Argent Capital Management LLC

Market Overview – January 2024

The stock market continued its winning ways to start the year. The S&P 500 finished January higher by 1.7%, adding to the strong gains in November (8.9%) and December (4.4%) and leaving the index with a notable 15% three-month return. The all-time highs, last hit in January 2022, were finally surpassed, breaking a streak of 512 days without a fresh record.

After a stellar 2023, it was reasonable to expect mega-cap technology stocks to cool off, particularly the "Magnificent 7" – Alphabet (Google), Apple, Amazon, Meta Platforms, Microsoft, Nvidia, and Tesla. They did not. Instead, the group of seven tacked on an additional 1.8%, and 5.6% if excluding the 25% decline in Tesla shares. Growth stocks outperformed value, and large-cap stocks outperformed small-caps, keeping with last year's trend.

If the largest companies in the world perform well, they will naturally account for a significant percentage of the market's performance. The median stock trailed behind, as they have for some time, but it is a misnomer to characterize the market's performance and leadership as unusually narrow. A more appropriate description is bi-furcated and the fourth-quarter earnings season helps explain it.

By the end of January, about 65% of the S&P 500 constituents had reported earnings. Forecasts are for 2% growth in Q4, but that figure has been increasing as more companies have announced results. There is a wide disparity beneath the surface. For instance, while tech-related and consumer discretionary earnings are expected to grow by more than 20%, earnings for financial, energy, and materials companies are expected to show a decline of more than 20%. There is a fundamental reason the stocks in the former sectors are outperforming the latter.

Economic data of late has proven stronger than estimates, including the addition of 353,000 new jobs in the January payroll data, nearly twice the expected number. Atlanta Fed GDPNow forecasts for first-quarter GDP growth hit 4.2%. The Federal Reserve has thus talked down the odds of its expected rate cuts to begin in March, awaiting more affirming data on decelerating inflation while finding comfort in the cushion a buoyant economy provides.

Stocks that would be expected to perform well in a strong economy have been rewarded. Companies in the construction, machinery, housing, and consumer services industries are not generating the same headlines as technology stocks exposed to artificial intelligence-related demand but are nonetheless generating significant performance. The industrial sector in the small-cap Russell 2000 index sits near an all-time high, contrary to the narrative that only a few giant technology stocks are keeping the market afloat.

The Federal Reserve has made it clear that interest rates will be lowered from their currently restrictive level over the course of the year. A hardy economy and labor market that affords the FOMC more time to affirm lower inflation is a good thing. A wide variety of individual stocks with industry tailwinds, resilient business models, and healthy earnings growth have been rewarded accordingly.

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Sincerely,

Ward Brown

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