First Carolina Wealth

April 8, 2024

THOUGHTS TO START YOUR WEEK

Tax Filing Countdown

Tax Day is Monday, April 15.

- Remember that if you file an automatic extension through October 15, 2024, you still must pay your tax liability before April 15! The extension is only to file your return…you must pay now. Pay on the high side if you wish to avoid potential interest and penalty.
- Ensure that your CPA or you double check the numbers. The most common reason for IRS review is incorrect addition or typographical errors in your inputted numbers. If you use a tax preparation software, be sure to correct every error it flags on your return. The IRS has similar software that detects similar issues.
- Make sure that you have addressed every Form 1099 that may have been filed on your behalf in 2023, by anyone who paid you any sum, whether as compensation or any distribution from a retirement account or investment.
    - Unreported income is a close second to typos on the IRS notice list. Your reported income on your return must equal that income reported by payers on Form 1099s and W-2s that have been filed with the IRS.
    - IRS computers will detect any difference between your tax return and any Form 1099s filed with your tax ID number. Always best not to have the IRS reviewing your return, even if for only typos or miscalculations. Who knows what they might question once they start looking?!
- If it helps, **do not be shy,** hum ***"The Star-Spangled Banner"*** while you either press send on your computer keyboard or drop the envelope into the U.S. Mail slot. I have found it to relieve the heartburn (at least temporarily)!

Weekly Economic Insights From Our Investment Managers

We've been writing the past few weeks about the fact that when valuations get a little ahead of themselves and everyone gets complacent, conditions are potentially ripe for volatility to rear its ugly head. That's exactly what we got last week as the equity markets digested geopolitical tensions in the Middle East and a bout of tough Federal Reserve rhetoric. In fact, the economic data we received was decidedly positive for growth; however, that can be a double-edged sword when trying to combat inflation…

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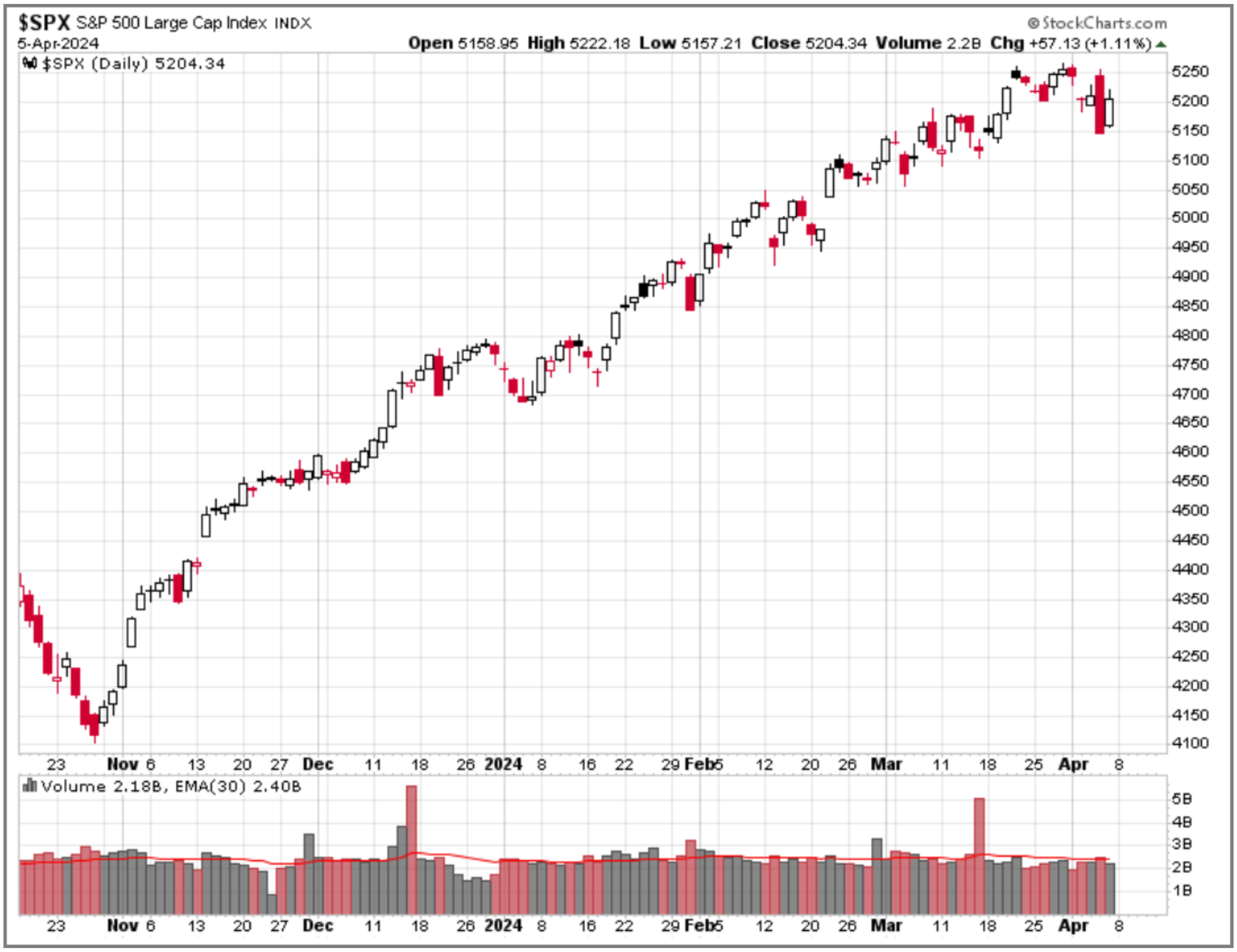

