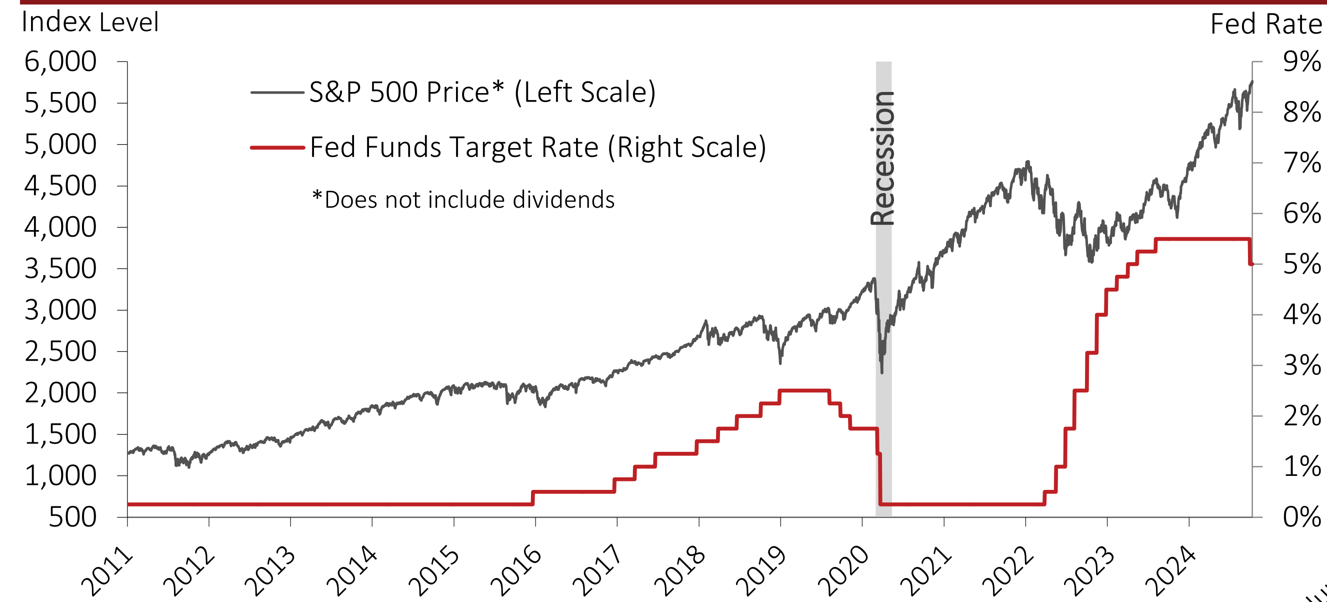
Capital Market Review

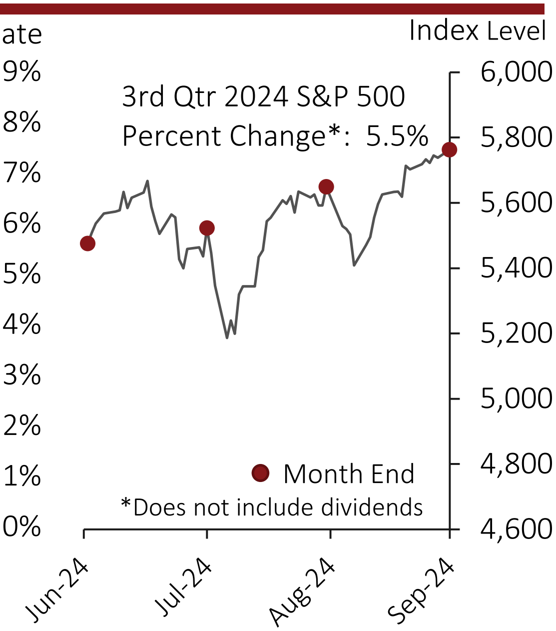
September 30, 2024




Watch the Capital Markets Review Key Takeaways Video

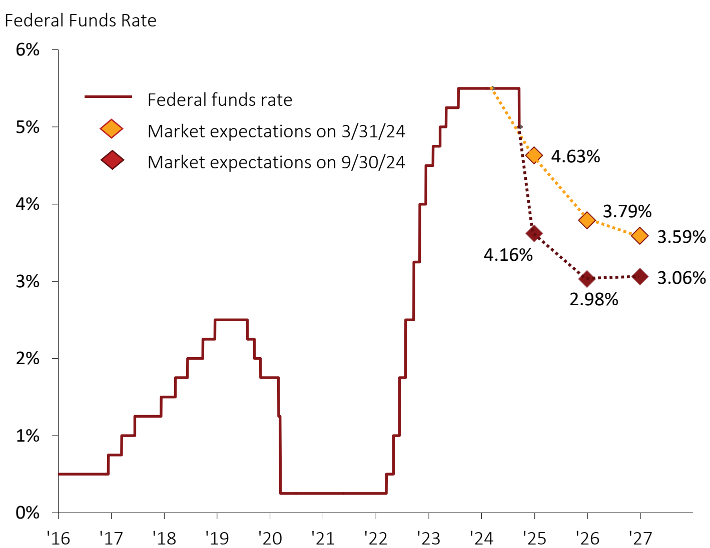
Rate Cuts Begin





Source: Standard & Poor's, Federal Reserve

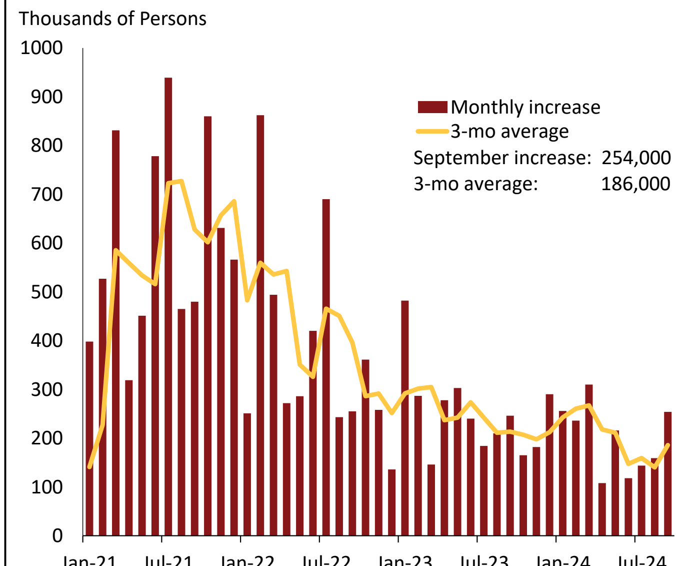
Federal Funds Rate Market Expectations



Source: Federal Reserve, J.P. Morgan

The Federal Reserve finally cut interest rates 50 basis points in September in response to signs the economy is slowing. The chart to the right shows how the trend line of employment gains have slowed considerably in the past 18 to 24 months. That, along with the rate of inflation moderating, resulted in the yield curve shifting downward. The 10-year Treasury opened the quarter at 4.34% and closed it at 3.80%, a drop of 54 basis points. As more evidence of moderation, the chart