Q1 MARKET INSIGHTS

Spring 2024

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KEY TAKEAWAYS

The first quarter of 2024 marked the eighth time that the S&P 500 Index has posted consecutive double-digit quarterly gains since World War II. Historically, this has been a bullish signal, as six of the prior seven occurrences were all followed by positive twelve-month gains.

Whether or not this trend can continue will likely be dependent upon monetary policy and corporate earnings growth.

Monetary policy: Incoming inflation data suggests that interest rates will probably be higher for longer, possibly creating a headwind for equities.

Corporate Earnings: The ability of companies to deliver on earnings growth will play a central role in determining the trajectory of equity markets in the coming months.

The U.S. equity markets are off to a strong start in 2024, as robust corporate earnings, buoyed by advancements in areas such as artificial intelligence, cloud computing, and digital transformation, helped propel stocks higher. In our opinion, U.S. equities have showcased remarkable resilience despite investors recalibrating expectations regarding the timing and magnitude of future interest rate cuts by the Federal Reserve (the "Fed"), and the heightened geopolitical tensions. The S&P 500® Index rose 10.56% during the first three months of the year for its best first-quarter performance since 2019. Continuing its tremendous run since October of last year, the S&P 500 has now posted two straight quarters of double-digit percentage gains for only the eighth time since the end of World War II. Internationally, foreign markets posted solid quarterly gains but still underperformed the U.S. Looking deeper, foreign developed markets outperformed emerging markets thanks to better-than-expected economic data and rising expectations for early summer rate cuts from the European Central Bank and Bank of England. Emerging markets, meanwhile, logged only slightly positive returns for the quarter due to mixed Chinese economic data, which was met with a lack of substantial Chinese economic stimulus. Foreign developed markets, represented by the MSCI EAFE Index, increased 5.83% during the first quarter, while emerging markets, represented by the MSCI Emerging Markets Index, finished the quarter up 2.13%. Switching to fixed income markets, the leading benchmark for bonds, the Bloomberg Barclays US Aggregate Bond Index, finished the quarter down 0.78%. Disappointing inflation readings were the primary reason for the weakness in bonds, as they delayed the expected start of Fed rate cuts and caused bond investors to consider that rates may be higher than previously expected over the medium and longer term.

> **"The S&P 500® Index rose 10.56% during the first three months of the year for its best first-quarter performance since 2019."**

The S&P 500's current streak of gains is nothing short of extraordinary. Again, this past quarter marked the eighth time that the index has posted consecutive double-digit quarterly gains since World War II. Historically, this has been a bullish signal, as six of the prior seven occurrences were

S&P 500 up 10%+ in Back-to-Back Quarters: 1945-2024

Second 10%+ Quarter	First Quarter (%)	Second Quarter (%)	S&P 500 Performance %			
			One Month	Three Months	Six Months	One Year
12/31/1954	10.61	11.36	1.81	1.67	14.04	26.40
12/31/1958	10.65	10.29	0.38	0.42	5.90	8.48
6/30/1975	21.59	14.19	(6.77)	(11.89)	(5.25)	9.55
3/31/1986	16.04	13.07	(1.41)	5.00	(3.17)	22.10
9/30/2009	15.22	14.98	(1.98)	5.49	10.63	7.96
12/31/2010	10.72	10.20	2.26	5.42	5.01	0.00
3/31/2012	11.15	12.00	(0.75)	(3.29)	2.29	11.41
3/31/2024	11.68	10.56	??	??	??	??
Average			**(0.92)**	**0.40**	**4.21**	**12.27**
Median			**(0.75)**	**1.67**	**5.01**	**9.55**

Source: Bespoke Investment Group

all followed by positive twelve-month gains with average and median total returns of 12.3% and 9.6%, respectively. In addition, the one time when the twelve-month performance was not positive, the return was flat (see table courtesy of Bespoke Investment Group above).

Looking ahead, the question we must ask ourselves is whether this historic trend can be repeated. As discussed in our last quarterly update, we believe monetary policy and corporate earnings growth are poised to remain pivotal forces in shaping equity market performance in 2024. Both factors have historically exerted significant influence on investor sentiment and market valuations. Below, we provide an update as to how we believe each of these dynamics will play a role in determining if equity markets can achieve positive returns in the months ahead.

