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Doll's Deliberations®

Weekly Investment Commentary

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Summary

Stocks advanced last week (S&P 500 +1.72%), with small caps (Russell 2000 +2.63%) leading the way. Fedspeak, Trump cabinet picks, and retail earnings dominated the headlines. Best sectors included consumer staples (+3.15%) and materials (+2.97%); worst sectors were communication services (-0.30%) and consumer discretionary (+1.58%).

Key takeaways

1. U.S. October retail sales and the Empire Manufacturing survey beat expectations. The marked improvements represent demand being pulled forward in anticipation of tariffs. (Expectations for future activity ticked down, as did expectations for future new orders.)

2. The rolling 12-month federal deficit surpassed $2 trillion.

3. The U.S. 10-year yield has risen 15 basis points (bps) since the election (after rising 65 bps post the September Fed rate cut before the election). That yield could potentially rise further, as President-Elect Trump is likely to pursue a large reconciliation bill next year with various fiscal spending priorities.

4. Earnings growth for the third quarter is expected to finish at about 8.8%, which is 0.3% above the July 1 estimate. But, from the beginning of the 3Q reporting season, 3Q earnings per share (EPS) are pulling from 4Q EPS almost one for one.

5. The back-up in long-term rates, Powell's comments that he is in no hurry to cut rates, and concerns over some of Trump's appointments has taken the air out of the Trump Trade.

6. We continue to believe we are late in the economic cycle, the economy has been slowing and financial conditions have tightened on hopes that growth will accelerate. Assets remain priced for perfection. With the Trump election, odds of a return in inflation have increased, as have the odds of a "hard-landing."

7. A choppy trading environment over the coming months with volatility has increased in likelihood in the face of a data-dependent Fed and the post-election transition.

8. Trump themes, small caps, and cyclicals continue to stand out, while big tech lags.

9. Our military is currently not as capable as it was in Trump's first term. Our ability to choose whether to escalate/de-escalate and impact outcomes because of our superiority on land, air, sea, space, and cyber has diminished.

10. Global population growth will slow for the rest of this century. Of particular concern: The working age cohort will outright shrink in many countries, and at the same time, the number of retirees will swell—stressing dependency ratios and potentially forcing governments to go much deeper into debt.

EQUITY MARKETS (INDEX TOTAL RETURN %)	LAST WEEK	YEAR-TO-DATE
DJIA	2.03	19.49
S&P 500	1.72	26.70
NASDAQ	1.77	27.41
RUSSELL 1000	1.58	26.17
RUSSELL 1000 GROWTH	1.72	30.80
RUSSELL 1000 VALUE	2.45	21.55
RUSSELL 2000	2.63	18.01

S&P EQUITY SECTORS (INDEX TOTAL RETURN %)	LAST WEEK	YEAR-TO-DATE
COMMUNICATION SERVICES	-0.30	32.83
CONSUMER DISCRETIONARY	1.58	24.17
CONSUMER STAPLES	3.15	19.00
ENERGY	2.55	19.17
FINANCIALS	1.70	36.54
HEALTHCARE	1.65	7.07
INDUSTRIALS	2.51	26.47
INFORMATION TECHNOLOGY	1.60	34.71
MATERIALS	2.97	11.12
REAL ESTATE	2.61	12.90
UTILITIES	2.74	31.76

Policy change uncertainty creates volatility in both directions

Investors are digesting the selection of Team Trump. The next and more important hurdle will be getting clarity on the actual new policies that will be enacted by the incoming administration. There are a wide range of proposals, which could cause changes in the economic landscape and, thus, have meaningful market impacts. It is too early to make aggressive bets on the likely outcomes, especially in view of Trump's record of abruptly shifting course, especially when the going gets tough. However, it is not too early to map out the potential opportunities and risks, since Trump did make several major policy changes during his first term.

For now, we expect that the U.S. economy will continue to expand. The pre-/post-election stampede into U.S. assets has crested but not reversed, as there are high hopes for pro-growth policies, at least initially (via fiscal policy). Treasurys may remain under pressure from an economy with solid momentum and sticky inflation.

The avoidance of most non-U.S. equity markets and currencies has persisted. The growth outlook was already favoring the U.S., and has been enhanced further because of the election outcome. Moreover, other economies are perceived to be at greater threat from the likelihood of a trade war. Until the dust settles on what is actually going to occur, global investors are unlikely to make the contrary trade of betting against the U.S. in favor of non-U.S. markets.

Geopolitical tensions remain elevated versus recent decades, and seem to have edged higher. The main transmission mechanism from current geopolitical tensions to undermining the global economic expansion would be via much higher energy prices and reduced supplies, which have not occurred thus far.

The healthy credit market backdrop (very tight corporate and high yield spreads) underscores that the tightening in overall monetary conditions since 2021 never reached restrictive territory on a global basis, although some weak-link counties and sectors are struggling due to higher debt-servicing burdens. In aggregate, these negatives so far are more than offset by areas of economic strength.

INTERNATIONAL EQUITY MARKETS (INDEX NET RETURN %)	LAST WEEK	YEAR-TO-DATE
MSCI ACWI	1.08	18.78
MSCI ACWI EX U.S.	0.16	6.44
MSCI EAFE	-0.15	4.16
MSCI EM	0.06	8.32

FIXED INCOME MARKETS (INDEX TOTAL RETURN %)	LAST WEEK	YEAR-TO-DATE
BLOOMBERG U.S. AGGREGATE BOND	0.14	1.48
BLOOMBERG U.S. CORP HIGH YIELD	0.29	8.20
BLOOMBERG U.S. GOV/ CREDIT	0.11	1.43
BLOOMBERG U.S. T-BILL 1-3 MONTH	0.05	4.77

ALTERNATIVES (INDEX TOTAL RETURN %)	LAST WEEK	YEAR-TO-DATE
REAL ESTATE (FTSE NAREIT)	1.57	11.04
COMMODITIES (DJ)	3.08	5.11
GLOBAL LISTED PRIVATE EQUITY (RED ROCKS)	2.14	21.37
CURRENCIES (DB CURRENCY FUTURE HARVEST)	0.29	12.35

The corporate profit backdrop has supported a pro-growth investment stance. However, given the potential for some dark clouds to form in 2025, we recommend a closer-than-normal monitoring of the risks, and greater use of stops to protect profits as the risk-on climate advances.

Recent inflation reports from a number of G7 countries highlight that core inflation is generally proving sticky. The U.S. has the most positive output gap, and thus is most at risk of higher inflation. This results from having had the strongest economy this decade, aided by excessively easy monetary and fiscal policies. With both policies set to ease further, this could lead to continued above-potential economic growth, with U.S. inflation trending up.

Conclusion

For now, the economic outlook is good and policy rate cuts should keep bond markets relatively calm for a while. This combination is conducive to more risk-on in the near run. While it is uncertain whether protectionism will come to dominate the macro backdrop, it is a risk that needs to be monitored as it could undermine the global economic expansion and finally end the bull market in corporate profits.

Data from Bloomberg as of Nov. 22, 2024

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