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GLOBAL INVESTMENTS

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2Q24 Investment Update

Bob is a financial services industry veteran with over 40 years of experience managing large cap equity strategies as well as long and long-short equity strategies. His weekly, quarterly, and annual investment commentaries focus on key themes and risks driving equity markets, monetary policy, and the global economy. Bob is a regular guest and contributor to multiple media outlets such as CNBC, Bloomberg TV, Moneywise, and Fox Business News.

S&P 500 4-year history

Source: Bloomberg as of March 31, 2024

Introductory observations

- We are in a high-risk, highly valued bull market driven by momentum.
- Predicting the end of a momentum run is a fool's game.
- Focus on earning predictability, earnings persistence and good cash flow generation in equity selection.

"Inflation is sticky; markets disagree or don't care."

– Nancy Lazar, March 2024

"Prices reflect near perfection, yet today's world is particularly imperfect and dangerous."

– Jeremy Grantham, March 2024

A good question

Q: Hey Team

I am a simple man in many respects.

I do not know how you get S&P 11% EPS growth and 5% revenue growth in the same year as 6 Fed rate cuts (2024 consensus).

You guys are very bright, what am I missing here?

Cheers,
Client

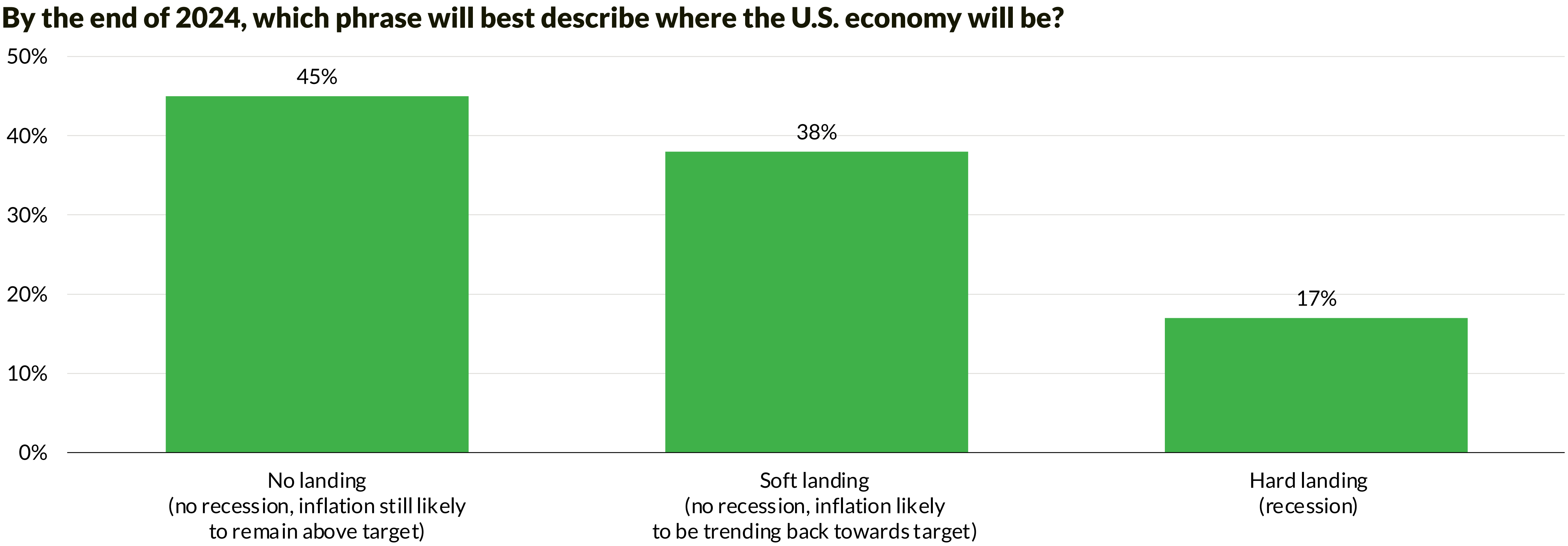
Now 11% for 2024 and 13% for 2025

Now 3 cuts

The equity market seems as convinced about a soft landing in 2024 as it was convinced of a recession in 2023.

Source: Strategas

Recent market survey



Source: Deutsche Bank

Goldilocks remains a fairytale

(You can't have your cake and eat it, too)

Consensus

1. Economy slows some but is A-OK.
2. Inflation continues to fall.
3. Fed cuts rates multiple times.
4. Earnings grow double-digits.
5. Multiples above 20x

Intractable imbalances/problems

1. There are consequences to the Fed raising rates from 0% to 5.25% in 18 months.
2. 10+ years of quantitative easing (essentially zero interest rates) will go in history books as a major policy error.
3. The U.S. is running a high federal budget deficit at essentially full employment.

Recession questions

Why has there been no recession?

- Excess savings from COVID
- Significant government spending
- Massive private credit borrowing

Why is a recession still likely?

