APRIL: STOCKS & BONDS DECLINE
INFLATION, INTEREST RATES & ECONOMIC GROWTH

Figure 1: 4/30/2024 Returns (source: Bloomberg)
Conditional formatting: green (high) to red (low) for each time period

Bonds	ETF	Month	YTD	1YR	vs. 52-wk High	vs. 52-wk Low
US Aggregate Fixed Income	AGG	-2.5%	-3.2%	-1.5%	-5.2%	4.0%
Investment Grade Corp Bonds	LQD	-3.2%	-4.1%	-0.3%	-5.8%	6.9%
U.S. Treasury Bonds	GOVT	-2.4%	-3.1%	-2.7%	-6.2%	2.6%
U.S. 20+ YR Treasuries	TLT	-6.4%	-9.9%	-14.1%	-17.2%	7.0%
Muni Bonds	MUB	-0.9%	-1.2%	1.9%	-2.3%	5.5%
US High Yield	HYG	-1.3%	0.1%	7.5%	-2.3%	6.4%
Non-US Corp Bonds	IBND	-2.1%	-4.3%	0.6%	-6.1%	6.6%
Emerging Markets Bond LC	EMLC	-2.2%	-4.6%	0.3%	-9.2%	2.6%
Global Equity						
ACWI Global Equity	ACWI	-3.6%	4.4%	17.0%	-3.8%	20.2%
ACWI Global Equity ex US	ACWX	-2.4%	2.1%	8.1%	-3.1%	16.0%
International Developed	EFA	-3.2%	2.5%	8.3%	-3.5%	17.6%
Emerging Markets	EEM	-0.2%	1.9%	7.6%	-2.4%	12.7%
Global Equity by Region						
United States	VTI	-4.3%	5.2%	22.4%	-4.8%	24.2%
Europe	IEUR	-2.5%	2.6%	6.9%	-3.1%	19.8%
Asia ex-Japan	AAXJ	0.6%	2.4%	4.5%	-3.5%	11.9%
China	MCHI	5.4%	2.8%	-9.2%	-16.2%	17.7%
Japan	BBJP	-5.5%	5.4%	17.4%	-6.4%	16.0%
Latin America	ILF	-3.7%	-5.8%	16.8%	-8.2%	15.5%
US Equity						
US S&P 500	IVV	-4.0%	5.9%	22.6%	-4.3%	24.4%
NASDAQ 100 QQQ	QQQ	-4.4%	3.8%	32.5%	-5.5%	34.8%
US Large Growth	IWF	-4.2%	6.6%	31.7%	-5.3%	33.8%
US Large Value	IWD	-4.2%	4.2%	13.2%	-4.5%	19.6%
US Eqwt S&P 500	RSP	-4.8%	2.6%	12.9%	-5.1%	20.9%
US Mid Cap	IJH	-5.9%	3.3%	16.8%	-6.4%	23.4%
US Small Cap	VTWO	-6.9%	-2.2%	13.5%	-7.6%	21.1%

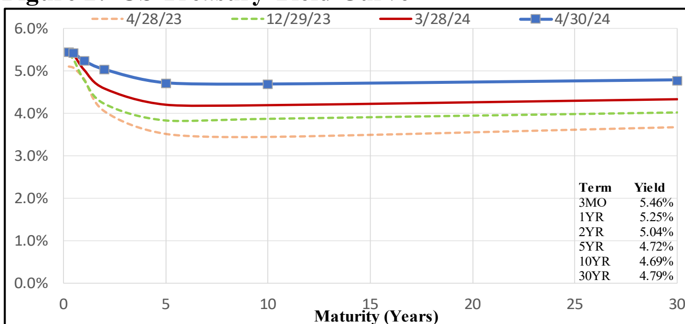
Bond yields rose sharply in April as stubborn inflation dashed hopes for imminent Federal Reserve (Fed) interest rate cuts, pushing stock and bond prices lower. Performance highlights for the month and year-to-date (YTD) are summarized below.

- Bonds: The US Aggregate index (AGG) fell 2.5% this month (-3.2% YTD) as yields spiked. Long-term Treasuries (TLT) are highly sensitive to interest rates, falling 6.4% (-9.9% YTD). Corporate bonds (LQD) lost 3.2% (-4.1% YTD), and high yield (HYG) lost 1.3% (+0.1% YTD). Non-US bonds were down and have under-performed YTD as the US dollar strengthened.
- Global equity (ACWI): -3.6% in April (+4.4% YTD).
- US Equity: The broad market (VTI) fell 4.3% (+5.2% YTD), and the S&P 500 (IVV) was down 4.0% (+5.9% YTD). Small stocks (VTWO) fell 6.9% (-2.2% YTD), and midcaps (IJH) lost 5.9% (+3.3%YTD). Ten out of eleven sectors posted losses for the month, led lower by real estate stocks (XLRE), which are very sensitive to interest rates (bond proxies); only utilities (XLU) posted gains for the month. The energy sector (XLE) is still up 12.4% this year as oil prices have risen to $82 per barrel.
- Non-US Equity: Developed markets (EFA) fell 3.2% in April (+2.5% YTD), with weakness in Japan (BBJP -5.5%, +5.4% YTD) and Europe (IEUR -2.5%, +2.6% YTD). Emerging market stocks (EEM) fell just 0.2% (+1.9% YTD) as China equities (MCHI) surged 5.4% (+2.8% YTD); Latin American stocks (ILF) were down 3.7% (-5.8% YTD). Stocks in India (INDA) logged marginal gains and are up 27.6% over the past year.

