Q3 MARKET INSIGHTS

Fall 2024

BEAUMONT
FINANCIAL PARTNERS

KEY TAKEAWAYS

The S&P 500 finished the 3rd quarter at all-time highs on the back of the highly anticipated start of the Federal Reserve's (the "Fed") rate cutting cycle.

Keep your investment strategy separate from political considerations. Historical data demonstrates that financial markets perform well no matter which party occupies the White House. Attempts to time the market based on political outcomes are not recommended.

Potential gridlock in D.C.: A non-unified government should limit the winning candidate's ability to significantly change fiscal policy. However, no matter who wins, we expect debt and deficits to continue to rise.

The Fed changes its focus from fighting inflation to supporting the labor market. Job growth appears set to sustain economic momentum into early next year, but time will tell whether the Fed's strategy will be successful in engineering a soft landing.

Investors were treated to a white-knuckle ride in the third quarter, as political turmoil and anxiety over mixed economic data caused volatility to rise. This was highlighted by a selloff in early August, sparked by renewed fears of a recession (due to some disappointing employment data) and the sudden unwind of the global "Yen-carry" trade. However, the long-awaited start of the Fed's rate cutting cycle in September, coupled with new stimulus in China, helped to soothe investor concerns and support a strong rally in stocks into the quarter end. The S&P 500® Index finished September at a new all-time high, posting a return of 5.89% for the third quarter (+22.08% YTD). Looking internationally, foreign developed markets saw a solid rally in the third quarter as investors anticipated additional rate cuts from the European Central Bank and other major global central banks, while emerging markets received a boost from the stimulus measures in China. For the quarter, foreign developed markets, as represented by the MSCI EAFE Index, registered a positive 7.35% return (+13.55% YTD), and emerging markets, as represented by the MSCI Emerging Markets Index, were up 8.82% (+17.13% YTD). Switching to fixed income markets, the leading benchmark for bonds, the Bloomberg Barclays US Aggregate Bond Index, rose 5.20% for the quarter (+4.45% YTD) thanks to a combination of falling inflation and expectations of an aggressive rate cutting cycle from the Fed.

> **"The S&P 500® Index finished September at a new all-time high, posting a return of 5.89% for the third quarter (+22.08% YTD). "**

KEEP POLITICS OUT OF YOUR PORTFOLIO

The past three months of the 2024 presidential campaign have been nothing short of unprecedented, marked by dramatic developments that have reshaped the political landscape. First, in a surprising announcement, President Joe Biden declared his withdrawal from the race less than four months before the election. Second, this campaign season has been marred by several incidents, including two assassination attempts on Donald Trump's life, which underscore the increasingly volatile nature of the country's political discourse. While it is easy to get caught up in the rhetoric, especially with today's influence of social media, it is important to maintain the proper perspective. As we have shown in previous updates, equity markets have demonstrated a remarkable ability to climb higher regardless of which party occupies the White House.

Over the past century, both Democratic and Republican administrations have presided over periods of robust stock market performance, challenging the notion that one party is inherently "better for business" than the other. Instead, investors should keep their focus on the fundamentals, which are the key long-term drivers of market performance.

To highlight this point further, the National Bureau of Economic Research performed a study following the 2016 U.S. presidential election. Their research revealed that investors in Republican-leaning areas increased their equity exposure after the election, while those in Democratic-leaning areas reduced their equity positions. This divergence, which persisted for months, highlights how political beliefs can cloud financial judgment and lead to potentially suboptimal investment decisions. Perhaps most concerning was the finding that some investors made drastic changes to their portfolios, with a small but significant group altering their equity exposure by 50% or more. Such large swings, likely driven more by political sentiment than by sound financial analysis, underscore the risks of allowing partisan views to dictate investment strategy. As markets generally rose in the months following the election, those who reduced their equity exposure based on political disappointment may have missed out on substantial gains.