MONETARY POLICY

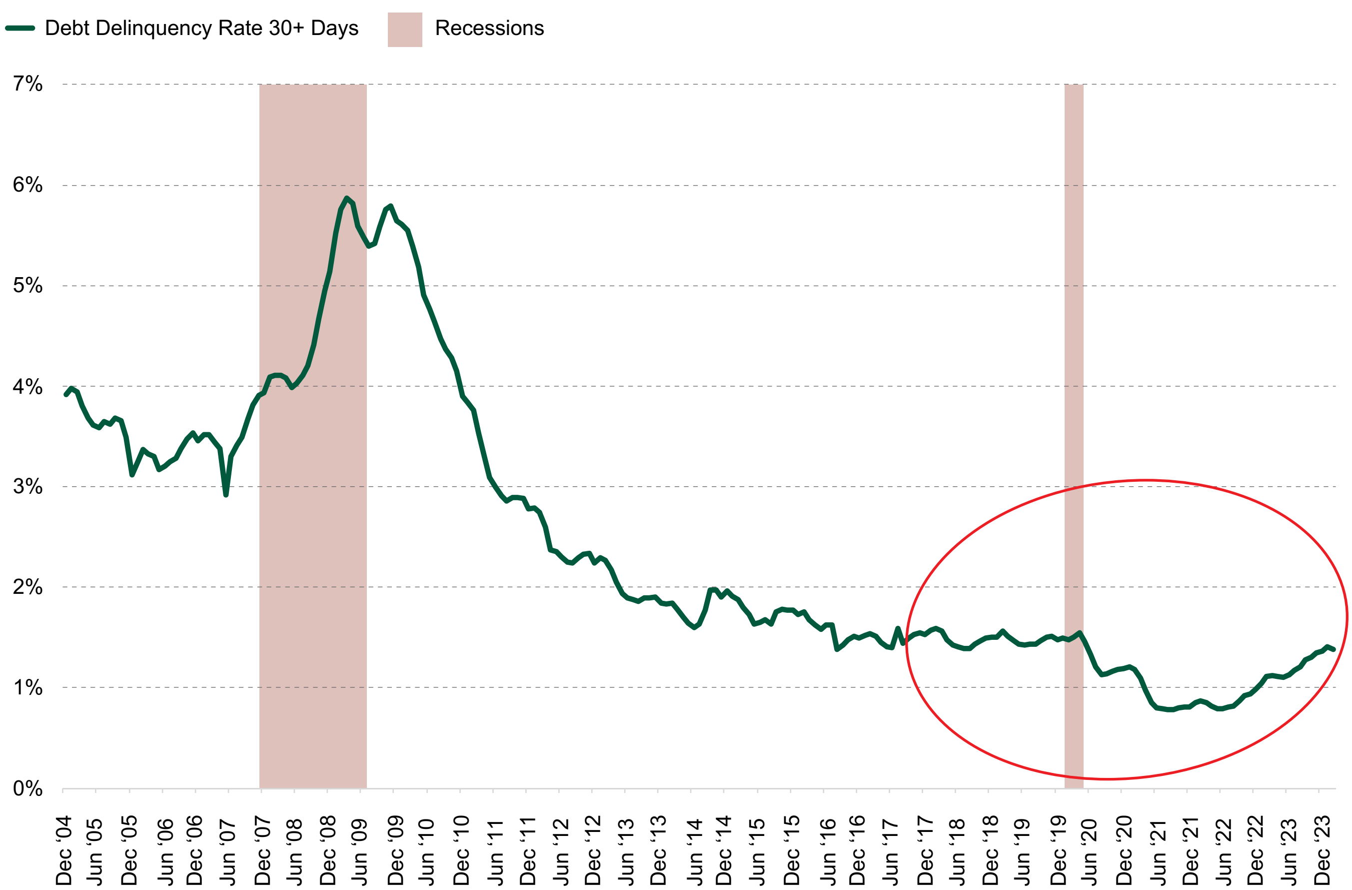
As mentioned earlier, U.S. equities were surprisingly resilient during the quarter, given the change in the investor outlook for interest rates. Whereas the rally in the fourth quarter of 2023 was mostly due to a dramatic shift in expectations for lower rates stemming from an expected pivot in Fed policy, the continuation of equity gains in the first quarter occurred despite meaningful changes in these expectations. Coming into 2024, investors (based on the Fed Funds futures market) were pricing in the likelihood of six 0.25% rate cuts during 2024, a stark divergence from the Fed's messaging of only three 0.25% cuts. However, as the quarter unfolded, inflationary data began to paint a different picture than initially anticipated. While the Consumer Price Index ("CPI") has fallen from its high of 9.1% in June of 2022, the last few months have seen inflation stabilize rather than continue its decline. In fact, the CPI edged slightly higher to 3.5% for the month of March, as disinflation in the prices for goods moderated and inflation for core services remained stubbornly high. These trends are expected to persist in the coming months and will probably make it more difficult for CPI to reach the Fed's target of 2%. Consequently, investor expectations for the magnitude of future rate cuts moderated, and the initial fervor for six rate cuts gave way to a more tempered outlook, aligning more closely with the Fed's guidance of three potential cuts. In addition, the minutes from the most recent Fed meeting showed that Fed officials were growing more concerned about the recent inflation data. The central bank does not want to reverse course on monetary policy prematurely and risk seeing price growth reaccelerate as it begins to cut rates, as this scenario was problematic for the Fed and the economy in the 1970s. If these inflationary pressures do persist, it is likely that interest rates will stay higher for longer than previously expected. As such, we believe that monetary policy will probably be a headwind for equities unless the Fed decides to be more aggressive in cutting interest rates.

