



AUGUST 2024

# Capital Markets Commentary

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## Market Performance

August continued demonstrating the resilience of equity markets, with the S&P 500 Total Return Index gaining 2.43%, bringing its year-to-date return to an impressive +19.53%. This performance highlights the strength of large-cap stocks, particularly those with diversified revenue streams that can better navigate the current above-average interest rate environment.

For the first time in a long time, investors saw Large Cap Value stocks outperform their Growth peers on a relative basis. As of August 31, 2024, the Russell 1000 Value Index posted a monthly return of +2.68%, outpacing the Russell 1000 Growth Index, which gained +2.08% for the same period. Year-to-date, growth stocks are still ahead with a return of +21.12%, compared to +15.08% for value stocks. However, the recent shift in momentum towards value and away from growth-oriented technology stocks could indicate changing market sentiment.

### AS OF AUGUST 31, 2024

	MONTH	YTD
Russell 1000 Growth TR USD	2.08%	21.12%
Russell 1000 Value TR USD	2.68%	15.08%
S&P 500 TR	2.43%	19.53%
S&P MidCap 400 TR	-0.08%	12.24%
Russell 2000 TR	-1.49%	10.39%
MSCI EM NR USD TR	1.61%	9.55%
MSCI EAFE NR USD TR	3.25%	11.96%
Bloomberg US Agg Bond TR	1.44%	3.07%

SOURCE: MORNINGSTAR

U.S. Mid-cap and small-cap stocks, represented by the S&P MidCap 400 and the Russell 2000 indexes, have lagged their large-cap counterparts. The S&P MidCap 400 has gained +12.24% year-to-date, while the Russell 2000 has delivered +10.39%. The underperformance of smaller companies reflects their greater sensitivity to borrowing costs and economic volatility, making them less able to adapt to the Fed's restrictive monetary policy.

Away from the equity market, fixed-income investors experienced turbulence in early August as spreads widened, reflecting the growing economy. However, the bond market saw a turnaround in the latter part of the month.. This recovery propelled the Barclays U.S. Aggregate Index to post a solid gain of +1.44% for August, boosting its year-to-date return to +3.07%. The late-month rally provided a much-needed reprieve for bondholders as investor sentiment improved amidst easing inflation and clearer expectations from the Fed.

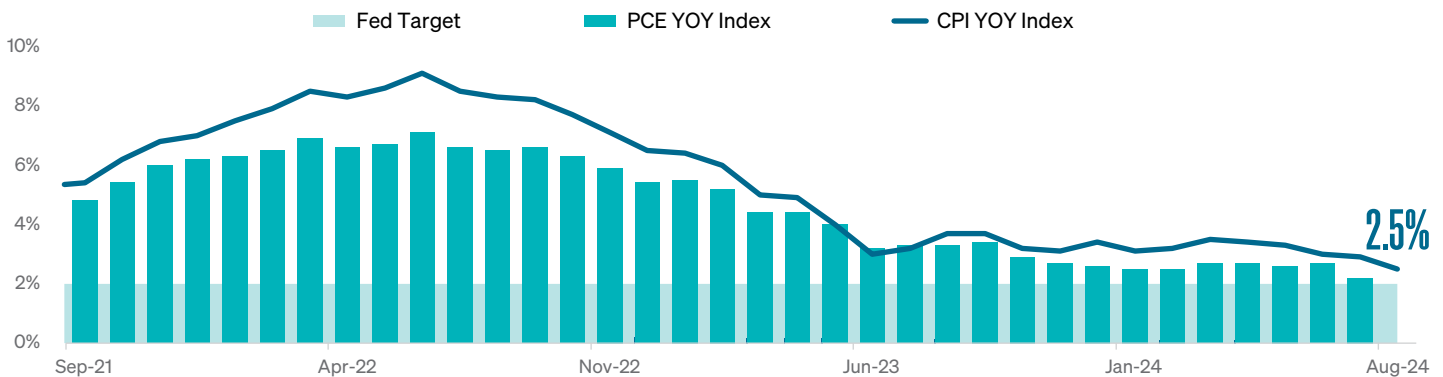
## Inflation and the Fed

Inflation continues to cool, but the Federal Reserve remains at a crossroads. August's Consumer Price Index (CPI) fell to 2.5% year-over-year, slightly below expectations of 2.6%, marking the fifth consecutive month of declining inflation. Additionally, the Personal Consumption Expenditures (PCE) Price Index—a key inflation gauge for the Fed—rose by just 2.5% year-over-year in July, below consensus estimates.

Since March 2022, the Fed has raised interest rates 11 times, pushing the overnight lending rate to a range of 5.25%–5.50%. This aggressive tightening has created the most restrictive real Federal Funds rate since 2007. While the Fed projects the long-term neutral rate to be between 3% and 3.5%, the pace and timing of future rate hikes are uncertain.

