FINANCIAL LIFE CONCEPTS

"Financial Planning with Integrity"

Looking Back at the Markets in January and Ahead to February 2024
Presented by Christopher Phelps

In general, markets edged up last month. U.S. markets continued their rally at a slower pace as interest rates bounced around, which also constrained fixed income returns. International markets were more mixed, with developed international markets roughly even and emerging markets down, primarily due to weak performance in China.

Looking Back

The markets and the Fed. Last month's mixed markets were a battle between rates, which moved above a 4 percent yield for the U.S. Treasury 10-year note, and the economy, which continued to do well and support corporate earnings growth expectations. Higher rates typically mean lower stock prices, and we saw a dip in the middle of last month, only to see the market bounce back as rates dropped near month-end.

Looking forward, things appear more challenging. The January Fed meeting ended with Chair Powell pretty much ruling out a rate cut at the next meeting, which disappointed markets. Other Fed commentators also seemed more hawkish than markets had assumed, and rates have climbed substantially so far this month.

Economic growth. That increase is not just about the Fed. Strong economic news raised the possibility that inflation won't continue to decrease. Fourth-quarter economic growth came in stronger than expected, and projections indicate that this could be the case for this quarter, too. Job growth was not only strong last month but accelerated, and both wage growth and spending increased. Rising consumer confidence should keep those trends in play, and business confidence also showed signs of improvement. Last month's data showed a strong and resilient economy—one that is likely to keep inflation reasonably hot and rates higher for longer.

Looking Ahead

Earnings and valuations. The good news is that the strong economy is showing up in corporate earnings reports. So far, earnings growth is coming in ahead of expectations, which should be a cushion for share prices. While interest rates and valuations could be a challenge, the strong economy and earnings growth will potentially more than offset that. This means that we may have a reasonable prospect of growth.

International and political risks. While overall conditions remain positive, there are still risks. Besides the Fed and interest rates, the ongoing war in the Middle East shows signs of expanding and affecting trade routes and supply lines, which could hurt inflation and growth. Domestic politics remain a concern as the election gets closer. But with the fundamentals reasonably healthy and the macro picture stabilizing, many economic fears that pulled markets back last year may be subsiding.

Monitoring inflation. As we move away from the start of the year, the key issues will be how fast the economy grows and what that means for inflation. Market expectations on rates have changed rapidly but are now more aligned with reality, so the effects of the Fed are likely to be less negative going forward. That said, all of this is data-dependent, and we will need to keep an eye out.

Potential Volatility Ahead

And that's the bottom line here: While conditions are good, volatility is very possible. We saw some turbulence in January, and we aren't out of the woods with inflation yet. So, while the trends remain positive, risks could increase over the next couple of months. This is something to watch out for but not worry about too much, given the strong economic fundamentals.

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