Wealth Advisory Market Update

July 7, 2024

Market Update

Equities:

The equity market, as measured by the S&P 500, rose by 3.47% in the last month of the quarter. The index is now up 14.67% year to date. This is the best first half performance in an election year since 1976. The same theme of the past few months continues to drive this market higher. Narrow leadership, fueled by multiple expansion in the face of troubling economic readings. Inflation continues to remain above the Federal Open Market Committee's (FOMC) 2% goal leading to uncertainty of when the first rate- cut will occur. Historically, the first rate - cut has not been a good omen for the market or the overall economy.

Through the middle of June, the Bloomberg Magnificent Seven Index has accounted for 71% of the S&P 500 index gains this year. Five stocks in that index account for 60% of the market gains this year, a level not seen since the 1960s. Breaking it down even further, one stock accounts for 33% of this year's return. We pay close attention to market fundamentals for many reasons, one of which is future profit growth expectations. Current market multiples imply future growth expectations of 17% per year over the next five years. To put that into perspective, over the past century the long - run average over a five-year period is 6% per year, which is in line with overall economic growth. The narrow leadership of a small group of stocks has stretched market valuations to extremes. At some point, there will be a mean reversion event and we have positioned portfolios accordingly.

So far, 2024 has not gone as we expected. We felt coming into the year that we would see a rotation from the vastly overvalued areas of the market into areas that are trading below historical averages. The exact opposite has taken place, as money continues to move into the AI trade. At some point, AI will have to have a transformative application. Trillions of dollars have been pouring into an idea without a true way to increase profits as of yet. We will see a lot of volatility in that space if not.

Economic Indicators and Monetary Policy:

The FOMC met in June and market participants paid close attention, particularly since it was the first meeting since March to include the Fed's Summary of Economic Projections (SEP). This release coincided with the Consumer Price Index (CPI), which provided the market with some relief as it came in lower than expectations; the last couple of reports were hotter than expected. The release of this SEP before the meeting showed some changes since March's. The FOMC now only predicts having one rate cut after previously expecting to see three. Inflation forecasts were raised by 20 basis points from March's numbers in both headline and core Personal Consumption Expenditures (PCE) index for the year. The unemployment rate forecast was left unchanged at 4%. The SEP displayed hawkishness from the FOMC after the first quarter inflation reports showed troubling data.

After the release, the market shifted attention to Fed Chairman Jerome Powell's press conference. It was here that Powell, as usual, pushed back on the hawkish forecasts. When asked about the state of the inflation battle, he stated there has been significant progress towards inflation and employment goals. He noted the FOMC will need more data and greater confidence before adjusting monetary policy. He did note that the labor market data can be tricky to read due to the divergence in the household survey number and the Bureau of Labor Statistics (BLS) survey. The BLS survey has been overstated and revised down consistently over the past year.
After initially expecting to see six rate cuts for the year, the market is now only pricing in two. Economic data continues to show recessionary signs. Hard data surveys are now approaching the soft survey data. The price of

oil has seen a steady increase back to April highs which will likely be displayed in the headline inflation readings. We are closely monitoring the development of military tensions between Israel and Lebanon as further escalation can lead to an oil price spike. As we have mentioned previously, the constant liquidity being pumped into the economy via fiscal spending has kept the economy out of a recession. This amounts to nearly 1 trillion Dollars every 100 days which is fiscally irresponsible if you want to keep a sound dollar. The country has never had a budget deficit this large when it was not already in a recession. Powell does not see this as sustainable, and neither do we. A slowdown will likely occur once spending is reduced.

Strategy:

Given the economic landscape, we remain cautious and defensive. We advocate investing in businesses with strong market presence, pricing power, and consistent demand. Quality stocks that are trading below intrinsic value have not really paid off over the past eighteen months. However, we still believe that a diversified approach of focusing on companies trading below intrinsic value will come back into favor. In fixed income, we are extending duration in the intermediate segment of the yield curve, prioritizing high-quality credits over high yielding. Mortgage-Backed Securities (MBS) continue to be favored due to their favorable yield spreads in recent market conditions.

As we navigate this challenging environment, we appreciate your support and the opportunity to collaborate in achieving your financial goals.

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