## INFLATION DATA CONTINUES TO FALL

US PCE Inflation Index YOY % and US CPI Inflation Index YOY% (as of 8/31/2024)



SOURCE: TRADING ECONOMICS

## Labor Market Cooling

The labor market is showing signs of cooling, catching the attention of both investors and policymakers. The Bureau of Labor Statistics (BLS) announced a significant downward revision in nonfarm payrolls for the one-year period ending in March 2024, reducing the figure by 818,000 jobs. Downward revisions are common, but the magnitude of this change was significant. Surprisingly, the market reaction to this news was muted. Some investors speculate that this is additional proof that the labor market is softening, and it might prompt the Federal Reserve to consider larger rate cuts at its September meeting.

In his speech at the Jackson Hole symposium, Fed Chair Jerome Powell acknowledged the cooling labor market but emphasized a cautious approach. He stated, "We do not seek or welcome further cooling in labor market conditions. The time has come for policy to adjust." This statement underscores the delicate balance the Fed must strike between managing inflation and sustaining employment.

## Yield Curve and Interest Rates

The 10-year and 2-year Treasury yield curve shifted from being inverted and closed the month with a positive slope after being inverted for 783 days. This inversion exceeded the 623-day inversion that began on August 18, 1978 and lasted through May 1, 1980. Yield curve inversions are significant because an economic recession has historically followed every yield curve inversion. It will be interesting to see if this change marks the beginning of a new trend or if it is a temporary anomaly.

## Housing

The U.S. housing market is also showing signs of strain, with the inventory of single-family homes for sale in the U.S. reaching its highest level since February 2008. This surge in inventory, combined with persistently high mortgage rates, could exert downward pressure on home prices and dampen demand further. The housing market, often a bellwether for broader economic trends, will be crucial to monitor in the coming months.

## Institute of Supply Management

The manufacturing sector continues to struggle, with the Institute of Supply Management (ISM) Manufacturing PMI coming in at 47.2 in July, below the forecasted 47.5. This contraction suggests that weak demand for new orders is weighing on the sector. In contrast, the ISM Services PMI was slightly above expectations at 51.4, indicating moderate expansion in the services sector, which has shown more resilience than manufacturing.

## Looking Forward

The economic environment remains uncertain as we move toward the Fall of 2024. With inflation easing, the labor market softening, and mixed performance signals from various sectors, the Federal Reserve's decisions will be pivotal in shaping the market's trajectory. The recent positive slope of the yield curve and the shift towards value stocks add further complexity to the outlook as investors speculate on the timing and magnitude of potential Fed rate cuts.

While broader equity markets have delivered strong returns, the divergence in performance across sectors and market capitalizations highlights the need for vigilance and diversification. As the Fed navigates the delicate balance between controlling inflation and supporting economic growth, investors should remain prepared for potential volatility and be ready to adjust their portfolios accordingly.

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## INDEX DESCRIPTIONS

**Bloomberg US Aggregate Bond Index:** The Index is a broad-based flagship benchmark that measures the investment-grade, US dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, fixed-rate agency MBS, ABS, and CMBS (agency and non-agency). Provided the necessary inclusion rules are met, US Aggregate-eligible securities also contribute to the multi-currency Global Aggregate Index and the US Universal Index. The US Aggregate Index was created in 1986, with history backfilled to January 1, 1976.

**MSCI EAFE Index:** The Index is an equity index that captures large and mid-cap representation across 21 Developed Markets countries around the world, excluding the US and Canada. With 783 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.

**MSCI EM Index:** The Index captures large and mid-cap representation across 24 Emerging Markets (EM) countries. With 1,440 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.

**Russell 1000 Growth:** The index measures the performance of the large-cap growth segment of the US equity universe. It includes those Russell 1000 companies with relatively higher price-to-book ratios, higher I/B/E/S forecast medium-term (2 year) growth and higher sales per share historical growth (5 years). The index is completely reconstituted annually.

**Russell 1000 Value Index:** The index measures the performance of the large-cap value segment of the US equity universe. It includes those Russell 1000 companies with relatively lower price-to-book ratios, lower I/B/E/S forecast medium-term (2 years) growth, and lower sales per share historical growth (5 years). The index is completely reconstituted annually.

**Russell 2000 Index:** The Index is constructed to provide a comprehensive, unbiased barometer of the small-cap segment of the US equity market. A subset of the Russell 3000 Index, it includes approximately 2,000 of the smallest securities based on a combination of their market cap and current index membership.

**S&P 400 MidCap Index:** This index serves as a gauge for the U.S. mid-cap equities sector and is the most widely followed mid-cap index. To be included in the index, a stock must have a total market capitalization between \$5.8 billion and \$15.8 billion.

**S&P 500 Index:** The Index tracks the stock performance of 500 of the largest companies listed on stock exchanges in the United States. It is one of the most followed equity indices and includes approximately 80% of the total market capitalization of U.S. public companies.



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