> **"Failure by Congress and the new administration to extend the TCJA tax cuts would likely leave individuals exposed to higher tax rates and other increases beginning in 2026. For example, the top personal tax rate would revert to 39.6% from the current 37%. Estate taxes would revert to a top 40% rate from the current 32%, and the estate tax exclusion amount would be more than halved, falling from $13.6 million to $5.5 million per individual."**

Lastly, preconceived notions about how certain presidential candidates will impact specific industries can often lead to misguided investment strategies. For instance, despite concerns over escalating trade tensions between the U.S. and China throughout the Trump administration, Apple—heavily exposed to China—saw its shares soar by 351%, significantly outperforming the S&P 500's 81% gain during that period. Similarly, the iShares Clean Energy ETF rose by an impressive 309% under Trump, defying expectations that his policies would hinder the clean energy sector while traditional energy stocks plummeted by 30%. Even more surprising, the S&P 500 Energy Sector Index has surged 137% under President Biden, countering fears of an anti-fossil fuel agenda. Meanwhile, the iShares Clean Energy ETF has lost half its value amid record oil and gas production. These cases highlight the risks of making sweeping thematic bets based on perceived political dynamics (see table at left).

Sector Surprises

Index/Security	Returns Under Trump 1/19/2017-1/19/2021	Returns Under Biden 1/19/2021-9/30/2024
S&P 500	81.3%	60.5%
S&P 500 Energy Sector	-29.5%	137.0%
iShares Clean Energy ETF	309.2%	-51.2%
Apple Inc	350.8%	86.2%

Source: Bloomberg

Historically, the key drivers of equity market performance have been macroeconomic factors like corporate earnings, economic growth, and interest rates. Other dynamics, like monetary and fiscal policy, have had a much greater impact on market sentiment than any soundbite we have heard from politicians. Still, there are some fundamental

> "Both major political parties have exhibited a propensity to embrace policies that prioritize short-term economic goals over long-term fiscal responsibility. Therefore, our view is that no matter who wins, the deficit is going to continue to rise."

differences between Kamala Harris and Trump that could impact fiscal policy. Major elements of the 2017 Tax Cut and Jobs Act (TCJA) are set to expire at the end of 2025. Trump has lobbied for extending the TCJA along with additional tax cuts, including an end to federal income taxes on Social Security benefits. Trump is also seeking to cut the corporate tax rate to 21% and increase tariffs on most imports. Failure by Congress and the new administration to extend the TCJA tax cuts would likely leave individuals exposed to higher tax rates and other increases beginning in 2026. For example, the top personal tax rate would revert to 39.6% from the current 37%. Estate taxes would revert to a top 40% rate from the current 32%, and the estate tax exclusion amount would be more than halved, falling from $13.6 million to $5.5 million per individual. Harris's proposals appear to align with those of President Biden, as she supports keeping some provisions in the TCJA in an effort to protect households making under $400,000 from higher taxes. Harris is advocating for higher taxes on households with annual incomes above $400,000 and levies on household wealth, including unrealized capital gains. Harris also favors a new tax on unrealized capital gains for a subset of wealthy individuals (those with at least $100 million in assets). In addition, Harris is looking to increase the tax rate paid by corporations.