Key Takeaway:

The chart above demonstrates the consistent advance in the S&P 500 since late October. Last Thursday's decline stands out on the chart; however, a look at the volume indicator in the bottom pane tells us there was not a lot of involvement. Market internals are still trending upward, and the economic backdrop is still positive, so, for now, we may view this most recent bout of volatility as the markets simply blowing off some steam.

The Week Ahead:

All eyes will be on Wednesday's Consumer Price Index (CPI) and Thursday's Producer Price Index (PPI), which give us a glimpse into everyone's favorite topic: inflation. We will also get the FOMC minutes, a look at consumer confidence, and, of course, Thursday's jobless claims. Most importantly, we want to see a continuing trend of lower inflation – any surprises here could send markets into a tizzy when considering the already heightened alert status from last week.

Tidbits & Technicals: (New developments noted in *italics*)

Current Headwinds:

- Valuations are frothy given the current rate environment, leaving the markets subject to a potential swift pullback
- "Higher for Longer" – Risk that the Fed waits too long to begin lowering rates and threatens economic growth
- *10-year treasury yields broke out to new highs for the year, signaling that bond investors may be beginning to believe in the "Higher for Longer" thesis*

Current Tailwinds:

- Optimism surrounding Artificial Intelligence (AI)
- Fed pivoting from raising rates to potentially cutting in the future
- Strong labor market
- Solid economic growth
- Continued earnings growth (the pace of which may be slowing)
- Momentum
- Participation is broadening with value, cyclicals, and smaller-sized companies beginning to show a strong upward bias

Sentiment:

- Credit spreads remain tight, signaling the bond market (aka "smart money") is not worried about a recession in the near future.
- *The VIX (CBOE Volatility Index) exploded higher last week, breaking through these years' "complacency zone."*
- *The CNN FEAR & Greed Index remains above neutral in the "Greed" category, showing investors' current appetite for risk is strong; however, the index has broken below these years' "complacency zone."*

Intermarket Trends:

- The major indices (Dow Jones Industrial Average, S&P 500, and NASDAQ) all posted new highs in the past few weeks, signifying a positive trend.
- *Bond investors have been pricing in the idea of "Higher for Longer" recently, with 10-year treasury yields above this year's trading range to make new highs.*
- The US Dollar is trading near the upper end of this year's trading range due to foreign central banks being the first to cut rates and others taking further rate hikes off the table while the Fed continues its campaign of tough rhetoric.
- Gold continues to set record highs.
- Industrial metals caught a bid recently, and copper recently broke out of a multi-month trading range to the high side. Discussions on supply shortages are emerging.
- Oil is trading near the top of its 2024 range but well below last year's highs.

Tying it all together:

The recent uptick in market volatility, marking the first significant fluctuation since the rally began in October 2023, isn't unexpected given the high equity valuations and recent investor complacency. Concerns about the prospect of prolonged higher interest rates are emerging among bond investors, evident in the surge of longer-term interest rates to new yearly highs. If these concerns spill over into the equity markets, we could see some turbulence ahead. While robust economic indicators are generally positive, they do present a challenge to the Federal Reserve's efforts to combat inflation and warrant our attention.

This week's inflation data could prove to be pivotal in shaping the market's short-term trajectory and deserves careful monitoring. We've been advocating for profit trimming and reallocation to levels where investors feel comfortable for the past few weeks, and I still believe this is the prudent course of action. Please know these adjustments are essential risk management strategies for navigating potentially volatile markets in the near future and do not imply any imminent disaster. In fact, we believe any near-term market weakness could be seen as an opportunity to increase exposure to areas of the market that may currently be underweight in one's portfolio given the favorable economic conditions and historical trends during election years.

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