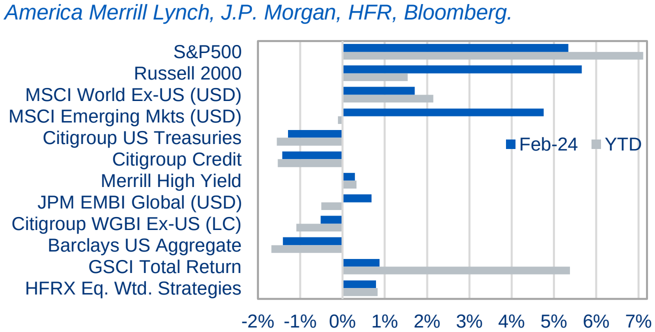
Global Market Review

Global equity markets surged higher in February. The S&P 500 and NASDAQ indexes reached all-time highs and the Japanese equity market reattained the level prevailing at its pre-bubble peak some 34 years ago. A frenzy fed by speculation over the transformative potential of an AI technological revolution was a main driver of the U.S. equity market gain. Hopes for continued disinflation and resilient economic growth also contributed to the rally. However, markets priced in a somewhat more realistic outlook on the timing of a Fed pivot to easing. Reflecting this reassessment, U.S. Treasury yields rose, and investment grade credit markets lost ground. High yield bonds, however, managed a small gain. The SEC's approval of Bitcoin ETFs has accorded a veneer of respectability to the crypto market, resulting in large inflows and a spike in Bitcoin prices. Oil prices rose in February adding to January's strong gains. The U.S. dollar appreciated marginally against most major currencies.

Performance of Major Market Indices

Sources: S&P, MSCI, FTSE Russell, Barclays, Citigroup, Bank of America Merrill Lynch, J.P. Morgan, HFR, Bloomberg.



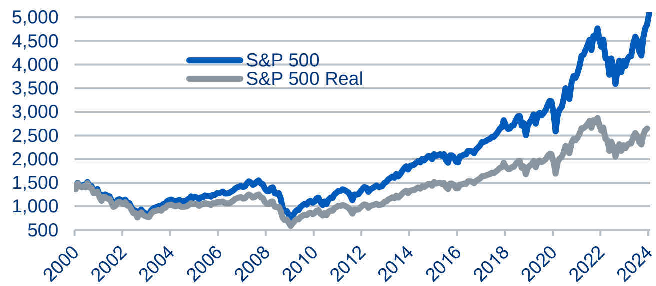
AI frenzy propels U.S. equities to record heights.

NVIDIA! The Magnificent One

The S&P 500 index rose 5.3% in February, its fourth successive monthly gain, propelling the index above 5,000 for the first time. In real terms, however, the index remains below its 2021 high (Exhibit 1). The NASDAQ index also reached an all-time high in February.

Exhibit 1. S&P 500 Index Breaches 5,000

Source: Bloomberg. S&P 500 index in nominal and real terms.



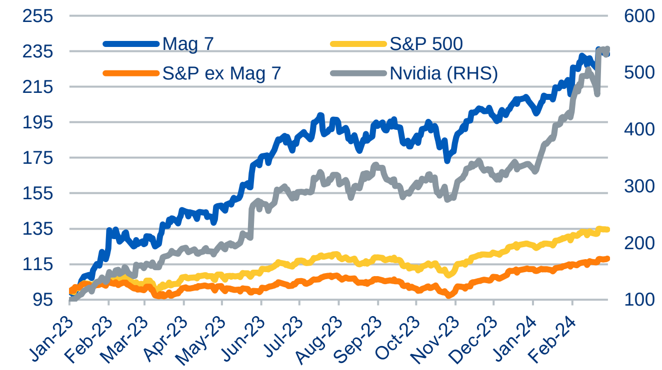
The chief catalyst for these gains has been speculation that AI will be the "next big thing" – a general-purpose technology that, like electricity, will have a transformative impact across sectors, boosting productivity and economic growth. The promise of an impending technological revolution has propelled to high levels the stock prices of firms thought most likely to be early AI beneficiaries. The Magnificent 7, comprising Apple, Microsoft, Google, NVIDIA, Meta, and Tesla, is up 14.7% so far this year. The poster child of this group is NVIDIA, the producer of chips powering AI applications. Its stock price has gained 64.4% in the first two months of the year and 442% since end-2022 (Exhibit 2). The stellar performance of this mega-cap tech stock has contributed to high levels of market concentration and inflated market valuations. The Magnificent 7's share of the S&P 500's market cap is 29%. NVIDIA and the Magnificent 7 have trailing P/E ratios of 65.7 and 40.8, respectively, levels that are predicated on continued heady growth in earnings.

Exhibit 2. Mag 7 Pricing Predicated on Stellar Growth

Source: Bloomberg. Returns in percent. Market Cap in % of S&P 500.

	2023	2024	Cumulative	Trailing P/E	Market Cap
Nvidia	238.9%	64.4%	442.0%	65.7	4.5%
Mag 7	107.0%	14.7%	133.4%	40.8	29.1%
S&P 500	26.3%	7.1%	34.5%	22.8	100.0%
S&P ex Mag 7	12.3%	5.2%	18.2%	19.8	70.9%

Exhibit 3. NVIDIA's Vertiginous Surge Continues
Source: Bloomberg. Index January 1, 2023 = 100.

