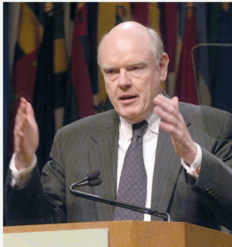
# Economic & Market Commentary

Fall 2024



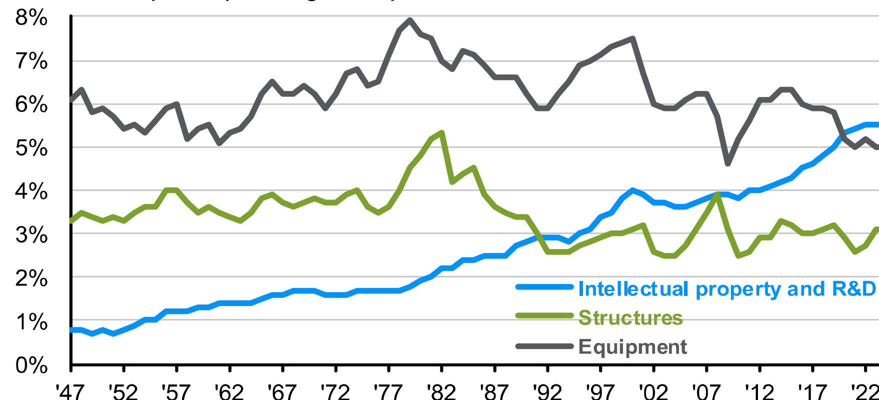
***We have the most flexible and adaptive economy. Making sure we sustain the ability of the American economy to perform well is really the priority of economic policy. - John W. Snow***

John W. Snow (b. 1939) is an American economist and attorney. He served as Secretary of the Treasury under President G. W. Bush, CEO of CSX Corp., and is currently Chairman of Cerberus Capital Management, a major participant in alternative asset investing.

This quote captures the essence of American economic exceptionalism. We have the most productive workforce in the world. We are self-sufficient in most raw materials, food and energy production, and enjoy the ability to turn these assets into goods and services to help advance the world economy. While we often focus on the negatives facing us (and there are many!), our strengths far outweigh the weaknesses.

## Our Changing Economy

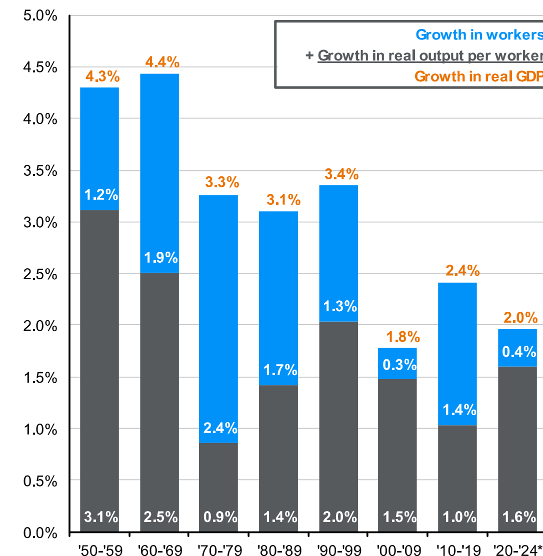
The economic history of the U.S. is built on ingenuity, opportunity, and the increasing productivity of a growing workforce. This remains true, but the inputs are changing. Capital spending in the U.S. is increasingly directed toward technology (read: AI) and away from bricks and mortar. And, at the same time, U.S. workforce growth is trending more toward immigration as the 'baby boom' generation retires and native birth rates wane. The components of a growing economy are evolving, but their importance is not. Leadership moving forward must acknowledge these realities and encourage market-based policies which allow our nation to continue setting pace for the rest of the world.




Source: J.P. Morgan Asset Management; DOD, DOJ; (right) BLS; (Right and left) BEA. GDP drivers are calculated as the average annualized growth in the 10 years ending in the fourth quarter of each decade. Future working-age population is based on Census Bureau projections released in November 2023, controlled for military enrollment, growth in institutionalized population and demographic trends. DOD Troop Readiness reports used to estimate percent of population enlisted. Numbers may not sum due to rounding. Forecasts, projections and other forward-looking statements are based upon current beliefs and expectations. They are for illustrative purposes only and serve as an indication of what may occur. Given the inherent uncertainties and risks associated with forecasts, projections or other forward-looking statements, actual events, results or performance may differ materially from those reflected or contemplated. *The latest period reflects 4Q19to 1024. **Data for 2024 reflects year-to-date average. Guide to the Markets -U.S. Data are as of June 30, 2024.