Interest Rates and the Economy

The yield curve (Figure 2) plots the interest rates (vertical axis) for various US Treasury maturities (horizontal axis). Yields rose sharply in April as recent data suggested that inflation remains stubbornly high (March CPI +3.5%), dampening hopes for Fed rate cuts in the near future. Just today, the Fed acknowledged the lack of progress on inflation in recent months, even as they again held rates steady. The inverted yield curve (short-term > long-term yields) signals economic slowdown or recession ahead. The benchmark 10-year US Treasury now yields 4.69%.

Figure 2: US Treasury Yield Curve

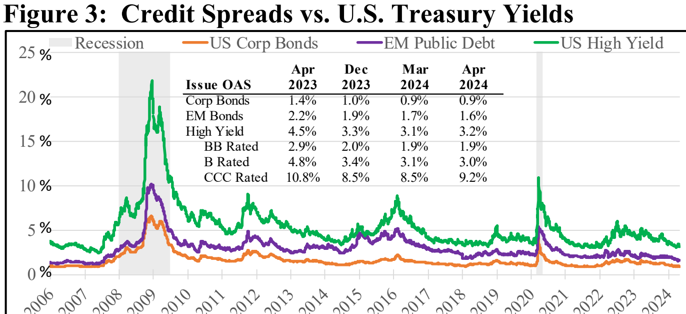


Source: Board of Governers of the Federal Reserve System via St. Louis Fed (FRED)

For bonds other than US Treasuries, we track the option-adjusted spread (OAS) between their yields and Treasuries of comparable maturities (Figure 3). Low or narrowing spreads signal optimism, while high or widening spreads signal fear. Spreads were mixed in April but remain very low by historical standards.

- Investment grade corporate bond spreads were unchanged at +0.9% this month, well below year-ago spreads of +1.4%.
- High yield (non-investment grade) spreads widened to +3.2% but are still down from +4.5% in the last year. Spreads of the riskiest bonds (rated CCC & below) widened to +9.2% over Treasuries but are still below the +10.8% spreads one year ago.
- Emerging market spreads narrowed to +1.6% and have tightened steadily versus +2.2% a year ago, indicating that investors see relatively low risk in emerging market debt.

Figure 3: Credit Spreads vs. U.S. Treasury Yields

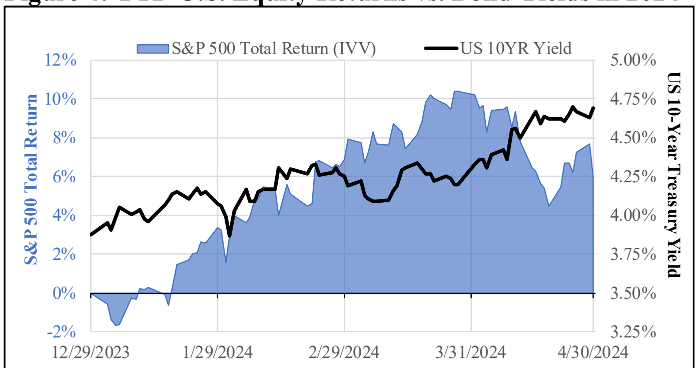


Source: Ice Data Indices, LLC via St. Louis Fed (FRED)

Interest Rates, Inflation & GDP Growth

Financial markets continue to be focused on the future path of interest rates. Stocks surged after the Fed announced in October that moderating inflation reduced the need for further rate hikes, stating that three rate cuts were likely in 2024 (0.25% each). From November to March, benign inflation data led to even more aggressive rate cut expectations, sending stocks ever higher. That changed in April as economic data (strong job growth and persistent inflation) pushed potential rate cuts farther into the future, driving yields higher and stocks lower; just one 0.25% rate cut in 2024 is now priced into the market. The relationship between yields (interest rates) and stock prices is shown in Figure 4.