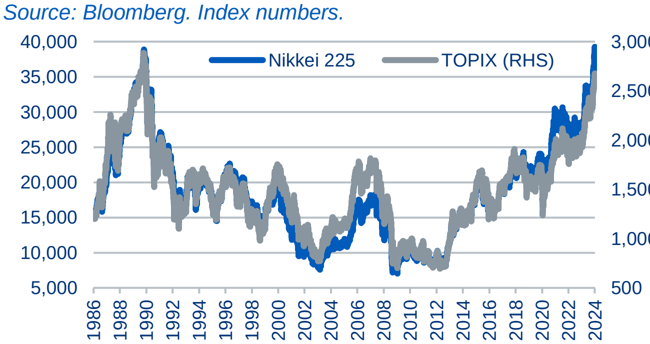


Although the market focus has naturally been on the eye-popping returns of NVIDIA and its Magnificent 7 brethren, the U.S. equity market rally so far this year has been broad based (Exhibit 3). The S&P 500 excluding the Magnificent 7 is up 5.2% so far this year, and its trailing P/E ratio of 19.8 appears more reasonable.

Japanese Equities Recover Pre-Bubble Peak

Japanese equity and property markets experienced a momentous bubble in the 1980s. Between 1980 and 1989 when the equity and property market bubbles burst, Japanese equities rose by a factor of 5.7 times and property prices reached outlandish levels. At the bubble's peak, the 1.3 square miles occupied by the Imperial Palace was valued to be worth more than all of the real estate in California. When the bubble finally burst, there followed a prolonged period of economic stagnation and deflation, made worse by a series of monetary policy missteps. Japan's equity market at long last reattained in February its peak prevailing in 1989 just prior to the bubble's bursting (Exhibit 4).

***Exhibit** 4. Japanese Equities Recover to Pre-Bubble Highs*
Source: Bloomberg. Index numbers.



Advanced and emerging equity markets also rose in February. The MSCI World ex-U.S. index of advanced equity markets rose 1.7% while emerging market equities were up 4.8%. Emerging equities were buoyed by a strong bounce in Chinese equities which gained 8.4% in February but remain down 3.1% for the year. Non-U.S. markets continue to lag the exceptionally strong performance of the U.S. market so far in 2024. For the year as a whole, advanced economy bourses are up 2.2%, while emerging markets are down 0.1%, compared to the U.S. market's 7.1% return.

Bond Markets Reassess Pace of Fed Easing

Vacillating views on the timing and pace of Fed rate cuts continue to dominate bond markets. At its most optimistic late last year, the market had been pricing in six rate cuts in 2024, notwithstanding admonitions by the Fed that those expectations were unrealistic. Sentiment has since become more realistic. The market is now pricing in 2-3 rate cuts this year with the first cut expected in June.

Reflecting the reassessment of the pace of Fed policy easing, U.S. Treasury yields rose in February as the yield curve steepened. As a result of this shift, U.S. Treasuries and investment grade credit markets both declined in February. Declines were steepest for bonds at the long end of the maturity spectrum, with Treasuries and investment grade bonds having maturities of 10 or more years falling by 2.3% and 2.6%, respectively. High yield bonds, in contrast, managed a small gain of 0.3% thanks to their shorter durations.

SEC Accords Bitcoin a Veneer of Respectability

Bitcoin prices rose above $60,000 in February and are up 44.5% in the first two months of the year (Exhibit 5). Flows into Bitcoin ETFs approved in mid-January by the SEC have been the main catalyst for the spike in Bitcoin prices. Since the SEC's approval through end-February, net inflows into newly formed Bitcoin ETFs totaled $16 billion, with the bulk of these flows captured by ETFs sponsored by BlackRock and Fidelity.

Exhibit 5. Bitcoin Breaches $60,000
Source: Bloomberg. Bitcoin price in U.S. dollars.

Performance of Major Market Indices through 02-29-2024
Sources: MSCI, FTSE, Barclays, Citigroup, Bank of America Merrill Lynch, J.P. Morgan, S&P GSCI, HFR, Bloomberg.

	1-Month	QTD	YTD	1-Year	3-Year	5-Year
S&P500	5.3%	7.1%	7.1%	30.5%	11.9%	14.8%
Russell 2000	5.7%	1.5%	1.5%	10.0%	-0.9%	6.9%
MSCI World Ex-US (USD)	1.7%	2.1%	2.1%	14.0%	4.7%	6.9%
MSCI Emerging Mkts (USD)	4.8%	-0.1%	-0.1%	8.7%	-6.3%	1.9%
Citigroup US Treasuries	-1.3%	-1.6%	-1.6%	2.3%	-3.3%	0.2%
Citigroup Credit	-1.4%	-1.5%	-1.5%	5.9%	-2.8%	1.7%
Merrill High Yield	0.3%	0.3%	0.3%	11.0%	1.9%	4.0%
JPM EMBI Global (USD)	0.7%	-0.5%	-0.5%	9.0%	-2.1%	0.8%
Citigroup WGBI Ex-US (LC)	-0.5%	-1.1%	-1.1%	3.6%	-3.9%	-1.3%
Barclays US Aggregate	-1.4%	-1.7%	-1.7%	3.3%	-3.2%	0.6%
GSCI Total Return	0.9%	5.4%	5.4%	5.0%	15.4%	7.2%
HFRX Eq. Wtd. Strategies	0.8%	0.8%	0.8%	3.9%	0.6%	2.6%