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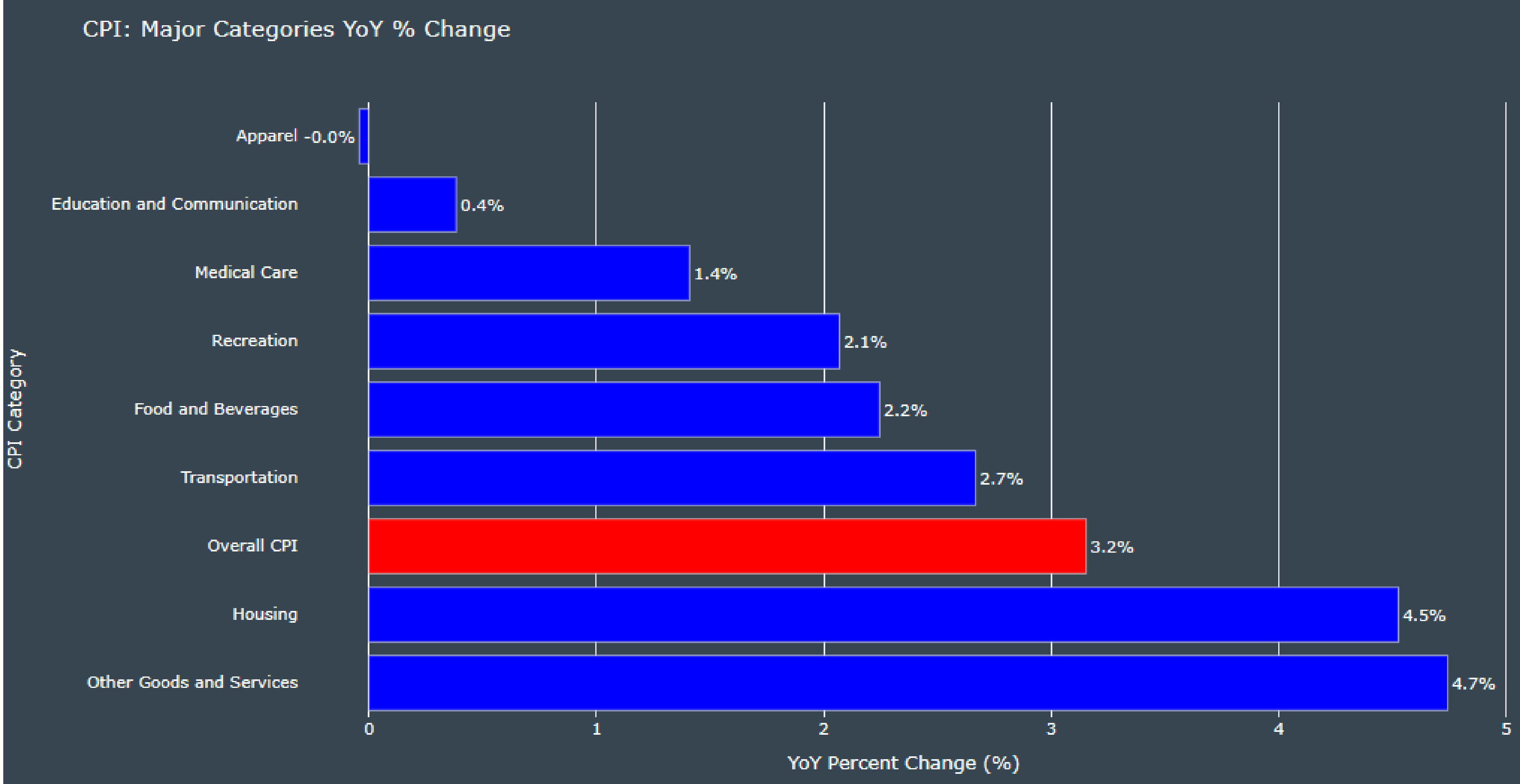
