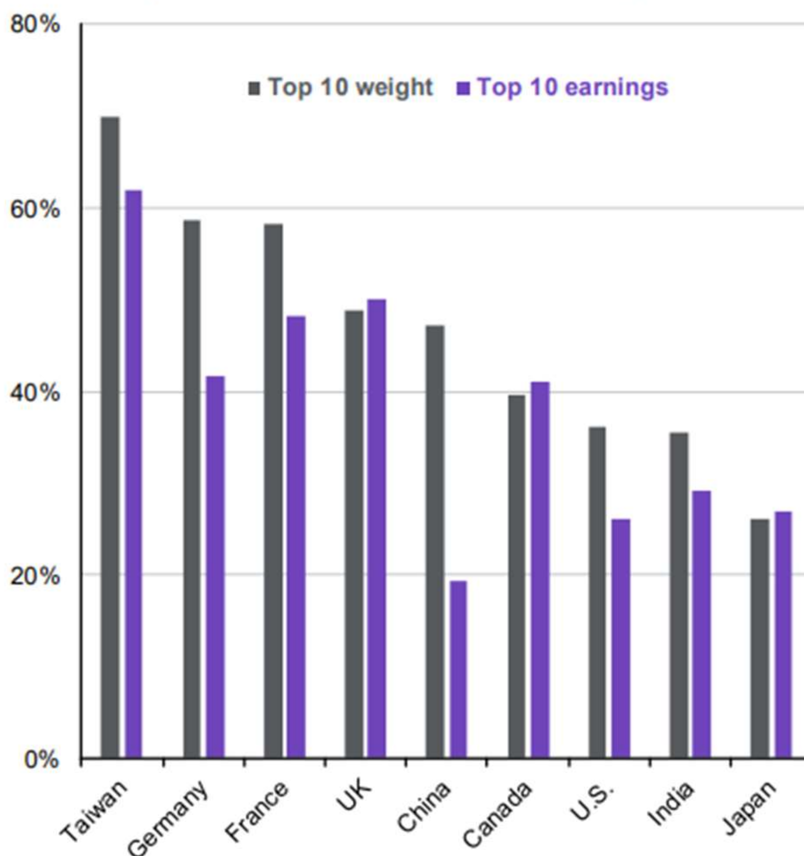
Total Return Performance for the Major U.S. and International Stock Market Indexes

Equity Index	*YTD September 30, 2024*
United States	
Dow Jones Industrial Avg.: 30 Stock Composite	**13.93 %**
S&P 500 Composite: U.S. Large Cap	**22.08 %**
NASDAQ Composite: Technology Heavy	**21.84 %**
S&P 600 Small Cap: U.S. Small Cap	**9.29 %**
International	
MSCI EAFE Large Cap: Europe, Asia & Far East Large Cap	**13.55 %**
MSCI EAFE Small Cap: Europe, Asia & Far East Small Cap	**11.58%**
MSCI EM Emerging Market: Emerging Market Countries	**17.13 %**

Source: Bloomberg, L.P.

World Equity Markets

A lot has been written about the market concentration in the U.S., with the largest seven companies in the S&P 500 being named "The Magnificent Seven", including technology companies such as Apple, Microsoft and Nvidia. The chart below highlights that a number of markets outside the U.S. are actually more heavily concentrated in their largest companies. Also note that these large company weights have correspondingly high earnings. For this reason, we are not overly concerned with the current market makeup. Reviewing the S&P 500 over the last 50 years shows that high concentration at the top of the market is not at all unusual. Interestingly, the makeup has changed over this period with large companies such as IBM moving down the list and being replaced by companies like Apple. That is part of the dynamic nature of our economy.