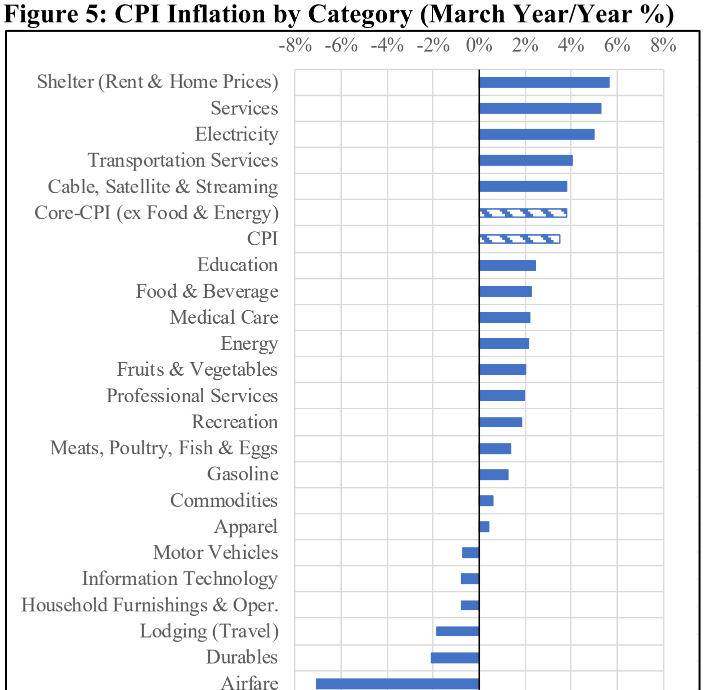
Figure 4: YTD U.S. Equity Returns vs. Bond Yields in 2024



Sources: Board of Governors of the Federal Reserve System (US), Bloomberg, Yahoo! Finance

After stabilizing around 4.25% in the first quarter, the US 10-year Treasury yield spiked in April, and the stock market plunged. The downturn accelerated after the most recent inflation data was released: Headline Consumer Price Index (CPI) inflation remained at 3.8% with run-rate of well over 4% (annualized three-month inflation rate). After peaking at 9.0% in June 2022, inflation has come down significantly, but the "last mile" of progress toward the Fed's 2% target is proving difficult and uneven. Figure 5 plots the year-over-year inflation of multiple CPI sub-components.

Figure 5: CPI Inflation by Category (March Year/Year %)

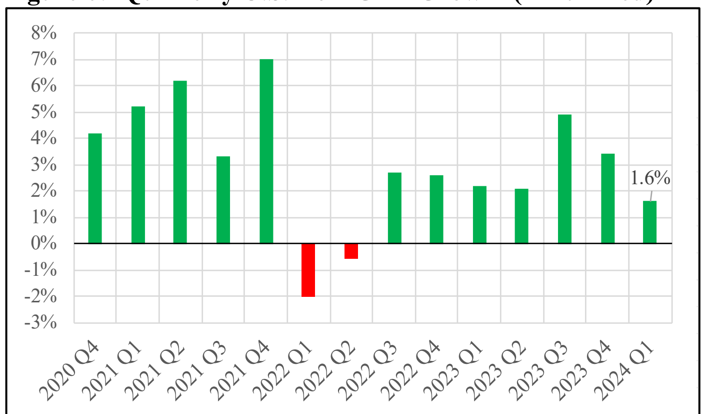


Source: U.S. Bureau of Labor Statistics

Over the past year, inflation has been broadly under control across most of the categories, with several showing actual price decreases, including airfare, durables (substantial goods with a multi-year life, e.g. washer/dryer or refrigerator), lodging (hotels, etc.), household goods, technology and new/used vehicles. Elevated inflation is currently being driven Shelter (rent & home prices), which is more than half of the core CPI and Services inflation calculations; soaring rents and home prices must moderate for inflation to sustainably decline. Electricity prices have spiked over the past year, as have Transportation Services (primarily auto insurance and repair). These "sticky" inflation categories suggest it will take time to reach the Fed's 2% inflation target.

Meanwhile, economic growth has been resilient but may be slowing. Last week, the Bureau of Economic Analysis (BEA) reported that U.S. real GDP grew at an annualized rate of 1.6% in the first quarter of 2024. (Note: Real GDP stands for Gross Domestic Product, the value of all final goods and services produced in the U.S., adjusted for inflation.) This is a slowdown from the 3-5% growth rates observed in the second half of 2023 and is now below the 2011-2019 average annual growth rate of 2.4%. Figure 6 plots quarterly growth rates in the post-COVID era.

Figure 6: Quarterly U.S. Real GDP Growth (annualized)



Source: U.S. Bureau of Economic Analysis

Bottom Line

Investors remain hyper-focused on each new economic data point, searching for clues as to when the Fed will begin cutting interest rates and by how much. Stocks rallied strongly from November to March as Fed guidance and incoming data pointed to moderating inflation and imminent interest rate cuts. In April, the tone changed as another stronger-than-expected employment report and higher-than-expected inflation data suggested that while the Fed may not increase rates further, they probably will not cut rates until later this year at the earliest. In today's Fed announcement and press conference, Chair Powell clearly stated that "gaining the confidence to cut" is taking longer than originally thought.

In general, rising interest rates are not good for the stock market; conversely, stocks tend to thrive in a falling interest rate environment. Investors will continue to adjust their expectations with every new economic data release (including the April jobs report this week and the next CPI report due on May 15), and market volatility is likely to continue. Diversification continues to be critical, with solid bond and cash yields offering an attractive complement to stocks as the story continues to unfold, providing a cushion to offset further potential equity market volatility.

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