- Lagged impact of massive Fed interest rate increases
- Inverted yield curve
- Leading economic indicators

Prediction 1

The U.S. economy experiences a mild recession as the unemployment rate rises above 4.5%

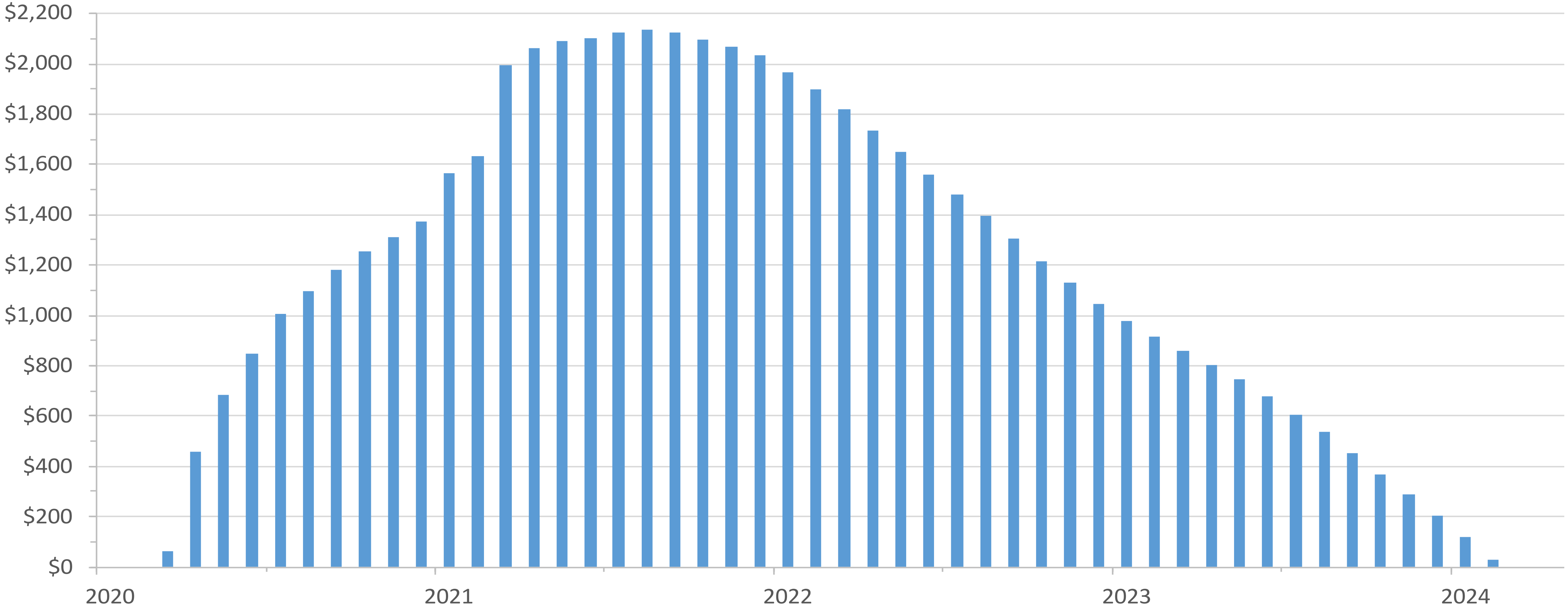
2024 economy	
Tailwinds	**Headwinds**
1. Good nominal GDP/revenue growth	1. Lagged impact of higher Fed funds
2. Good labor market/wage gains	2. Lagged impact of higher bond yields
3. Strong consumer/jobs	3. Banks tightening lending standards
4. Government spending	4. Credit card borrowing
5. Declining gasoline prices	5. Some 401(k) borrowing/cashing in
	6. Savings shortage at low/middle incomes
	7. Negative jobs revisions
	8. Inverted yield curve
	9. Commercial real estate excess (esp. office)
	10. Geopolitical turmoil

Source: Piper Sandler

Prediction 1

The U.S. economy experiences a mild recession as the unemployment rate rises above 4.5%

Cumulative excess savings held by U.S. households ($B)



Source: Federal Reserve Bank of San Francisco

Prediction 1

The U.S. economy experiences a mild recession as the unemployment rate rises above 4.5%

We're just entering the timeframe when tightening triggers a downturn

Fed funds initial hike	First quarter of recession	Quarters from liftoff
3Q 1958	3Q 1960	8
4Q 1967	1Q 1970	9
2Q 1972	1Q 1974	7
2Q 1977	2Q 1980	12
4Q 1980	4Q 1981	4
4Q 1986	4Q 1990	16
2Q 1999	2Q 2021	8
3Q 2004	1Q 2008	14
Average		10
1Q 2022	?	10

Source: Piper Sandler

Prediction 1

The U.S. economy experiences a mild recession as the unemployment rate rises above 4.5%

