



Market Commentary
January 12th, 2024

English Version

Insigneo Weekly Dispatch

Promises, Expectations, and Probabilities

A quick look at what may lie ahead for the S&P 500 in 2024.

Guidance on investments and the major structural factors behind your clients' portfolios.

insigneo

**By Mauricio Viaud**

PM and Senior Investment Strategist
Insigneo

Promises, Expectations, and Probabilities

A new year brings new promises and new expectations. At the beginning of the year, many of us promise ourselves that we will eat healthier, exercise more, or simply spend less time looking at our mobile phones. We might have the best intentions in mind, but a key to keeping these promises is setting reasonable expectations. I can promise myself to eat healthier, but if I say that I will not eat any chocolate during the entire year, I will be setting myself up for failure. To be successful at achieving my goal, I have to be realistic.

The same thing could be said for the stock market. A new year brings new possibilities and expectations for U.S. equities. Then again, after an albeit choppy year where the S&P 500 saw intermittent drops of 10% and 15% yet closed the year 26% higher, I am not sure what better results could be expected for 2024. However, investors appear to be expecting another year of perfection, where the Fed achieves the elusive soft landing and quickly cuts interest rates based on a healthy balance between low inflation and a strong job market. The market appears so convinced that this tedious balance will happen, that it is expecting 6 rate cuts, with a 63% probability that 100 basis points of these cuts will be in place by the end of the first quarter. This, even after the Fed said that it expects to cut rates only three times in 2024, based on a data-dependent framework that is agnostic to time. We are not saying that what the market is expecting is impossible. In fact, a soft landing in some form or another appears like a real possibility. What we are

saying is that the expectation of the series of perfect outcomes implied by the market appears unreasonably high, and it could be setting itself up for disappointment. Purely based on math, the higher the number of low-probability events that we expect to happen all at once, the lower that probability becomes. We all know that the chances of flipping a coin and it landing on “heads” is 50%. However, the probability of flipping two coins at the same time and both landing on “heads” drops to 25% ($0.5 \times 0.5 = 0.25$). Granted, this is a simple example with only two observations, but it helps convey the idea that the probability of a series of events happening all at once decreases as we add more events into the mix.

But what if expectations are too high and the market is setting itself up for disappointment? What would that look like? We believe that this is a very real possibility, which could make 2024 a volatile year. There is an old stock market adage that says that as the month of January goes, so goes the rest of the year. This is just an observed behavioral pattern in the market that works most of the time, though not all the time. However, looking at the last couple of years, the S&P 500 was down 5.4% in January of 2022 and closed the year down almost 20%, and was up 6.3% in January of 2023, and closed the year up 26%. So far, during the first full week of trading in 2024, the S&P 500 saw its worst one-week open in 20 years. It has then bounced back and is essentially flat as of the time of this writing.

The average Wall Street analyst estimate for the S&P 500 for the end of the year is 4,850. The index currently sits at 4,780, implying an upside of approximately 1.5%. We believe that this outcome is dependent on whether a soft landing is achieved, or

whether the economy falls into recession. If a soft landing is achieved, the market could continue to drift higher, likely even breaking above 5,000. However, if the economy falls into recession, a move down to 4,000 or lower would not be out of the realm of possibilities. Again, evaluating the situation purely based on mathematics, a move higher from the current level of 4,780 towards 5,000 implies upside of approximately 5%, while a move down towards 4,000 implies downside of approximately 16%. Based on these numbers, and our expected probability of recession over the next 12 months of 55%, we can calculate an approximate expected return for the S&P 500 of -6.5% for the year. Granted, these numbers are subject to change as the data changes, but it shows that as of today, the direction of market returns is skewed to the downside. That being said, the market still appears convinced that a low probability event will occur this year that will nudge the index higher. However, if that rather improbable event does not occur, the potential downside is large. Said a different way, the market is focusing on events that have a relatively low chance of happening in order to capture seemingly limited upside. At the same time, it appears to be ignoring another event that could potentially happen and could lead to meaningful downside. The market could be right in the end, but the risk/reward potential currently seems to be skewed to the downside. What will most likely happen is a tug-of-war of expectations, as market participants digest last year’s outsized returns and reconcile these with the ebbs and flows of data throughout this year. This dynamic will likely lead to a volatile year for U.S. equity markets.

