

# PALLAS PERSPECTIVE

AUGUST 23, 2024

## **MARKET REFLECTIONS: PALLAS CAPITAL'S STRATEGIC FOCUS AMID MARKET CALM**

Following a few weeks of turbulence in the financial markets, a calmer week allowed the Pallas team to refocus on mid- and long-term priorities. As we reviewed the market and macroeconomic developments from last week, the following topics were top of mind for our investment team:

### **CAN WE EXPECT A SOFT LANDING?**

There has been significant debate about whether we are headed for a recession or a soft landing. Several notable points lead us to believe in the soft-landing narrative. This week's economic data—July retail sales, initial jobless claims, New York Federal Reserve Survey of Consumer Expectations (which showed 3-year inflation expectations at the lowest point in the series' history), and Consumer Sentiment (which rose for the first time in five months)—all support the narrative of cooling growth without indicating an economy on the brink of collapse. For our clients, this suggests there is still some room for risk assets to perform, making it important to stay invested in equities while gradually seeking diversification. It is also time to reduce duration bets on either side and ensure that duration remains neutral relative to the Bloomberg Aggregate Index.

### **DID EARNINGS DELIVER ENOUGH OPTIMISM FOR MARKETS TO CONTINUE GOING UP?**

With approximately 90% of companies reporting earnings, we reflected on what these earnings were indicating at a high level. What we liked about Q2 earnings:

1. 10.9% EPS growth for Q2 2024 was the best since Q4 2021
2. The number of firms expressing recession fears was the lowest in the past 5 years
3. 79% of companies exceeded EPS estimates, above the 5-year average of 74%
4. Cost savings were a major driver, as revenue surprises were down 60% compared to the average of 69%

Given the strong equity market returns, analysts were expecting equally strong EPS delivery and surprises, as reflected in the 1.9% outperformance for companies beating EPS estimates versus a 1.4% decline for companies that missed EPS estimates. Looking forward, analysts expect 10.1% EPS growth in 2024 and 15% in 2025. Broadly, returns have kept pace with earnings, which is what we anticipate at this stage of the cycle. Our expectation is that markets are likely to deliver single-digit returns (7% over the next 12 months), provided earnings deliver approximately 10% EPS growth in 2025.

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