OBSERVATIONS

- The S&P 500 remained volatile last week with a sharp rally on Thursday (+2.3%) helping to bring the S&P 500 back to unchanged on the week. The Russell 2000 dropped -1.3% while the 10-Year US Treasury rose +15bps to close the week at 3.9%.[1]
- The Japanese Nikkei Index—a broad index of large cap equities akin to the US Dow Jones Index—sold off -19.6% from 31-Jul to 5-Aug after the Bank of Japan (BoJ) raised interest rates to 0.25%, their highest level since 2008. The Nikkei, however, recovered some of those losses gaining +9.5% on a single day (6-Aug), after the BoJ vowed to keep rates at this level for some time to allow markets to adjust and stabilize.[1]
- The ISM Services PMI improved in July rising to 51.4—any number above 50 indicates expanding economic activity—from June's 48.8 figure and suggests the service sector of the economy remains on solid footing.[1]
- The Senior Loan Officer Opinion Survey on Bank Lending shows that most banks tightened lending standards, but demand was steady for commercial and industrial loans while there was weaker demand for loans across all categories of residential real estate as well as for commercial real estate.[1]
- The New York Federal Reserve report on aggregate household debt showed that overall debt levels increased only modestly in Q2, largely due to slow growth in new mortgages, but that approximately 9.1% of credit card balances and 8.0% of auto loan balances transitioned to delinquency which is above pre-Covid averages for both measures and is increasing sharply for those under 30-years of age.[1]
- Mortgage applications increased last week by 6% compared to the week prior—but remain depressed on par with levels last seen in the mid-1990s—as mortgage rates fell to about 6.5% for a 30-year fixed rate, which is their lowest level since February 2024.[1]
- Initial jobless claims for the most recent week fell to 233k from the previous week's revised figure of 250k while the 4-week moving average now sits at 240k which is the highest mark since August 2023.[1]

EXPECTATIONS

- Earnings season is near complete: 91% of S&P 500 companies have reported results, 78% reported positive earnings surprises, and 59% reported positive revenue surprises. The blended (actual + forecast) earnings growth for Q2 is now near +10.8% on a year-over-year (YoY) basis—the highest YoY figure since Q4 of 2021.[2]
- During the worst of the recent sell-off, markets aggressively priced in a 100% chance of a half point rate cut for the Fed's September meeting. As equity markets recovered last week, interest rate cut expectations were ratcheted back with Fed Funds futures markets now looking for a 100% chance of a quarter point cut with a 50% chance for a half point cut in September. As of now, we are in the quarter point cut camp.[1]

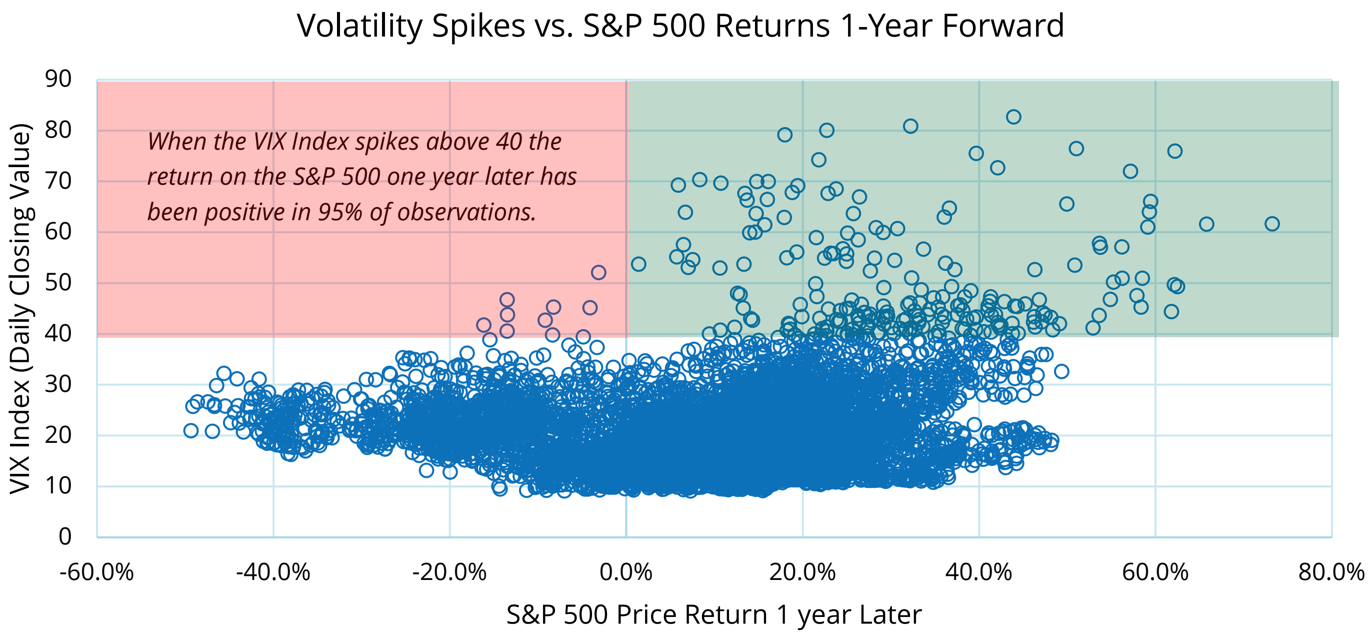
ONE MORE THOUGHT: Volatility spikes create investment opportunities—getting a little in the weeds.[1]