In 2023, many investors, particularly momentum-oriented institutional investors, got forced back into

the market, having to participate in its move higher, or risk getting left behind and underperforming their benchmarks and peer groups. After years of operating as an institutional investor, I came to learn that this is sometimes the harsh reality of the institutional world, hold your nose and jump into the market as it races higher, or risk getting left behind and posting an underperforming year. When the page turns to the new year, however, many of these institutional investors digest the previous year's performance and reassess whether it will continue in the year ahead. This process can lead to pronounced ebbs and flows in the market.

Given the uncertainty in the economy, the upcoming earnings season, which coincidentally starts today, will give us a better picture of what the year ahead might look like for the markets. Paying close attention to companies' guidance and outlooks will be key. Given that last year's outperformance was mainly driven by multiple expansion and not necessarily earnings growth, determining if earnings growth will match high valuation multiples will be crucial in determining whether the market can hold on to its gains from 2023. Data will flow and change throughout the year and the market will likely react to these changes in data. Volatility will likely remain high, and we would not be surprised if the market experiences a pullback at some point in 2024. Not all is gloom and doom though, as pullbacks sometimes turn out to be attractive entry points for long term investors. This will be determined by the data at hand, and we will advise

accordingly. In the meantime, maintaining a long-term perspective and sticking to a disciplined investment process based on facts, not emotions, is the best way to navigate turbulent times.

By definition, probabilities are not guaranteed to happen. The events they attempt to quantify may happen in a perfect fashion or not happen at all. Nothing is guaranteed, especially in the investment world. However, as investors, we have the best chance of sustained long-term success by basing our decisions on factual probabilities, not raw emotions. Emotions currently appear to be running high in the equity markets. Again, these are the times when sticking to a disciplined investment process pays off. Going back to my example at the beginning of the article, I might feel strongly about the fact that I will not eat a single piece of chocolate for the entire year. In reality, I know that this has a very low probability of happening and should adjust my expectations accordingly.



Click or scan this code to access more insights at insigneo.com/insights

Important Legal Disclaimer

Insigneo Financial Group, LLC comprises a number of operating businesses engaged in the offering of brokerage and advisory products and services in various jurisdictions, principally in Latin America. Brokerage products and services are offered through Insigneo International Financial Services, LLC, headquartered in Puerto Rico, and through Insigneo Securities, LLC, headquartered in Miami. Both are members of the Financial Industry Regulatory Authority (FINRA) and Securities Investors Protection Corporation (SIPC). Investment advisory products and services are offered through Insigneo Advisory Services, LLC, an investment adviser registered with the Securities and Exchange Commission. In Uruguay, advisory services are offered through Insigneo International Asesores de Inversion Uruguay, SA, Insigneo Asesores de Inversion Latam, SRL, and Insigneo Asesores de Inversion de Uruguay, SRL, in Argentina through Insigneo Argentina, SAU, and in Chile through Insigneo Asesorias Financieras, SPA. Collectively, these eight operating businesses make up the Insigneo Financial Group. To learn more about the Broker Dealers including their conflicts of interest and compensation practices, please go to <https://insigneo.com/disclosures/> or via www.finra.org. To learn about Insigneo Advisory Services, LLC and any conflicts related to its advisory services, please see its Form ADV and brochure which can be found at Investment Advisor Public Disclosure website <https://adviserinfo.sec.gov/>

FOR AFFILIATES LOCATED IN CHILE

Insigneo Asesorias Financieras SPA se encuentra inscrito en Chile, en el Registro de Asesores de Inversión de la Comisión para el Mercado Financiero. Este informe fue efectuado por área de Research & Strategy de Insigneo Securities LLC, o sus proveedores, en base a la información disponible a la fecha de emisión de este. Para evitar cualquier conflicto de interés, Insigneo Securities LLC dispone que ningún integrante del equipo de Research & Strategy tenga su remuneración asociada directa o indirectamente con una recomendación o reporte específico o con el resultado de una cartera.

