March Commentary 2024

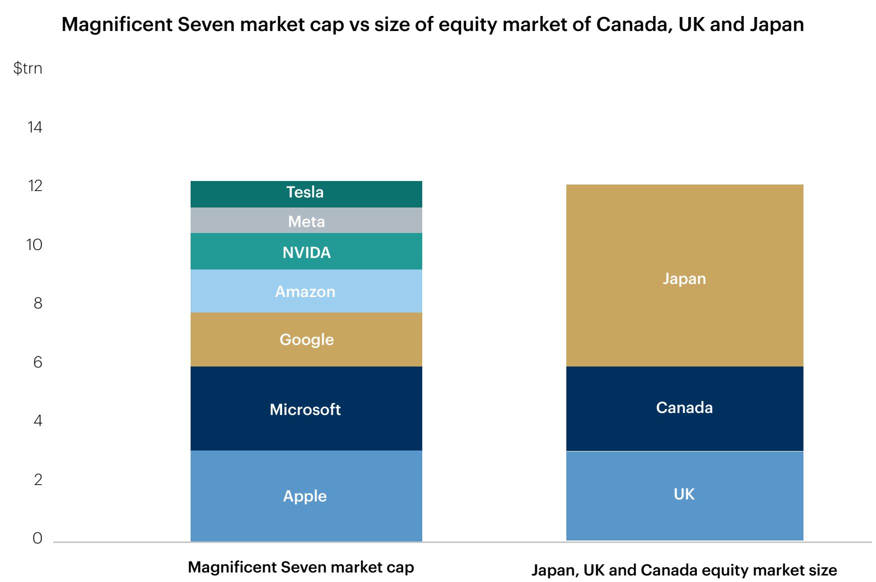
Wall Street, the media, and market signs sounds like another adventure novel from C.S. Lewis. All three tell their own unique story, but which one tells the truth about our economic future?

Who represents Wall Street?

Many players represent the wealthiest companies and people in the world portrayed through stock exchanges, investment banking firms, commercial banks, brokerages, broker-dealers, financial services, and underwriting firms. Examples of these include the New York Stock Exchange (NYSE), American Stock Exchange (AMEX), NASDAQ, Goldman Sachs, Morgan Stanley, Bank of America, JP Morgan Chase, Wells Fargo, Raymond James, UBS, and the like. Their objective is to make money for themselves and utilize whatever tools are necessary for their success. The more services and products they sell, the more successful Wall Street firms become, regardless of the impact it has on the customer.

Wall Street is guiding investors to invest more and more in equities, especially the S&P 500, the NASDAQ, and the so-called "Magnificent Seven" (Apple, Amazon, Alphabet, Meta, Microsoft, Tesla, and Nvidia). It's hard to blame Wall Street. Who doesn't want to talk about the innovative technologies that are changing our daily lives? Wall Street claims that these stocks are fairly priced, citing 12-month forward sales and earnings analysis, forward price-to-earnings (P/E) ratio, and 10% discounted cash flow analysis, to name a few of their methodologies.

The Mag Seven's market value is greater than all individual country stock markets globally except the U.S.

