RBC Wealth Management

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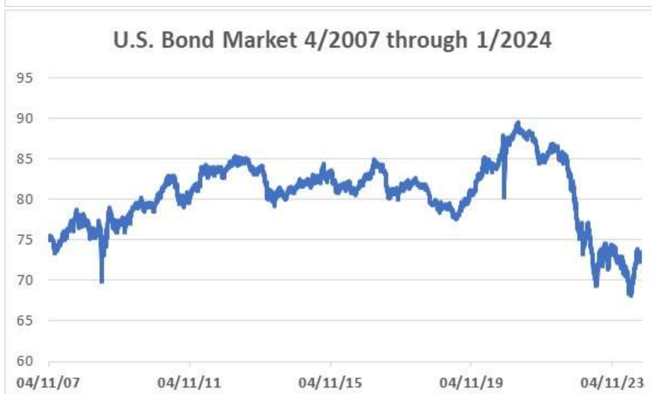
January 2024 Crescent Commentary

The month of January brought the first green shoot that financial markets have seen in over two years. Specifically, the U.S. stock market briefly exceeded its all-time high level previously set over two years ago in November 2021. As the chart below shows, the past two years have been a wild ride for U.S. stocks, with a crash of over 20% in 2022, followed by a partial recovery in 2023. For the full month of January 2024, U.S. stocks did end back below their 2021 all-time high, which they only exceeded for one day. The U.S. bond market remained at the same level set almost 17 years ago in 2007. Bond prices remain 18% below their all-time high levels set in 2020. Of course, the good news for bonds is that they pay higher interest than they have for the past 17 years. The combination of a stock market flat for over two years and a bond market flat for nearly 17 years gives investors a feeling of running in place for several years now. In terms of private markets, there wasn't a lot of news in January. Transactions remain below the the levels set in 2021 as higher interest rates make financing more expensive.[1]



Source: Yahoo Finance

So that's where financial markets stood at the end of January. The biggest piece of news for the month was the Fed's policy announcement on January 31st. Ever since the Fed began increasing interest rates to fight inflation in 2022, commentators and speculators have hung on the Fed's every word. In fact, the recovery in the U.S. stock market began last March after a string of bank failures. If that seems strange, yes it is. The reason bank failures fueled a recovery in stocks was that speculators started to bet the Fed would have to cut interest rates sooner rather than later as a result of the bank failures and economic weakness they could cause. Of course, we now know that rather than cut rates, the Fed continued to increase interest rates for most of 2023. On 1/31/24, the Fed said it doesn't expect more rate increases, but that there's no timeline to begin cutting rates. The Fed's current stance seems to conflict with speculator expectations.[2][3]

Why all the discussion about interest rates? Interest rates act as gravity to lower the value of all assets, both public and private. Higher interest rates lead to lower asset values, and lower interest rates lead to higher asset values. When the bank failures last March led speculators to believe the Fed would have to reduce interest rates sooner rather than later, it sent stocks on a recovery that continued through the end of last month. So now stocks are in the strange position of having recovered in anticipation of interest rate cuts, which we haven't had yet. The question now is whether speculator hopes for imminent rate cuts will become a reality. And that remains to be answered.

Given the uncertainty of the situation, we remain cautiously optimistic in our recommended investment positioning. Yes, we want to own assets that will thrive if the Fed cuts rates and U.S. economic growth continues. But we want to own them in diversified amounts so that if the future isn't flawless, your investments won't suffer. We also want to own assets shown to have protective qualities in the event that something unexpectedly bad happens, which happens from time to time.

As we've discussed in previous commentaries, the Fed's interest rate increases have a lag in terms of their economic impact. It could be a couple more years before we know the full economic impact of the Fed's rate increases. This is another reason we remain cautiously optimistic and recommend owning a diverse mix of assets. While investment markets as a whole seem to reflect just one possibility for the future – continued growth – it's important to recognize that many different outcomes are possible, and your asset allocation should reflect the possibility of many different outcomes.[(4)]

In other news last month, we saw that Bitcoin ETFs were approved for investors. The fact that the SEC approved this leaves us shaking our heads. While investors certainly have the right to invest or gamble their money wherever they want, creating an ETF makes it too easy for people to put money into a vehicle they don't fully understand, and which has shown incredible volatility that many investors are unlikely prepared for. Investors should also understand that the rush to offer Bitcoin ETFs is being pushed by fund companies so that they can make money off of investors. It isn't being pushed so that investors can make money for themselves. Many of the world's most successful and long-lived investors and business executives have warned against the dangers of crypto currencies. Last month, JP Morgan Chase CEO Jamie Dimon called Bitcoin a "pet rock" that does nothing except help with fraud and money laundering. Investors should pay attention to these people who have seen decades' worth of past investment innovations end in disaster.[(5)]

On a final note, we saw that U.S. GDP growth continued at a strong pace last month. This is part of what gives us our current stance of cautiously optimistic about the U.S. economy. One mistake we see other investors making right now is to invest as if our economy will not experience hiccups. We know for a fact we will experience hiccups along the way, and that's why the better strategy is to diversify and own a mix of assets that will benefit from continued growth but also protect you if problems arise. We will continue to do this for you.[(6)]

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Forbes Best-In-State Wealth Management Team 2024

Sources:
(1) Yahoo Finance
(2) CNBC
(3) The Wall Street Journal
(4) Board of Governors of the Federal Reserve System
(5) Fortune
(6) Reuters