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Clark Capital Management Group

Commentary

Navigator® Market Update

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Fed Pivot 2023

The Fed left rates unchanged for the third consecutive FOMC meeting and signaled that rate hikes are finished, priming the market for rate cuts to come in 2024. The Fed's statement was updated to acknowledge that growth has "slowed" from the strong pace of Q3 GDP, and the characterization of inflation was updated to recognize that inflation has "eased over the past year" but still "remains elevated."

The median dot in the Summary of Economic Projections (SEP) showed 75 basis points (bps) of cuts in 2024, 100 bps in 2025, and 75 bps in 2026 for a cumulative 250 bps of cuts between 2024-2026. At 2.875%, the median dot for 2026 sits modestly above the median longer run dot, which was unchanged at 2.5%. The Fed also expects core inflation to come in at 2.4% next year, GDP growth of 1.4%, and the unemployment rate to rise modestly rise to 4.1%.

The message was very dovish. Dare I say that Chairman Powell's statements were the most dovish since the infamous Powell pivot in January 2019. Powell said the Fed will have to cut rates before inflation hits its 2% target and mentioned that if they wait for the 2% level to be reached, it would be too late.

The market cheered the message of forthcoming rate cuts. The stock and bond rally that began in November extended further on the news. The equity market surged, and Treasury yields plunged. While the S&P 500 remains slightly below its 1/3/2022 all-time closing high (-1.87%), it has reached a new all-time high on a total return basis, which includes the reinvestment of dividends. Today alone, 2-year Treasury yields plunged 30 bps to 4.43% while 10-year Treasury yields dropped 18 bps to 4.02%. The 10-year Treasury yield has now fallen by almost 100 bps since peaking near 5.0% in mid-October.

Coming into the Fed meeting, the market was pricing in 3 rate cuts in 2024. After the Fed meeting and statements, the market is now pricing in 5-6 rate cuts over the next 12 months. That seems too aggressive, especially in a presidential election year. Nonetheless, rate cuts are in the offing, and we believe the headwind of rising rates has abated.

Data this week confirmed that inflation remains on a glidepath lower. The Consumer Price Index (CPI) hit 3.1% year over year (YoY) while the Producer Price Index (PPI) has risen just 0.9% YoY. In our 2023 Market Outlook we said, "CPI should fall to 3% with the potential for a downside surprise. Base effects, slowing housing data, and commodity round trip supports the moderation of inflation." That has now played out, and we expect further moderation of inflation in 2024.

Importantly, corporate earnings have rebounded from last year and are expected to continue to grow. We believe this positive fundamental backdrop, along with the increasing potential for a soft landing for the economy, sets the stage for lower interest rates and higher stock prices.

Interested in more insights? Register for our 2024 Market Outlook on Tuesday, January 9th at 4 p.m. EST.

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