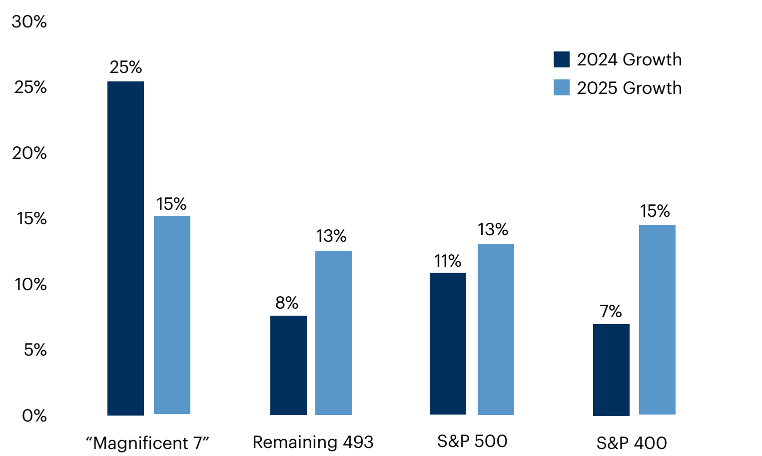


Source: Bloomberg/Apollo Chief Economist

Wall Street loves to publish data that uses cherry-picked facts to support its narrative, like these examples from J.P. Morgan Wealth Management and Goldman Sachs. J.P. Morgan and Goldman are trying to boost consensus surrounding the growth of the Mag Seven, but they provide no relative dataset of past objectiveness. These out-of-context stats are only meant to tug on investors' behavioral need to not miss out:

The Magnificent 7 is expected to continue to outpace the earnings growth of the broader market

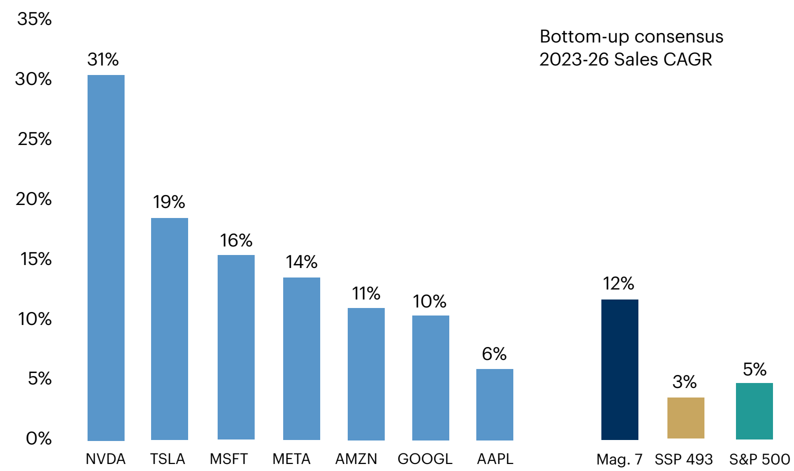
Consensus expectations for YoY earnings per-share growth



Source: FactSet. Data as of February 8, 2024.

Consensus expects the 7 to grow sales at 4x the rate of S&P 493

as of February 1, 2024

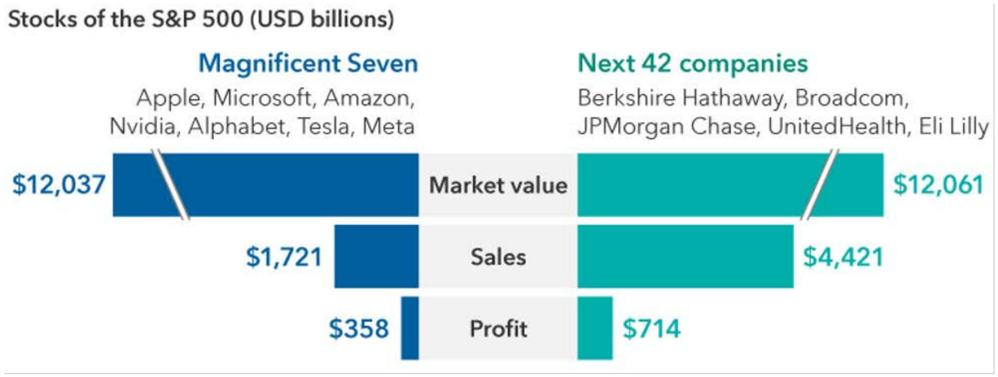


Source: Factset, Goldman Sachs Global Investment Research

The reality is the Mag Seven has a forward P/E of 31, the remaining 493 stocks have a forward P/E of 19, and the broader index of the S&P 500 has an expected P/E of 20. These facts tell us that the Mag Seven is priced for perfection. Investors are now paying 50% more for owning the Mag Seven. Robert Shiller's Excess CAPE Yield is expecting long-term returns to be lackluster and possibly negative in the future.