to the left shows the change in expectations for Fed funds rates in just six months. The market is now expecting a more aggressive rate-cutting Fed than one that will keep rates "higher for longer."

Monthly Change in Nonfarm Workers



Source: FRED - Federal Reserve Bank of St. Louis, DeMarche

INDEX	3rd Qtr	YTD	1-YEAR	3-YEAR	5-YEAR	10-YEAR
MSCI World	6.4	18.9	32.4	9.1	13.0	10.1
Russell 3000	6.2	20.6	35.2	10.3	15.3	12.8
S&P 500	5.9	22.1	36.4	11.9	16.0	13.4
MSCI EAFE USD	7.3	13.0	24.8	5.5	8.2	5.7
MSCI Emerging Markets USD	8.7	16.9	26.1	0.4	5.7	4.0
Bloomberg Aggregate	5.2	4.4	11.6	-1.4	0.3	1.8
Bloomberg Global Aggregate	7.0	3.6	12.0	-3.1	-0.8	0.6
FTSE Non-US Gov't Bond	8.6	1.9	12.0	-6.3	-3.4	-1.1
NAREIT (Public RE)	16.2	13.7	33.7	3.0	4.7	7.7
Bloomberg Commodity	0.7	5.9	1.0	3.7	7.8	0.0

Notes: Data are presented as percent returns. All 3-, 5-, and 10-year returns are annualized.