CORPORATE EARNINGS

Despite the recalibration in rate cut expectations, the stock market remained buoyant, as investors shrugged off the impact of higher interest rates and appeared to focus on future earnings growth. Remember that equity market valuations are influenced by both earnings growth as well as changes in valuation multiples (like the price/earnings or "P/E" multiple). It's important to note that the bulk of the market's recent gains have been driven by multiple expansions rather than substantial growth in underlying earnings. In fact, according to FactSet, the earnings-per-share (or "EPS") growth for the S&P 500 for the last twelve months ending March 31, 2024, is expected to be only 2.2%, while the S&P 500 returned 29.9% during that same timeframe. As such, the majority of the return came from an uptick in valuation multiples as the trailing 12-month P/E ratio increased from 18.8 to 23.5 over the same period (for a frame of reference, the 10-year average trailing 12-month P/E ratio for the S&P 500 is 21.2). Given where valuation multiples are, the sustainability of future investment returns will depend heavily on the trajectory of EPS growth. According to FactSet, Wall Street analysts expect S&P 500 EPS growth for fiscal year 2024 to be 10.6% (or $243 per share). If we assume that the S&P 500 meets these earnings estimates and valuation multiples stay *at current elevated levels*, then we could possibly see the S&P 500 finish the year around 5,700 or about 8.5% higher than where we finished the first quarter. Therefore, for the market to continue delivering positive returns, companies will need to demonstrate strong and consistent earnings growth.