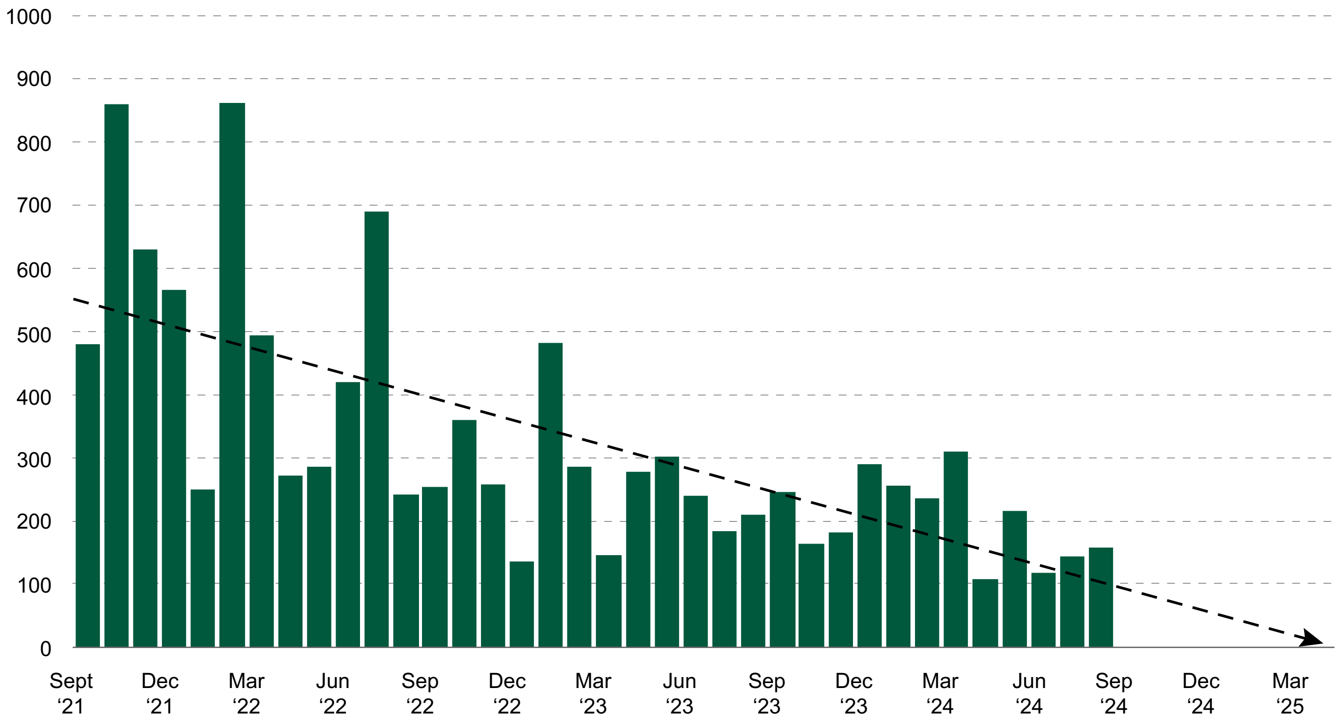
We have received numerous inquiries regarding the market implications of these proposed tax policies, particularly Harris's plan for taxing unrealized capital gains. However, we believe that many of these policies are unlikely to be enacted as initially proposed, due to the high probability that we will continue to have a non-unified government—where one party controls the presidency but the chambers of Congress are split—following the November elections. Current polls indicate a statistical dead heat in the presidential race, with Republicans holding a slight edge in the Senate while Democrats may have better prospects for a majority in the House. When one party controls the White House along with majorities in both chambers of Congress, the potential for meaningful legislative change increases significantly. Conversely, a divided government typically complicates the passage of sweeping reforms, as compromise becomes essential and limits the scope of tax or regulatory policy shifts. This dynamic allows the status quo to persist, enabling firms and investors to make decisions without the looming threat of major fiscal changes. Often, investors and markets view a divided government favorably, as it reduces uncertainty, curtails the potential for drastic policy swings, and shifts the focus back to fundamental drivers such as economic performance, monetary policy, and corporate earnings.

In our opinion, neither candidate will be able to fully implement their policy proposals due to a divided government. Based on our observations, the one key takeaway from both Harris and Trump's platforms is that there has been no mention of deficit reduction. Addressing the ongoing budget deficits is something that nobody in Washington D.C. seems to want to deal with, as it involves navigating a range of politically challenging options (including unpopular choices such as cutting entitlements or raising taxes). Both major political parties have exhibited a propensity to embrace policies that prioritize short-term economic goals over long-term fiscal responsibility. Therefore, our view is that no matter who wins, the deficit is going to continue to rise.

