

## Commerce Trust Market Brief with Scott Colbert 01/29/2024

**Scott Colbert:** Good morning. It's January 29th and the markets are open. So far this year, we've seen a continuation of last year's fairly narrow market returns. The S&P 500 (Index) is positive, up 2.62%, having broken into new technical high territory on January 19th. Smaller cap stocks have not participated, the Russell 2000 (Index) is down 2.37%, international stocks (as measured by the MSCI EAFE Index) are slightly negative (-0.57%), and emerging market stocks (MSCI Emerging Markets Index) are deeply negative, down 3.73%, basically being pushed down by the problems over in China. Even interest rates have risen, which has pushed bond prices negative. Year to date both municipals (as measured by the Bloomberg Municipal Bond Index) and taxable bonds (as measured by the Bloomberg Aggregate Bond Index) are down a little more than 1%.

What are the markets paying attention to, and what is likely to begin to push the markets around going forward? Essentially, we think it's basically three things: Number one is growth, economic growth, which continues to remain robustly positive. Secondly, inflation, which, of course, is coming down, rapidly cooling last year, but the question becomes how quickly will it cool this year? Then the interaction of those two with regard to the Federal Reserve (Fed) and the likely path that the short-term interest rate market will take as the Fed probably begins to cut interest rates at some point this year.

Real (gross domestic product) growth last year came in at 2.5%. That's up slightly from the previous year's, 2022's growth rate, of 1.9%. The most interesting part of that though is that the real growth is not being driven by accelerating nominal growth. It's being driven by the rapid rollover in inflation. In fact, nominal growth continues to cool, as you might expect, as higher interest rates begin to bite into economic activity.

What's helping inflation roll over? Employment growth remains firm, but it's cooling. We only added about half the number of jobs last year as we did in 2022. While wages and salaries are growing, they're down a bit from the 2022 growth rates. Our supply lines are largely unclogged and then probably at the margin, the Chinese troubles, particularly in residential real estate, also are acting as a deflationary force around the globe.

Just today (Jan. 29, 2024) in fact, Evergrande (Group), the second largest property developer in China, was declared bankrupt by the Hong Kong courts and basically forced to liquidate. They have \$300 billion in cumulative liabilities within their banking system, and they even have \$17 billion of U.S. dollar-denominated debt. Companies of similar size with similar U.S. dollar-denominated debt

include Caterpillar Tractor (Caterpillar, Inc.) and (The) Coca-Cola (Company) to show you how large that impact is likely to be.

With growth re-accelerating a bit, but inflation continuing to cool, what is the likely path of short-term interest rates? The Federal Reserve, of course, has the ultimate say in this, but the markets have been expecting the Federal Reserve to cut rates as soon as March. The Federal Reserve, on the other hand, with their dot plot, suggested they're likely to start cutting rates in May. I always harken back to the old phrase, "don't fight the Fed." I think the markets are likely to begin to listen more and more to the Fed as the year progresses and likely to temper their enthusiasm for interest rate cuts. Eventually, short-term interest rates are likely to begin to fall and this, of course, will help buoy financial markets as the year progresses.

We'll know more about this after this week's Fed meeting and be back in several weeks to talk about how all this economic news is impacting your investment portfolios.

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