Ropes Wealth Reflects on Legendary Advice for a View on Today's Market

We recently lost Daniel Kahneman, an Israeli American Nobel Prize-winning psychologist and best-selling author who was widely considered the grandfather of behavioral economics. When I was in my twenties at my first job, he delivered a guest lecture to young analysts like me and it was riveting. In the years since, I have often recalled one of his more famous observations: "*The brains of humans contain a mechanism that is designed to give priority to bad news."* Welcome to this month in financial markets.

The April air pocket in stock markets continued to rupture this week as certain growth stocks tumbled in the wake of weaker guidance in earnings reports versus reports of actual earnings misses. For example, Meta the Facebook parent provided lighter-than-expected second-quarter revenue guidance as CEO Mark Zuckerberg discussed spending in currently unprofitable pursuits such as artificial intelligence (AI) and mixed reality. Meta's first-quarter earnings and revenue both came in above analysts' estimates, however. Meta wasn't alone in miring in some malaise, as both IBM and Intel stocks were down due to sales forecasts that disappointed investors. And even though oil prices have surged, both Exxon and Chevron slipped after falling short of revenue forecasts.

In contrast, Microsoft Corp. and Google owner Alphabet Inc. trounced Wall Street estimates with their latest quarterly results, lifted by a surge in cloud revenue fueled by booming use of AI services. For those companies, the AI halo remains firmly in place.

As a general statement of sentiment almost halfway through earnings seasons, stock reactions have been underwhelming, with better-than-expected results seeing below average upside, while those missing estimates are being penalized by more than usual. It is probably also the case that with the 10-year Treasury note back up to 4.68% today (remember in March it was as low as 4.10%!) and inflation numbers spooking investors about hopes for declining interest rates, it is not unexpected to see the market wobble here. Remember, our brains give priority to bad news.

The first read of U.S. GDP also did not help yesterday, showing growth of only 1.6% annualized, following last year's blistering 4.9% and 3.4% numbers delivered in the third and fourth quarters, respectively. This weaker-than-expected showing occurred despite still solid activity in terms of consumption – at least on the services side – as well as business investment. However, a lack of inventories, a widening trade balance, and more modest government spending were a drag. But more concerning to investors were further signs of accelerating price pressures that will likely prevent the Fed from lowering its benchmark funds rate anytime soon. The core PCE price index spiked from 2.0% to 3.7%. While this is lower than the peak reports in 2021 and 2022, this move higher is a warning sign. In the 25 years preceding the pandemic, there were no core PCE price indices reported this high and only two quarters ever reported above 3.0%.

Reinforcing that sobering report was today's news that the Federal Reserve's preferred gauge of underlying U.S. inflation rose at a brisk pace in March, underpinning concerns of persistent price pressures. The so-called core personal consumption expenditures price index, which strips out the volatile food and energy components, increased 0.3% from the prior month. From a year ago, it advanced 2.8%. The overall PCE price measure also rose 0.3% from February and 2.7% from the prior year. That said, adjusting for inflation, real consumer spending rose 0.5%, while real income increased 0.2% in March following a 0.1% decline in February. Over the past twelve months, real spending rose 3.1%, a three-month high, while real disposable personal income gained 1.9%, the smallest increase in five months.

With growth momentum clearly waning and a further backup in cost pressures, the euphoria around rate cuts is dissipating. And with that, the market's wobble continues. As we have expressed to you in a cadence of meetings through this period, your investment plan must be built for years, not months or minutes, and markets relying on the Fed for a catalyst can easily become whipsawed. The current anxiety around inflation and growth reflects a reality check that was expected, but in some ways, it offers a bit of a window to review and adjust allocations and optimize them for your planned liquidity needs and growth goals. While it is not our style to advocate market timing, a market experiencing a reasonable setback like this can offer an entry point for cash on the sidelines and remember that both bonds and stocks have had a moment of reset here.

Finally, I will offer another one of Daniel Kahneman's finest quotes on human behavior: *"It's a wonderful thing to be optimistic. It keeps you healthy and it keeps you resilient."* Well said Mr. Kahneman and RIP.

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

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