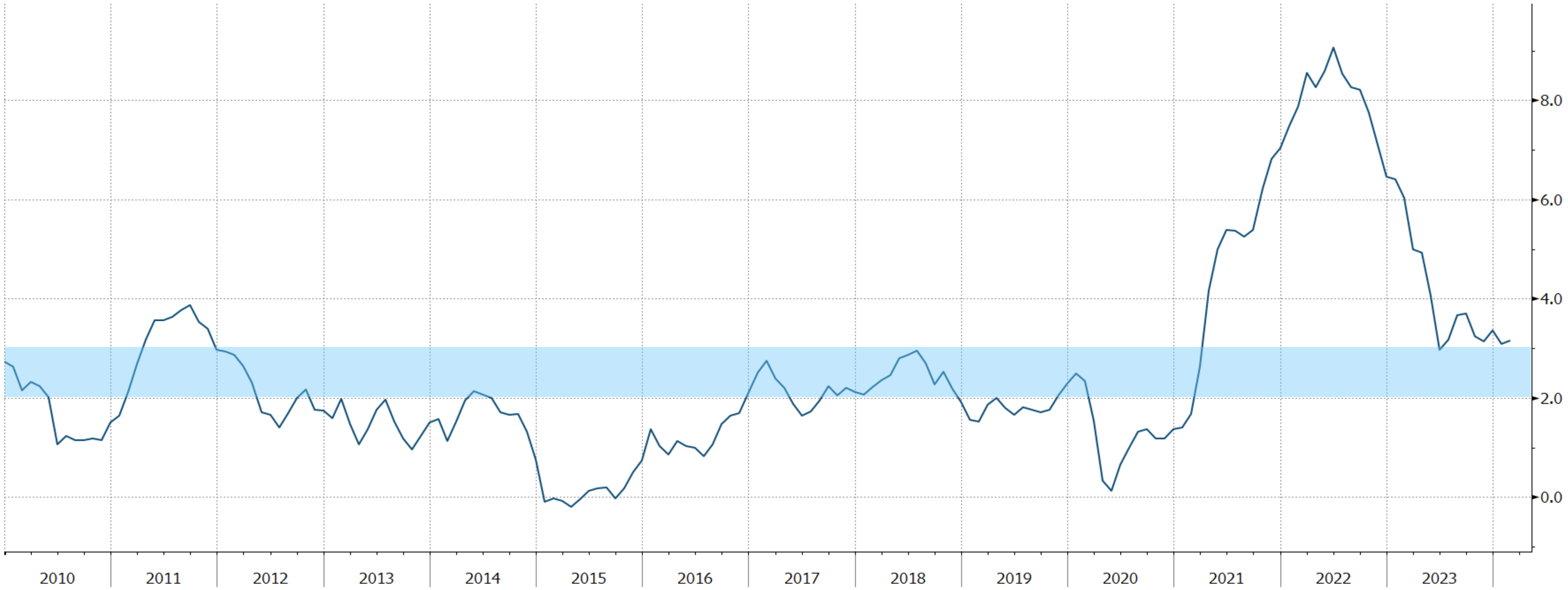
U.S. unemployment rate total in labor force (seasonally adjusted)

Source: Bloomberg

Prediction 2

The 2-3% inflation ceiling of the 2010s becomes the 2-3% inflation floor of the 2020s

U.S. CPI inflation year over year (%)