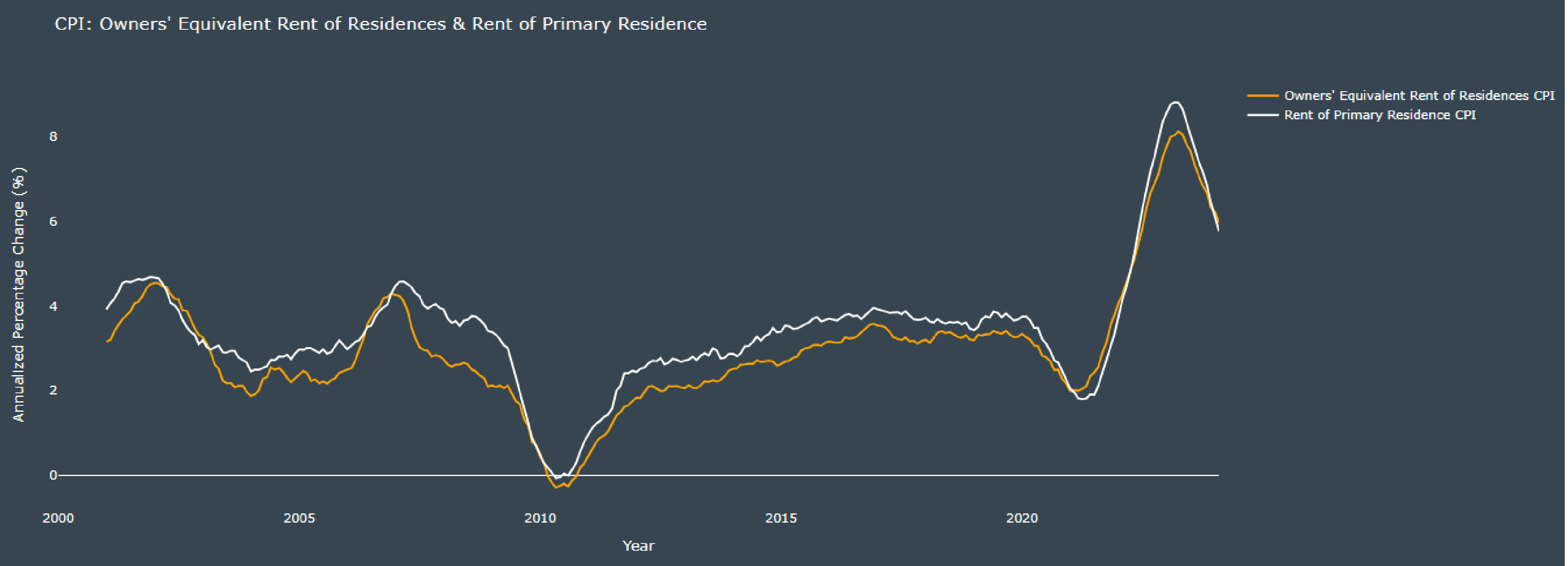
Consumer Price Index Was Ignored

