Thinking Out Loud

Passengers, Fasten Your Seat Belts

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In our 2H24 Halftime Update, we suggested investors could expect near-term volatility across capital markets driven by mounting evidence of a slowing economy combined with uncertainty surrounding the 2024 U.S. Presidential Election. These concerns were amplified following the first Presidential Debate. Since publishing that note, markets have endured events that have increased geopolitical instability, which has the potential to shock capital markets further.

July kicked off with a Supreme Court ruling regarding former President Trump's immunity assertion, which may have influenced the dismissal of the Trump classified document case and has delayed the criminal sentencing of his New York state hush-money case. Then, President Biden's lackluster attempt to reassure the electorate of his mental and physical acuity during an ABC Interview failed to stem significant donor defections and drove several democratic leaders to call for his withdrawal from the Presidential Race. The U.S. job market exhibited noticeable weakness, alongside softness in several other economic indicators (retail sales, LEIs, housing, PMIs). Let us not forget the 10%+ retracement in Large-Cap Technology over the last month, which has led many to believe that the "Great Rotation" into Small Caps and Value has begun. If this were not enough, investors were further tasked to discern signal from noise following the attempted assassination of former President Trump, a somewhat dysfunctional Republican National Convention, and pandemonium surrounding President Biden's historic decision to finally withdraw from the 2024 Presidential Race. Internationally, limited progress associated with Gaza and/or Ukraine was amplified by questions regarding the stability within U.S. executive branch. However, Vice President Harris has since garnered enough support to clinch the Democratic Nomination for President, temper some geopolitical anxiety, and close the lead former President Trump holds in polls or prediction markets.

We continue to monitor the macroeconomic and geopolitical backdrop alongside the 2Q24 earnings season, which seems better than expected at first glance. **But we reiterate our caution regarding equity valuations and remind investors that "timing" a sell-off is difficult. Further, the fluidity of certain geopolitical events makes it even more challenging to soothsay the winners/losers of any potential "Trump Trade" (deregulation/lower taxes/higher deficits).** Still, we have raised about 5-6% cash for certain equity models into short-term Treasuries (portfolio insurance) as we continue to barbell our Technology/AI positioning. We believe short-term interest rates will fall faster than long-term interest rates. Hence, we favor Staples and Healthcare as Value beneficiaries, while Real Estate has already started to embrace lower borrowing costs. Consumer Discretionary may encounter additional headwinds after removing activist intentions for names like SBUX. We applied this overall macro positioning across our client portfolios roughly four months ago (not incorporating the recent 5% cash raise). **Therefore, there are no structural changes to our positioning**. We still expect at least 75bps of FOMC rate cuts in 2024, with the first leg down starting in September. This should further support a Bull Steepener narrative and maybe help long-duration (aka "interest rate sensitive") fixed income styles and sectors to recover.

The current environment remains unprecedented, fluid, and volatile, but we continue to strive and help tailor portfolio solutions for our clients. We continue to believe equity markets may exhibit a modest correction in the near-term, but recover later in the year.

We'd love to hear your thoughts!

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