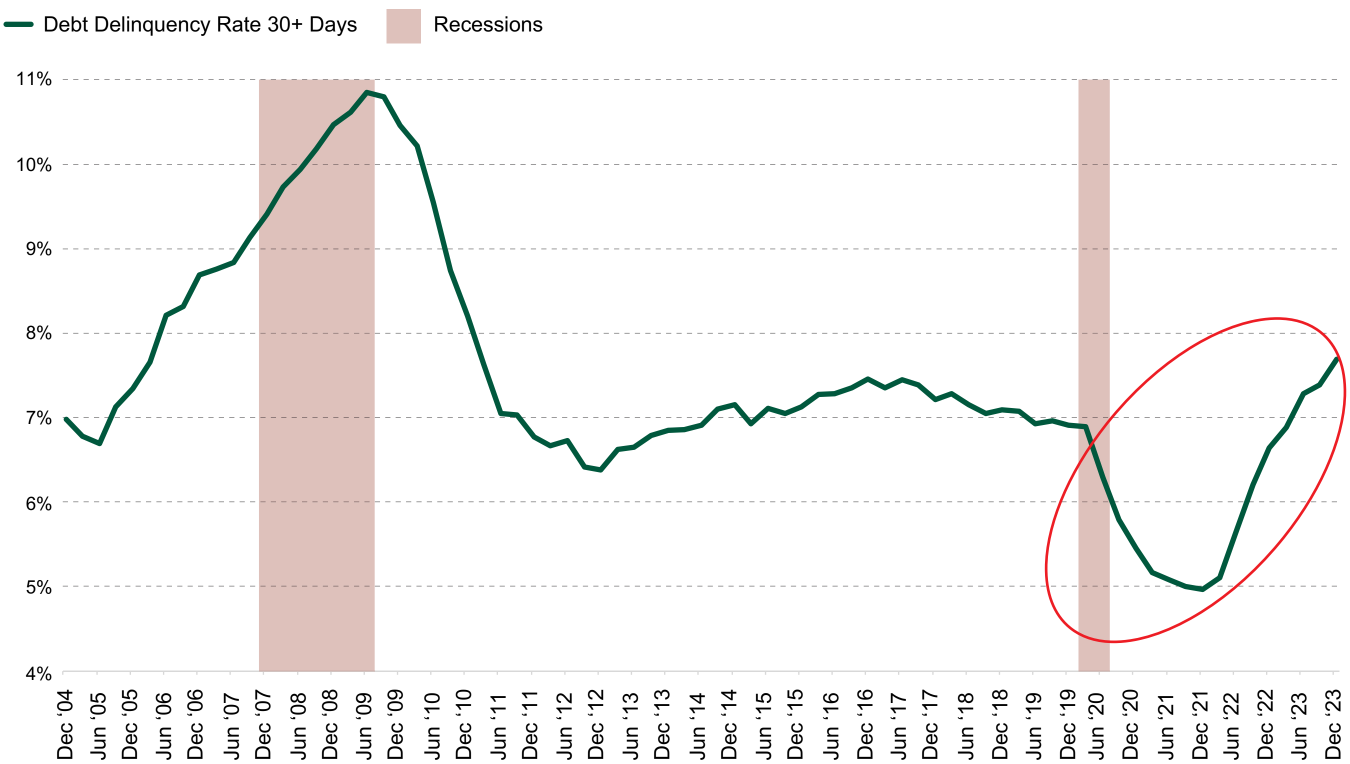
Is 10.6% EPS growth achievable? In the fiscal year 2023, EPS for the S&P 500 grew less than 0.5%, as the so-called Magnificent Seven stocks (Apple, Microsoft, Alphabet, Amazon, Meta, Nvidia, and Tesla) essentially drove all of the S&P 500's returns and profit growth, with earnings growing 12% on a market cap weighted basis, compared to

U.S. Credit Card Delinquency Rate 30+ Days Through February 29, 2024



Source: Bloomberg

U.S. Auto Loan Debt Delinquency Rate 30+ Days as of December 31, 2023



Source: Bloomberg

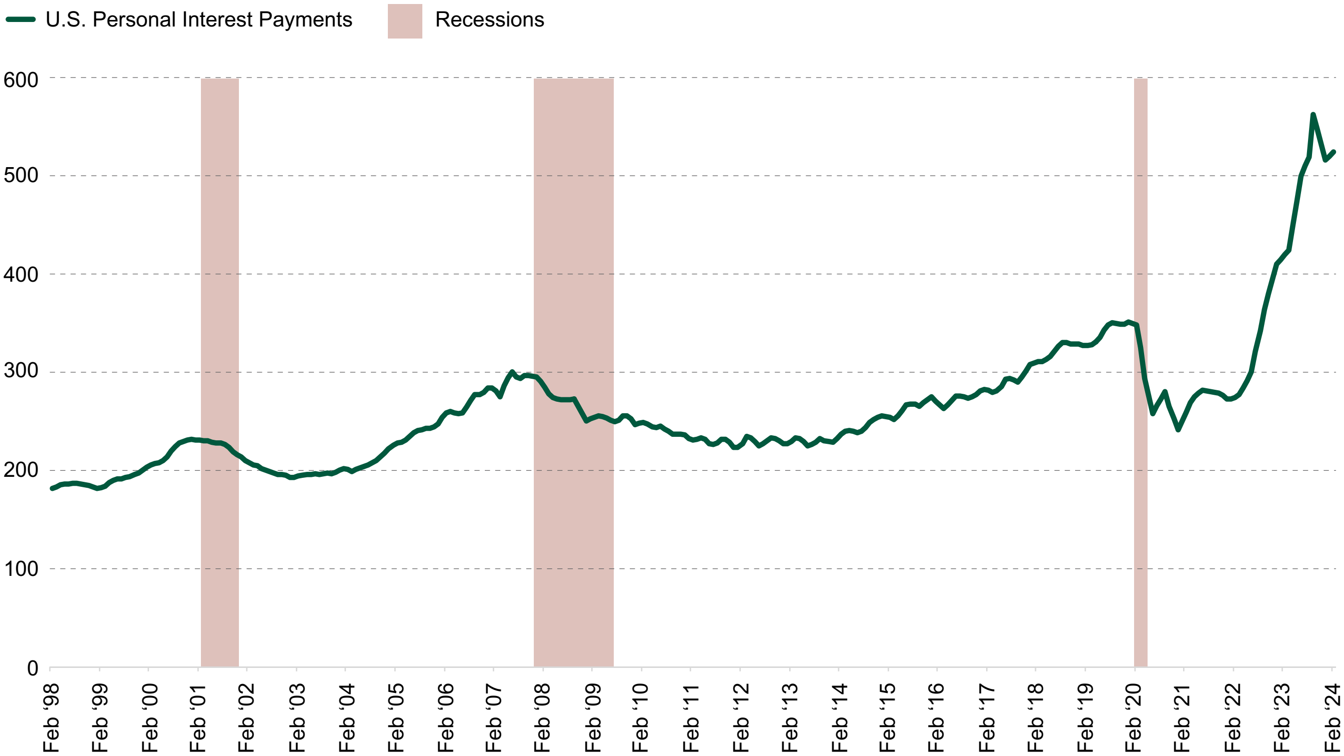
profits contracting for the remaining 493 companies in the S&P 500. The prospects for the Magnificent Seven for the coming year look promising as well, with earnings for these companies expected to continue to grow considerably. As such, the Magnificent Seven are estimated to make up 4.4 percentage points of the overall forecasted profit growth of 10.6%. Therefore, in order to achieve the projected EPS growth for the S&P 500 in fiscal year 2024, companies outside the Magnificent Seven will need to step up and demonstrate strong performance.

