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Mitch on the Markets

Portfolio Manager Investing Insights

What History Tells Us to Expect in 2024

2024 already feels like a unique year to be an investor.

There are two ongoing wars with simmering geopolitical tensions, which threaten deeper U.S. involvement. The Federal Reserve appears poised to cut interest rates in 2024, but the timeline is far from certain. And perhaps most obviously, there are critical elections happening across the developed world, the most consequential of which is the U.S. presidential election.[1]

In thinking through all of these various factors affecting the global economy and markets, it is often useful for investors to look back on history. The past doesn't predict the future, of course. But history can serve to remind investors of what the economy and markets are capable of overcoming, and it can help us identify patterns useful for assigning probabilities.

Let's start with geopolitics. The breakout of new crises and regional conflicts tends to hurt sentiment, create short-term uncertainty, and drive volatility. But in my view, we're likely past the uncertainty phase with the Israel-Hamas war and the Russia-Ukraine war—markets have had plenty of time to price in each war's likely effect on global economic output.

To be fair, very recent escalations could easily change this calculus if U.S.-led retaliatory strikes on Iran-backed militias expand into something much bigger. This will be something to watch closely in the weeks ahead.

But we also know that looking back at conflicts since 1925 (when reliable S&P 500 data became available) such as the Korean War, Vietnam, the Cuban Missile Crisis, the Iran/Iraq War, and two U.S. wars in Iraq, it was only World War II and the Russia-Ukraine war that coincided with a bear market. I would argue that World War II was the root cause of that bear market, while inflation and the shock of aggressive monetary policy were the root causes of 2022's bear market—not necessarily Russia's invasion.

ABOUT MITCH ZACKS

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Mitch is the CEO & Senior Portfolio Manager at Zacks Investment Management. Mitch has been featured in various business media including the Chicago Tribune and CNBC. He wrote a weekly column for the Chicago Sun-Times and has published two books on quantitative investment strategies. He has a B.A. in Economics from Yale University and an M.B.A in Analytic Finance from the University of Chicago.

In terms of Fed policy, I think there's too much emphasis being placed on predictions about rate cuts in 2024. Investors are too focused on when and how many times the Fed will cut rates in the new year, grossly underappreciating the most important takeaway of all: that the Fed is poised to cut rates during an economic expansion. Historically, that's quite rare.

In the past 50+ years, there have only been five instances when the Fed engaged in rate cuts during an economic expansion. As seen in the table below, in three of these instances, the Fed cut rates by 75 basis points, which aligns with current projections moving the benchmark fed funds rate from 5% - 5.25% down to 4.25% - 4.5%. In every cycle when the Fed cut rates during an economic expansion, the S&P 500 delivered positive returns—and often very strong returns.

Rate Cuts During Economic Expansions, i.e., "Soft Landings"

Final Rate Hike	**Final Rate Cut**	**Change in Fed Funds Rate**	**S&P 500 Performance During This Stretch**
August 1971	December 1971	-225	+6%
August 1984	August 1986	-587	+49%
February 1995	January 1996	-75	+35%
March 1997	November 1998	-75	+44%
December 2018	October 2019	-75	+20%
	Average:	**-207**	**+31%**

Finally, there's the election year. The primary contests are ongoing, but if the U.S. gets a Biden-Trump rematch in the general election, it will be the first time since 1892 that the two parties' candidates have already been president. That last time was Cleveland versus Harrison.

This is an interesting fact, sure. But in my view, it's also a very important insight for markets. It means there's already a reasonably good understanding of policy positions and proposals from each candidate, which could theoretically equate to fewer uncertainties about taxes, property rights, and the business environment no matter who wins. Fewer uncertainties are a good thing.

Historically, markets have followed similar patterns during election years, with volatility in the runup to the general and a 'relief rally' once the contest is decided. It's worth noting, too, that in both years when Trump (2016) and Biden (2020) were elected, stocks delivered above-average returns. I think that's a testament to the fact that stock market performance is a lot less about the candidates and a lot more about the economic and earnings backdrop.

Bottom Line for Investors

It's only February, and it feels like there's quite a bit of concerning information out there to process. Geopolitics is center stage, but the possibility of another contentious U.S. presidential election and uncertain timing of interest rate cuts are also likely to weigh on investor sentiment.