Indicator Year Ending 9/30	2024	2023	2022	2021	50-YEAR Average
GDP Annual Growth Rate*	3.2	2.9	1.7	4.7	2.7
Unemployment	4.1	3.8	3.5	4.7	6.2
Inflation (CPI)	2.4	3.7	8.2	5.4	3.7
10-Year Interest Rates	3.8	4.6	3.8	1.5	5.9

**Note: Prior to the GDP quarterly release from BEA, we show the annual GDP Growth rate from OECD weekly tracker as the most recent year.*

Calendar Year Broad Market Returns

2014 - '23 10-Yr Ann. Return	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	YTD 2024
Russell 1000 11.8%	Russell 1000 13.2%	Russell 1000 0.9%	Russell 2000 21.3%	MSCI Emg Mkt 37.3%	Bloomberg Aggregate 0.0%	Russell 1000 31.4%	Russell 1000 21.0%	Russell 1000 26.5%	ICE BofA High Yield -11.1%	Russell 1000 26.5%	Russell 1000 21.2%
Russell 2000 7.2%	Bloomberg Aggregate 6.0%	Bloomberg Aggregate 0.5%	ICE BofA High Yield 17.3%	MSCI EAFE 25.0%	ICE BofA High Yield -2.3%	Russell 2000 25.5%	Russell 2000 20.0%	Russell 2000 14.8%	Bloomberg Aggregate -13.0%	MSCI EAFE 18.2%	MSCI Emg Mkt 16.9%
MSCI EAFE 4.3%	Russell 2000 4.9%	MSCI EAFE -0.8%	Russell 1000 12.1%	Russell 1000 21.7%	Russell 1000 -4.8%	MSCI EAFE 22.0%	MSCI Emg Mkt 18.3%	MSCI EAFE 11.3%	MSCI EAFE -14.5%	Russell 2000 16.9%	MSCI EAFE 13.0%
ICE BofA High Yield 4.5%	ICE BofA High Yield 2.4%	Russell 2000 -4.4%	MSCI Emg Mkt 11.2%	Russell 2000 14.6%	Russell 2000 -11.0%	MSCI Emg Mkt 18.4%	MSCI EAFE 7.8%	ICE BofA High Yield 5.3%	Russell 1000 -19.1%	ICE BofA High Yield 13.4%	Russell 2000 11.2%
MSCI Emg Mkt 2.7%	MSCI Emg Mkt -2.2%	ICE BofA High Yield -4.6%	Bloomberg Aggregate 2.6%	ICE BofA High Yield 7.5%	MSCI EAFE -13.8%	ICE BofA High Yield 14.4%	Bloomberg Aggregate 7.5%	Bloomberg Aggregate -1.5%	MSCI Emg Mkt -20.1%	MSCI Emg Mkt 9.8%	ICE BofA High Yield 7.9%
Bloomberg Aggregate 1.8%	MSCI EAFE -4.9%	MSCI Emg Mkt -14.9%	MSCI EAFE 1.0%	Bloomberg Aggregate 3.5%	MSCI Emg Mkt -14.6%	Bloomberg Aggregate 8.7%	ICE BofA High Yield 6.2%	MSCI Emg Mkt -2.5%	Russell 2000 -20.4%	Bloomberg Aggregate 5.5%	Bloomberg Aggregate 4.4%
Spread between best and worst asset classes											
10.0%	18.1%	15.8%	20.3%	33.8%	14.6%	22.7%	14.8%	29.0%	9.3%	21.0%	16.8%

Source: DeMarche Associates, Inc.

- Global markets continued to move forward in the quarter, contributing to strong one-year returns. In this quarter, international stocks, both developed and emerging markets, outpaced the S&P 500 for the first time in quite a while.
- Bonds finished the quarter in strong fashion, responding positively to the Federal Reserve rate cut. Falling rates provide a tailwind to bond prices, and the Aggregate Index posted a 5.2% return for the quarter as interest rates along the yield curve fell.
- The U.S. dollar weakened against a trade weighted basket of currencies in the third quarter due to the Fed cutting rates. Interest rates in the U.S. have been relatively attractive compared to global rates, thereby boosting the strength of the dollar. That trend reversed in the third quarter.
- Large cap domestic stocks have been the winners for five of the last six time periods shown in the chart on the left, and have strung together some fairly robust returns. Between 2015 and 2019, each calendar year had a different winner, which was a time of rising interest rates. Over the near term, broad asset class diversification has not benefitted investors as the market leadership has been narrow.