Based on analyst expectations, earnings from the remaining 493 companies in the S&P 500 will need to increase 8.7% in 2024 for the index to meet its 10.6% growth target. In our opinion, there are a couple of sectors that should see some profit tailwinds in 2024, including energy and healthcare, as they bounce back after experiencing weakness in 2023. As we look ahead, we believe that corporate earnings growth will depend upon the health of the consumer. Consumer spending in the U.S. has remained strong post-COVID, bolstered by a strong job market and massive government support programs. This allowed for increases in both wages and savings, which provided consumers with more disposable income to spend on goods and services. However, consumption will likely be less of an economic growth driver in the coming months as excess savings created by the financial stimulus programs fade and households feel the strain of higher borrowing costs (with the Fed keeping rates higher for longer). Recent data provides evidence that pandemic-related excess savings are finally being depleted. For example, delinquency rates for credit cards and auto loans are on the rise. The chart at the bottom of page 3 shows the percentage of credit card balances that are more than 30 days past due. As you can see, credit card delinquency rates are back to pre-pandemic levels (highlighted in the red circle), as a greater share of people are revolving all or part of their card balances (due to a drop in excess savings).

In addition, the chart above displays the percentage of auto loans that are 30 days past due. In this case, delinquencies ***have surpassed*** pre-pandemic levels (see red circle).

The rising delinquencies are coming at a time when the cost of debt is the highest it has been in recent memory, with the next chart illustrating the increase in personal interest payments in the U.S. due to higher interest rates.

U.S. Personal Interest Payments in Billions of USD- Monthly through Feb 29, 2024



Source: Bloomberg

With excess savings appearing to dwindle, the dynamics of consumer spending are poised to undergo a significant transformation. In this context, continued strength in the job market will probably be an important determinant of future consumer spending growth and ultimately earnings growth. A robust labor market characterized by low unemployment, rising wages, and ample job opportunities tends to bolster consumer confidence and purchasing power, thereby stimulating spending on goods and services. Conversely, a weak job market marked by layoffs, stagnant wages, and labor market uncertainty can dampen consumer sentiment and constrain spending, providing a headwind to profit growth.

