Ropes Wealth Reviews Credit, Inflation, and High Hopes

Next time you are found, with your chin on the ground
There's a lot to be learned, so look around
Just what makes that little old ant
Think he'll move that rubber tree plant
Anyone knows an ant, can't
Move a rubber tree plant
But he's got high hopes, he's got high hopes
He's got high apple pie, in the sky hopes

Sinatra's lyrics came to mind this week when I was thinking about the stock market vs. the economy right now. The stock market's got high hopes and seemingly nothing is going to get in the way of those. Not even a flare-up in consumer inflation or surging consumer credit balances could rattle equities, which have fully recovered from any small losses created by profit-taking at the start of the year. Not even the anniversary of an insurrection or a failure of the government to follow through on a budget compromise has caught the markets' focus. And not even the U.S. and UK military strikes on Houthi-controlled areas of Yemen caused much of a waver in confidence in end of week trading.

Early Thursday, the Labor Department reported the overall and core rates of the Consumer Price Index (CPI) each rose 0.3% in December from November, both above expectations for increases around 0.2%. Compared to year-ago levels, overall CPI also accelerated slightly, posting a 3.4% increase in December versus a 3.1% gain in November. The core rate, which excludes volatile food and energy prices, posted a 3.9% year-over-year increase in December, down from a 4% rise in November and the first sub-4% core rate increase since mid-2021. High shelter prices accounted for more than half of the headline CPI figure which is no surprise.

In contrast, this morning, the Producer Price Index (PPI) unexpectedly fell just -0.1% in December following a similar decline in November and a -0.4% drop in October. Year-over-year, the core PPI increased 1.8% in December, down from the 2.0% annual gain in November and the smallest annual increase in three years. Notably, declining energy prices helped to keep producer prices down through December, but as I write this, oil prices are spiking due to the activity in the Middle East.

No doubt, though, inflation gauges generally remain in a longer-term downtrend, albeit still above the Fed's 2% long-term target. Cleveland Fed President Loretta Mester spoke to this point, saying: "It just suggests we have more work to do, and that work is going to take restrictive monetary policy. My own forecast is that we'll continue to see inflation move down this year, but I think March is probably too early in my estimate for a rate decline." Her sentiments have been echoed by other central bankers since the start of this year, which may mean the Fed is likely to proceed deliberately with any rate cuts and may not lower rates as soon as some believe.

Consumer credit jumped $23.8b in November, nearly three times the $8.6b increase expected and the largest gain for non-real estate balances in a year. Eighty percent of the increase related to a big jump in revolving credit balances, primarily associated with credit cards and potentially related to a solid start to holiday shopping. The 17.7% annualized gain marked the 30th increase in revolving credit balances in 31 reports and was the sharpest since March 2022. Meanwhile, the interest rate charged on all credit card accounts, reported every third month, rose from 21.2% to a new record high of 21.5%.

In other markets, the Securities and Exchange Commission (SEC) approved exchange-traded funds (ETF) linked to the spot bitcoin market late Wednesday. The spot market, also known as the cash market, refers to forums where commodities, securities, and other assets can be immediately exchanged between buyers and sellers. The move opens up a new crypto inroad for investors who might otherwise avoid holding actual bitcoin. Bitcoin prices have tripled since the start of 2023, reaching a high of $49,000, partly reflecting anticipation of the SEC decision and amid hopes of easing interest rate policy.

In summary, markets have pinned their high hopes on easing interest rate policy, and that the boost from that pivot will be enough to offset slowing economic activity, geopolitical instability, and uncertainty related to earnings growth and profitability. We think these hopes are not unfounded, but we also think it is important to stay focused on your plan in this moment. With that, while it is often more exciting to think about stocks, this is also a moment to reexamine your bond exposure, ensuring a nice laddering formation among your individual holdings, or a more core bond fund versus a short-maturity bond fund that has been in vogue over these more recent years when rates have been rising. We would also flag less of a preference for extensive money market holdings as yields are resetting lower in anticipation of Fed rate cuts. Short- and intermediate-term U.S. Treasuries or municipals can lock in your yield on cash held as a cushion or for more intermediate purposes. We urge you to review cash holdings with us and in your bank accounts, making sure you optimize your investment strategy there as the time for rising rates is coming to an end (or so we hope).

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