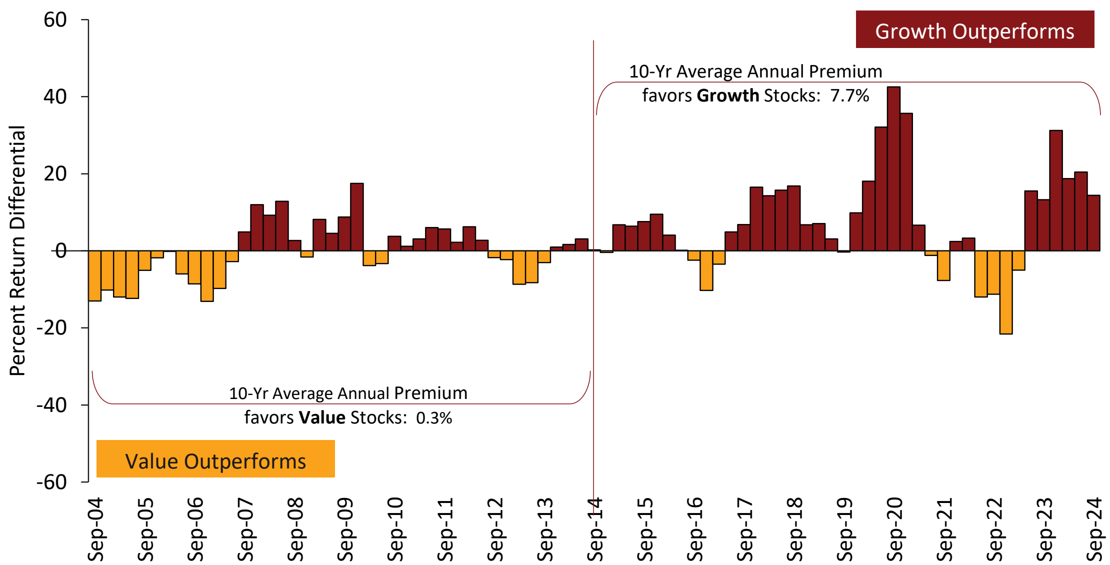
DeFact

The Federal Reserve cut the Fed funds rate on September 18th by 50 basis points. In recent history, the Fed began similar deeper cutting cycles three times, in January 2001, September 2007, and when the Covid-19 pandemic began to spread in March 2020, each time leading with a cut of 50 basis points. In each instance, soon after the cuts, the economy entered a recession. ~WSJ

INDEX	3rd Qtr	YTD	1-YEAR	3-YEAR	5-YEAR	10-YEAR
S&P 500	5.9	22.1	36.4	11.9	16.0	13.4
S&P Mid-Cap 400	6.9	13.5	26.8	7.5	11.8	10.3
S&P Small-Cap 600	10.1	9.3	25.9	4.0	10.2	10.0
Russell 1000	6.1	21.2	35.7	10.8	15.6	13.1
Russell 1000 Growth	3.2	24.5	42.2	12.0	19.7	16.5
Russell 1000 Value	9.4	16.7	27.8	9.0	10.7	9.2
Russell 2000	9.3	11.2	26.8	1.8	9.4	8.8
Russell 2000 Growth	8.4	13.2	27.7	-0.4	8.8	8.9
Russell 2000 Value	10.2	9.2	25.9	3.8	9.3	8.2

Notes: Data are presented as percent returns. All 3-, 5- and 10-year returns are annualized.

Growth Stocks (Russell 1000 Growth) Minus Value Stocks (Russell 1000 Value)
Rolling One Year Performance Differential



Source: DeMarche

- Growth stocks' leadership of the past reversed itself in the quarter. Large cap value stocks outperformed growth for the first time since the fourth quarter of 2022. The resurgence of value was led by the financial and industrials sectors, two of the largest three sectors in the Russell 1000 Value index.
- Small cap also outperformed large cap for the first time since the fourth quarter of 2023 and only for the second time in the past eight quarters. Falling interest rates tend to boost confidence in small cap stocks and benefit financial stocks, which are the largest weight in the Russell 2000 Index.
- As you can see, small cap value has held up compared to growth in the past number of years. Small cap growth has a large weight in health care stocks, which have performed poorly on a relative basis.
- Large cap value stocks have performed well this quarter but it has been a long time since value has consistently outperformed growth. The chart shows that in periods of economic weakness or uncertainty, value stocks make up ground on growth stocks. This is primarily because the earnings growth of growth stocks is harder to predict in an uncertain economy.