Source: JPMorgan Guide to the Markets 9/30/2024

World Strife

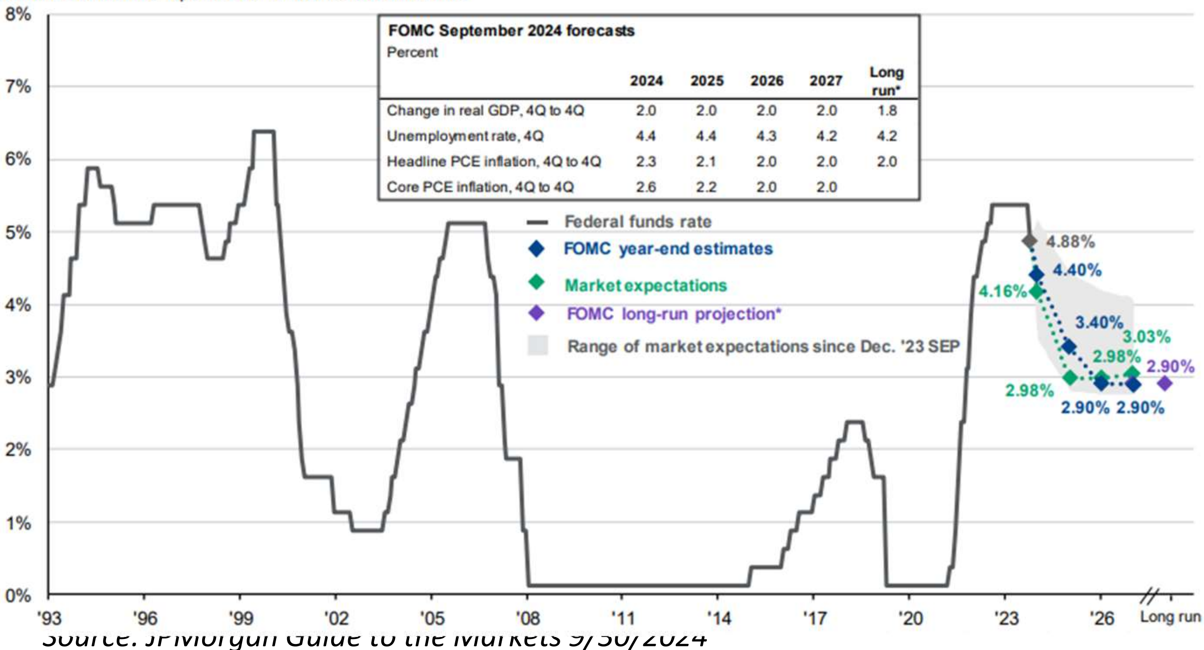
We are deeply saddened by the continued conflict in the Middle East. Despite the recent escalation, world equity and energy markets have largely indicated through their tranquility that they do not believe it will negatively impact trade or oil supplies. While the situation is fluid and subject to change, we believe there is a high likelihood that the conflict will not have a significant impact on world markets. There may be a short spike in oil prices if shipping lanes are blocked or oil fields are struck, but we would expect these to be temporary. The endless war in Ukraine is a human tragedy but has little impact on world economies or markets as Russia is largely out of the world economic system and Ukraine is not a large economy.

Inflation, Interest Rates & Fixed Income

Inflation continues to moderate as the U.S. consumer price index (CPI) has now fallen for five straight months and currently sits at 2.5% at the end of August, down from a peak of 9.1% in June 2022. In response to the moderation and an increase in unemployment from 3.7% at the end of 2023 to 4.2% in August, the Federal Open Market Committee (FOMC) had sufficient data to cut interest rates by 0.5% (50 basis points) at their last meeting. This is reflected in the graph below, which also highlights expectations for further cuts ahead.

We are pleased that interest rates have been cut as they were too high for a much lower inflation environment. However, it is premature to declare victory in the inflation fight. As is demonstrated by the recent longshoreman strike on the East Coast, pent up wage pressure still exists. Also, money supply growth, after declining for most of 2022 and 2023, is now rising again. Monetarists believe this growth is the primary determinant for inflation as was evidenced by the high correlation between money supply growth and inflation in the 2020-2022 time period.

While interest rates have recently fallen, they are still at attractive levels for fixed income investors. Barring a significant economic contraction, we do not believe that the FOMC will resort to the draconian interest rate cuts that we experienced during the 2007-2008 Financial Crisis or the 2020 Covid pandemic. For this reason, we continue to be attracted to high quality fixed income instruments.