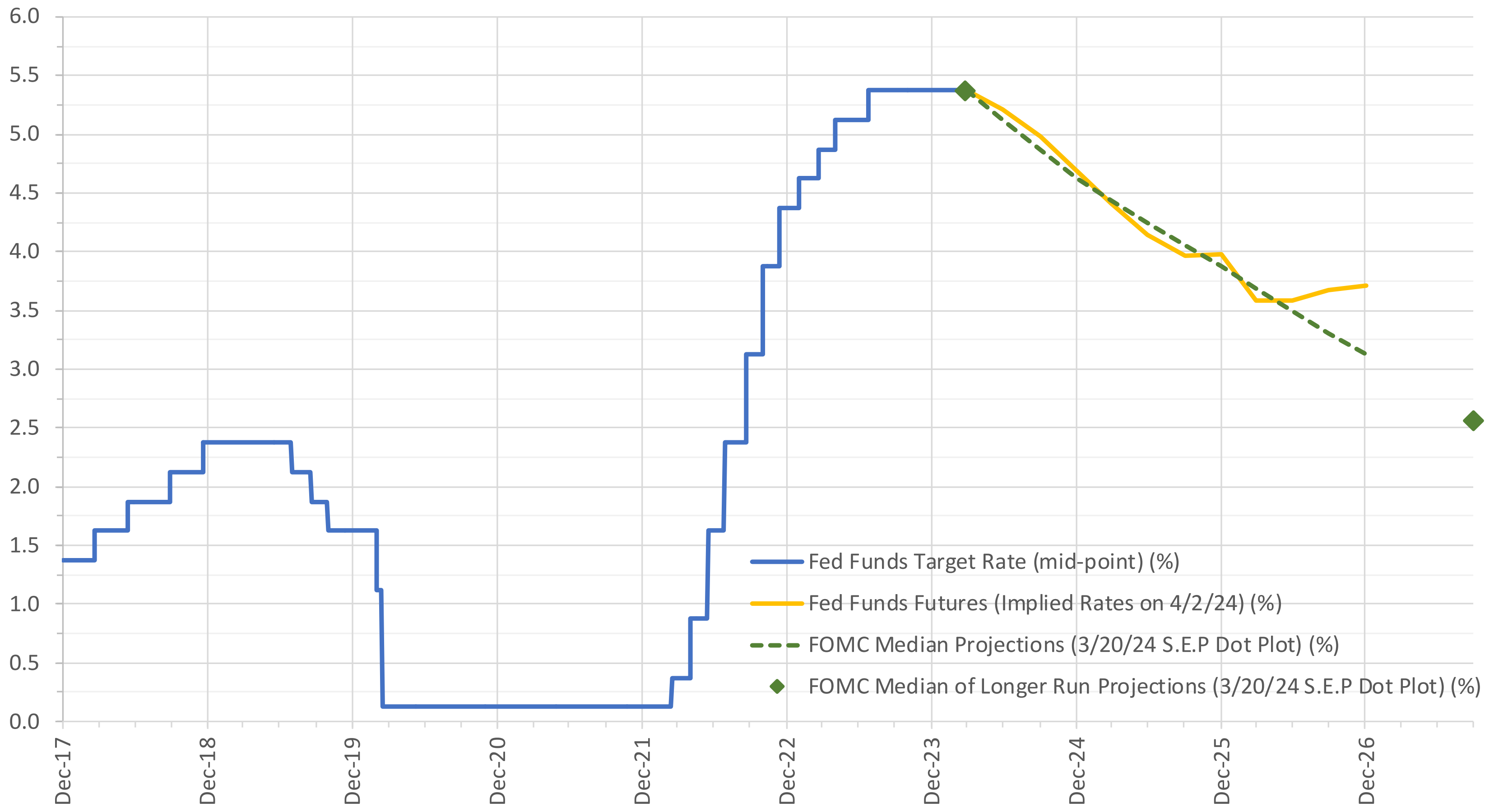


Source: Bloomberg

Prediction 3

The Fed cuts rates fewer than the six times suggested by the Fed funds futures curve

Fed fund futures implied rates (%)



Source: Bloomberg as of April 2, 2024

Prediction 3

The Fed cuts rates fewer than the six times suggested by the Fed funds futures curve

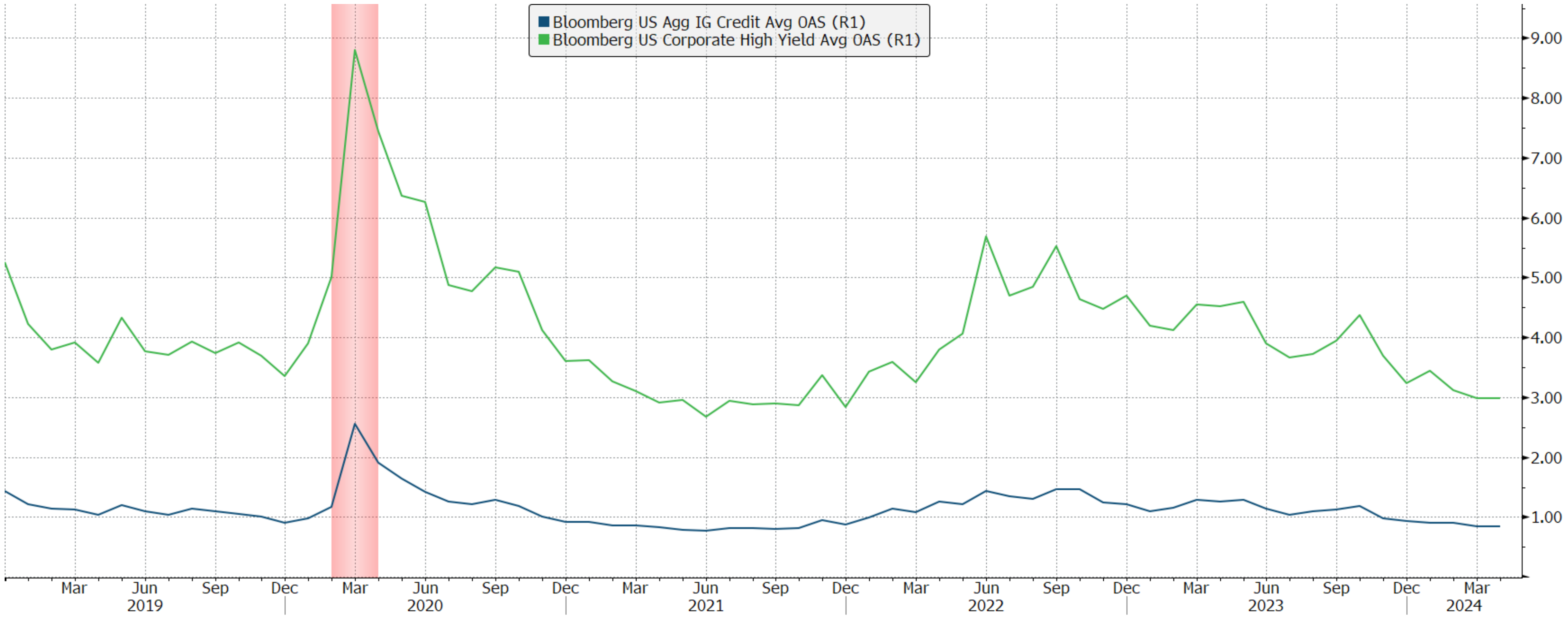
Is mission accomplished?

	CPI trailing 12 months	
	Headline	**Core**
February 2023	6.0%	5.5%
February 2024	3.2%	3.8%