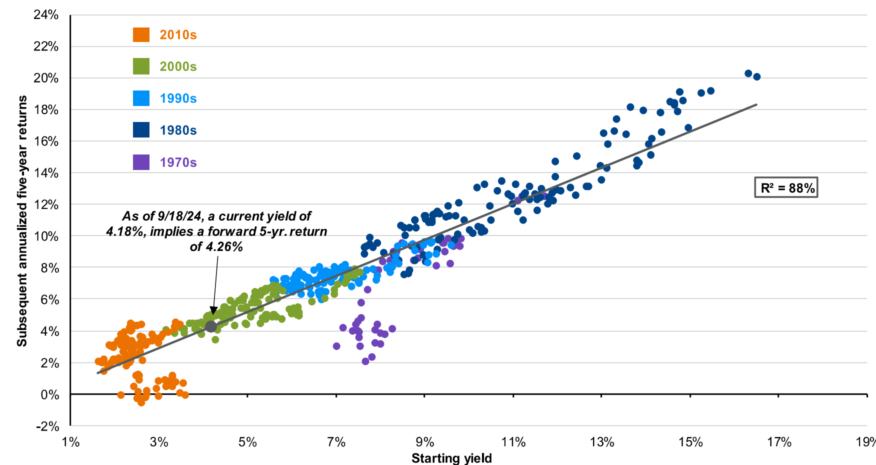
## The Fed Reaches Its Comfort Level

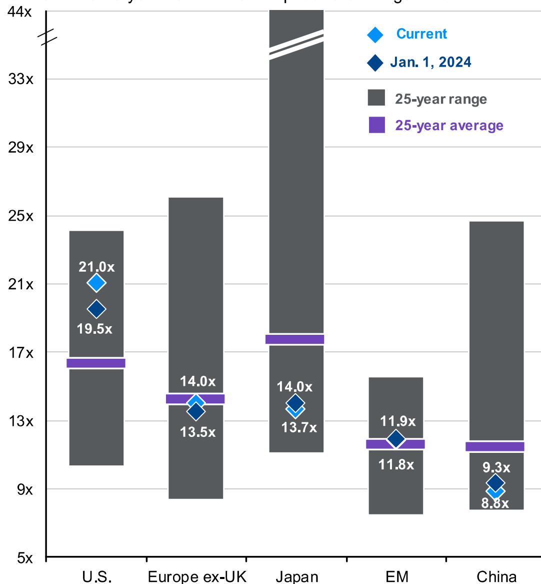
After holding rates steady for over a year at their highest level in more than two decades, the Federal Reserve lowered its target rate by 0.50% in mid-September. Both the Fed and financial markets expect this to be the first of several cuts over the next several quarters. Short term rates remain well above current and expected inflation levels – monetary policy remains restrictive but is taking the first steps toward neutrality. The unanswered question is whether subsequent cuts will be significant and rapid enough to keep economic activity from stalling out. This Fed leadership was 'behind the curve' on the way up – will it be the same on the way down? Early signs are mixed at best.



Although longer term rates are below their peaks from a year ago, a diversified bond portfolio still offers significant inflation-adjusted (real) returns. And, history shows a very strong relationship between yields at the time of purchase and the total return realized over a holding period.

Bond portfolios under our management are high quality, intermediate term, and spread across government, corporate, and global markets. We believe these provide a solid foundation of safety and yield, a combination that has been difficult to achieve in the last few years.



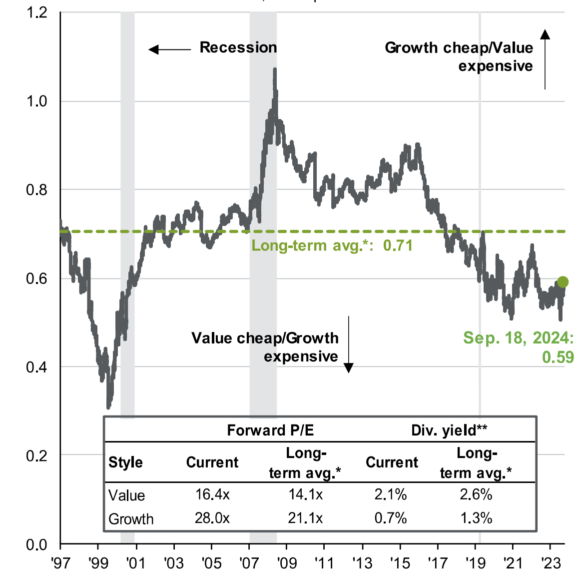




## Equity Focus on Valuation and Diversification

Clients and longtime readers of these commentaries know our emphasis on valuation as *the* core component of a conservative equity strategy. First, how do domestic markets compare to those of the rest of the world? The evidence is clear – U.S. market valuations are well above those of international markets. And, U.S. markets are alone in the world in standing well above their average valuations over the last quarter-century. This tells us that a healthy exposure to international markets provides opportunity and support not available in broad U.S. markets.

Inside the U.S., the dichotomy between growth and value themes remains stark. The valuation difference of growth themes (technology and telecommunications, AI, healthcare, etc.) versus value (industrials, finance, energy, consumer goods, etc.) is still stuck at historic extremes surpassed only in the dot-com bubble of the late 1990s. Performance chasing during that period did not end well; we maintain that perspective today.

At the same time, we have long noted that valuation is not a timing device. Just because sectors are statistically cheap to history does not imply a reversion to the mean over the near term. Over the (undefined) long term, however, a strong value orientation – accompanied by broad diversification – are the best strategies to provide *both* appreciation potential and downside protection in volatile environments. Our strategy is well-suited to accomplish these goals.




| | Forward P/E | | Div. yield** | |
|---|---|---|---|---|
| Style | Current | Long-term avg.* | Current | Long-term avg.* |
| Value | 16.4x | 14.1x | 2.1% | 2.6% |
| Growth | 28.0x | 21.1x | 0.7% | 1.3% |

## In Sum

Economic activity is slowing and the Federal Reserve has turned its attention away from inflation to employment. We believe the likely outcome is the long sought-after 'soft landing', but the path to this is narrow. Longer term interest rates will remain relatively elevated as the Treasury is forced to finance trillion-dollar deficits with no end in sight. Broad inflation is improving, but core consumer spending segments (food, energy, housing) will not materially benefit from a few short term rate cuts. Commercial real estate is still adjusting to the changing nature of work patterns. Again, the evolving nature of our economy suggests that the path forward may not conform to traditional expectations. Still, we are confident of America's ability to adapt and overcome. A conservative, diversified, fully-invested status is justified.

*Economic & Market Commentary is written by the Investment Services Department at Security National Wealth Management.*