Inflation's persistence has confounded many economists' initial forecasts, underscoring the complexity of reining it back to target levels. The assumption that reducing inflation from 3-4% to the Federal Reserve's 2% target would be a straightforward task has been challenged by recent economic data. The Consumer Price Index (CPI) and Producer Price Index (PPI) data for February, released last week, provided mixed signals to the market. While CPI data elicited a muted response, the PPI figures triggered a negative reaction. The differing market responses to CPI and PPI data underscore the complexity of interpreting inflation signals. Despite CPI rising slightly above expectations at 3.2% year-over-year against an anticipated 3.1%, and Core CPI at 3.8% versus the forecasted 3.7%, these figures don't necessarily indicate a re-acceleration of inflation but rather affirm its sticky nature. This has led to speculation about the Federal Reserve's monetary policy path, particularly regarding the timing of interest rate cuts. Current market sentiment anticipates rate cuts by June, hinging on the belief that unless new economic data leads the Federal Reserve to reconsider, the next move will be lower. This outlook persists even as inflation measurements slightly diverge from projections, suggesting that the market is willing to accept the present inflation rates, provided they do not meaningfully shift the expected course of monetary policy.

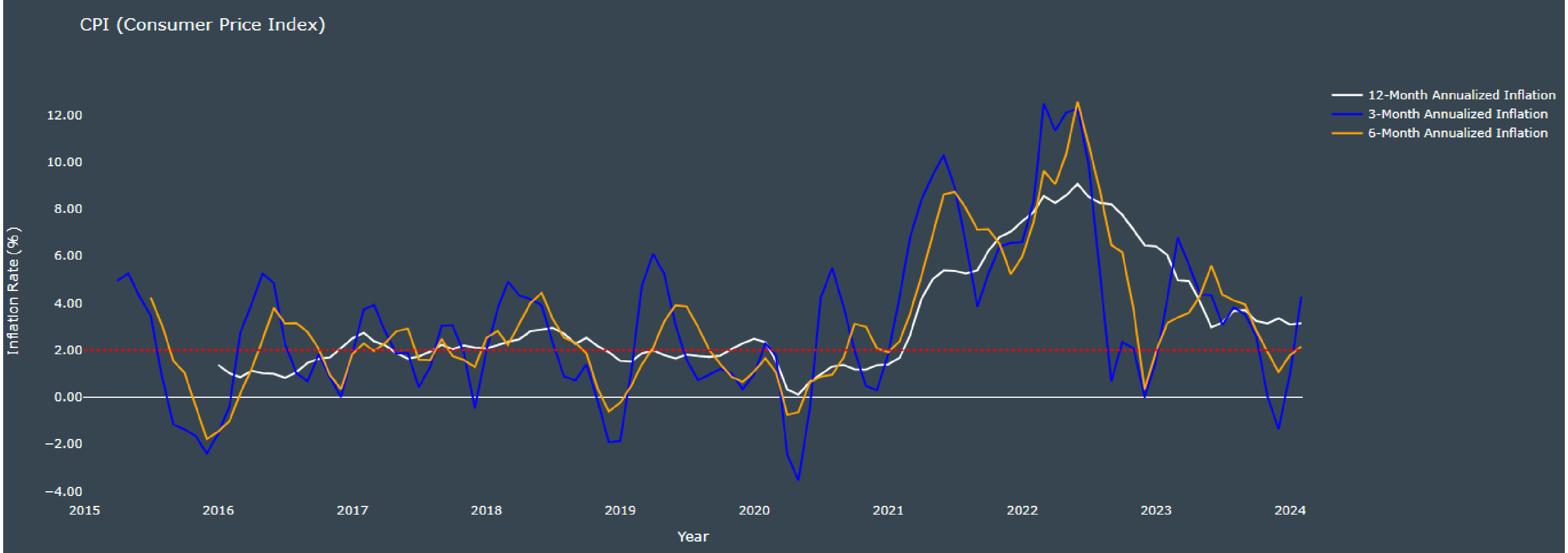
Housing is over 33% of CPI and the major driver of the stickiness we see in inflation



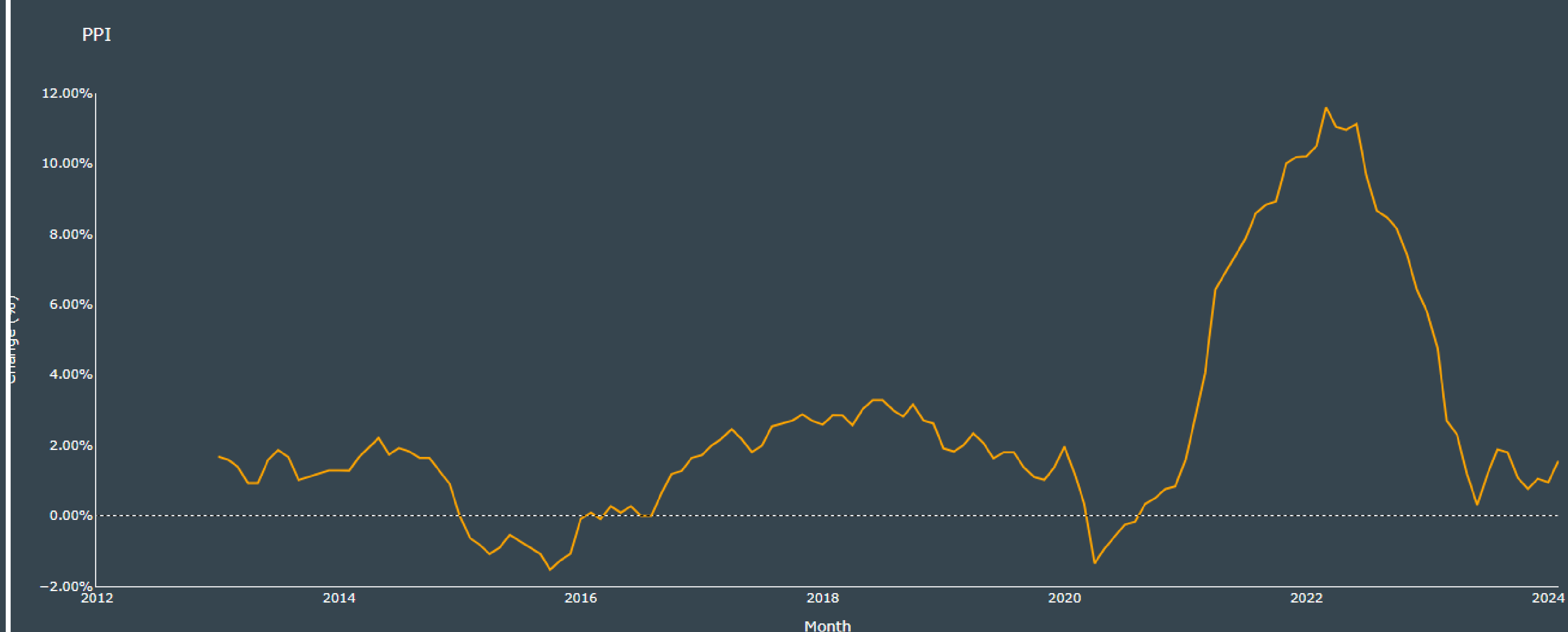
Within housing, both Owner's Equivalent Rent (OER) and Rent of Primary Residence continue to exhibit rates above 5%. OER, which carries a greater influence in calculations, is derived from a survey asking homeowners to estimate the rental value of their homes. In contrast, Rent of Primary Residence is based on actual amounts renters are paying currently.