Source: Bloomberg as of March 31, 2024

Prediction 4

Credit spreads widen as interest rates decline

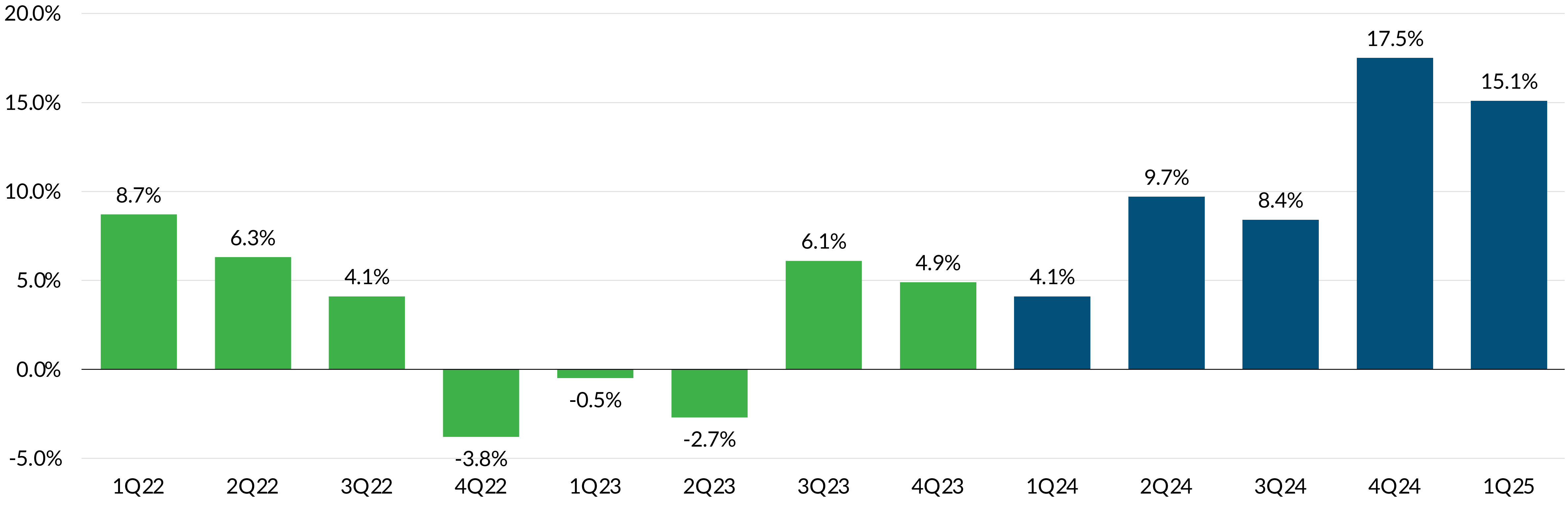


Source: Bloomberg

Prediction 5

Earnings growth falls short of the double-digit percentage consensus expectation.

Consensus: The earnings recession is likely over



Source: FactSet as of April 1, 2024

Prediction 5

Earnings growth falls short of the double-digit percentage consensus expectation

Our guess (S&P 500 EPS)

	Baseline	Mild recession	Bull case	Consensus[1]
2022	$219	$219	$219	$219
2023	$220	$220	$220	$220
2024 E	$235 + 6%	$200 - 9%	$245 + 11%	$244 + 11%
2025 E	$250 + 6%	$230 + 15%	$270 + 10%	$276 + 13%

1 Source: FactSet as of April 1, 2024

Prediction 6

Stocks record a new all-time high early in the year, but then experience a fade

Real GDP range	# Instances	Average return (%)	Median return (%)
< 0%	11	+18.3	+23.5
0 – 2%	9	(4.3)	0.0
2 – 4%	29	+8.6	+10.8
> 4%	27	+9.6	+12.4
All years (1947–2022)	76	+8.9	+11.1

Source: RBC

Miscellaneous observations

Multiple expansion has been the cause of market appreciation since October low (+28%) as earnings estimates have hardly changed (P/E: 17x → 21.5).

Future upward moves in stocks will probably require rising earnings estimates (already +11% for 2024 and +13% for 2025).

High-end consumers – still buying, keeping prices high, enjoying stock market gains

Low-end consumers – cutting back, tapping credit cards and 401(k)s

Technical position

25% of S&P 500 hit 52-week highs on March 21 (best reading since mid-2021)

- New highs often peak well before index does
- Financials up 30% from October low

S&P 500 history

Quintile	1st quarter returns (%)	1Q 2024 (%)	Rest of year average returns (%)
1	8.6 – 21.6	+10.2	+2.9
2	4.6 – 8.6		+10.1
3	0.2 – 4.6		+6.3
4	-4.9 – +0.2		-2.3
5	-20.0 – -4.9		+15.0
			Average: +6.4