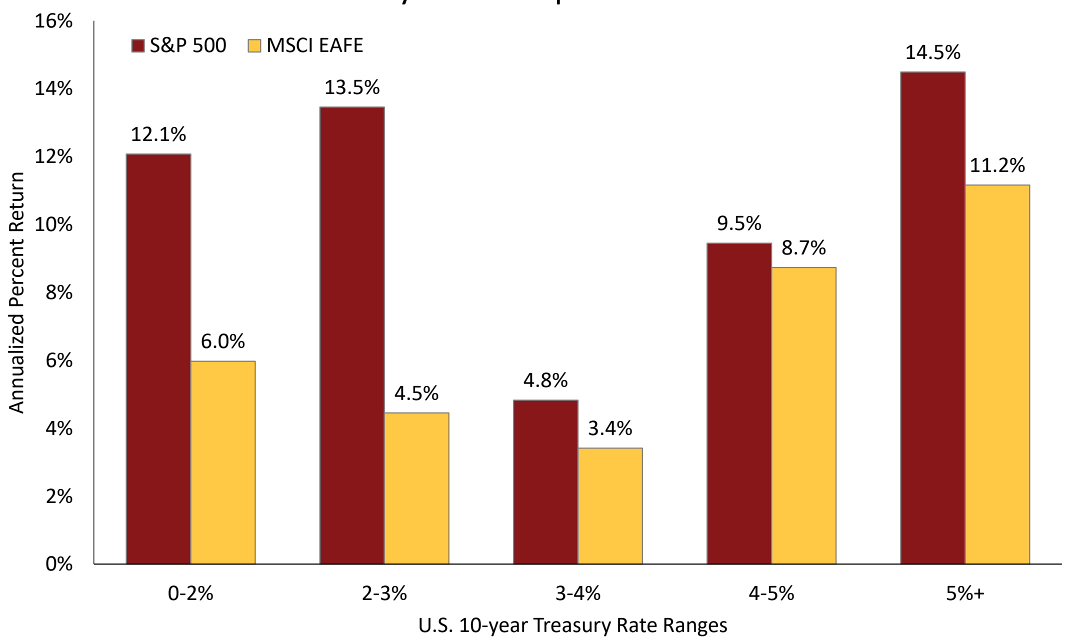
DeFact

We don't know who had this fact on their bingo card, but the Utility sector of the Russell 1000 is the best performing stock market sector year-to-date, passing information technology. After nine months utilities have outperformed 30.2% versus 29.8% respectively. Utilities posted a 16.9% return for the quarter, bolstered by rate cuts and the overall rotation into value stocks. ~JPMorgan, Standard and Poor's

INDEX	3rd Qtr	YTD	1-YEAR	3-YEAR	5-YEAR	10-YEAR
MSCI EAFE Local	0.8	12.0	17.5	7.9	8.8	7.4
MSCI EAFE USD	7.3	13.0	24.8	5.5	8.2	5.7
Growth	5.7	12.3	26.5	1.9	7.7	6.6
Value	8.9	13.8	23.1	8.9	8.3	4.6
MSCI All Country-ex US	8.1	14.2	25.4	4.1	7.6	5.2
MSCI AC Asia-ex Japan	10.4	21.2	28.9	0.6	6.6	5.4
MSCI Emerging Markets	8.7	16.9	26.1	0.4	5.7	4.0
MSCI EAFE Small Cap	10.5	11.1	23.5	-0.4	6.4	6.2
MSCI Japan	5.7	12.4	21.6	2.7	7.1	6.4
MSCI China	23.5	29.3	23.9	-5.6	0.8	3.4
MSCI Germany	10.7	16.9	32.1	4.0	7.6	4.7
MSCI France	7.7	5.5	16.4	5.9	8.4	6.7
MSCI UK	7.9	15.4	23.3	9.8	7.9	4.1

Notes: Data are presented as percent returns. All 3-, 5- and 10-year returns are annualized.

Equity Performance in Different Interest Rate Environments
January 1979 - September 2024



Source: FRED - Federal Reserve Bank of St. Louis, DeMarche

- International developed stocks outperformed the S&P 500 for the first time since first quarter 2023 and for only the second time in eight quarters. The weakening dollar certainly helped performance. When quoted in local currency, the MSCI EAFE returned 0.8%, and when translated into dollars, the return zoomed to 7.3% for the quarter.