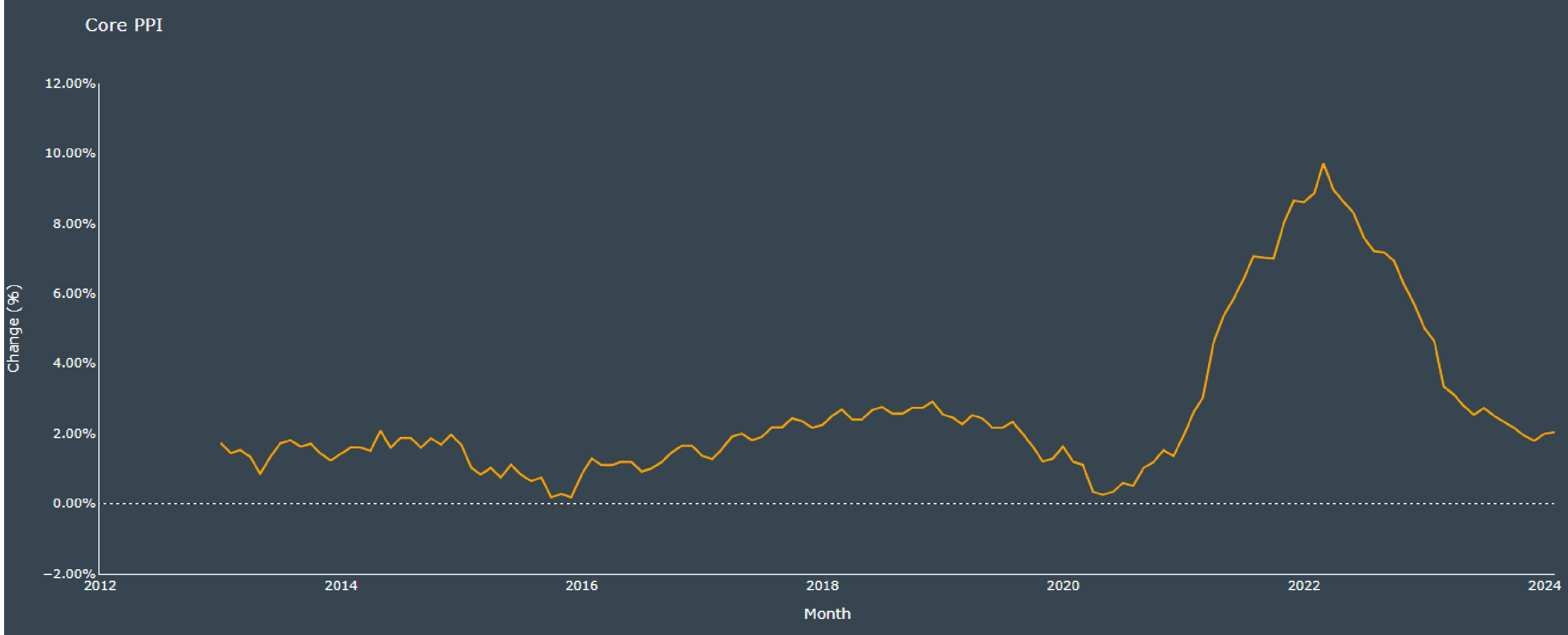


12 month annualized inflation has begun consolidating sideways, but with this months report 3 and 6 month annualized inflation look to be Turning higher

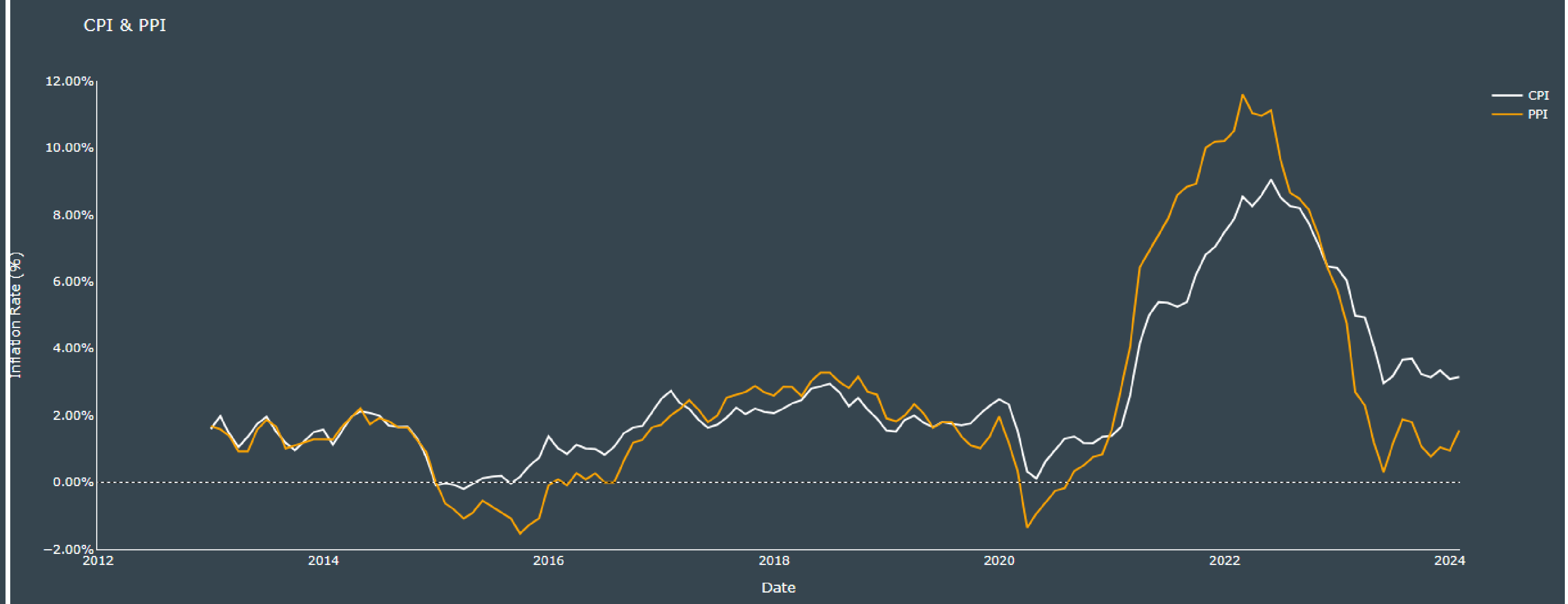


As stated above the stock and bond market gave little reaction to that news. However, on Thursday, the release of the Producer Price Index (PPI) figures attracted attention: the PPI was reported at 1.6% year-over-year, and Core PPI, which excludes volatile items like food and energy, was at 2.0% year-over-year. Although these rates are relatively low, both the headline and core numbers suggest a bottoming out, followed by a slight uptick based on trends from the past few months.





