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Market Musings

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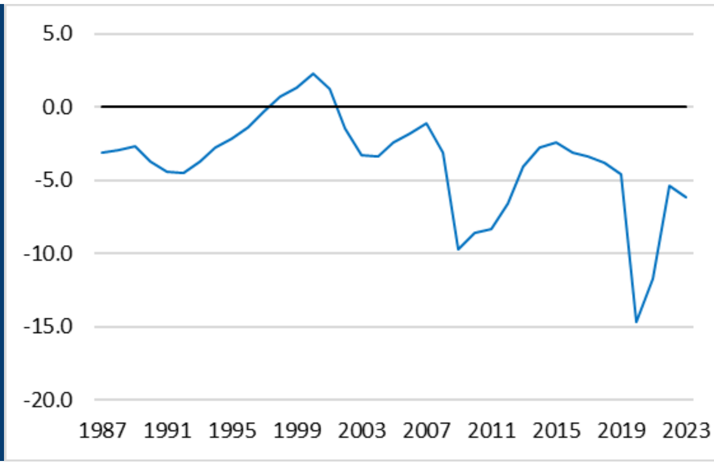
The chart represents the balance of the federal budget. A budget is in deficit when the line is below zero. Note the dramatic increase in the deficit in 2020 during the Covid crisis. An increasing deficit during the current economic expansion indicates that inflation could remain a problem.

(data source: St. Louis FRED)



Summer is a Time to Step Back and Look at Where We Are!

The first half of 2024 was good for investors. While the MAG 7 had a strong first half, the balance of equities did okay in the face of higher interest rates that the Federal Reserve was using to slow the economy to contract inflation. So far, policies are proving effective as inflation has dropped to the 2-3% annual rate, sufficient to trigger an interest rate reduction in September. Both equity and fixed-income markets rallied in the face of this expected policy move as lower interest at the end of July when he said a rate cut in September is “on the table.” One piece of good news was that July witnessed a broadening out of the stock market as laggard stocks surged and technology stocks weakened. Expectations for continued declines in interest rates are expected to keep the stock market rally intact and produce a favorable response from borrowers who have been waiting for a decline in interest rates.

The excessive government spending and related boom in consumer outlays may be coming to an end. The problem is that federal debt is running at about 7% of gross domestic product (GDP), an accepted measure of how well the economy is doing. Given this stage of the economic cycle, this ratio is at a very high level. As a result, the level of inflation is higher because of this excess spending. However, such spending will also add to GDP growth in coming quarters so that consumers may benefit from the expected decline in inflation along with lower interest rates. At the same time, a slowing economy may produce a gradual increase in unemployment. While we have a good idea of what the Fed will be doing for the year's balance, we are not so sure about government spending and the size of the federal deficit. The likelihood of a surge in spending as we approach the election is unlikely as candidates spend most of their time campaigning and not making serious decisions about changing fiscal policy. We will likely have new spending priorities in the long term since both parties look differently at government spending.

“One of the great mistakes is to judge policies and programs by their intentions rather than their results. ”

- Milton Friedman

Market Commentary

July was a month of rotation in domestic stocks…mostly out of the names that had huge gains for the first six months of the year as investors poured into cyclical stocks and rate-sensitive sectors such as U.S. small-caps. Across the pond, many European equity markets have logged double-digit gains this year, in addition to a select few in the Asia Pacific, most notably Japan and Taiwan. Also, domestic fixed-income markets rallied, bringing the yields of two-year treasuries from 4.72% to 4.27% and the ten-year treasury yields from 4.34% to 4.03%, respectively. These yields are the lowest since February/March. The U.S. dollar remained unchanged versus the Euro while the Japanese yen rallied off record lows.

Assembly Bill 2927, once signed by Governor Newsom, will make California the 26th state to require a personal finance course for every high school student graduating in 2031 and beyond.

Source: EdSource