November 7, 2024
Commentary

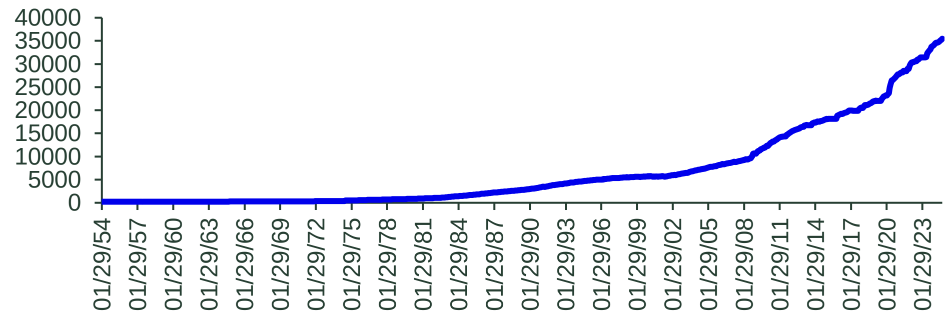
Weekly Market Update

Insight of the Week

US Public Debt as Record High

A country's debt level escalates when its spending constantly exceeds its revenue from taxes and other income sources. As of September 2024, the US national debt totaled $35.4 trillion- the highest on record-with no signs of abatement. This accumulation of debt stems primarily from chronic overspending. In FY 2024, the government overspent by around $1.83 trillion relative to its revenue collection. To finance the deficit, the government resorts to borrowing, often through issuance of marketable securities such as treasury bonds.

Total Debt of US Government (USD Billions)



Source: FactSet. Monthly data as of September 2024.

Given such elevated debt levels, how does the country maintain operational functionality? The answer lies in the debt to GDP ratio, which serves as a critical indicator of a nation's ability to service its debt. Currently US debt to GDP stands at approximately 120%. While this is elevated, several other developed nations exhibit even more precarious fiscal situations. For example, Japan's debt to GDP ratio exceeds 200%.

Many economies have accumulated significant debt in the last four years as they resorted to aggressive deficit spending during the pandemic. Servicing this debt is becoming increasingly burdensome. Such high levels of debt has led to growing fiscal sustainability concerns worldwide and in our recent piece The Tidal Wave of Global Debt we examine the profound implications this fiscal backdrop will have on economies and investors in the years to come. Additionally, we explore this topic more closely in the Fixed Income section below.

Source: FactSet, State Street Global Advisors.

Equities

Markets React to Change in Leadership

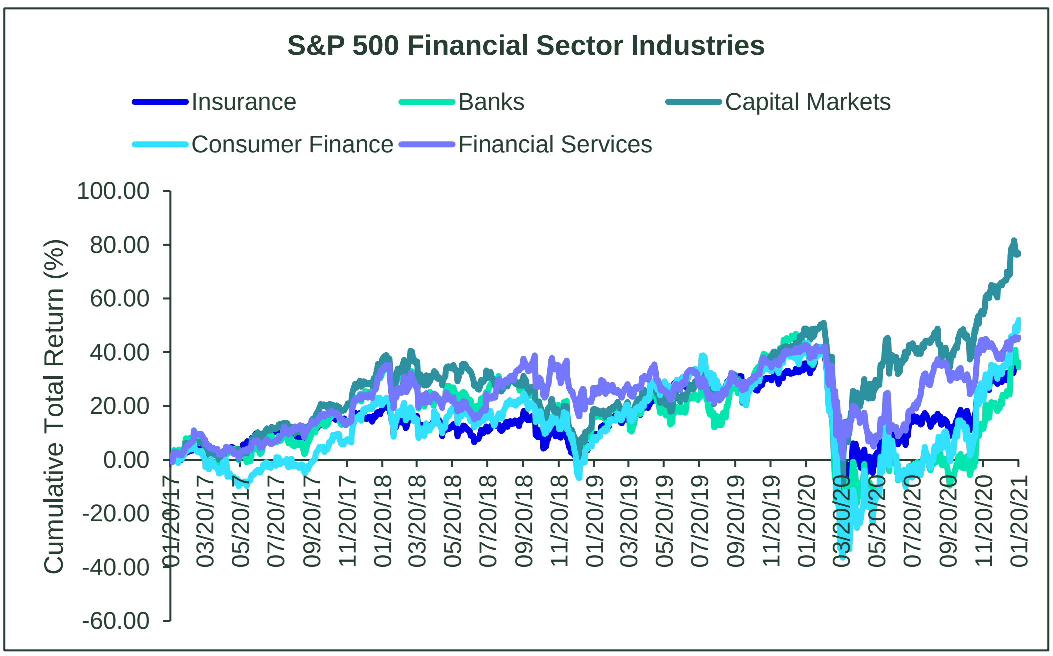
In what was expected to be a highly contested, razor thin margin election, things turned out to be quite orderly. This was welcomed by markets with the CBOE VIX retreating from 21.9 to 20.4 to 16.2 from November 4-6.

