



	QTD	YTD
S&P 500 Total Return	5.89%	22.08%
NASDAQ	2.76%	21.84%
Dow Jones	8.72%	13.93%
Russell 2000	9.27%	11.17%
World ex. US	3.31%	14.68%
Gold (\$2,635/oz)	12.83%	26.54%
Oil (\$68.17/bbl)	-16.54%	-4.86%
Long Term Treasury (4.08%)	7.80%	3.02%

As of September 30, 2024

The S&P 500 returned 5.9% in the 3Q, the best 3Q since 2020, in what is typically the seasonally weakest quarter of the calendar year. Generally positive economic data continued to illustrate the resiliency and strength of the American economy while inflation is slowing to levels approaching the Fed target of 2%. A normalizing and steady state US economy gave the Fed the confidence to finally cut rates after a historic rate hike cycle that saw the Fed Funds Rate steadily increase from a Covid pandemic “level zero” to 5.5% from March 2022 to July 2023, and remain there until this September. While monetary policy still remains relatively restrictive, the 50-basis point rate cut was a bold step and marks the beginning of what the market expects to be an easing cycle that brings Fed Funds down to 4% over the next 6-12 months. The Fed has now joined Europe, China and other global central banks in cutting rates in a coordinated synchronous easing in global monetary policy. All of this is good news for stocks generally, and we saw a broadening of the rally beyond the Magnificent 7 and mega cap tech reflecting an increased confidence in the economic outlook and a more friendly Fed. This broadening of stocks participating in the rally is welcome news because a broader foundation supports a sustainable bull market. This was reflected in a 3Q where the more “old school” DJIA (Dow Jones 30 blue chip index), the equal-weighted S&P 500, and the Russell 2000 small cap index all outperformed the S&P 500 after a lengthy period of underperformance since this bull market began in October 2022.

While the fundamental backdrop is solid and favorable for equities - moderating inflation, steady economic growth, a healthy jobs market, strong corporate earnings - there are a few developments to keep a close eye on. The 2024 Presidential Election is in the homestretch and brings some uncertainty to the 4th quarter. This is a historic election; both sides regard it as one of the most important in their lifetime and we could see heightened volatility as it plays out. At the same time, ongoing global wars pose threats to American business and consumers including supply chain disruptions. In particular, the war in the Middle East threatens to widen in dramatic fashion. It is possible the US and its allies could find themselves at war with both Russia and Iran before November 5th. The mix of two global conflicts reaching a critical juncture against the backdrop of the US election and leadership uncertainty should not be underestimated.

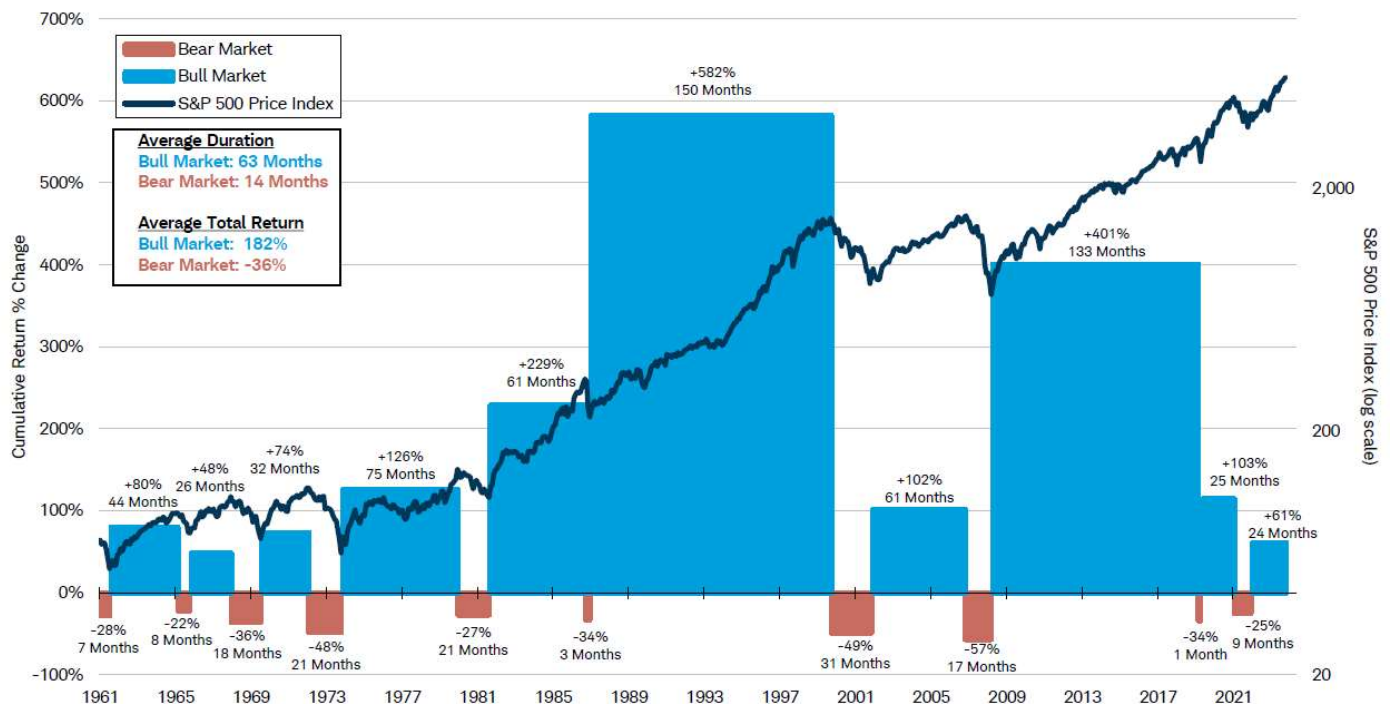
The unprecedented \$35T level of the National Debt (those interested should visit usdebtclock.org) continues to pose a looming challenge to interest rates, inflation and economic growth. The sheer size of the federal debt and the interest expense on that debt could at some point overwhelm the bond market, forcing interest rates higher to entice buyers for a growing debt market, raise inflation, and choke economic growth if not addressed. In sum, war and debt are the principal threats to the market and American prosperity, and they are fundamentally related given the ongoing fiscal burden of war.

