

OBSERVATIONS

- Large cap equities declined last week, but small cap equities surged for a second straight week before giving up some of their gains late in the week. The S&P 500 fell by -2.0% while small caps (see One More Thought) gained +1.7% and the yield on a 10-year Treasury rose by +6 basis points to end the week at 4.24%.¹
- Headline retail sales were tepid in June showing no sign of an increase from May—+0.0% month-over-month (MoM)—but May's retail sales figure was revised higher. However, removing the volatile auto and gasoline sales, retail sales were +0.8% MoM and excluding autos and gasoline were also revised higher in May.¹
- New home builder sentiment declined in July to 42—figures less than 50 denote a majority of home builders are pessimistic about the near-term outlook—largely due to high interest rates and low foot traffic of prospective buyers.¹
- Housing starts increased in June from May by +3.0% MoM, and May's new housing starts figure was revised higher. Year-to-date (YTD) through June, total housing starts are down -1.0% compared to the first six-months of 2023, however, all the decline is being driven by fewer construction starts in multi-family housing units, while single-family housing starts are up +14% YTD in 2024.¹
- Industrial production increased in June by +0.6% MoM with gains across all three subcomponents—mining, manufacturing, and utilities—and capacity utilization increased to 78.8% in June from May's 78.3% figure.¹
- Initial unemployment claims jumped last week by +20k to reach 243k—claims can be volatile this time of year as many manufacturing firms shut down production for annual maintenance activities.¹
- The Conference Board Leading Economic Index (LEI) for the U.S. declined by 0.2 percent in June, but over the H1-2024, the LEI fell by -1.9%, which is a smaller decrease than its -2.9% contraction over H2-2023.¹

EXPECTATIONS

- The Trump campaign outlined a series of economic policies at last week's Republican National Convention (RNC) including wide-ranging tariffs on most imports, a push to reduce the corporate tax rate below 20%, efforts to reduce regulations on wide swathes of the economy including cryptocurrencies, and an extension of the income tax cuts he enacted in his first term.²
- The European Central Bank left its main policy rate unchanged last week at 3.75% but emphasized the possibility for a second -25 basis point rate cut this year when it meets next in September.¹
- Q2 earnings season is picking up pace and about 14% of the S&P 500 having reported as of last Friday. Thus far, the blended estimate for Q2 earnings growth is +9.7% with 80% reporting a positive earnings surprise—which is above the five- (77%) and ten-year (74%) averages for positive earnings surprises.³
- Over the weekend President Biden announced he was dropping out of the election race and supporting Vice President Harris to be the Democratic nominee to compete against former President Trump. The logistics of officially nominating VP Harris as well as who will run has her VP will become clearer in the coming weeks ahead of the Democratic National Convention that kicks off on Monday 19-August in Chicago.¹

ONE MORE THOUGHT: Small Cap Stocks Go Crazy for Five Straight Days¹

A confluence of factors emerged over the past several days that have pushed small cap stocks (Russell 2000 Index) over +6.7% in just the first three weeks of July. First, was the better-than-expected inflation data for June, which

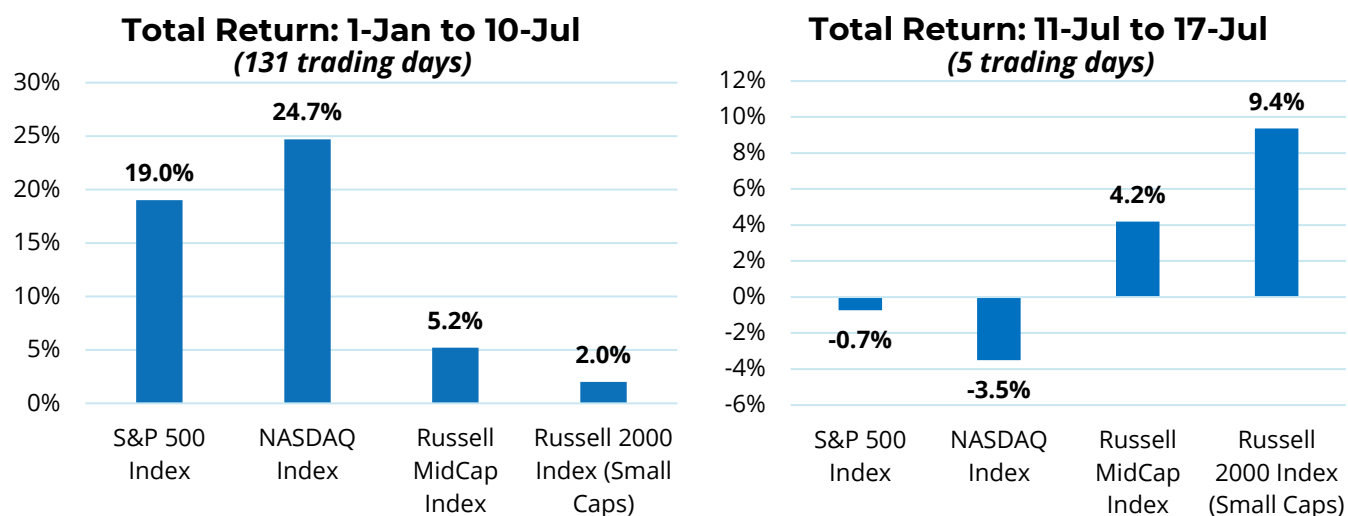
¹ Bloomberg LP, 7/19/2024

² <https://www.bloomberg.com/features/2024-trump-interview/>

³ https://advantage.factset.com/hubfs/Website/Resources%20Section/Research%20Desk/Earnings%20Insight/EarningsInsight_071924.pdf

seemed to be just the kind of economic data that the Federal Reserve would want to see to gain more confidence that inflation is steadily heading to their 2% target. Soon after this data was released, markets began pricing in a Fed rate cut in September and a second one in December. Then just a few days later, former President Trump survived an assassination attempt—which seemed to boost his popularity in recent polls—and used last week’s RNC to build further momentum towards winning the election in November. With echoes of what transpired in late-2016, investors seemingly began to rotate out of mega-cap, AI and semiconductor stocks and into sectors and stocks that may benefit from some of Trump’s economic policies. Small cap stocks—already buoyed by the market’s greater confidence in looming rate cuts—rallied further on the prospect of lighter regulations, perhaps lower tax rates, and less foreign competition due to potential tariffs. The rally in small cap names compared to their large cap peers was stunning. Over a five-day stretch the Russell 2000 Index outgained the S&P 500 by nearly 10 percentage-points, which is the largest five-day positive small cap outperformance between the two of them since the Russell 2000 index was created. For most of this year (see Chart of the Week), small cap stocks had significantly lagged their large cap peers, but in less than two weeks small caps have closed over half of the gap. Through last Friday, the S&P 500 has gained +16.3%, while small caps (Russell 2000 Index) have gained +8.6%. Time will tell if this rotation continues on as we head through the summer, but it behooves investors to take note that market sentiment can shift quickly, and prudent rebalancing pays dividends when market environments shift, and yesterday’s laggards become today’s winners.

CHART OF THE WEEK



Source: Clearstead, Bloomberg 7/19/2024

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