FED SWITCHES GEARS

The post-pandemic U.S. economy has demonstrated notable resilience, primarily driven by strong job growth. Despite waning economic data over the past several months—such as a sluggish manufacturing sector, negative leading economic indicators, and tighter lending standards—the labor market has remained a crucial pillar of support for the broader economy. Historically, these indicators have often foreshadowed recessions, but the sustained strength in employment has supported consumer spending, which accounts for a significant portion of GDP. However, recent declines in labor market data have prompted the Federal Reserve to adjust its approach to monetary policy. In September, the Fed kicked off its much-anticipated rate cutting cycle by reducing the Fed Funds rate by 0.50%—a move aimed at stimulating economic growth amid various pressures. The decision was seen as a signal of the Fed's

U.S. Non-Farm Payrolls (MoM Change in Thousands) Through August 2024



Source: Bloomberg

responsiveness to economic data and its willingness to adapt to changing circumstances. This move also underscored the Fed's commitment to its dual mandate of fostering maximum employment and stable prices. Since it began its rate hiking campaign in March of 2022, the Fed has been solely focused on bringing inflation down to its target rate of 2.0%. With the Consumer Price Index ("CPI") sitting at an annual rate of 2.5% as of August (falling from a peak of 9.1% in June of 2022), the Fed has shifted its focus to providing support for the labor market. While inflation isn't quite to the Fed's liking—with services inflation having remained somewhat sticky—recent declines in the labor market have become a greater concern. The chart above shows the monthly additions in non-farm payrolls over the last three years (the green bars), while the black line denotes an autoregression showing the broader trend in job growth. As you can see, the U.S. economy continues to add jobs, however the pace of job growth is trending lower. Recognizing that the health of the labor market is paramount, the Fed is now focusing on rate cuts to stimulate economic activity. Given the lagged effect of monetary policy, it may take some time before these rate cuts have any impact. If the current trend in job gains were to stabilize or reverse, then the potential for achieving a soft landing—where the economy slows down without entering a recession—is likely. But if this trend continues, it may indicate minimal job gains heading into the first quarter of the new year.

In our opinion, based on the job growth data, the labor market appears strong enough to sustain economic momentum through the remainder of this year and into the first quarter of next year. After that, the critical question will be whether the Fed's timing was appropriate in deciding when to cut rates. Only time will tell.

FINAL THOUGHTS

With the start of the Fed's rate-cutting cycle now behind us, investor focus should shift towards economic growth. Prior to these announced cuts, expectations for aggressive rate reductions allowed investors to overlook some of the soft economic data, as the anticipation of easier monetary policy created a cushion that helped bolster market sentiment. Now that those cuts are a reality, market dynamics are likely to change. We believe investors will look to incoming economic data to determine if the Fed was ahead of the curve (engineering a soft landing) or behind the curve

> **“Earnings growth is a fundamental driver of stock returns over the long term, as it reflects a company’s ability to generate profits and create value for shareholders. Hence, we believe that it remains important to own companies that demonstrate strong and consistent profit growth."**

(causing a recession) in reversing monetary policy.

(causing a recession) in reversing monetary policy. In addition, without the anticipation of easier monetary policy, equity returns are likely to become increasingly dependent on earnings growth. Now, as the focus shifts away from monetary policy adjustments, it appears that companies will need to deliver solid earnings growth to sustain market performance. Therefore, we believe that it remains important to own companies that possess the structural fundamentals to achieve sustained earnings growth during both favorable and adverse economic conditions. This includes owning companies that exhibit strong characteristics such as high barriers 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. Earnings growth is a fundamental driver of stock returns over the long term, as it reflects a company’s ability to generate profits and create value for shareholders. Hence, we believe that it remains important to own companies that demonstrate strong and consistent profit growth.

While inflation has continued to come down, it has yet to reach the Fed’s target. In our opinion, there is a risk that these rate cuts could reignite inflation and put upward pressure on intermediate and long-term interest rates. In addition, with the long-term inflationary impact of ever-increasing deficit spending and debt growth by the U.S. government (which will likely increase no matter who gets elected in November), we believe it is prudent to maintain exposure to short-term bonds, specifically U.S. Treasuries, within fixed income allocations. Furthermore, it may be practical to incorporate exposure to stores of value such as gold and bitcoin within appropriate portfolios, in order to protect one’s purchasing power.