Source: Bloomberg

Prediction 6

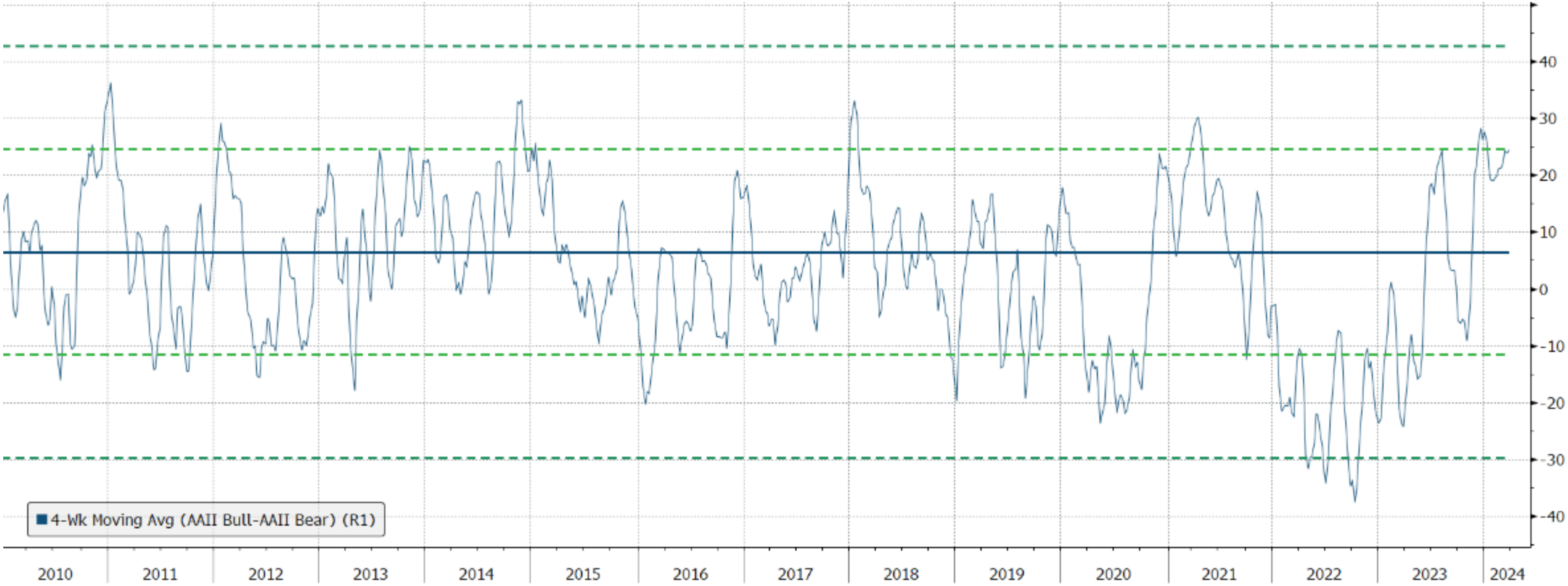
Stocks record a new all-time high early in the year, but then experience a fade

Valuation metric	S&P 500	
	Current	Historical percentile
Forward P/E	18.8x	81%
EV/EBITDA	13.4x	88%
EV/sales	2.8x	93%
Free cash flow yield	4.2%	43%
Price/book	4.3x	88%
U.S. market cap/GDP	196%	94%

Prediction 6

Stocks record a new all-time high early in the year, but then experience a fade

Bulls starting to dominate again (unlike the end of 2022)



Source: Bloomberg, AAII

SPX close price predictions

Source: Bloomberg as of March 31, 2024

Prediction 6

Stocks record a new all-time high early in the year, but then experience a fade

	S&P 500 average forward returns (%)			
Starting P/E	1-year	3-year	5-year	10-year
<10x	13.4	11.2	12.3	11.5
10-12	14.9	13.0	10.4	10.5
12-14	10.5	9.1	8.5	9.6
14-16	12.4	10.9	9.8	9.3
16-18	6.4	6.3	5.3	5.2
18-20	7.4	6.0	5.5	4.4
>20	3.9	4.4	5.5	3.0

Source: Strategas

Prediction 6

Stocks record a new all-time high early in the year, but then experience a fade

Source: Professor Robert Shiller, Yale School of Management; Strategas

Prediction 7

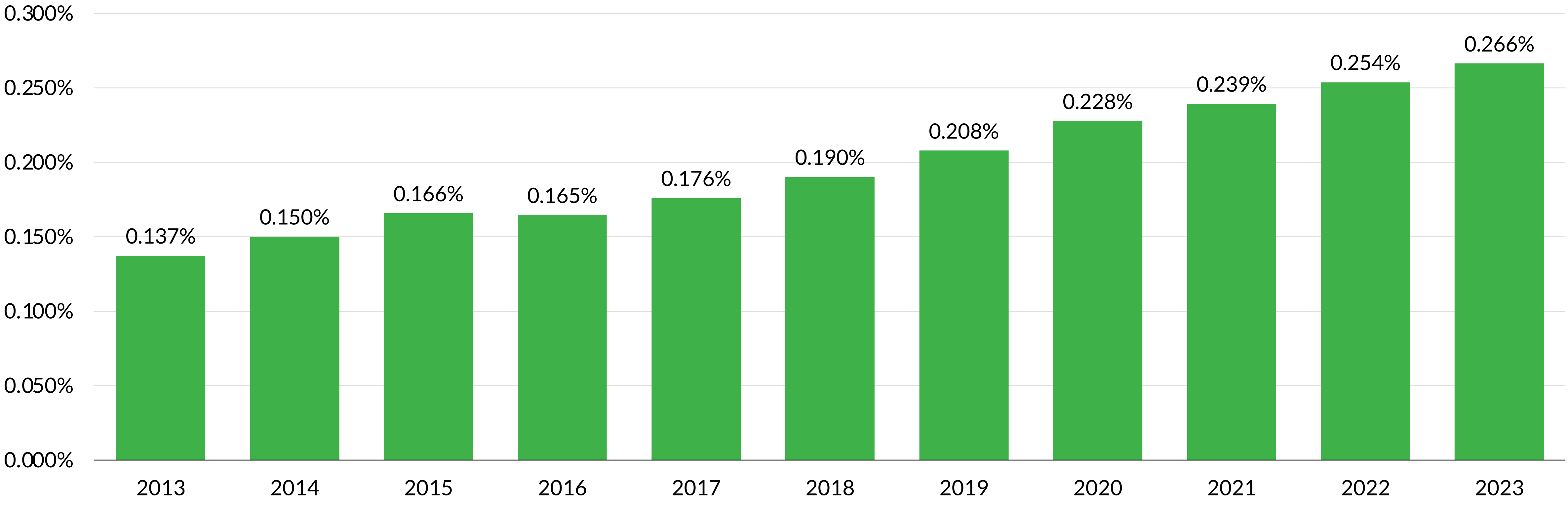
Energy, financials and consumer staples outperform utilities, healthcare and real estate