The Producer Price Index (PPI) tracks the prices businesses pay for the raw materials and services that feed into their final products. These costs frequently get passed down to consumers. Initially, when inflation emerged prominently in 2021, PPI was the first indicator to rise. Subsequently, the Consumer Price Index (CPI) increased as companies adjusted their selling prices upwards to offset the heightened input costs, aiming to preserve their profit margins.

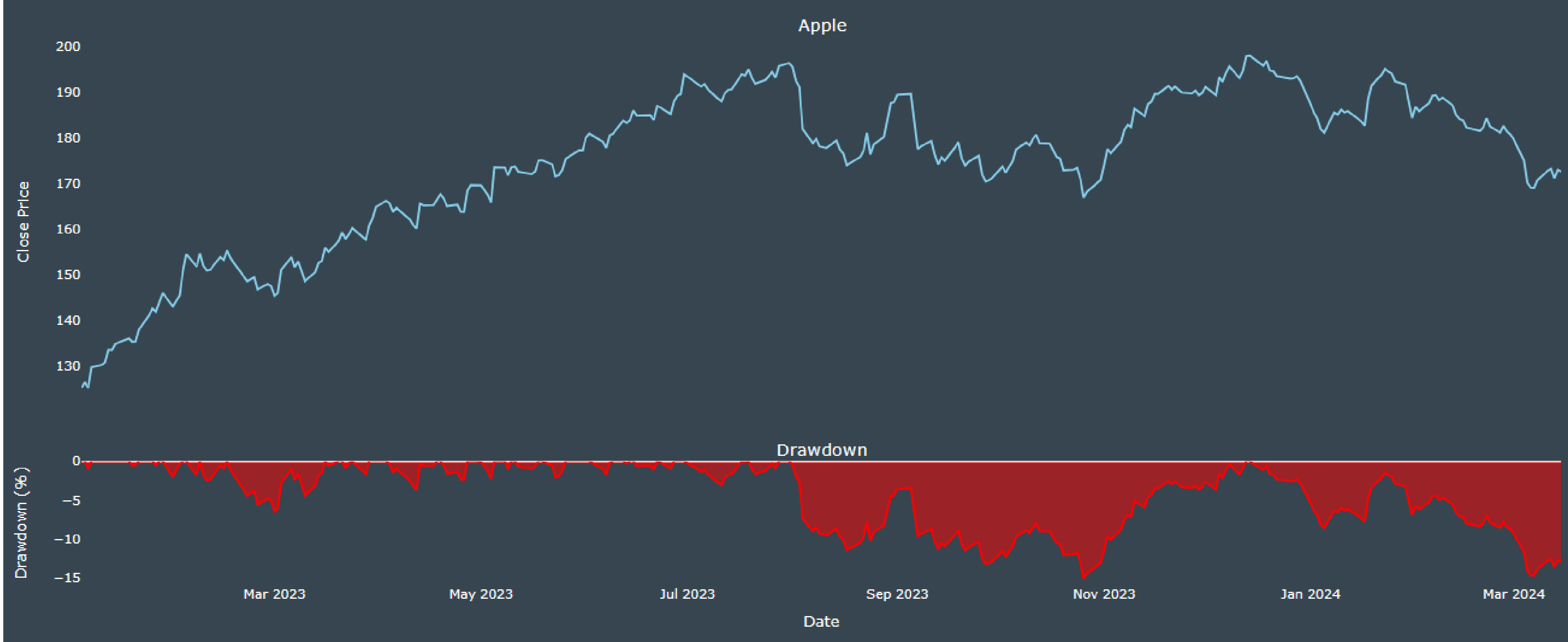


The large cap indexes have been trading in a rising wedge pattern for the last 5 months. All it takes is one negative catalyst to cause a break of that trend which would likely spur a 5-10% correction considering we have been in a straight line higher. Thursdays PPI report caused the markets to move broadly lower and this continued into Fridays session. As far as Sectors, Energy was the sole sector that rallied both days while everything else was mixed to slightly down. The S&P 500 broke the trendline that has been supporting the rally and is now sitting on its 20 DMA. Going into next week that will be an important level to watch as a break of that will likely bring the index to its 50 DMA at 4,950 or support at its previous all time high of ~4,800. The S&P 500 currently trades at 5,086.