In closing, while it’s natural—and even civically important—to have strong political convictions, we feel it’s essential to recognize that, historically, whoever occupies the White House has had very little impact on investment returns. The recent shift in monetary policy by the Fed—and its impact on interest rates and economic growth—should have a larger influence on asset valuations than any president or political party. By keeping your investment strategy separate from political considerations, you should be better positioned to effectively navigate market cycles and capitalize on long-term growth. Political climates can shift, but sound investment principles grounded in fundamental analysis should provide a stable path toward achieving your financial goals. We believe that maintaining a well-planned, long-term focused asset allocation allows you to remain resilient and adaptable to market changes, regardless of the prevailing political landscape.

We sincerely thank you for your ongoing confidence and trust in us. If you have any questions or would like to discuss your portfolio allocation, please don’t hesitate to reach out to your relationship manager. We’re here to support you in making informed decisions that best serve your interests.

Happy Autumn!

BEAUMONT
FINANCIAL PARTNERS

TRUST | TRANSPARENCY | TEAMWORK

Definitions:

S&P 500® Index is a registered trademark of Standard & Poor's Financial Services LLC, a division of S&P Global ("S&P"). S&P 500 Index is an unmanaged index used as a measurement of change in U.S. equity markets. Performance numbers for the index are total return with dividends reinvested in the index.

MSCI makes no express or implied warranties or representations and shall have no liability whatsoever with respect to any MSCI data contained herein. The MSCI data may not be further redistributed or used to create indices or financial products. This correspondence is not approved or produced by MSCI.

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 corporate 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.

Leading Economic Indicators (LEI), a composite of economic data points put together by The Conference Board designed to signal peaks and troughs in the business cycle. The Conference Board is a global independent business membership and research association working in the public interest.

Please contact us for more information on how we can assist you with your financial needs.

Disclosures:

Past performance is no guarantee of future results. An investment cannot be made directly in an index. Investment return and principal value will fluctuate; you may have a gain or loss when positions are sold.

As with all investments, there are associated inherent risks including loss of principal. Although not specified below, these risks are also present in private investments and institutional interval funds. Stock markets are volatile and can decline significantly in response to adverse issues, political, regulatory, market, or economic developments. Sector, commodity, and factor investments may concentrate in a particular industry and the investments' performance could depend heavily on the performance of that industry and be more volatile than the performance of less concentrated investment options. Foreign securities are subject to interest rate, currency exchange rate, economic, and political risks, all of which are magnified in emerging markets. The risks are particularly significant for securities that focus on a single country or region. Fixed income investments are subject to inflationary, credit, market, and interest rate risks. Cash positions are subject to inflation risk.

Cryptocurrency is more volatile than traditional currencies. Their value is speculative, given that they are not currently, widely accepted as a medium or exchange, is derived by market forces of supply and demand, and may be impacted by the continued willingness of market participants to exchange fiat currency for cryptocurrency.

Cryptocurrencies are not covered by either FDIC or SIPC insurance. Bitcoin, Ethereum and other cryptocurrencies are very speculative investments and involve a high degree of risk. An investment in cryptocurrency is not suitable for all clients. Clients must have the financial ability, sophistication/experience, and willingness to bear the risks of an investment, and a potential total loss of their investment. Fees and expenses associated with a cryptocurrency investment may be substantial.

This material is provided for informational purposes only and does not in any sense constitute a solicitation or offer for the purchase or sale of securities nor does it constitute investment advice for any person. Investment themes and individual securities mentioned may or may not be held in any or all client accounts.

The material may contain forward or backward-looking statements regarding intent, beliefs regarding current or past expectations. The views expressed are also subject to change based on market and other conditions.

The information presented in this report is based on data obtained from third party sources. Although believed to be accurate, no representation or warranty is made as to its accuracy or completeness.