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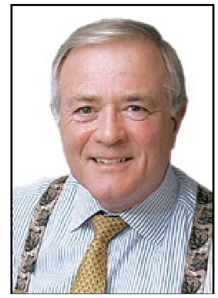
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Riding the wave of innovation: a surge in market optimism| Opinion

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As companies reported earnings in February, evidence of the broad acceptance and monetization of AI tools powered stocks to new record highs.

The Dow Jones was up 2.2 percent, reaching an all-time high of 39,131.53 on Feb. 23. The NASDAQ Composite ended the month at a closing record high of 18004.87, up 6.2 percent on the month and 8 percent for the year, fueled by three of its largest constituents: Nvidia, Amazon and Alphabet (Google). The S&P 500 also reached new highs, rising 5.2 percent in February and 6.8 percent year to date, surpassing 5,100. As of this writing, the S&P 500 has achieved 15 new highs since the beginning of the year.

History says February is a terrible month for the market, so what happened?

On Feb. 21, AI chip maker Nvidia reported Q4 2023 earnings which handily beat analyst estimates and, more importantly, gave positive guidance for continued strong growth in 2024. As of the end of February, Nvidia stock was up over 25 percent on the month, 60 percent for the year-to-date and 249 percent for the trailing 12 months.

The day after reporting earnings, the chipmaker added $277 billion to its stock market valuation, the largest daily gain ever achieved by a single company. Its market capitalization reached $2 trillion. The AI halo effect spread to other technology stocks and then to the market as a whole, underscoring the adage that “a rising tide raises all boats, even the leaky ones”.

Economic data released in February reflected the ongoing balance between inflationary pressures, employment and the underlying strength of the U.S. economy. The CPI, which measures the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services, rose by 0.3 percent in January 2024, with a year-over-year increase of 3.1 percent. This rise in CPI of 50 percent higher than the Fed target of 2 percent indicates ongoing inflationary pressures, particularly in services, which is significant given that the U.S. is predominantly a service economy.

On the producer side, the Producer Price Index (PPI) increased more than anticipated, also growing by 0.3 percent in January, the largest increase since July 2023. Of the various components of the index, goods saw a decrease of 0.2 percent, while services increased by 0.6 percent, as workers sought to have wages catch up with prior increases in the CPI.

A major component of this increase was the rising cost of hospital outpatient care due to higher wages, which often do take effect at the beginning of a year.

The Fed appears to be in a stalemate regarding inflation, neither winning nor losing the battle.

Amid these inflationary trends, the unemployment rate remained below the 4 percent threshold, at 3.7 percent for January. This robust employment picture suggests that the Federal Reserve may not lower rates soon. The consensus among economists is that unemployment would need to rise above 4 percent for the Fed to consider lowering rates — a scenario that seems more unlikely in 2024.

The possibility of no rate cuts in 2024 continues to gain traction, but, as of this writing, has not yet curtailed the market's upward trajectory.

Credit markets ended February with yields falling across the curve. There had been some concern that the higher-than-expected CPI numbers would cause upward pressure on rates, but this did not occur despite a heavy Treasury debt issuance calendar. China's increased purchasing of U.S. securities took some pressure off rising yields.

As the month drew to a close, the financial markets stood at a crossroads, buoyed by both technological innovation, with increasing optimism about its ability to mitigate inflationary pressures, and corporate earnings strength. Yet the underlying economic challenges of inflation and concerns about its impact on consumer behavior remain.

The broadly strong earnings reports for the fourth quarter and calendar year-end helped support the sustainability of the stock market rally. The innovation and economic resilience of the broad-based U.S. economy continues to prevail amid global, and at times, domestic turmoil.

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