Overweights	1Q24 return	Underweights	1Q24 return
Energy • Cheap; strong earnings generation • Strong and growing cash flow • Global energy security concerns **Risk: World peace**	+12.7%	**Utilities** • Dividend yield less attractive • Payouts high • Not cheap vs. bonds **Risk: Late cycle outperformance track record**	+3.6%
Financials • High quality/low leverage vs. history • Historically inexpensive • Eventually positive yield curve **Risk: Regulatory risk; commercial real estate**	+13.0%	**Healthcare** • Typical election year underperformance • Poor drug pipeline • Not particularly cheap **Risk: Good defensive characteristics**	+8.4%
Consumer staples • Defensive characteristics if recession • Weakening dollar beneficiary • Valuations have de-rated **Risk: Will lag in economy and market recovery**	+6.8%	**Real estate** • Commercial/office space risk • Tough to secure investment capital • Patience required given headwinds **Risk: Dividends strong**	-1.4%

Prediction 8

Faith-based share of industry AUM rises for eighth year in a row

Faith-based market share (percentage of total industry AUM)



Sources: Morningstar and Crossmark as of Dec. 31, 2023

Prediction 9

Geopolitical crosscurrents multiply but have little impact on markets

Geopolitical issues

1. Extreme polarization within U.S. (on lots of issues, especially wars)
2. Two highly unpopular leaders running for president
3. Ukraine-Russia war
4. Middle East war
5. Iran nuclear threat
6. China cold war
7. Global political uncertainty: 40% of countries, 41% of population, nearly 60% of global GDP and nearly 80% of stock market capitalization experiencing national elections in 2024

Recent developments

- U.S. - Israel alliance under pressure
- Fed on hold (delayed rate cuts)
- House Speaker Mike Johnson and Democrats passing legislation (e.g., budget)
- Terrorism in Russia
- RFK Jr. in double-digits

Future?

- Chinese economy implodes
- Gaza truce
- Presidential candidate health issue
- Fed put is back.

Prediction 10

The White House, Senate and House all switch parties in November

Key issues
1. Tax policy (extension of Trump tax cuts)
2. Massive fiscal deficits/increased interest expense/entitlements
3. Relationship with China (trade, technology, Taiwan)
4. NATO commitment/Ukraine funding
5. Middle East war funding/Middle East relationship
6. Possible tariffs (more nationalism)
7. Southern border/drug traffic/cities and crime

Will the Supreme Court play a significant role in the election?

Recessions have been a determining factor for presidential re-elections

No recession two years before re-election		
President	**Recession?**	**Re-elected?**
Obama	No	Yes
Bush II	No	Yes
Clinton	No	Yes
Reagan	No	Yes
Nixon	No	Yes
LBJ	No	Yes
Eisenhower	No	Yes
Truman	No	Yes
FDR	No	Yes
FDR	No	Yes
FDR	No	Yes

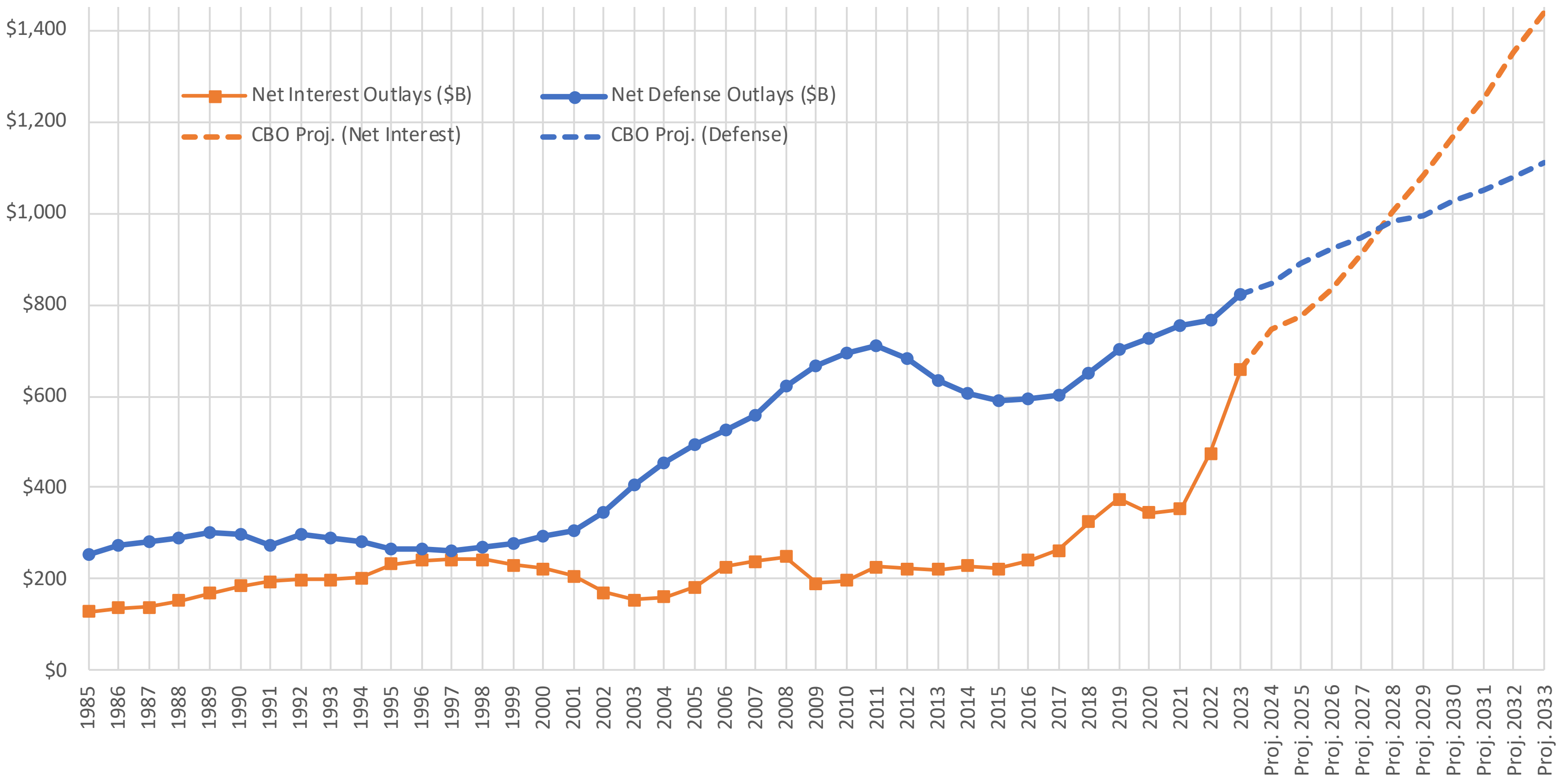
Recession two years before re-election		
President	**Recession?**	**Re-elected?**
Trump	Yes	No
Bush I	Yes	No
Carter	Yes	No
Ford	Yes	No
Hoover	Yes	No
Taft	Yes	No

