MARKIN MICKELSON
FINANCIAL GROUP
of Wells Fargo Advisors

Monthly Market Commentary

January 2024

US Economy

The US economy continues to surprise to the upside, as fourth quarter's advanced Gross Domestic Product (GDP) release showed a 3.3% quarter-over-quarter expansion, considerably above expectations. On a year-over-year basis, GDP saw a relative increase, coming in at 3.1% versus third quarter's 2.9%. Furthermore, hiring accelerated in January, as nonfarm payrolls rose by a seasonally adjusted 353,000, nearly twice the expected gain of 185,000 and above the upwardly revised gain of 333,000 in December[1]. The January unemployment rate was stable at a seasonally adjusted 3.7%, rather than rising to 3.8% as surveyed economists had expected.

Looking ahead, labor markets are grappling with cross currents reinforcing our view of shallow employment declines and a potential modest rise in the unemployment rate during 2024. A resilient economy is keeping labor-market conditions tight, despite marginal softening from a rebalancing of pandemic-related distortions in labor supply and demand. Catch-up hiring could continue to unwind in 2024 and combine with an economic slowdown to gradually lift the unemployment rate over the course of the year.

US Markets

Large-cap US equities, as defined by the S&P 500 index, trended higher in January, amid signs of economic strength signaling that the economy may avoid a recession. Further aiding large-cap equities was the Federal Open Market Committee's (FOMC) widely anticipated decision to leave interest rates unchanged along with labor market data showing the economy continues to outpace expectations. That said, the more cyclically sensitive small-cap equities, as defined by the Russell 2000, trended slightly lower, as interest rates crept up, after the Federal Reserve alluded to holding off on interest rate cuts until later this year. Looking ahead, Fed actions, economic developments, the level and direction of interest rates, China, and geopolitics are likely to be the markets' main macro focus points for the foreseeable future.

Fixed Income

The FOMC met in January and kept the federal funds rate unchanged at 5.25% - 5.50% for the fourth straight meeting. The FOMC stated that "it will not be appropriate to reduce the federal funds target range until inflation moves sustainably toward 2%." The Fed stated recent indicators suggest that economic activity has been expanding at a solid pace. Job gains remain strong, and the unemployment

[1] https://www.bls.gov/news.release/pdf/empsit.pdf

rate has remained low. Furthermore, inflation has eased over the past year but remains elevated. The FOMC judges that the risks to achieving its employment and inflation goals are moving into better balance. The economic outlook is uncertain, and the Fed remains highly attentive to inflation risks.

Looking forward, in considering any adjustments to the target range for the federal funds rate, the FOMC will carefully assess incoming data, the evolving outlook, and the balance of risks. Also, the Fed does not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward 2%. The FOMC will continue to take into account a wide range of information, including readings on labor market conditions, inflation pressures, inflation expectations, and financial and international developments. We believe the Fed has reached its terminal policy rate for this cycle and that additional rate hikes are likely off the table in the near term. Most of the attention will now focus on the timing and the extent of rate cuts during 2024.

International Markets

We believe Europe's economic slowdown gathered enough momentum at the end of 2023 to push the region into a recession. A composite index of Eurozone business activity contracted for a seventh straight month, hurt by manufacturing under pressure from soft global trade, and further aggravated by weakening service-sector activity. Last year's aggressive rate hiking by the European Central Bank (ECB) tightened credit conditions, weighing on spending plans among industrial firms. However, disinflation is sustaining household consumption, likely limiting the region's downturn.

Asia's trade-sensitive economies remained pressured in December by China's fragile recovery and broader weakness in global trade. China's manufacturing activity fell to a six-month low, while service-sector growth virtually flatlined. Weak consumer demand and the ongoing property market slump continue to hinder China's economic rebound, increasing the likelihood of more accommodative fiscal and monetary policy in 2024 to support growth. A manufacturing-led slowdown in Taiwan worsened under weak semiconductor demand, while South Korea's November manufacturing rebound proved short-lived as its gauge slipped back into contraction. Japan's manufacturing slump deepened last month, although the nation's services sector rebounded to a three-month high amid unexpected retail strength. India, Indonesia, and the Philippines were supported by strong domestic demand in bucking the broader Asian manufacturing downtrend.

Commodities

In late 2023, the US achieved record crude oil production of 13.3 million barrels per day, as more efficient drilling boosted supply growth. Given the record production volume, and slowing economic conditions in the US, we would usually expect crude inventories to rise. However, US crude inventories remain quite low, and have even fallen below their 5-year average. The culprit behind lower US oil inventories, even while production is growing, is the rise in exports. Year-over-year, US oil exports are up 23% as of January 12, 2024, while US oil production is up roughly 9%.[1]

The US is exporting more crude oil because emerging markets are demanding it, especially China.

[1] https://www.eia.gov/dnav/pet/pet_move_wkly_dc_NUS-Z00_mbblpd_w.htm

According to the Energy Information Administration's data through October 2023, US crude oil exports to China were on track to double from year-end 2022 to year-end 2023. As a result, China's average share of US crude exports was also on track to double from 6% to 12%.[2] The bottom line is that US oil production did rise in 2023, but US oil inventories did not. Much of the US' extra oil production was exported to emerging markets, such as China. Emerging markets continue to be the main source of oil demand globally, and US oil exports specifically. We anticipate emerging market oil demand to rise throughout 2024, and global oil prices with it.

What Does This Mean to Me?

As the markets face tight Fed policy, sticky inflation, slowing economic growth, and geopolitical tensions, we continue to advocate focusing on quality in investment portfolios. Our view is that earnings for all equity classes may have peaked and could move lower as the economy weakens, and revenue growth stalls. In the near term, we anticipate pressure on earnings as well as prices with bouts of weakness and range trading. Once the economic slowdown appears to be fully priced into market valuations, we likely will look for an opportunity to position for an emerging early cycle recovery later in 2024. As is most often the case, that time will likely come while the economy is still within the grips of the slowdown. More cyclically oriented equities could benefit the most when the economy gains its footing and corporate earnings begin to grow again. As such, we continue to encourage investors to remain patient and strategically deploy sidelined cash.

If you have any questions or concerns, please do not hesitate to reach out to us at any time.

Sincerely,

Chad E. Mickelson, CRPC®, CFP®
Managing Director – Investments
Financial Advisor

Clint A. Markin, CRPC®, CFP®
Managing Director – Investments
Financial Advisor

[2] https://www.eia.gov/dnav/pet/PET_MOVE_EXPC_A_EPC0_EEX_MBBLPD_M.htm

Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability, and different accounting standards. This may result in greater share price volatility. Investing in emerging markets accentuates these risks.

Investments in fixed-income securities are subject to market, interest rate, credit, and other risks. Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in interest rates can cause a bond's price to fall. Credit risk is the risk that an issuer will default on payments of interest and/or principal. This risk is heightened in lower rated bonds. If sold prior to maturity, fixed income securities are subject to market risk. All fixed income investments may be worth less than their original cost upon redemption or maturity.

PM-08052025-6364008.1.1