FOMC September 2024 forecasts
Percent

	2024	2025	2026	2027	Long run*
Change in real GDP, 4Q to 4Q	2.0	2.0	2.0	2.0	1.8
Unemployment rate, 4Q	4.4	4.4	4.3	4.2	4.2
Headline PCE inflation, 4Q to 4Q	2.3	2.1	2.0	2.0	2.0
Core PCE inflation, 4Q to 4Q	2.6	2.2	2.0	2.0	

Source: JPMorgan Guide to the Markets 9/30/2024

Election Thoughts

As we approach the November election many investors are attempting to handicap the impact each candidate will have on industries and market sectors. While this is an admirable goal, history has shown it to be of little value. We have always viewed market sell-offs due to perceived risks from a particular candidate as buying opportunities. Also, the idea of moving to cash until after presidential elections has not proven to be an effective method of maximizing long-term returns. From an investment standpoint the winning strategy during election years is to simply ignore politics and stay invested.

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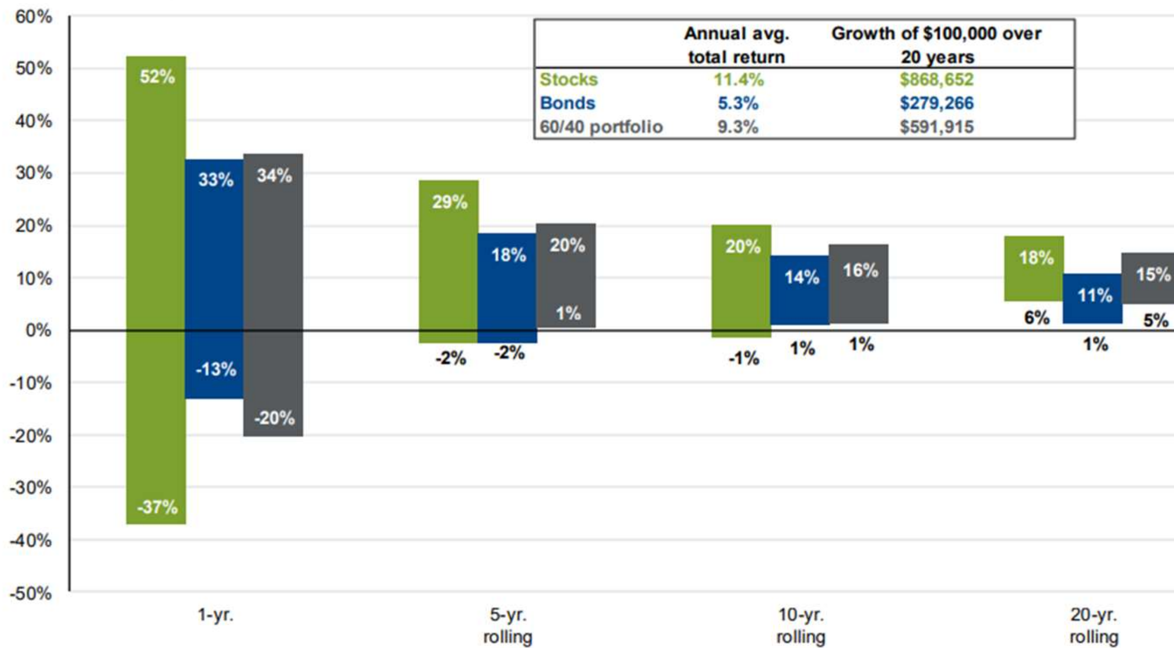
Summary

During volatile periods in the market, it pays to remember that portfolios with a 60/40 blend of stocks and bonds respectively, have never had a loss for 5, 10, and 20-year rolling periods since 1950 as illustrated in the table below. Markets are inherently volatile which is unsettling, but during these times it is important to remember that riding through these periods will ultimately be rewarded.



Source: JPMorgan Guide to the Markets 9/30/2024

The media continues to pelt us with worrisome news and the possibility of trouble ahead. Remarkably, very little news highlights the good things that are happening in the world, as only bad news sells. Markets have been buoyant in 2024, interest rates are beginning to decline, employment is strong, and the U.S. economy continues to grow. Even if the economy were to slow a little going forward, the FOMC has plenty of room to cut interest rates to help counteract this. We acknowledge that the strong equity markets we have enjoyed for the last 10 years does bring with it the possibility of somewhat lower returns going forward.

The U.S. still is the envy of the world for its opportunity and dynamism. Keep these thoughts in mind when news is gloomy. Better yet, go for a walk and enjoy the fall colors!

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