Source: Strategas

Prediction 10

The White House, Senate and House all switch parties in November

Major components of Federal spending



Source: Congressional Budget Office (CBO)

Summary observations

1. The bid under U.S. stocks will persist for as long as the economy/earnings are okay and bond yields don't rise in a disorderly manner. Having said that, high valuations are increasing risk levels.
2. High valuation and narrow corporate bond spreads suggest that monetary policy is not restrictive.
3. Earnings growth should broaden (as should the market), but growth expectations are full/excessive.
4. Inflation will remain sticky.
5. Globally, economies are picking up from recessionary or near-recessionary levels.
6. Global trade will pick up cyclically, even as the secular decline continues.
7. Dollar is likely to weaken as U.S. slows some and non-U.S. economies recover.

Conclusions

1. The delayed recession shows up in 2024.
2. Inflation continues to fall but central bank targets (2%) remain elusive.
3. The Fed lowers rates, but less than expected.
4. Earnings fall short of expectations, even without a recession.
5. Stocks are expensive on most all measures.
6. Own stocks with good earnings predictability and persistence, and strong cash flow.
7. Do some dollar-cost averaging into international.
8. Expect dollar weakness.
9. Geopolitical threats continue to create uneasiness.
10. Election crosscurrents continue to accentuate polarization.

What to do?

1	Expect choppy markets (buy dips/trim rallies).
2	Focus on earnings growth and free cash flow (not P/E expansion).
3	Own some quality fixed income.
4	Diversify across asset classes and geographies (more non-U.S.).
5	Own high-quality value and less expensive growth.
6	Consider an absolute return strategy to complement market exposures.
7	Be prepared to step up if significant weakness.

Equity preferences

Themes

- Strong earnings predictability
- Strong earnings persistence
- Strong cash flow generation

Example stocks	
Software	Autodesk, Cadence Design, Intuit, Salesforce
Other tech	Applied Materials, IBM, Lam Research, Qualcomm
Healthcare	CIGNA, Gilead, McKesson, United Health
Financial services	American Express, Mastercard, PNC, Visa
Consumer	Booking Holdings, Home Depot, Nike, Target

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All investments are subject to risks, including the possible loss of principal. Past performance does not guarantee future results.

Equity investments generally involve two principal risks—market risk and selection risk. The value of equity securities will rise and fall in response to general market and/or economic conditions (equity market risk). The value of any individual equity security will rise and fall in response to the market's perception of the issuer's revenues, earnings, balance sheet, credit worthiness, business plan, and overall perception of the viability of the issuer's business (selection risk).

Fixed income investments generally involve three principal risks—interest rate risk, credit risk, and liquidity risk. Prices of fixed-income securities rise and fall in response to interest rate changes (interest rate risk). Generally, when interest rates rise, prices of fixed-income securities fall. The longer the duration of the security, the more sensitive the security is to this risk. There is also a risk that the issuer of a note or bond will be unable to pay agreed interest payments and may be unable to repay the principal upon maturity (credit risk). Lower-rated bonds, and bonds with longer final maturities, generally have higher credit risks. As interest rates rise and/or the credit risk associated with a particular issuer changes, bonds held within a portfolio may become difficult to liquidate without realizing a loss (liquidity risk).

Many municipal bonds also include call features that allow the issuer to call the bonds—repaying the principal before maturity—usually done in the context of a refinancing transaction if/when interest rates fall. When a bond is called, the holder does not incur a loss, but cash received from the call must be re-deployed, generally in a less favorable interest rate environment (call risk).

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Q&A

Thank you

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