NorthStar Capital Market Highlights Fall 2024

Economic

- September Consumer Confidence dropped to 98.7, as economy slows
- Retail sales rose 0.4% in September, with auto sales at 15.2 million units, below estimates
- Non-farm payrolls increased to 254,000, above estimates of 140,000
- Unemployment held steady at 4.1%, with underemployment rising to 7.6%
- U.S. industrial production fell to a 0.3% pace in September, after a 0.8% gain in August
- Housing prices rose 4.5%, as the supply of homes remains tight at 4.3 months
- New home construction numbers were 1.3 million in September, below estimates
- Existing home sales were lower at 3.84 million in September, with mortgage rates remaining high
- U.S. manufacturing is flat, with September ISM at 47.2, below estimates
- Personal income was up 0.2% and consumer spending was up 0.2% in September
- GDP was up 3% in the second quarter of 2024, with Q3 advanced estimate at 2.8%

Inflation

- September core inflation rose 3.0% for CPI and 0.2% for PPI, above estimates
- Crude oil dropped from $78 to $65 and is now at $70
- Inflation has held steady, possibly allowing another Fed cut in November

Monetary Policy

- The Fed cut rates by a half point in September, on hopes that inflation is stable
- The Fed Funds rate now stands at 4.75%- 5% and the Discount Rate at 5%
- The Fed looks to remain data dependent, as more economists move to a soft landing scenario

International

- U.S. has helped Israel defend itself against a barrage of 150 missiles from Iran
- Israeli Prime minister Netanyahu took out the mastermind of October 7th attack
- Ukraine continues to fight Russia and lobby for more foreign aid
- China did a blockade of Taiwan in a war game surrounding the island in September

Interest Rates

- Ten-year Treasury yields fell to 3.6%, and now stand at 4.2%
- Secure overnight finance rate (SOFR), inter-bank lending standard, is 4.82%
- Mortgage rates dropped from 7.4%, to 6.1%, as Fed rate cuts take effect
- England, Canada, and China have cut their interest rates to boost their economies

Earnings

- S&P 500 companies reporting with 79% beating on earnings and 64% on revenues
- The AI boom is boosting earnings as the hyperscalers will spend $68 billion in 2024
- 2024 earnings are projected to rise 11% and then 14% in 2025

Market Outlook

- The S&P 500 is up 21.6% through September recovering from the August drop
- Market volatility has picked up in Q3, with the August sell off, as the VIX hit 38
- Utilities, Technology, and Communication Services were the best performing sectors in Q3
- The S&P 500 is trading at 21 times forward earnings, above its 25-year average

Current Investment Outlook

Stocks rose another 5% in the third quarter, bringing the gains to more than 20% for the year through September. Technology stocks lagged for the first time since 2022 and the market began to show significant breadth of leading stocks and sectors. This is a healthy sign for a rising and expanding market. There remains a great deal of skepticism, which is another positive factor. The market reflects concerns about stubborn inflation, signs of economic weakness, and the heightened risk of escalated hostilities overseas. Despite extended valuations for many stocks, we expect the market to continue to move higher with rising earnings and the possibility of lower interest rates. Stocks will pause and even correct from time to time, but the trajectory remains higher. We are confident that sound stock selection will continue to be rewarded.

The S&P 500 finished the third quarter with a 5.5% gain, though the performance was uneven across sectors. With the index now being approximately 30% technology-focused, the tech sector's lagging performance during the quarter was a notable deviation from the strong gains seen earlier this year. Interestingly, nine of the eleven S&P 500 sectors outperformed the index in Q3, with utilities up 19% and leading the pack. This performance stands in stark contrast to the energy sector, which was the only sector to finish in the red, down over 7%.

The Federal Reserve began to reduce rates in September with a 50 basis point cut, although Federal Reserve Governor Waller advises caution on any further rate cuts, citing concerning inflation and employment data. Inflation seems to have slowed, but we know that the published data do not accurately capture what consumers actually see and feel. The Federal Reserve would love to cut rates further through the end of the year, but inflation and the bond market may or may not comply.

Economic statistics paint a favorable picture, but the reality seems to be much weaker. The strong stock market has rewarded wealthy Americans and given them the opportunity to remain confident in the face of higher prices. Middle and lower income consumers are struggling with lower real incomes and significantly understated inflation numbers. For them, we are in a recession, bordering on depression. Student debt and credit card debt are high and rising, and delinquencies are following in line. The strong employment picture looks much weaker after the overstatement of 818,000 jobs was announced by the Bureau of Labor Statistics. Everything considered, we remain a nation with two distinctly different economies.

Similarly, the stock market has been a tale of two markets. Technology stocks have dominated and almost exclusively led the market higher. The fundamentals for these stocks have been strong, with high profitability, rapid growth, and impressive returns on equity. But, the enthusiasm for the stocks went over the top, and these stocks have now lagged for most of the past quarter. Fundamentals are important, but valuations matter.

As 2024 is a Presidential year, we continue to watch the political scene with great interest and care. This has already been a campaign year for the ages, and it still has time to go. The difference between the two candidates and their parties is profound in terms of policy views and solutions. The amazing thing for the market is that all of these political developments tend to matter less and make much less of a difference than one would ever expect. Partisans on both sides would be inclined to disagree, and we are amazed to make this observation, but history shows this to be the case.

International developments remain very much on edge. China continues to struggle to turn its huge economy around, with billions in real estate losses yet to be recognized. There seems to be no end in sight for the war in Ukraine, and Israel remains locked into a fight to the death with Hamas, Hezbollah, and the Houthis. We have just learned that Israel has responded to the missile attacks from Iran. They took out the Russian-built Iranian anti-aircraft systems and important missile production facilities. Oil prices declined as Netanyahu chose for now not to target the oil or nuclear facilities. If Iran responds, there will be a much more forceful attack. The stakes are higher than a parlor game of checkers, but we do not expect all of this to lead us into a much wider war in the Middle East.

As we move into the final quarter of the year, our outlook remains cautiously optimistic. There is a suggestion that inflation may be cooling, and despite a mixed performance across sectors, the broader market continues to move higher. Deloitte's latest projections show a 2.7% increase in real GDP for 2024, with more subdued growth of 1.5% for 2025. Brian Moynihan at Bank of America and Ed Yardeni at Yardeni Research no longer expect a recession in 2024/2025. A soft economy and stubborn inflation call for a highly disciplined approach to portfolio management. Despite the Federal Reserve's 50 basis point rate cut, the bond market is cautious and reflects concerns about inflation and a lack of confidence in the health of the overall economy. Still, corporate earnings remain strong, with 64% of companies reporting higher revenues than expected and 79% reporting higher earnings. Goldman Sachs raised their year-end S&P 500 price estimate to 6000, suggesting a modest gain from current levels. The market is currently trading at a price-earnings (PE) multiple of 21.9 times, which is at the high end of historical levels. Importantly, we do not count on our investments being carried higher by the general market and believe that a strategy of superior individual stock selection will prevail, with a careful focus on outstanding growth and fair valuation.

Thank you for reading the NorthStar Capital Q3 outline.

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