Ropes Wealth Reviews Earnings and Powell's Earnest Plea for Adult Conversation

"It's probably time, or past time, to get back to an adult conversation among elected officials about getting the federal government back on a sustainable fiscal path." So said Federal Reserve Chairman Jay Powell to Scott Pelley on *60 Minutes* on Sunday. Jay, we could not agree more. Especially as, a few days following, the Congressional Budget Office (CBO) released their update showing total federal debt outstanding has risen $10.9 trillion since January 2020 to $34.2 trillion. The CBO also predicted the budget deficit will rise from $1.6 trillion in fiscal year 2024 to $2.6 trillion over the next ten years, raising the ratio relative to the size of the economy from 5.6% in 2024 to 6.1% in 2034. According to the report, higher interest rates and rising government outlays are the catalyst for the nearly two-thirds increase in the budget deficit.

While commenting on fiscal policy is not the typical purview of monetary policy makers, the Fed is keenly aware of the implications of a further expansion of the federal government's balance sheet. A ballooning deficit adds to inflationary pressures, which by extension pose a growing challenge to a Fed still struggling to reinstate price stability. It is no surprise, then, that Powell was so resistant in his primetime interview to say interest rate cuts were imminent. Powell instead insisted that the Fed can approach the decision to cut rates with patience and wait for further improvement in inflation.

But then, to keep us guessing, he also said the Fed does not need to achieve their target of 2% inflation before reducing rates. A Monday market swoon was then corrected, such that by week's end, the market is in the green and investors feel confident rate cuts will arrive just in time for Mother's Day (or so this economist hopes!).

The Fed was busy providing other updates on the economy this week, including a report on household debt and credit that showed outstanding balances increased by $212 billion in the fourth quarter to $17.5 trillion, a 1.2% increase from the third quarter. The aggregate change reflected increases across all debt categories. Notably, credit card balances continued their rapid climb, rising $50 billion to $1.13 trillion, a new series high. The report also noted, *"delinquency transition rates increased for all product types, except for student loans."* The deterioration in timely payments was most pronounced for auto loans and credit cards. In a separate report, the Federal Reserve's Senior Loan Officer Survey described how lending standards continued to tighten as 2023 came to a close: *"In addition, banks reported expecting loan demand to strengthen across all loan categories, and loan quality to deteriorate across most loan types."*

Meanwhile, following up on last week's strong reading on the manufacturing sector, the ISM Services Index recovered more than expected from a twelve-month low of 50.5 to a 53.4 reading in January, thanks to a jump in employment demand for service industries consistent with last week's blockbuster jobs report.

And once again, we have Taylor Swift to thank for not just saving the NFL, but Disney too, as the House of Mouse announced a partnership with Swift for streaming rights to "The Eras Tour" as well as with "Fortnite" maker Epic Games. This news was in addition to a strong earnings report and a 50% dividend increase. The earnings season is at its halfway mark, and tech companies continue to captivate investor focus, defying concerns about narrow market breadth. The other 10 sectors in the S&P 500 are an average of about 15% below their all-time highs, and none of the non-tech sectors established a new record in January. Meanwhile, a small-company stock index like the Russell 2000 is about -20% below its all-time high set in November 2021. While the narrow foundation of the recent record highs doesn't guarantee that indices are setting up for a decline similar to the one that began in 2000, diversification is looking compelling right now. The "Magnificent Seven" companies may be expensive, but the rest of the market is not, and may be overlooked. Sometimes cheering for the underdog makes sense, and not just in the Superbowl (though with the Detroit Lions eliminated, is there an underdog?). Thank goodness for the commercials!

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