According to Capital Group's David Polak, the Mag Seven has a market cap of around $12 trillion. Looking further into the market, the sales and profitability of the next $12 trillion in market cap are represented by 42 companies.

Can the Mag Seven continue their dominance?



Source: Capital Group, LSEG. Next 42 companies represent stocks following the Magnificent Seven, ranked by market capitalization, with the above stocks topping the list. Sales are the net sales (or revenues) of the relevant item reported in the last 12 months. Profit is represented by the trailing 12-month operating profit. As of December 31, 2023.

As always, investors vote with their dollars, while advisors need to weigh the facts and advise prudently. Markets can always go higher, and for longer, than anyone expects, and we believe investors need to have a defined plan when things turn the other way.

The Media

Depending on where you get your information, there are degrees of bias. Most media channels unfortunately have become political and continually press their agendas. The media remains in the throes of fear and greed to gain our attention. It plays with people's emotions and behavioral biases, such as:

- Fear of missing out (FOMO)
- Loss aversion
- Herding mentality
- Narrative fallacy
- Hindsight bias
- Confirmation bias

The media's desire is to keep people watching, reading, and listening for as long as possible to increase their ratings and enhance their ability to charge more for advertising. Today's media is here to take care of their best interests before that of their viewers. Is it just about how much more they can squeeze out financially while utilizing almost any means necessary to achieve their objectives? We hope not.

As markets swing from bullish to bearish and back again, pay particular attention to the number of similar voices the media spotlights. For example, when things are bullish, the media will highlight more and more guests and points of view that are fueling the greed factor and a very limited number of vantage points that are to the contrary, and vice versa when markets are bearish.

Market Signs

Billionaire investor Stanley Druckenmiller believes that the best market indicators are within the markets themselves.

With the media and Wall Street spotlighting the U.S. markets hitting all-time highs, what is the truth? Does the market really show that even more highs are likely going forward?

Market Trends

- Multiple market trends are signaling heavy winds ahead:
  - Transportation stocks, Lumber/Gold, Copper/Gold, Stocks/Gold, Oil/Gold, and Small/Large cap are all experiencing negative trends
- The S&P 500 and NASDAQ are both trending higher

In the first part of 2024, several negative sectors and signs are developing:

- Small-cap vs large-cap equities: -5.4%
- Microcaps: -5.3%
- Transportation stocks: -3.15%
- Regional banks: -6.69%
- Home builders: -3.48%
- High beta: -3.98%
- Retail: -6.36%
- Semiconductors: -7.77%
- Metals and mining: -5.39%
- PPI (manufacturing): -3.32%

Bigger picture revealed:

- Leading Economic Indicators (LEI) have been down for 21 consecutive months
- Value on a relative basis is down 21% over the past 12 months
- Small caps are lagging large caps by 13.5% over the past 12 months
- International vs. domestic equities are at all-time lows on a relative basis
- Delinquencies for credit cards and auto loans are at 2008 credit-crisis levels
- ISM services have been trending down for over two years
- Labor market shows a significant increase in part-time jobs
- Continued growth in government jobs (which historically contributes to the slowing of our economy)
- Growth has been slowing along with inflation for around two years
- 80% of the loans in our $3 trillion commercial real estate market reside in U.S. regional banks and they are expecting to drop around 40% in the coming quarters