Aunque los antecedentes sobre los cuales ha sido elaborado este informe fueron obtenidos de fuentes consideradas confiables, no podemos garantizar la completa exactitud e integridad de estos, no asumiendo responsabilidad alguna al respecto Insigneo Securities LLC, Insigneo Asesorias Financieras SPA ni ninguna de sus empresas relacionadas.

Este material está destinado únicamente a facilitar el debate general y no pretende ser fuente de ninguna recomendación específica para una persona concreta. Por favor, consulte con su ejecutivo de cuentas o con su asesor financiero si alguna de las recomendaciones específicas que se hacen en este documento es adecuada para usted. Este documento no constituye una oferta o solicitud de compra o venta de ningún valor en ninguna jurisdicción en la que dicha oferta o solicitud no esté autorizada o a ninguna persona a la que sea ilegal hacer dicha oferta o solicitud. Las inversiones en cuentas de corretaje y de asesoramiento de inversiones están sujetas al riesgo de mercado, incluida la pérdida de capital.

La información base del presente informe puede sufrir cambios, no teniendo Insigneo Securities LLC ni Insigneo Asesorias Financieras SPA la obligación de actualizar el presente informe ni de comunicar a sus destinatarios sobre la ocurrencia de tales cambios. Cualquier opinión, expresión, estimación y/o recomendación contenida en este informe constituyen el juicio o visión de área de Research & Strategy de Insigneo Securities LLC, o sus proveedores, a la fecha de su publicación y pueden ser modificadas sin previo aviso.

FOR AFFILIATES LOCATED IN URUGUAY

En Uruguay, los valores están siendo ofrecidos en forma privada de acuerdo al artículo 2 de la ley 18.627 y sus modificaciones. Los valores no han sido ni serán registrados ante el Banco Central del Uruguay para oferta pública.

FOR AFFILIATES LOCATED IN ARGENTINA

Insigneo Argentina S.A.U. Agente Asesor Global de Inversión se encuentra registrado bajo el N° 1053 de la Comisión Nacional de Valores (CNV) e inscripto ante la Inspección General de Justicia (IGJ) bajo el N° 12.278 del Libro 90, Tomo -, de Sociedades por Acciones. Este informe fue efectuado por área de Research & Strategy de Insigneo Securities LLC, o sus proveedores, en base a la información disponible a la fecha de su emisión. Para evitar cualquier conflicto de interés, Insigneo Securities LLC dispone que ningún integrante del equipo de Research & Strategy tenga su remuneración asociada directa o indirectamente con una recomendación o reporte específico o con el resultado de una cartera. Aunque los antecedentes sobre los cuales ha sido elaborado este informe fueron obtenidos de fuentes consideradas confiables, no podemos garantizar la completa exactitud e integridad de estos, no asumiendo responsabilidad alguna al respecto Insigneo Securities LLC, Insigneo Argentina S.A.U. ni ninguna de sus empresas relacionadas. La información base del presente informe puede sufrir cambios, no teniendo Insigneo Argentina S.A.U. la obligación de actualizar el presente informe ni de comunicar a sus destinatarios sobre la ocurrencia de tales cambios.

Este material está destinado únicamente a facilitar el debate general y no pretende ser fuente de ninguna recomendación específica para una persona concreta. Por favor, consulte con su ejecutivo de cuentas o con su asesor financiero si alguna de las recomendaciones específicas que se hacen en este documento es adecuada para usted. Este documento no constituye una oferta, recomendación o solicitud de compra o venta de ningún valor negociable en ninguna jurisdicción en la que dicha oferta o solicitud no esté autorizada o a ninguna persona a la que sea ilegal hacer dicha oferta o solicitud. Las inversiones en valores negociables están sujetas al riesgo de mercado, incluida la pérdida parcial o total del capital invertido. Cualquier opinión, expresión, estimación y/o recomendación contenida en este informe constituyen el juicio o visión de área de Research & Strategy de Insigneo Securities LLC, o sus proveedores, a la fecha de su publicación y pueden ser modificadas sin previo aviso.