

Perspectives

A Quarterly Newsletter for Clients of Parsons Capital Management



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Strong June S&P 500 performance saved what was, to that point,

a lackluster quarter. Building on the first quarter, the index finished the first half of 2024 with 31 record closes, as the market seemed to easily digest any exogenous events. While the headline return for the S&P 500 was certainly attention grabbing, looking deeper at the drivers of the returns showed a notable trend: For the first half of the year, the 10 largest stocks in the index were responsible for 73% of the total gain (11.13% of the 15.29%). For the second quarter, the concentration became even more pronounced as the 10 largest names returned 5.60%, meaning the other 490 stocks in the index had a negative total return for the quarter as a group. With growth names dominating the list of largest companies, it follows that the Russell 1000 Growth index handily outperformed the Value index. Weakness continued down the capitalization scale, with the Russell Midcap and 2000 indices both posting negative returns for the quarter. Internationally, the EAFE index joined in the negative returns while Emerging Markets set themselves apart and actually bested the S&P 500 in Q2. After a roaring start to the year, some of the air came out of the Bitcoin balloon.

Data as of June 30, 2024	June '24	Qtr. 2 '24	YTD '24
S&P 500	3.59%	4.28%	15.29%
MSCI AC World Index (incl. US)	2.26%	3.01%	11.58%
MSCI EAFE (Europe, Asia, Far East)	-1.59%	-0.17%	5.75%
MSCI EM (Emerging Markets)	4.01%	5.12%	7.68%
Russell 1000	3.31%	3.57%	14.24%
Russell 1000 Growth	6.74%	8.34%	20.70%
Russell 1000 Value	-0.94%	-2.17%	6.62%
Russell Midcap	-0.66%	-3.35%	4.97%
Russell 2000	-0.93%	-3.28%	1.73%
Bitcoin	-7.11%	-12.12%	48.31%

Data provided by Tamarac Inc.



Fixed Income Markets

A strong June, with a 0.95% return, pulled second quarter Bloomberg Aggregate U.S. Index return positive to the tune of 0.07%. This minor positive return was not enough to overcome weakness in the first three months of the year; at the halfway point, the U.S. Aggregate return sits at a negative -0.71%. Long bonds were, again, the source of weakness in the second quarter with the U.S. Treasury 7-10 year, 10-20 year and 20+ year baskets all posting negative total return figures. This performance flipped, however, in June as longer-dated bonds showed the best returns. High yield remained a standout, with the Bloomberg U.S. High Yield Composite enjoying a 1.09% return for the quarter, bringing the year-to-date total to 2.59%. Municipal bond broad indices have been essentially flat for the second quarter and year to date.

Countdown to a cut is on...

Curve remains anything but ordinary looking...

Headline commodity prices contained...



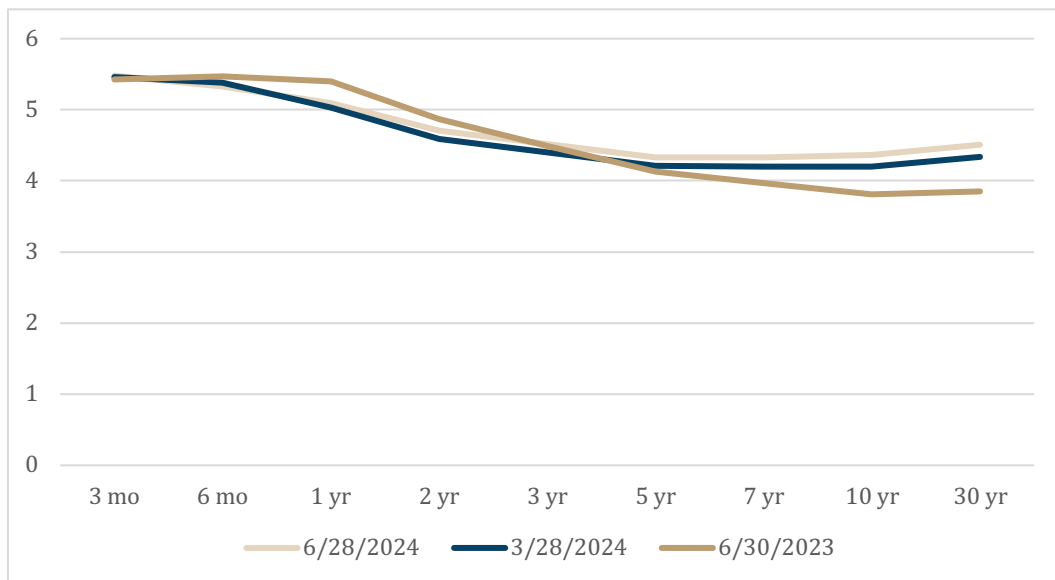
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US Treasury Yields

