NBC | SECURITIES

INVESTMENT STRATEGY STATEMENT | August 2, 2024

Equity Market Rotation

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Performance Review & Outlook

Disinflation Trend Continues
The June CPI reading showed consumer prices fell -0.1% m/m and up 3.0% y/y, giving us three consecutive months of lower y/y readings. This was the first negative m/m reading we've had since May 2020.

Labor Markets Slightly Cooling
Jobless claims and the job openings to job seekers ratio are showing some slack building in the labor markets. We believe this is a cooling of a previously overheated labor market, but we'll continue to monitor for anything deeper.

Equity Markets Continued to Advance in July
The S&P 500 was higher by 1% in July and is higher by 16.7% so far this year, but we also saw an increase in volatility.

Fixed Income Market Rally
Yields fell in July, with the 10-year closing the month at 4.03%—down over 30bps for the month and 70bps since the recent peak in late April.

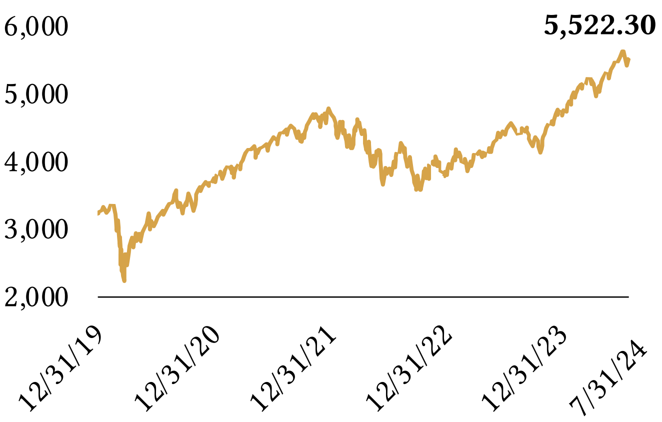
Significant Equity Rotation
Small caps, value stocks and interest rate sensitive sectors all broadly outperformed their large cap growth counterparts following the June CPI report.

Outlook Largely Intact
Although data has been mixed so far in 2024, our outlook on the key themes driving equity and fixed income markets remains intact.

Equity Market Overview

Equity markets posted another monthly gain in July, although we also saw an increase in volatility and some interesting rotations under the surface. The S&P 500 had a total return of 1.2% for the month, bringing the year-to-date gain to 16.7%. In terms of the cadence of returns during the month, the index peaked at a record high of 5,667 on July 16th, representing a gain of 3.8% over the June 30th closing value of 5,460. From there, the index fell -4.7% to an intramonth low of 5,399 on July 25th, before rallying the final week to close at 5,522.

S&P 500 Price Index (12/31/19 -7/31/24)



12-Month Percentage Change of Indices

Index (Local Currency)	Level	July	YTD	12 Month
S&P 500	5,522.3	1.2%	16.7%	22.1%
Dow Industrials (DJIA)	40,842.79	4.5%	9.5%	17.2%
Nasdaq	17,599.4	-0.7%	17.7%	23.7%
Russell 2000	2,254.484	10.2%	12.1%	14.2%
US 2yr Treasury	4.2575	-7.8%	0.2%	6.3%
US 10yr Treasury	4.0296	-4.1%	3.9%	17.8%
Gold (NY Spot $/oz)	2,447.6	9.8%	18.6%	23.0%
Silver (NY Spot $/oz)	29.0065	16.2%	21.9%	15.8%
Copper ($/metric ton)	9,102.28	3.8%	7.5%	6.1%
Oil (WTI Spot/bbl)	77.91	-6.3%	8.7%	1.5%
Oil (Brent Spot/bbl)	80.72	-7.7%	4.8%	1.5%
Natural Gas ($/mmBtu)	2.036	15.5%	-19.0%	-15.5%

Data as of July 31, 2024
Source: FactSet/Bloomberg

Moving to sector returns, the two biggest gainers in July were Real Estate (+7%) and Utilities (+7%), marking a sharp reversal from June as falling US Treasury yields helped bolster rate sensitive sectors. In fact, Real Estate had been the lone negative sector on the year prior to July, and now is higher by nearly 5%. For Utilities, the gain in July moves the year-to-date gain up to 16.6%, good for fourth best of the 11 GICS sectors.