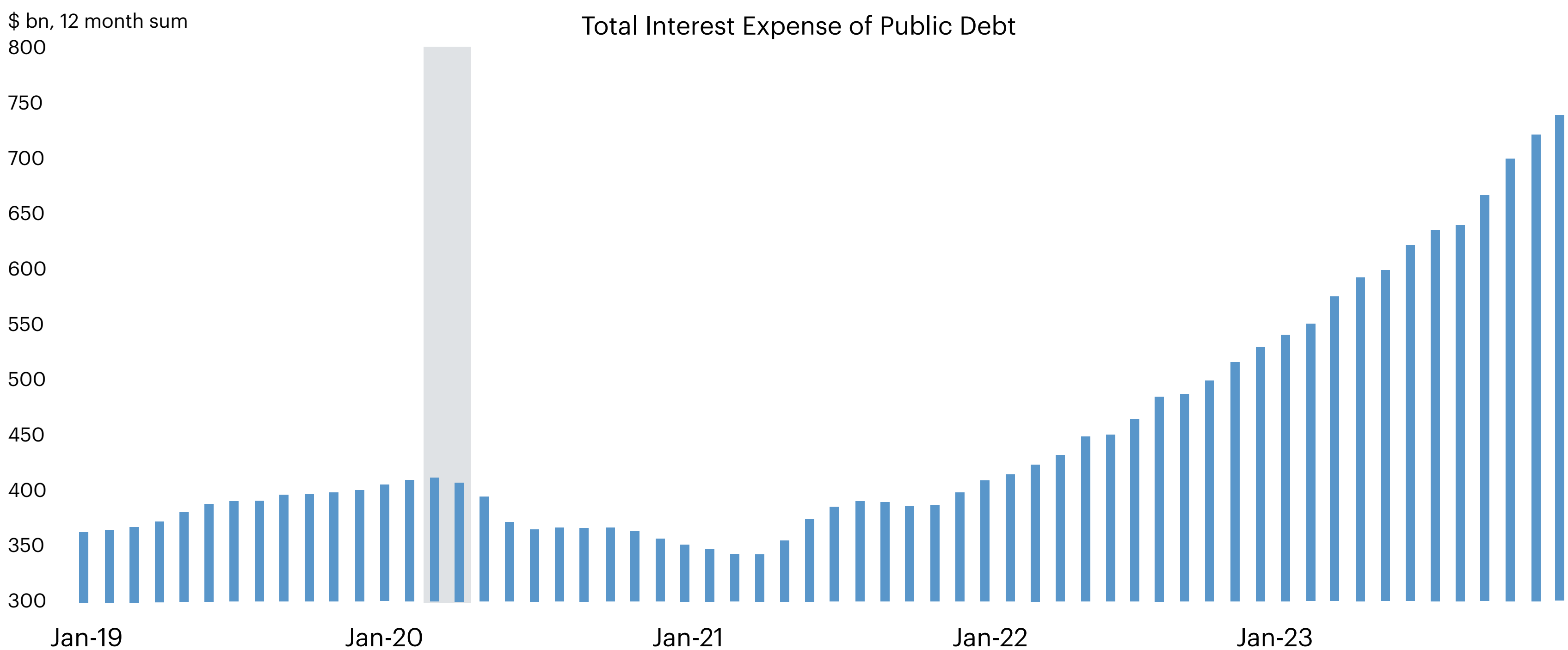
Valuation Methodologies

U.S. markets are experiencing significantly higher valuations no matter which methodology we examine:

- Cyclically adjusted price to earnings is 102% above average
- Q Ratio is 105% above average
- S&P 500 composite from its regression is 142% above average
- The market cap to GDP per country is 180%, and the U.S. is the highest in the world
- U.S. vs global equities is three standard deviations greater than the Nifty Fifty of the 1960s and one standard deviation greater than the Internet bubble of 2000

As credit continues to contract, the Federal Reserve focuses on lowering rates in the coming quarters, and maintenance of our national debts becomes massively restrictive, the underlying market signs, sectors, and fundamentals are clear: There are rough seas ahead for the global economy.

Government Debt Servicing costs have doubled since 2021



Source: Apollo Global

Summary

Points of awareness:

- The U.S. stock market is the most concentrated it has been since before the 1929 market crash
- U.S. vs. global equities is three standard deviations greater than the Nifty Fifty of the 1960s, and one standard deviation over the Internet bubble of 2000
- The S&P 500 is priced for perfection in the long-term
- The Federal Reserve is determined to lower Inflation to two percent. If you believe in not fighting the Fed, then the Fed will become dovish and lower rates sooner rather than later.

Our current economic and market conditions are not quite as rosy as what Wall Street, which is looking after its own interests, might suggest. That's why we recommend you have a heartfelt discussion with your advisor to devise a customized plan for your finances.

If you have any questions, please reach out.

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