- Emerging market stocks also performed well in the quarter. The weakening dollar certainly helped, but the performance of Chinese stocks were the primary driver of return. Chinese stocks rebounded strongly in the quarter and posted a 23.5% return. Over the longer term, performance has lagged other foreign markets due to the weakness in the Chinese stock market.

- The chart to the left shows that over time, international developed stocks tend to perform more competitively with domestic stocks when domestic interest rates are higher. The expectation is that higher interest rates provide a head wind to growth stocks more so than value stocks due to higher price multiples. Since international developed equities tilt toward value stocks in style, it seems reasonable to expect some competitive performance for international stocks going forward.

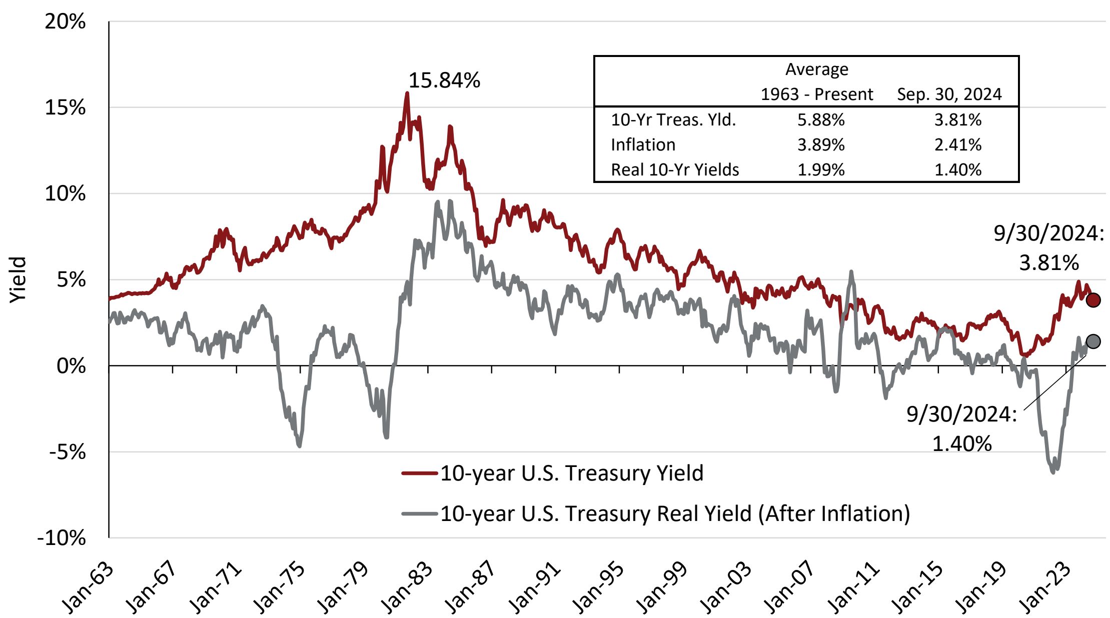
DeFact

China continues this quarter to hold global investors in thrall after late September’s sweeping series of monetary stimuli and measures to prop up their real estate and stock market. The hyperactive policy scramble kept going with China's central bank telling banks to lower mortgage rates for existing home loans before the end of October. The cumulative surge for the quarter has now wiped out both year-to-date and twelve-month losses. ~Reuters

INDEX	3rd Qtr	YTD	1-YEAR	3-YEAR	5-YEAR	10-YEAR
Bloomberg Aggregate	5.2	4.4	11.6	-1.4	0.3	1.8
Bloomberg 1-3 Gov Credit	3.0	4.4	7.2	1.5	1.7	1.6
Bloomberg Gov Credit Long	8.0	3.5	17.2	-6.2	-2.0	2.3
Bloomberg US TIPS	4.1	4.9	9.8	-0.6	2.6	2.5
ICE BofA Merrill Lynch High Yield	5.3	7.9	15.5	3.1	4.5	4.9
CSFB Leveraged Loan (bank loans)	2.0	6.6	9.6	6.3	5.6	4.9
Bloomberg Global Aggregate	7.0	3.6	12.0	-3.1	-0.8	0.6
JPM EmgMkt Bd Glbl Dvrsfd (hard)	6.5	8.0	18.5	-0.5	0.7	3.0

Notes: Data are presented as percent returns. All 3-, 5- and 10-year returns are annualized.