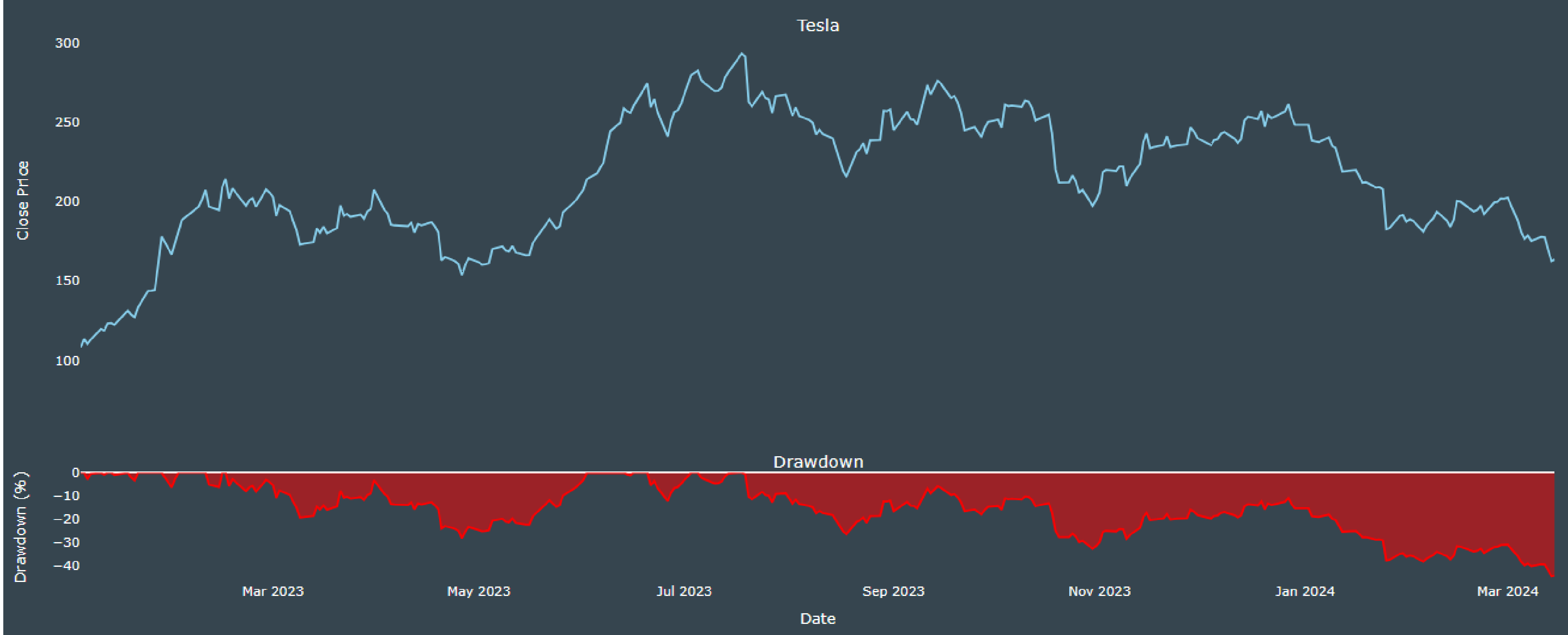
So far this year, yields have largely been inconsequential to market movements. However, coinciding with the recent selloff that concluded the week, there was a notable increase in yields, positioning them just beneath resistance. The 10-year yield approaching 4.3% appears to be a stress point for the stock market. A breach into the 4.3-5.0% range could precipitate a market correction.

The group known as the "Magnificent 7" has condensed into the "Magnificent 4" as three of its constituents have retreated more than 10% from their peaks. This shift hints at a rotation that briefly emerged at the start of 2024, until stocks like NVIDIA and META notably surged higher and the broader rotation didn't fully materialize. Given the circumstances described, a potential market correction of 5-10% in the coming months could unfold in nuanced ways. A key factor will be whether this correction is accompanied by a broader market rotation. Should the broader market support a rotation, with large-cap stocks taking a pause or slightly retracting, it could pave the way for the next upward movement. However, absent such rotation, the scenario might escalate into a more extensive sell-off. The direction of yields and the performance of the "Magnificent 7" will be critical in this context. If yields remain under control and the Mag 7 experiences a correction rather than a steep sell-off, this could merely set the stage for the rally's continuation. The market's response to these dynamics will be telling of its short- to medium-term trajectory.