IN CLOSING

While the recent expansion of the P/E ratio has propelled U.S. equities to new highs, whether the S&P 500's post-WWII winning streak will continue is likely to be contingent upon sustained EPS growth. As investors recalibrate their expectations and focus shifts towards fundamentals, the ability of companies to deliver on earnings growth will play a central role in determining the trajectory of equity markets in the coming months. As such, we believe that it remains important to own companies that possess the structural fundamentals to achieve sustained earnings growth during adverse economic conditions. This includes continuing to own some members of the Magnificent Seven, as these companies exhibit strong characteristics such as high barriers

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to entry, strong balance sheets, above-average revenue growth, and robust free cashflow generation while benefitting from strong market shares in many of the economy's most important sectors (artificial intelligence/computing power, data storage, eCommerce, software, electric vehicles, social media, smartphones, and media streaming). Earnings growth is a fundamental driver of stock returns over the long term, as it reflects the ability of companies to generate profits and create value for shareholders. Therefore, we believe that it remains very important to own companies that demonstrate strong and consistent profit growth.

The Fed will be walking a tightrope on the monetary policy front in the coming months. The central bank does not want to start cutting interest rates too early and see inflation reaccelerate. However, Fed policymakers must also guard against staying too restrictive and risk creating stress in parts of the economy (monetary policy often works with long and variable lags, and there continues to be a risk that tight monetary conditions could ultimately cause a recession here in the U.S.). While we expect the Fed to cut interest rates sometime later this year, we believe the declines will come at a somewhat slower pace due to sticky inflation. If that is the case, then short-term interest rates are likely to stay elevated for some time, making a strong argument for short-duration U.S. Treasuries in this type of environment.

Past performance is not indicative of future results, but history has shown that a long-term approach combined with a well-designed and diversified asset allocation based on your financial position, risk tolerance, and investment timeline is paramount to endure episodes of economic booms, recessions, and market downturns. In fact, one of the most compelling lessons from history is the power of compounding returns over time. Investors who commit to a long-term perspective harness the potential for their investments to grow exponentially, allowing them to weather short-term market fluctuations, and benefit from the upward trajectory of the market over extended periods.

We thank you for your ongoing confidence and trust. Please reach out to your relationship manager with any questions, or if you wish to discuss your portfolio allocation. Rest assured that our entire team remains dedicated to helping you successfully navigate these financial markets and are available to assist you with your financial needs. Our team members can be reached at 781-400-2800.

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The MSCI EAFE Index is a stock market index that is designed to measure the equity market performance of developed markets (Europe, Australasia, Far East), excluding the US & Canada. The MSCI EAFE Index is an equity index which captures large and mid-cap representation across Developed Markets countries around the world, excluding the US and Canada. With 913 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country. Indices are not managed and do not incur fees or expenses. Performance numbers for the index are total return with dividends reinvested in the index.

The MSCI Emerging Markets Index captures large and mid-cap representation across 24 Emerging Markets (EM) countries*. With 838 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country. Performance numbers for the index are total return with dividends reinvested in the index.

The Bloomberg Barclays US Aggregate Bond Index provides a measure of the total return performance of the U.S. dollar denominated investment grade bond market, which includes investment grade government bonds, investment grade corpo¬rate bonds, mortgage pass through securities, commercial mortgage backed securities and asset backed securities that are publicly for sale in the United States.

The Consumer Price Index (CPI) is issued by the U.S. Bureau of Labor Statistics and is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. Indexes are available for the U.S. and various geographic areas.

The price-to-earnings ratio (P/E) is the ratio for valuing a company that measures its current share price relative to its earnings per share. The price-to-earnings ratio is also sometimes known as the price multiple or the earnings multiple. P/E ratios are used by investors and analysts to determine the relative value of a company's shares. A company's P/E can be benchmarked against other stocks in the same industry or against the broader market, such as the S&P 500 Index It can also be used to compare a company against its own historical record or to compare aggregate markets against one another or over time.

Earnings per share (EPS) is calculated as a company's profit divided by the outstanding shares of its common stock. The resulting number serves as an indicator of a company's profitability. The higher a company's EPS, the more profitable it is considered to be.

Artificial intelligence (AI) is a wide-ranging branch of computer science concerned with building smart machines capable of performing tasks that typically require human intelligence. While AI is an interdisciplinary science with multiple approaches, advancements in machine learning and deep learning, in particular, are creating a paradigm shift in virtually every sector of the tech industry.

Artificial intelligence allows machines to model, or even improve upon, the capabilities of the human mind. And from the development of self-driving cars to the proliferation of generative AI tools like ChatGPT and Google's Bard, AI is increasingly becoming part of everyday life — and an area companies across every industry are investing in.

Please contact us at 781-400-2800 for more information on how we can assist you with your financial needs.

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