History tells us the economy and markets can absorb these challenges. From an economic standpoint, I think inflation data has even more room to improve in the coming months, and Zacks sees a strong year for earnings growth compared to 2023. If narratives turn more negative in 2024, which they easily can, remember to return to the question that matters most: *what are the economic fundamentals telling us?*

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[1] J.P. Morgan. February 2, 2024. https://www.jpmorgan.com/insights/outlook/market-outlook/groundhog-day-what-can-investors-learn-from-the-past

STEADY INVESTOR WEEK

- **Service activity and job growth expands**
- **More Americans are turning 65 in 2024**
- **An update on regional banking**

Service Activity and Job Growth Signal More Expansion in Q1

As of February 7, the Atlanta Fed's GDPNow forecasting tool shows growth of 3.4% in Q1. It's early days, but key economic indicators for January support this assessment. The first key indicator is activity in the U.S. services sector, whose importance far outweighs activity in manufacturing. According to the Institute for Supply Management's (ISM) services-activity index, activity rose from 50.5 in December to 53.4 in January – a substantial increase into expansionary territory and well above consensus estimates. New orders, business activity, and employment all posted readings in expansion territory, and a majority of respondents in the survey said business is steady or improving. Robust activity in the services sector tracks with gains we saw in the labor markets in January, with the Labor Department reporting jobs growth of 353,000 for the month. December's payroll gains were also revised higher, from the previously reported 216,000 up to 333,000.[1] Technology companies have garnered headlines recently as many job cuts have been announced at high-profile companies, but a closer analysis suggests that companies are recalibrating priorities towards A.I. while also cost-cutting in areas where they over-hired in the months following the pandemic. Overall, the unemployment rate held steady at 3.7% in January, and wages continue to rise faster than inflation. Wage growth notched 4.5% higher in January, while the latest headline CPI reading in December came in at 3.4%.[2]

More Americans are Turning 65 in 2024 Than Ever Before

There's a reasonably good probability that someone reading this week's Steady Investor is turning 65 this year. That's because more Americans than ever before are celebrating their 65th birthday in 2024, a trend that is set to continue through 2027. According to the Bipartisan Policy Center, about 4.1 million Americans will turn 65 this year, which averages to about 11,200 per day. For context, over the previous decade about 10,000 Americans turned 65 each day. One takeaway from this data is that the country should see a surge in new retirements over the next few years, but that may not necessarily be the case. According to a new report from the Pew Research Center, about 20% of Americans 65 and older had a job last year, which is nearly twice as many 65-year-old workers compared to 1990. What's more, over 60% of 65+ year-old workers are still on the job full-time, compared to about 50% in 1987. There are several reasons for this shift, but chief among them is improved health, longevity, and a renewed sense of purpose.[3]

Is the Regional Banking Crisis Back for Round Two?

Jitters abounded last week in the regional banking space, with major downgrades issued for New York Community Bancorp (NYCB). Moody's Investors Service cut NYCB's credit rating to junk status on Tuesday, citing "financial, risk-management and governance challenges," which followed Fitch Ratings moving the company to the lowest possible investment-grade rating. The credit rating cuts came on the heels of a disappointing Q4 2023 earnings report for the bank, which revealed a surprising loss and dividend cut. A key reason NYCB is receiving so much attention is its connection to last year's regional banking crisis, given it was the purchaser of failed Signature Bank New York. NYCB has issued statements saying its deposits are stable, but it's often a crisis of confidence that ultimately determines a bank's fate. NYCB tried to quell worries by issuing a filing with securities regulators, forecasting net interest income of $2.8 billion in 2024, down from $3.1 billion in 2023. But it's only February. While we believe the market has already priced in risk to the broader U.S. financial system, regional banks should be a continued focus for investors in 2024—especially given their exposure to commercial real estate loans.[4]

[1] Wall Street Journal. February 5, 2024. https://www.wsj.com/economy/central-banking/u-s-services-activity-expands-more-than-expected-says-ism-3fe80ef7?mod=economy_feat3_central-banking_pos2

[2] Wall Street Journal. February 2, 2024. https://www.wsj.com/economy/jobs/jobs-report-january-today-unemployment-economy-4f3a772e?mod=economy_feat2_jobs_pos1

[3] Wall Street Journal. February 6, 2024. https://www.wsj.com/health/america-has-never-had-so-many-65-year-olds-theyre-redefining-the-milestone-4383e769?mod=djem10point

[4] Wall Street Journal. February 6, 2024. https://www.wsj.com/finance/banking/new-york-community-bancorp-stock-dropping-again-fb7b948c?mod=djemMoneyBeat_us

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