CALADO CAPITAL

Week in review and ahead (vol.38)

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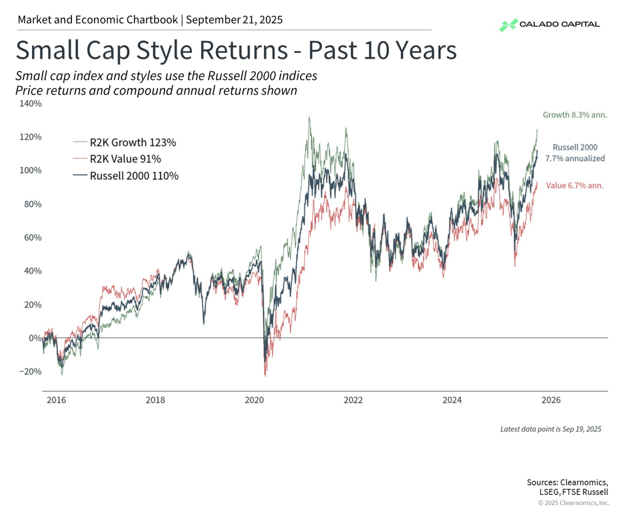
The market paused their rally during the Fed's announcement on Wednesday but ultimately resumed the rally thereafter with all US indices reaching new all-time highs, including the Russell 2000 for the first time since November 8, 2021, as the markets embraced the Fed's (pre-announced) pivot. The Fed's cut by 0.25% reduced the Fed fund rate to the range of 4%-4.25% signaling additional cuts. As such, the future markets show investors betting on interest rates falling below 3% by the end of 2026, below the Fed's median forecast of 3.4%.

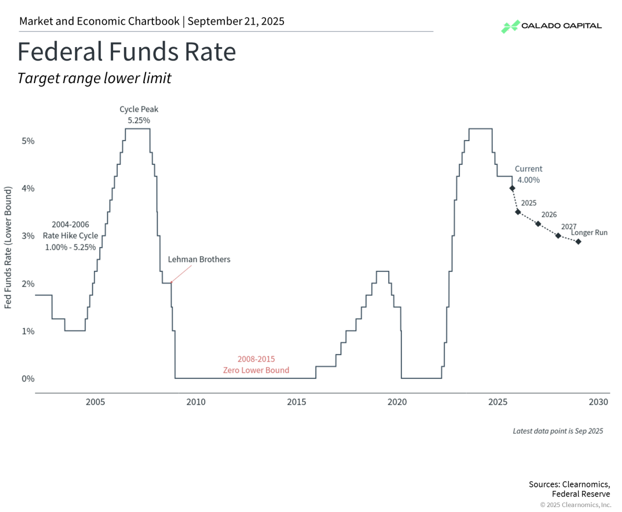
All major US indices advanced on the week with the S&P500, Nasdaq Composite, Dow Jones, and Russell 2000 ending the week higher by 1.2%, 2.2%, 1.1%, and 2.2%, respectively, all setting new all time highs in the process on Thursday or on Friday, albeit closing just below those records on Friday.

Internationally, the rally in equity markets continued as well but for China, the UK and Germany. In China, the SSEC declined by -1.3% on the week due to weak macro reports, specifically materially weaker reports on August industrial output and retail sales growth (hitting a 12-month low), while in the UK the FTSE100 declined -0.7% for the week on the Bank of England (BoE) keeping its rates steady and fiscal proposals to tax UK banks on interest earned from reserves held at the BoE. The German DAX declined -0.3% on the week on trade-related pressures and sector-specific issues, particularly in the automotive following the announcement that Porsche AG would be removed from the index. Technical indicators signaling a correction may have contributed to the risk-off sentiment.