+7%
Real Estate

+7%
Utilities

-4%
Comm. Services

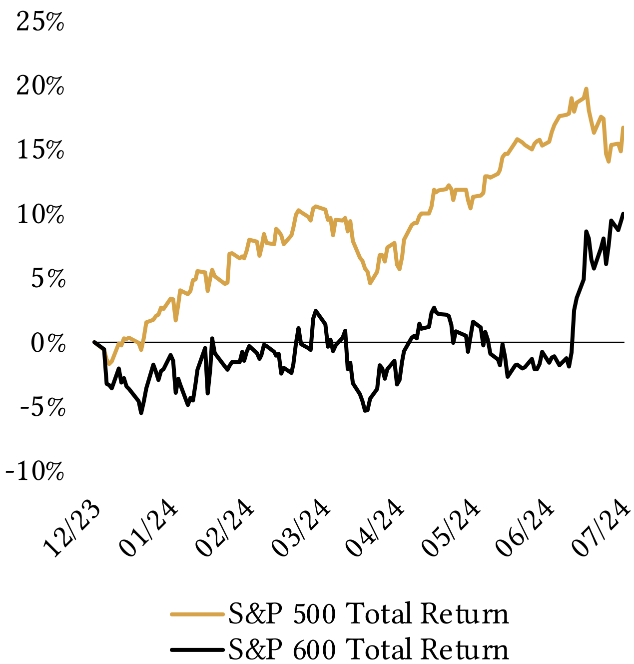
-2%
Technology

10 Year US Treasury Yields

On the downside in July, Communication Services (-4%) and Technology (-2%) were the worst performing sectors, as the rotation away from large cap growth into more rate sensitive sectors led to investors selling shares in each. Even with the declines, each sector remains higher by over 20% for the year and are the two best performers.

Speaking of reversals, last month we discussed the large divergence between the S&P 500, which is mainly driven by large cap companies, and the S&P 600 Small Cap Index. Through June, the S&P 500 was outperforming the S&P 600 by 16% as investors poured into the so called "Magnificent Seven" stocks at the expense of small cap and value stocks. July was a different story. While the S&P 500 did post a positive return of 1.2% for the month, the S&P 600 soared higher by 10.8%, narrowing the large cap year-to-date advantage to 6.7%. In addition to the sector and size rotations mentioned above, we also saw a clear preference for value stocks as the S&P 500 Value Index was higher by nearly 5%.

Total Return Since 12/23



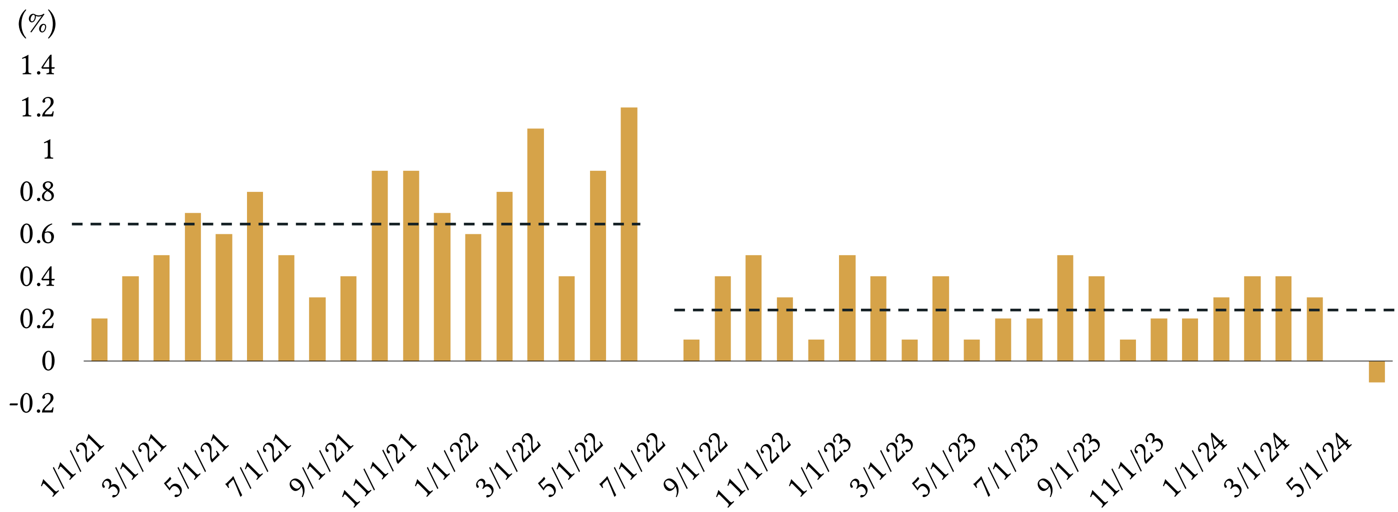
What brought about these reversals? It almost all took place following the June CPI report that was released on July 11th, showing consumer prices actually fell as compared to May, further supporting the case for Fed rate cuts this year and leading the yield curve to shift lower. Lower borrowing costs should support smaller companies that are more reliant on floating rate debt to fund their operations and lower yields offer less competition for higher yielding equity securities. We'll see if this trend continues.

Lower rates coupled with an economy that continues to grow should be supportive of equity valuations overall.

Fixed Income Market Overview

July 2024 proved to continue to be an interesting month for both economic news and interest rate markets as the Federal Reserve continued its "data driven" approach to monetary policy. But July also proved to be different in that for the first time, it seems that we saw a tangible shift not only in economic data, but also the Federal Reserve's willingness to begin the conversation about rate cuts. We saw strong economic data move to the forefront this month, starting with CPI coming in at 3.0% m/m, and then ending the month with second quarter GDP coming in at 2.8% annualized growth rate—a stronger number than forecasted. Jobs numbers throughout the month also continued to show signs of cooling but remained strong overall.

