

The Descent Is the Hardest Part

This week the Federal Reserve will almost certainly join other major central banks in easing monetary policy. It has been a long time coming. The Federal Funds target rate reached its peak of 5.25% - 5.50% last July. Having indicated last month that “the time has come for policy to adjust,” Fed Chair Jerome Powell has prepared markets for the initial decent.

As any seasoned mountaineer would tell you, a journey’s most perilous point occurs when coming down. For monetary policy and for investors, the risk begins with the size of the first step. Will the Federal Reserve cut its target rate by a customary 0.25% or make a larger cut of 0.50%? Economic data could support both decisions.

We do not know how large this week’s reduction in interest rates will be. What we know, however, is that markets have rallied over the last week in anticipation that this first step will be one of many. The 2-Year Treasury yield captures this anticipation succinctly; the spread between that rate and the Federal Funds effective rate is at its lowest level in over 15 years, a spread that reflects expectations that short-term interest rates will move sharply lower over the next two years. Last week’s rally in U.S. stocks reflects similar expectations—both in the path of interest rates and careful execution of their initial descent.

CHART OF THE WEEK

2-Year Treasury Yield – Effective Federal Funds Rate



Source: Bloomberg, through September 16, 2024.

Index Returns (%)

Equities	Level	1 Week	QTD	YTD	1 Year	3-Year Ann.
S&P 500	5633	3.01	3.48	19.30	28.43	10.00
Russell 1000 Growth	3677	4.39	0.33	21.09	33.24	9.44
Russell 1000 Value	1839	1.73	7.53	14.65	21.17	7.85
FTSE High Dividend Yield*	445	2.02	7.02	15.40	21.61	10.01
S&P Small and Mid Cap	17086	3.69	5.46	9.69	20.42	5.43
MSCI EAFE	2413	1.67	4.79	10.84	18.30	4.30
MSCI EM	1086	2.23	0.89	8.60	13.47	-2.24

* Bloomberg U.S Large Cap Dividend Yield Total Return Index used as substitute for index characteristics.

Index Characteristics

	NTM P/E	NTM P/E (20Y med)	NTM P/S	NTM P/S (20Y med)	Div. Yld
S&P 500	23.7	16.8	3.0	1.7	1.3
Russell 1000 Growth	31.5	19.8	5.4	2.0	0.6
Russell 1000 Value	18.6	14.9	1.9	1.4	2.0
FTSE High Dividend Yield*	14.1	14.2	1.6	1.6	4.0
S&P Small and Mid Cap	18.5	19.0	1.3	1.2	1.6
MSCI EAFE	14.8	14.7	1.5	1.1	3.1
MSCI EM	13.0	12.6	1.4	1.3	2.7

Fixed Income	Yield	1 Week	QTD	YTD	1 Year	3-Year Ann.
U.S. Aggregate	4.13	0.67	6.00	5.08	10.60	-1.45
U.S. Int. Gov/Credit	3.85	0.43	4.48	4.90	9.17	0.12
U.S. Corporates	4.66	0.83	6.39	5.79	13.05	-1.41
High Yield	7.08	0.55	4.56	7.43	13.89	2.76
Municipals (1-10)	2.89	0.14	2.45	1.72	5.53	0.31

Levels

Currencies	Last	1 Wk Ago	Prev YE	3 Yrs Ago
DX/¥	100.89	101.63	101.33	93.20
\$ per €	1.11	1.10	1.10	1.17
\$ per £	1.32	1.31	1.27	1.37
¥ per \$	142.41	142.44	141.04	109.93

Levels (%)

Key Rates	Last	1 Wk Ago	Last Qtr	Prev YE	1 Yr Ago	3 Yrs Ago
2-yr Treasury	3.55	3.60	4.76	4.25	5.06	0.22
10-yr Treasury	3.62	3.64	4.40	3.88	4.30	1.36
30-yr Treasury	3.93	3.96	4.56	4.03	4.39	1.90
3-mo. LIBOR	5.12	5.21	5.59	5.59	5.67	0.12
6-mo. CD rate	4.59	4.72	5.42	5.28	5.74	0.13
Prime Rate	8.50	8.50	8.50	8.50	8.50	3.25
30-yr fixed mortgage	6.59	6.66	7.26	6.99	7.55	3.00

Levels

Commodities	Last	1 Wk Ago	Prev YE	3 Yrs Ago
Oil (WTI)	71.19	65.75	70.98	57.09
Gasoline	3.20	3.25	3.12	3.19
Natural Gas	2.32	2.23	2.51	5.11
Gold	2570	2517	2063	1754
Copper	9173	8899	8464	9307
Wheat	576	559	628	709
BBG Index	231.39	222.36	226.43	208.31

LAST WEEK IN REVIEW

- **Consumer Price Index (Aug.):** 0.2%HL / 0.3%C (MoM), 2.5%HL / 3.2%C (YoY). Slight acceleration in core inflation from July unlikely to deter Fed from cutting rates.
- **Producer Price Index (Aug.):** 0.2%HL / 0.3%C (MoM), 1.7%HL / 2.4%C (YoY). In line with expectations, suggesting lower August PCE inflation than August CPI inflation.
- **U. of Mich. Sentiment (Sept.):** 69 – slight improvement from July.

THIS WEEK

- **Retail Sales (Aug.):** 9/17
- **Industrial Production (Aug.):** 9/17
- **Housing Starts & Permits (Aug.):** 9/18
- **FOMC Rate Decision & Forecasts:** 9/18
- **Leading Economic Indicators (Aug.):** 9/13

S & P SECTOR RETURNS