Inflation's Effect on U.S. 10-year Treasury Yields



Source: FRED - Federal Reserve Bank of St. Louis, DeMarche

- Bonds responded well to the Fed cutting interest rates. The Aggregate Index posted a 5.2% return for the quarter. During the first two quarters of 2024, the Aggregate performed poorly due to the belief the Fed would keep rates "higher for longer." Bonds are now poised to post two calendar years of positive performance, after posting negative returns for 2021 and 2022.
- While we saw investment grade bonds perform well in the quarter, high yield bonds also did well as higher coupon rates help returns. Credit spreads remain tight to Treasuries, signaling that concerns about corporate earnings are still a ways off in the future. Duration in the high yield index is shorter than the Aggregate Index, so the boost from falling interest rates did not provide the same tailwind to high yield (and bank loans) as it did to the Aggregate.
- The chart to the left shows that the real yield of the ten-year Treasury is back in positive territory after some time due to high inflation rates. Recall that real rates are nominal rates minus the rate of inflation. Now as expectations have moderated for economic growth and inflation, the interest rate of the ten-year Treasury is higher than the rate of inflation.

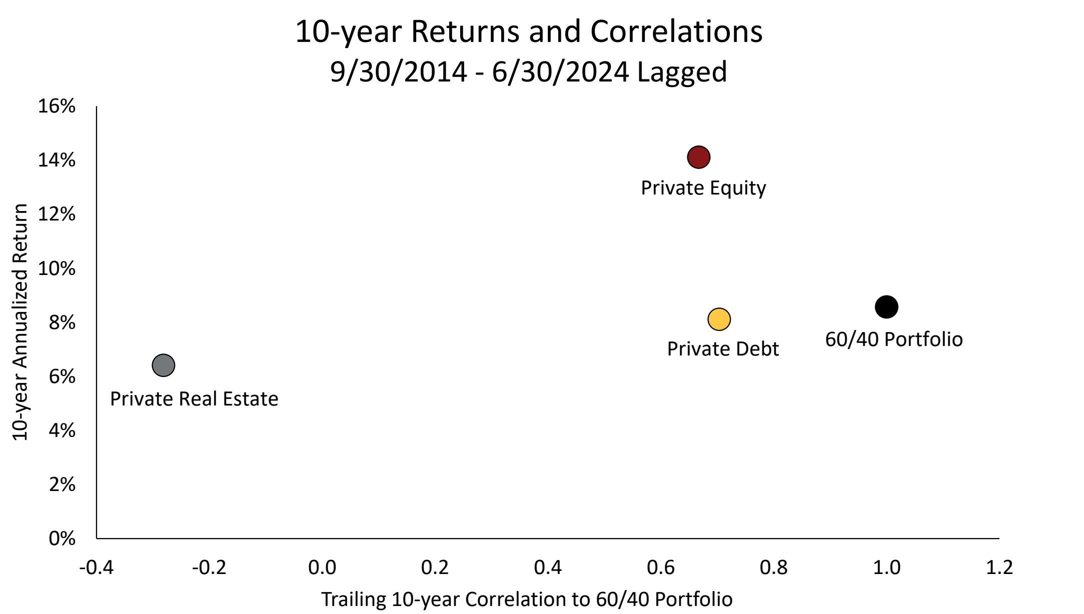
DeFact

During the quarter, the yield curve un-inverted between ten-year Treasuries and two-year Treasuries. Before September 6th, the yield curve had been inverted for 783 consecutive days, the longest such period in U.S. history. An inverted yield curve, where short-term rates are higher than long-term rates, has preceded every U.S. recession since the 1970s. However, the economy has not seen a recession so far. An un-inversion is seen as a positive sign that the Fed may have room to cut rates further. ~DeMarche

Less Liquid Strategies – Lagged One Quarter

INDEX	3rd Qtr	YTD	1-YEAR	3-YEAR	5-YEAR	10-YEAR
NCREIF ODCE	-0.4	-2.8	-9.3	1.9	3.2	6.4
NCREIF Property (Private RE)	-0.2	-1.1	-5.4	2.4	3.4	6.1
Residential	0.2	-0.8	-5.1	3.8	4.3	6.1
Industrial	0.2	0.4	-2.2	11.5	13.5	13.6
Office	-2.3	-6.0	-14.3	-8.1	-3.6	2.1
Retail	0.9	1.5	0.3	2.3	0.0	3.8
NCREIF Timberland	1.7	3.9	9.9	11.0	7.2	5.9
NCREIF Farmland	-0.2	0.5	2.5	6.8	5.9	6.9
HFR FOF Composite	0.4	4.6	8.5	2.1	4.8	3.5
Conservative	0.9	3.5	7.1	3.6	4.9	3.5
Diversified	0.6	4.9	8.4	2.8	5.1	3.6
Preqin Private Equity	1.4	1.4	6.1	6.4	15.0	13.8
Preqin Private Debt	1.7	1.7	8.8	9.1	9.5	8.0
Preqin Infrastructure	1.4	1.4	7.6	12.6	11.5	10.5