While the Fed remains on hold, investor expectations for Fed action have swung wildly throughout the year. Coming into 2024, market participants were betting the Fed would cut six times. As the months went by and inflation remained sticky, those expectations were ratcheted down to the point where there was some belief the next move would instead be a hike. Through official communication, Fed Chair Powell has made it clear that the hope/intention is to cut once there is greater confidence that inflation has been tamed. With continued moderation in recent data, the September Fed meeting could be live for the first rate cut in over four years.



Data from U.S. Treasury



Commodities

Similar to stocks and the S&P 500, the headline numbers in the commodities space blurred the action under the surface. The CRB Index just barely edged higher in the quarter, mostly held back by weakness in the energy complex. In the push/pull between OPEC+ (which wants to push oil prices higher through limiting supply) and the United States, where the government is taking steps to limit price gains, the U.S. came out ahead in the quarter. Beyond the drift lower in oil prices, gasoline prices came down 8% just in time for the summer driving season to begin.

Copper cooled from its march higher, falling -14% from its late-May high, but was still up 10% for the quarter and +13% year to date.

Gold is attracting investors as job growth data was revised downward and expectations grow for one or even two rate cuts in 2024.

Commodity	Qtr. 2 '24	Year to Date '24
CRB (broad index)	0.55%	5.68%
Oil	-1.96%	13.80%
Gold	5.51%	12.93%



Economic Overview

Inflation continues to cool...

Mixed data from economic surveys...

Hard data not much clearer...

Japan an international standout...



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The Fed has been on a mission to engineer a soft landing, keeping rates in a restrictive range (i.e., above nominal economic growth) to tame inflation before a recession occurs. Recent data shows that, while the job on inflation is not yet complete, progress has been made even as cracks are appearing in the growth outlook.

The June CPI (Consumer Price Index) measure of inflation came in below expectations, declining -0.1% from the May reading. This brought the year-over-year rate to 3%, compared to an expected 3.1%. This 3% print was the lowest since March of 2021. Core CPI, which excludes food and energy, rose 0.1% from May and 3.3% from last year, which was the smallest annual increase for this reading since April of 2021.

The Fed has been able to remain patient, holding off on cutting rates, because the economy (underpinned by a strong labor market) has been able to continue growing. While the jobs market still appears healthy enough, there have been mounting signs of economic weakness building in the most recent data.

For the first time since May of 2020, both the Manufacturing and Service ISM Indices dropped below 49. Readings below 50 signal contraction. The Manufacturing Index has been below 50 in 19 of the previous 20 months, but the weakness in the Service measure was a big miss from economists' expectation of 52.7.

While the ISM survey results paint an ominous picture of the U.S. economy, the PMI (conducted by Standard and Poor's and using a different methodology) has a vastly different outlook. Here, the S&P Manufacturing PMI rose slightly to 51.6 while the Service PMI moved up half a point to 55.3.

Looking at hard economic data doesn't offer a much clearer picture either. Retail sales & food services recovered from a drop in April, moving higher by 0.1% in May. Before the drop in April, February and March showed relatively strong gains, but that was preceded by a plunge in January. Housing starts continued their downtrend that began in 2022, but industrial production ticked up to 103.3 in May, which is near its best reading over the past 10 years.