The president-elect's victory pushed the S&P 500 up 2.5% on November 6th, and major beneficiaries were small caps (R2000 +5.8%), financials (S&P 500 Financials Sector +6.1%), and energy (S&P 500 Energy Sector +3.5%). Disappointed with results were Gold (NYM $/ozt -2.6%), real estate (S&P 500 Real Estate Sector -2.6%), and Europe (MSCI Europe -0.7%).

When Trump takes office some of his first priorities will likely be around tariffs and immigration, both of which he may be able to enact through executive order. However, longer term we expect to see a trend of deregulation, especially with a republican sweep. Prior to Trump's election, changes involving regulation were already in progress. For example the Supreme Court struck down the Chevron doctrine which originally deferred the interpretation of ambiguous language in statutes to government agencies.

A few areas we see potentially impacted further are the SEC with Trump likely to appoint a new chair with a more business friendly approach. Additionally, Basel III endgame which proposes increased capital requirements for banks is likely to be delayed or changed. Lastly, less regulation could mean less scrutiny around mergers and acquisitions as a whole.

One of the largest sectors to be impacted by this deregulatory trend is financials. A look at how each industry within the S&P 500 financials sector performed under the Trump administration is below. Consider that this positive performance was created even as the yield curve was flattening during much of Trump's presidency.



Source: FactSet. Data from 1/20/2017 to 1/20/2021.

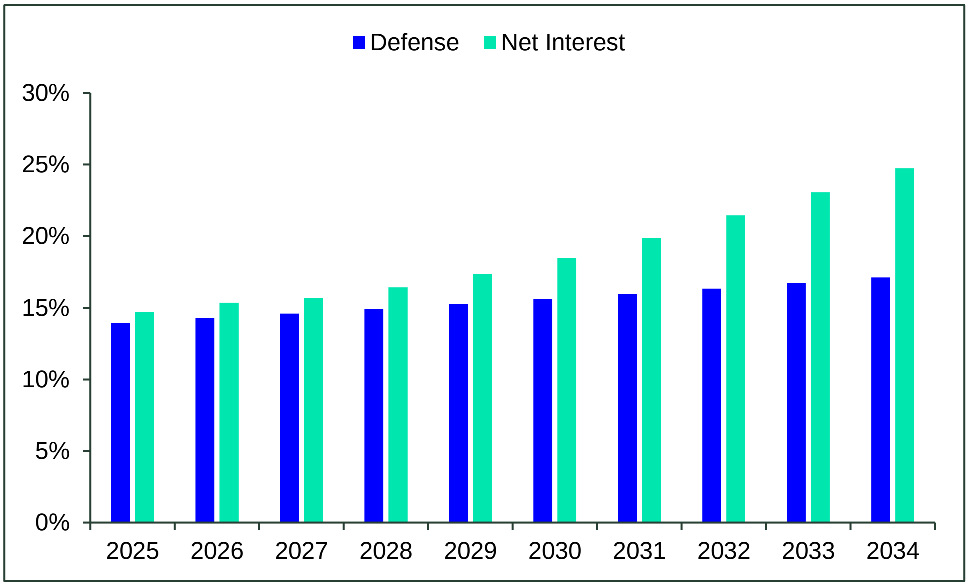
As we envision the policies that will shape the next term, de-regulation remains top of mind. This could provide a major tailwind to the financial industry, especially on the back of a steepening yield curve which we expect to come to fruition as the Fed continues to cut rates.

Source: State Street Global Advisors, FactSet. Data as of 11/6/2024 unless otherwise stated.

Fixed Income

Ballooning Interest Costs of U.S. Debt

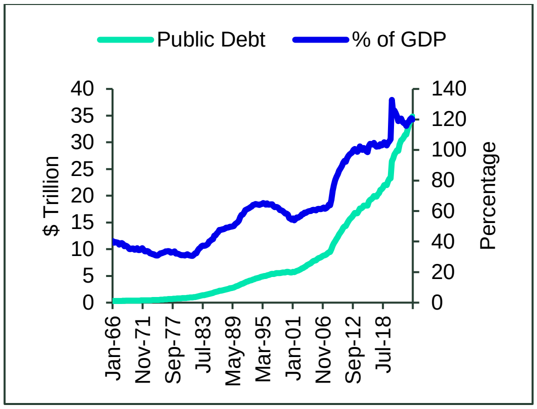
Since the start of the Covid Pandemic in 2020, the U.S. has added approximately $11 trillion of public debt to its balance sheet. Because much of this debt issuance happened alongside the Federal Reserve's rate hiking cycle, U.S expenditure on interest costs have skyrocketed. As of this year, the U.S. is spending more on interest costs to service its debt then it does on defense.