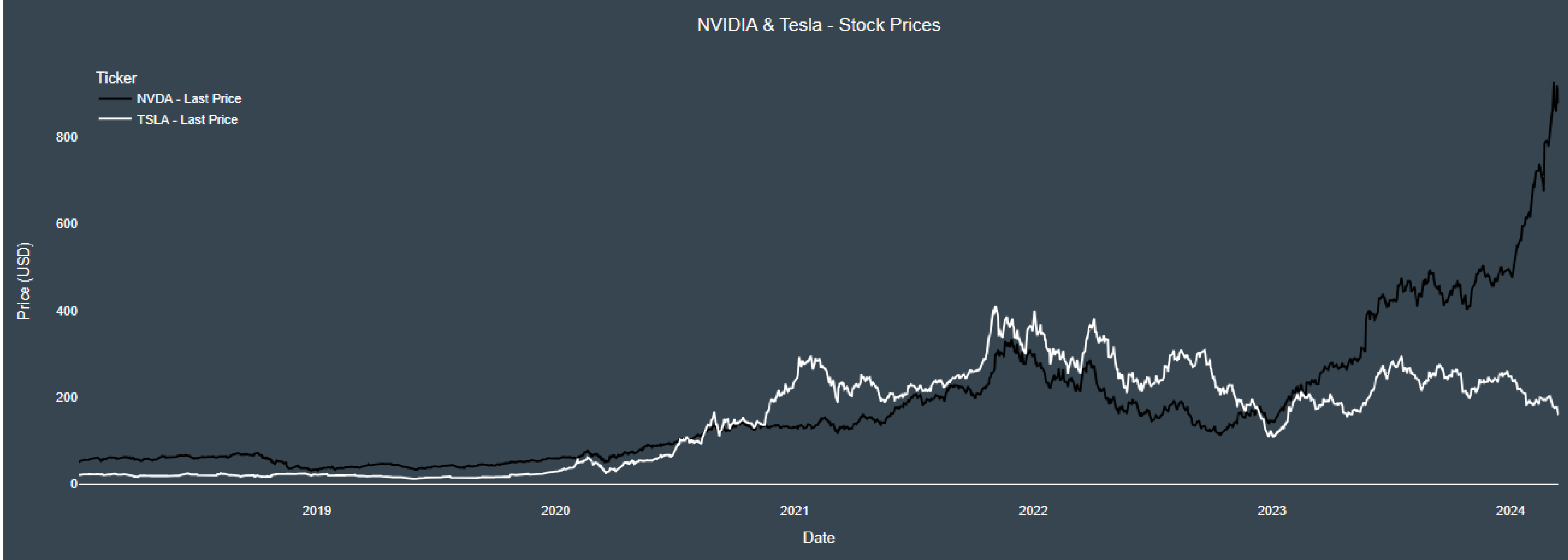
Apple is in a 12% Drawdown



Tesla is in a 44% drawdown and one of the worst performing stocks in the S&P 500 this year



Tesla was the original AI stock in terms of enthusiasm around it. Much of that enthusiasm surrounded its visionary projects, including self-driving cars, charging infrastructure, and data analytics. We have recently seen a shift in markets focus. Previously, investor excitement for Tesla was largely driven by these forward-looking ambitions. However, there's been a noticeable pivot towards evaluating the company on its fundamentals—a call many analysts have advocated for years. Critics have argued that, when the lofty expectations for future growth are set aside, Tesla's valuation appeared significantly inflated. With the demand for electric vehicles (EVs) showing signs of softening over the past year, Tesla has resorted to cutting vehicle prices, a move interpreted as preemptively writing down its inventory. Such price reductions have adversely affected its profit margins, diminishing some of the earlier enthusiasm surrounding the company. As Tesla's stock has declined by 35% in the early months of 2024, the spotlight has shifted to NVIDIA and the broader semiconductor industry, which have emerged as the new centers of hype in the tech sector. This transition is underscored by comparing the stock performance of Tesla and NVIDIA, illustrating a market reorientation from automotive innovations to AI brought to you through the stick and shovels play of semiconductor technologies.


NVIDIA & Tesla - Stock Prices
Ticker
NVDA - Last Price
TSLA - Last Price
Price (USD)
800
600
400
200
0
2019
2020
2021
2022
2023
2024
Date

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