Still in the Mid-Cycle

The American economy is performing better than any other industrialized market in the world. As discussed in recent commentaries, we see the U.S. market and economic strength reflective of a mid-cycle environment. Mid-cycle here refers to the long middle phase of an economic cycle that sets in after the initial early-stage recovery from an economic downturn (in this case the COVID Pandemic & the market decline of 2022) and before the economy reaches peak growth. It is typically characterized by moderate growth, healthy profitability and sees monetary policy turn increasingly neutral - benign. Mid-cycle expansions can go on for years: examples being 1984 -1989, 1993-1999, 2003-2007, 2012-2019. During those periods, several things usually happen: large cap stocks outperform small cap stocks, U.S. Large Caps outperform the Rest of World stocks, rates fluctuate around a narrow band and the U.S. dollar tends to be strong. We think these trends will continue albeit in the context of a more broadly performing domestic equity market. The profitability of the S&P 500 is significantly higher than it is for mid and small cap stocks. Moreover, the relative strength, profitability and competitive dominance of the top tier of the S&P 500 has continued to increase over the past decade. These companies represent unique best-of-breed assets and investments.

U.S. bull and bear markets

With the S&P 500 still up considerably this year, it is notable that bull markets have generally been longer in duration and greater in magnitude than bear markets, resulting in gains over time.



Source: Bloomberg as of 9/30/2024. Bull and bear markets as defined by Yardeni Research. Cumulative return is the total change in the investment over a set period of time. Logarithmic (log) scale is a way of displaying a wide range of data in a compact way by increasing the numbers exponentially. Indexes are unmanaged, do not incur management fees, costs and expenses, and cannot be invested in directly. For illustrative purposes only. Investing involves risk, including loss of principal. Past performance is no guarantee of future results.

Normalization in a Not So Normal Time

The ongoing Goldilocks (too hot/too cold/ just right) debate over growth, interest rates and inflation is also a mid-cycle phenomenon. While market expectations have fluctuated, growth has remained steady and inflation has slowly trended down to 2.5%. In reference to inflation, economist Ed Hyman at Evercore ISI, recently noted *“After years of increases, companies are rolling back prices”*. Additionally, the Social Security Administration set its 2025 cost-of-living adjustment at 2.5%, the lowest level in 5 years, and in line with its 30-year average. For reference, the COLA adjustment in 2021, 2022, and 2023 were 5.9, 8.7, and 3.2 respectively.

At this point we are seeing the economy and interest rates normalize. While there is some scope for the Fed to cut the funds rate down to the 4% level if inflation remains subdued, longer-term rates as measured by the 10-year Treasury Bond at roughly 4% appear to be at equilibrium with the economy based on 2% real growth and 2% inflation.

At the same time, market valuations are at the upper end of the historic range at 22.5 times 2023 estimated earnings. Stock gains from here will have to be earnings driven, given that longer term rates are about where they should be relative to the economy and there is little scope for PE expansion. We believe our portfolio remains well positioned to deliver solid long-term earnings growth.

POSITIVE	NEGATIVE
<ul style="list-style-type: none"> Inflation Concerns Diminishing 	<ul style="list-style-type: none"> Ongoing Wars in Ukraine and Middle East
<ul style="list-style-type: none"> Fed Policy Working -- Growth, Jobs and Inflation Approaching Equilibrium 	<ul style="list-style-type: none"> Widening Middle East Conflict Threatens Global Supply Chain
<ul style="list-style-type: none"> Fed Rate Cut Cycle 	<ul style="list-style-type: none"> Restructuring of Global World Order
<ul style="list-style-type: none"> Resilient Growth 	<ul style="list-style-type: none"> M2 Money Supply Growth Negative/Monetary Tightening Lag
<ul style="list-style-type: none"> Economy still in slow and steady mid-cycle 	<ul style="list-style-type: none"> Election Uncertainty Poses an Unknown for Markets & Economy in 4Q
<ul style="list-style-type: none"> AI & Technology Investment Spending Boom 	<ul style="list-style-type: none"> US National Debt at Record High Level (\$35T), @1.24x Greater than Nominal GDP