The jobs market, which has been the focus of the Fed's attempt at a soft landing, is also sending mixed signals. June unemployment claims remained near the post-Covid lows, yet have been in a minor uptrend over the past few months. Non-farm payrolls rose 206,000 in June, but this was offset by a negative revision totaling 111,000 to prior months. The unemployment rate was slightly higher at 4.1% due to a small increase in the labor market participation rate to 62.6%. The consumer remains supported by average hourly earnings growth of 3.9% year-over-year.

Internationally, the economic picture is less rosy than the domestic one. Chinese factory activity fell for the second straight month while service activity in June was at a five-month low. The unemployment rate is moving higher in Australia and New Zealand; German manufacturing data fell further into contraction territory.

One international standout is Japan. While other developed economies are cutting rates (EuroZone, Sweden, Canada) or at least on hold (U.S., England), the Bank of Japan has been hiking their rate. The BoJ has been able to buck the trend of so many other countries due to the relative strength in their economy. In the most recent TANKAN Business Survey, all industries surveyed reported improvement in the second quarter as business confidence rose for the first time in six months. If there is any blemish, consumer confidence remains restrained, although the Japanese consumer is not as essential to the economy there as the American consumer is in the U.S.



Investment Implications

U.S. positioned for a soft landing...

Volatility nearly non-existent...

Forget the Mag 7, a market of one...

An upcoming shift in the macro landscape...



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It once seemed improbable if not impossible, but it's beginning to look possible that the Fed is succeeding in guiding the U.S. into a soft landing while bringing inflation under control. In fact, there are growing signs around the world that inflation is leveling off. The odds are increasing that the Fed will join numerous other central banks in cutting rates after holding steady over their previous seven meetings.

Over the past year, there are certain notable dynamics evident in the stock market that are likely unsustainable. They center around volatility and concentration. Volatility has largely been absent as the S&P 500 has notched repeated all-time highs. At the end of the second quarter, it had been 340 days and counting since the last 2% daily decline for the S&P 500. Since 2000, there have only been two longer streaks, with 352 days spanning 2016 to 2018 and 950 days between 2003 and 2007. Further emphasizing the drop in volatility was the CBOE Volatility Index (VIX), a measure of market volatility over the coming 30 days, falling to 12.73 at the end of the quarter. This compares to the long-term average of 20.

The low volatility march higher in the S&P 500 has been driven by the performance at the top of the market. The significant outperformance of a few stocks at the top discussed on page one means that those 10 largest names now make up 37.5% of the S&P. Zooming in, performance concentration becomes even more notable when examining Nvidia. While the S&P 500 gained 15.29% for the first half of the year and 4.28% in the second quarter, removing Nvidia lowers those numbers to 10.96% and 2.47% respectively.

While the largest names have been able to power the market higher over the past year, there are major inflection points in the quarters to come that may test where further leadership comes from. The Fed's "pause" since July 2023 provided a Goldilocks backdrop for this low volatility high concentration march higher in indexes. With rate cuts now looking increasingly likely, perhaps as soon as the Fed's September meeting, the environment that has helped to underpin this latest phase of the bull market could soon be shifting. Stocks tend to do well during "pause" periods and, perhaps counterintuitively, not as well once the rate cuts start.

At the same time the odds are increasing for a Fed cut, the political backdrop is heating up in the U.S. We are officially in the Presidential election cycle three months earlier than usual and with lots of drama. While the policies favored by Republican and Democrat candidates rarely align, the current party platforms are about as divergent as we've seen, with vastly different potential impacts on the economy and markets. Election outcomes are exceedingly uncertain.

Despite some of the issues mentioned on page three, it's difficult to predict a major setback in the economy with the many persistent pockets of strength and monetary conditions moving toward more accommodation. Markets are probably ahead of themselves, fueled by excitement around AI and the end of the Fed's tightening cycle. Interest rates are a wild card and will sooner or later respond to the national debt and deficit spending. In our opinion, all of this calls for preparation for some binary outcomes and action when things become somewhat clearer.

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