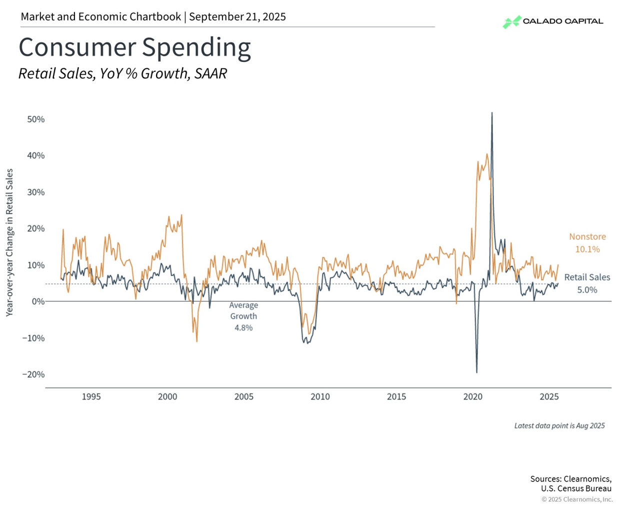
With markets squarely focused on the Fed's decision, other US macroeconomic data continued to show the US economy to be resilient. Specifically, US retail sales for August were better than expected, showing the US consumer's strength despite signs of a slowing labor market and a slumping housing market. US consumption accounts for approximately 68% of GDP.

Having pre-announced that it would pivot to prioritize the downside risks in the labor market over upside risks to inflation, the decision to cut rates by 0.25% and indicating additional cuts yet this year, was in line with the broader market expectations and did not really surprise markets, despite significant volatility on Wednesday afternoon just after the announcement and during Fed chair Powell's press conference. The sole question was what the markets had priced in leading up to the Fed's FOMC meeting. With the Fed's pivot to ease monetary policy, the future markets appear to expect a more aggressive pivot given the moderate growth expectations for the remainder of the year (with median Fed projections of 1.6% in 2025 and 1.8% in 2026) and that may further support or fuel an overall risk-on sentiment in markets and a continuation of the bull market in equities.



US retail sales on headline for August grew 0.6% as they did in July, and were well above the expected 0.3%. Excluding autos, or core retails sales, increased by 0.7% in August, outpacing expectations and the prior month’s increase of 0.4% by a large margin. Industrial production in August surprised with an increase of +0.1%, beating expectations of a decline by -0.1% and sequentially that recorded a decline of -0.4%. The weekly report on initially jobless claims equally surprised with 231K, after spiking to a revised 264K the week before and expectations of 240K. Continuing claims declined further to 1.92M from 1.927M the week before and expectations of 1.95M, albeit individuals who can no longer get unemployment are excluded from the report. With the downward revision of job growth since April last year, the number of marginally attached workers or discouraged work force is difficult to assert also because of the impacts from the immigration policy.

The weakness in the housing market continued with both, housing starts and building permits for August, coming in lower than expectations and sequentially, Housing starts in August were 1.31M compared to 1.37M expected and 1.43M in July, while building permits were the same 1.31M compared to the same 1.37M and 1.36M the month before. Accordingly, the home builder confidence index remained at historic lows with a reading of 32, the same as last month and below an expected reading of 33. For reference, the lowest ever reading of 30 was recorded in April 2020 at the onset of the COVID-19 pandemic.



Next week will be marked by many FOMC members' public speeches that will provide additional insight into last week's decision and vote and that may influence markets interpretation of current monetary policy stance. The Fed's closely watched PCE inflation index for August on Friday looks to provide an additional assessment for markets of any significant upside risks to inflation and in relation to the Fed's recent pivot. Besides, inflation markets will look to reports on the state of the US consumer as updates to personal income and spending are reported in addition to the University of Michigan's final read of consumer sentiment for September.

Additional macroeconomic data on the calendar for next week are US GDP's third estimate to Q2'25, to remain unchanged at 3.3%, existing and new home sales for August, durable goods orders for August, and preliminary estimates for manufacturing and service sector PMI by S&P.

If you have questions about how this may impact your investments, or how you should be positioned, please do not hesitate to contact us at claudio@caladocapital.com.

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