Ropes Wealth Considers Interest Rates, Inflation, and Themes Besides AI

In this week's news, the Fed concluded its two-day policy meeting on Wednesday by hitting "pause" on a year-long string of rate hikes leaving the target rate range unchanged at 5% to 5.25%. This pause was widely telegraphed by Fed officials and welcomed by the markets that the end may be near. Officials did signal an intent to continue with additional hikes at subsequent meetings. The median forecast for the target rate at year-end 2023 was revised up 50 basis points from 5.125% to 5.625%. In his post-meeting press conference, Fed Chair Jay Powell confirmed, "nearly all Committee participants view it as likely that some further rate increases will be appropriate this year."

Why? Powell was clear the Fed is disappointed at the slow progress on disinflation, noting, "if you look at core PCE inflation, …over the last six months, you're just not seeing a lot of progress." Sounding somewhat encouraged, however, Powell said, "I would almost say that the conditions that we need to see in place to get inflation down are coming into place, …but the process of that actually working on inflation is going to take some time." To that point, the Fed's projection for the target interest rate for year-end 2024 was revised to 4.625% and their median year-end 2025 projection for rates was revised to 3.375%.

Economic data this week was mixed, with inflation improving but ever so slowly. Year-over-year, headline consumer prices rose 4.0%, down from the 4.9% pace reported the month prior; year-over-year, the core CPI increased 5.3%, down from the 5.5% gain in April. More optimistically, producer prices declined as well, rising 1% year-over-year for the smallest annual gain since December 2020. On the consumer side of things, total retail sales rose 0.3% in May, topping economist expectations for a -0.2% decline. The stunner for the month was a huge bump in the sale of building materials. The consumer continues to demonstrate a surprising level of resilience surpassing expectations. However, going forward, as savings decline, stimulus fades, and student debt payments resume, consumer momentum is at risk of waning.

Also expected to decline are second quarter earnings reports, primed to fall -5% to -6.5% compared to a year ago. With that, how can markets continue to trend so strongly? Clearly the market's expectations that AI will gain widespread adoption explains some of the strength with just a few technology firms valued over $200 billion primarily carrying the U.S. equities rally so far this year. And yes, as we step forward day by day, we are seeing some other positive signs of a widening trend in stock market leadership, including a reprieve in some of the poor performance of smaller U.S. companies where potential recession impacts would be highest. We are watching those market shifts carefully, to see if the year-to-date rally is sustainable given the fundamentals and in the context of an economy faltering in its performance as the stresses of high interest rates and tightening credit conditions choke off demand.

We would do well to remember other themes that will shape our future too, including aging populations, rising geopolitical risks, a rewiring of supply chains, and the transition to a lower carbon economy. Those themes will require investment and some rethinking and will bring with them challenges and opportunities that we are contemplating in our investment plan for you. As this country commemorates Juneteenth on Monday, it is worth noting that our work is never done to strive to make a world where there is opportunity for all. We all have a role to play to make our world a place where justice and kindness prevail and our mistakes do not define us, but rather inspire us in our leadership for the future.

Thank you as always for your interest in our investment commentary. If you would like to speak personally with a member of our team at any time, please click **here.**

Ropes Wealth Advisors LLC
800 Boylston Street Boston, MA 02199-3600