Notes: Data are presented as percent returns. All 3-, 5- and 10-year returns are annualized.
All data in the table above are as of previous quarter.



Source: Preqin, NCREIF, S&P, Bloomberg, DeMarche

- Real estate is showing some signs of stabilization. While real estate returns continue to post negative results, the magnitude of negative returns is smaller in the nearer term. It suggests that the worst of the downward repricing of real estate may be behind us. Lower interest rates certainly can help in this regard.
- Higher interest rates have impacted the returns of private credit in a positive way. The majority of private credit loans are floating rate and adjust upward when rates increase. Conversely, we should see yields slightly fall as interest rates begin to decline under the Fed's rate cutting regime.
- The chart to the left shows the diversification benefits of private assets relative to a balanced public securities portfolio. Private equity and private debt both have about a 0.6 correlation to the 60/40 balanced portfolio. Real estate returns shows a negative correlation to a balanced portfolio. We have seen over time that public assets reprice more quickly to higher highs and lower lows than private assets.

DeFact

Higher interest rates make private market acquisitions harder by raising the cost of capital in addition to putting downward pressure on price multiples. Banks are still pulling back from financing buyout activity so private credit managers are active in the space, even with higher rates. In other words, higher rates make it more difficult to pile on leverage, leading to fewer company exits from private equity funds. ~Bain

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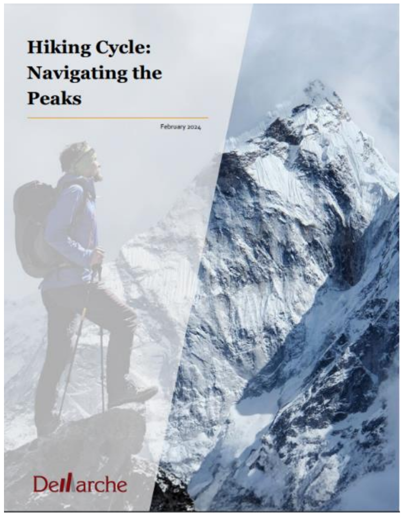
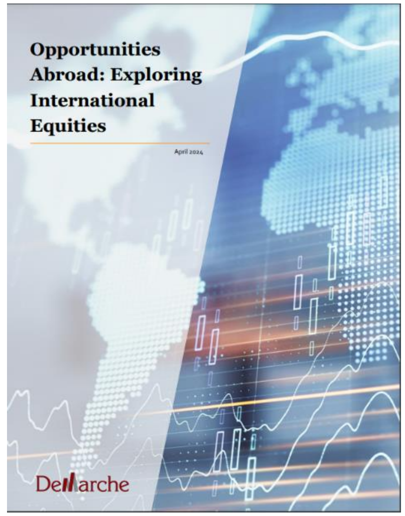
February



Hiking Cycle: Navigating the Peaks
Jim Dykstal, CFA; Matt Oakes; Luke Crawford

April



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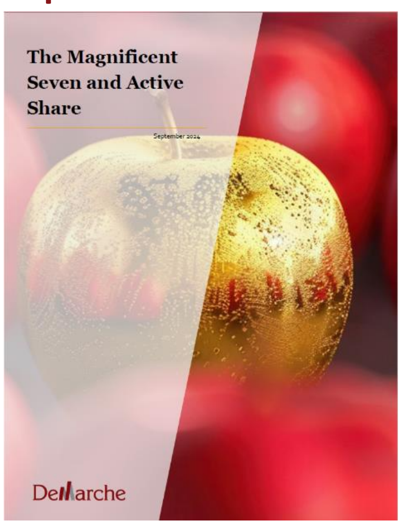
Peg VanWagoner; Hunter Swanson, CPA

September



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Don Lennard; Jansen McCabe

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