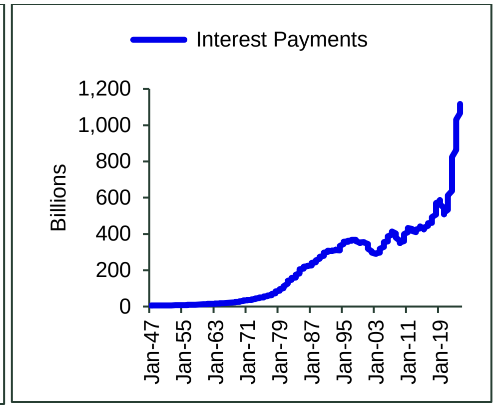


Source: Congressional Budget Office June 2024 Baseline Projections.

Today, total U.S public debt is approximately $35 trillion. With no fiscal restraint in sight, debt is expected to increase to at least $50 trillion over the next ten years according to the CBO.

Interest costs, currently 18% of federal revenue (versus 9% in 2021) are expected to reach 25% by 2034. About two-thirds of forecasted growth in interest costs are expected to stem from increases in the average interest rate on federal debt, and the remaining third reflects the expected increase in the amount of debt.





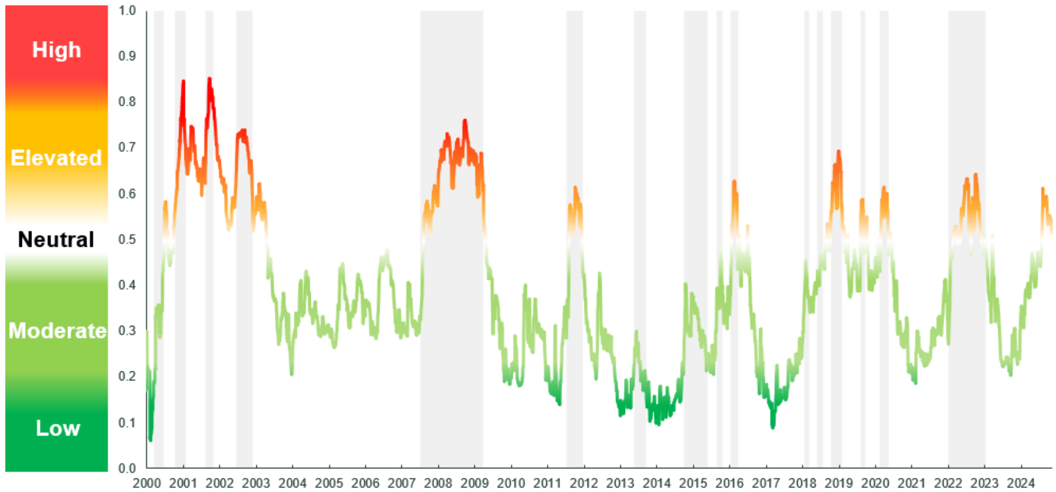
Source: Federal Reserve Economic Data, Federal Reserve Bank of St. Louis.

Historically, increases in U.S. debt have coincided with a low interest rate environment. However, debt issuance over last two years, coupled with higher interest rates has increased the cost to service debt, making it the third largest government outlay. Larger interest expenditure, in the absence of any foreseeable increase in taxes, could lead to larger deficits that would need to be funded at potentially even higher borrowing costs, putting even more stress on the U.S fiscal position.

Source: Bloomberg, State Street Global Advisors.

Market Regime Indicator

The Market Regime Indicator (MRI) represents a proprietary multi-asset class model designed to characterize risk appetites within the capital markets.



Source: State Street Global Advisors, Investment Solutions Group (ISG). As of November 6, 2024. The data displayed is not indicative of the past or future performance of any SSGA product. The above data represents a back-test of the MRI model, which means that those results were achieved by means of the retroactive application of the model which was developed with the benefit of hindsight. Data displayed beyond this date is not backtested, but is still generated by the model referenced. All data shown above does not represent the results of actual trading, and in fact, actual results could differ substantially, and there is the potential for loss as well as profit. The Market Regime Indicator (MRI) is a quantitative framework that attempts to identify the current market risk environment based on forward-looking market indicators. We believe the factors used are good indicators of the current risk environment as they are responsive to real-time market impacts and in theory should include all current and forward views of those markets. These factors are combined to create a single measure and used to identify one of four risk regimes: Low Risk, Moderate, Normal, Elevated and High Risk..

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*Pensions & Investments Research Center, as of 12/31/23.
†This figure is presented as of September 30, 2024 and includes ETF AUM of $1,515.67 billion USD of which approximately $82.59 billion USD in gold assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated. Please note all AUM is unaudited.

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Bonds generally present less short-term risk and volatility than stocks, but contain interest rate risk (as interest rates raise, bond prices usually fall); issuer default risk; issuer credit risk; liquidity risk; and inflation risk. These effects are usually pronounced for longer-term securities. Any fixed income security sold or redeemed prior to maturity may be subject to a substantial gain or loss.

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Exp. Date: 5/31/2025