

Cash Flow and Carey



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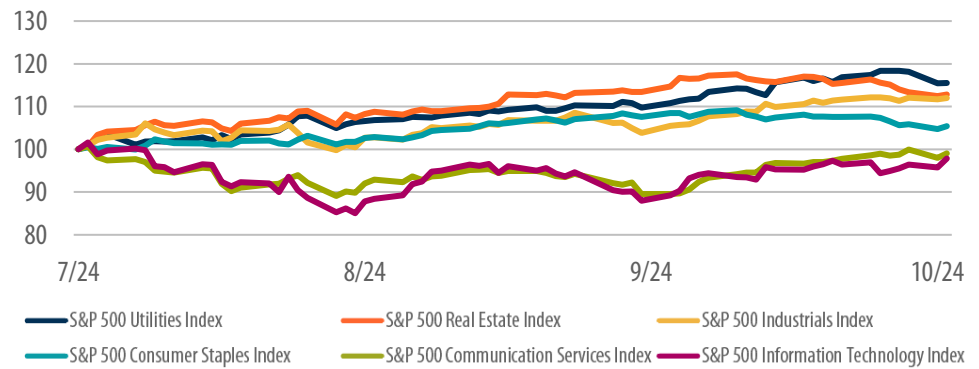
10/10/24

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Change In the Air?

Price Returns 7/9/24 – 10/8/24



Source: Bloomberg. Daily price returns, normalized to a factor of 100. Past Performance is no guarantee of future results.

View from the Observation Deck

For today's post we set out to highlight the impact of changes in policy rates (implied and actual) on sector performance. To do so we plotted the price returns of the three best and worst performing sectors between 7/9/24 to 10/8/24. We chose 7/9/24 as our starting point because on that day Federal Reserve ("Fed") chair Jerome Powell testified to Congress that the U.S. economy was no longer overheated, and that keeping interest rates too high for too long could jeopardize economic growth. On 9/18/24, just over two months later, the Fed voted to reduce its target rate by 50 basis points, setting the rate at 5.00% (upper bound).

As today's chart reveals, sector performance underwent a seismic shift in the wake of the Fed's comments and subsequent reduction in the policy rate. The total returns for the six sectors in today's chart were as follows (7/9/24 – 10/8/24):

S&P 500 Utilities Index: 16.37%	S&P 500 Consumer Staples Index: 6.07%
S&P 500 Real Estate Index: 13.64%	S&P 500 Communication Services Index: -0.75%
S&P 500 Industrials Index: 12.37%	S&P 500 Information Technology Index: -2.03%

For comparison, the total returns for these same sectors between 12/29/23 to 7/9/24 were as follows:

S&P 500 Information Technology Index: 34.21 %	S&P 500 Consumer Staples Index: 9.63%
S&P 500 Communication Services Index: 30.42%	S&P 500 Industrials Index: 6.82%
S&P 500 Utilities Index: 10.47%	S&P 500 Real Estate Index: -2.46%

Investor expectations regarding the depth of the Fed's interest rate cuts changed substantially since the end of June.

On 6/28/24 the federal funds futures market implied that the federal funds target rate would stand at 4.89% on 12/18/24 (the date of the Fed's final meeting in 2024). As of 10/8/24, that same futures market revealed that investors expect interest rates will decline to 4.33% by the Fed's final meeting of the year and may fall as low as 3.36% by the end of 2025.

Takeaway

As many investors are aware, the sectors that comprise the S&P 500 Index ("Index") often exhibit varying levels of sensitivity to changes in interest rates. Prior to the Fed's commentary in early July, the S&P 500 Information Technology and Communication Services Indices were the top performing sectors in the broader Index in 2024. Notably, those same sectors have been the worst performers in the Index since Powell's speech in July, declining by 2.03% and 0.75%, respectively, between 7/9/24 and 10/8/24. By contrast, Utilities and Real Estate, two of the more interest rate sensitive sectors in the Index, surged by 16.37% and 13.64%, respectively, over the same time frame. From our perspective, this dramatic change in performance can be explained, in part, by increasing expectations (and the eventual reality) of U.S. interest rate cuts. That said, the Fed is admittedly data-dependent when it comes to their policy decisions. On Friday, the Bureau of Labor Statistics reported that the U.S. economy added 254,000 in September 2024, well above the projected total of 140,000. Investors will want to keep close watch on U.S. economic data, in our opinion. Should the U.S. economy remain robust, the Fed may decide to adjust the timing of interest rate cuts to avoid reigniting inflation.