M/M Change in CPI



We closed this month with the July FOMC meeting, a fitting ending to a great month of economic data.

> *If there was one buzz word that seems to be going around financial news surrounding this month's FOMC meeting, it was "dual mandate."*

What is a dual mandate? The dual mandate is the Federal Reserve's mandate for monetary policy. An economy in which people who want to work either have a job or are likely to find one fairly quickly, and in which the broad measure of the price of goods and services purchased by consumers is stable. Achieving this goal would be exactly what the Federal Reserve has been pushing for the better part of the past two years—a soft landing.

NBCS Asset Management has hinted for several months that there was a possibility that the Federal Reserve could cut interest rates in September, and given the tone from this month's FOMC meeting, a September rate cut seems very possible. Fed Chairman Powell stated post FOMC meeting that "The broad sense of the committee is that the economy is moving closer to the point at which it would be appropriate to reduce our policy rate." In these comments he highlighted the strong economic data and reductions in overall inflation data seen this month in combination with a slightly cooler but still strong labor market. "The second quarter inflation readings have added to our confidence and more good data would further strengthen that confidence."

Powell stopped short of saying there will definitively be a rate cut in September, but barring an uptick in inflation, a rate cut now seems very likely as the CME's Fed Watch tool closed the month forecasting a 100% probability of a rate cut at the Federal Reserve's September FOMC meeting. With cooling in the labor market, and inflation goals continuing to move into "better balance," it seems the Fed is indeed achieving its policy of dual mandate. And increasingly, they may just get the soft landing they have been working towards after all.

Economic Overview

Key Economic Indicators

JOB MARKET

Job Gains
The headline jobs number was an increase of 206,000. Through June, the US has had positive job growth for 42 consecutive months—the fifth longest streak in history.

Unemployment Rate & Jobless Claims
The unemployment rate increased to 4.1% in June compared to 4.0% in May. Jobless claims have increased over the last few months, with the four-week moving average increasing to 238,000 from 205,000 at the end of last year. We believe this is a cooling of a previously overheated labor market, but we'll continue to monitor for anything deeper.

HOUSING MARKET

House Prices
The Case-Schiller 20-City Composite price index was higher by 6.8% over the last 12 months.

Existing Home Sales & Inventory
The inventory of existing homes for sale is 36.7% higher than this time last year, but still down -32.4% compared to levels seen between April 2017 and 2019. Existing home sales continue to hover near 30-year lows. Both measures continue to be impacted by higher rates causing a lock-in effect and keeping home prices elevated.

PERSONAL INCOME & SPENDING

Retail Sales
Retail sales were flat as compared to May and up 2.3% from a year ago. This is a bit slower than the pace in 2023 (up 4.0%), consistent with an economy that is growing at a slower pace.

Personal Income & Spending
Personal income came in slightly lower than expected, up 0.2% versus May. Retail spending came in as anticipated, rising 0.3% m/m.

Economic Overview

Key Economic Indicators

ECONOMIC GROWTH

GDP Growth
The Bureau of Economic Analysis reported that real GDP increased at an annual rate of 2.8% in the second quarter of 2024. This growth primarily reflects increases in consumer spending, residential fixed investment, nonresidential fixed investment, state and local government spending, and private inventory investment partially offset by a decrease in higher imports.

GDPNow Forecast
The (very early) read on Atlanta Fed's GDPNow tool is forecasting third quarter GDP growth of 2.55%. This would represent slightly slower growth versus the second quarter, but still above trend.

INFLATION

CPI
The June consumer price index was down -0.1% m/m and higher by 3.0% y/y, down from 0.0% and 3.3% in May, respectively. Importantly, we saw a deceleration in the shelter component, which has been the biggest and most persistent contributor to higher inflation over the last 2 years.

PCE
The June PCE price index increased 2.5% y/y, down from 2.6% in May and down from the recent peak of 7.0% in June 2022. The Core PCE price index increased 2.6% y/y, the same as May and down from the recent peak of 5.4% in February 2022. This remains the lowest core reading since March 2021.

Conclusion

July continued the flow of mixed but overall positive economic data. While we believe the slowing in consumer spending growth and the labor market are further evidence of the economy continuing to normalize, we'll continue to monitor the incoming data to see if it becomes anything more concerning. Interestingly, during Jerome Powell's press conference following the July FOMC meeting, he said the Fed was currently of the same mindset. The June CPI report showed consumer prices fell as compared to May, and we've now had 3 consecutive months of lower year-over-year readings. Importantly, we have now seen a few months of decelerating readings on the shelter component, which has been the biggest and most persistent contributor to higher inflation over the last two years. The economy grew at an annualized pace of 2.1% for the first half of the year, although at a slower pace than 2023. We believe this will lead to continued growth in operating earnings, the fundamental driver of equity markets. Lastly, we believe the rate hiking cycle for the Federal Reserve is over, and the next change they make will be a cut, possibly in September. Until this narrative changes, we continue to have a positive outlook for common stocks and fixed income.

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Disclosures