Recent market volatility seemingly marked a turn in investor sentiment from extreme bullish to more cautious now that the gravy train of leveraged momentum trading has hit a tough patch. Moments like this are always a good reminder to (a) know what you own and (b) make sure asset allocation is appropriately aligned with investing objectives. It's likely that equity markets are not out of the woods yet in terms of volatility, given continued economic slowdown concerns, the unknown standing of the so-called carry trade, election noise, and geopolitics. While a full-on correction may still be on the horizon, taking the S&P 500 to the 5,000 level, we see this recent volatility as a healthy clearing of speculation that had built in markets and should be viewed from an opportunistic

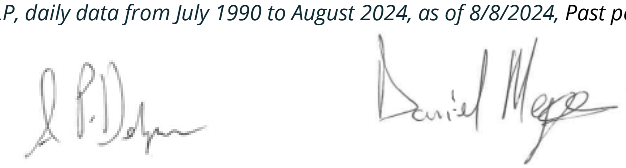
[1] *Bloomberg, LP 8/9/2024*
[2] *Factset Earnings Insight, 8/9/2024*

perspective. It is important to point out that credit spreads did not widen out commensurate with stocks declining, reinforcing the technical (i.e., non-fundamental) nature of the sell off—for now. One way to look at recent market action is through the lens of volatility, specifically the VIX Index (aka the Fear Index). *The VIX Index is derived using options markets where the index value is a measure of 30-day expected volatility of the S&P 500—the higher the index the higher the expected volatility.* Over the past 35 years the VIX Index has averaged 19.5, while it has eclipsed the 40.0 mark—a data point that we would consider a significant outlier—on just 209 daily occasions (or just 2.5% of all observations). During this recent selloff the VIX Index reached a closing high of 38.6 with an intraday high of over 65.0 (for context that compares to an intraday high during the worst of the pandemic of over 85). So, while not quite reaching the closing mark of 40.0, it is important to point out that those were index levels that have tended to mark short term bottoms where returns for the S&P 500 have generally been positive in the year following. The S&P 500 has produced positive returns in +95% of observations where the VIX spiked above 40.0 with a median 1-year forward return of +30.4% from the date of the VIX spike (see Chart of the Week; each dot represents the VIX on any given trading day (y-axis) and the 1-year forward return of the S&P 500 (x-axis)). While we may yet test 5,000 on the S&P 500, we think this data is good to hearken back to in the event that volatility spikes again.

CHART OF THE WEEK



Source: Clearstead, Bloomberg LP, daily data from July 1990 to August 2024, as of 8/8/2024, Past performance is not an indicator of future results



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