PACIFIC GLOBAL

Investment Update • April 2024

All the major indices extended gains during the quarter on the strength of the labor market, optimism over the burgeoning field of artificial intelligence (AI) and the outlook for interest rate cuts in 2024. The prospect for a soft economic landing continued; to some extent, though, optimism for interest rate cuts seemed to run ahead of the economic data. Year-over-year, the Consumer Price Index (CPI) edged up from 3.4% in December to 3.5% while the core CPI slowed from 3.9% to 3.8%. The Producer Price Index (PPI) rose year-over-year from 1.0% in December to 2.1% while the core PPI rose from 1.8% to 2.4%. Even so, consumer sentiment rose to the highest level since July 2021 on expectations for lower inflation. For the quarter, the Nasdaq added 9.11% to the 43.42% gain in 2023. The S&P 500® Index added 10.16% to 2023's 24.23% gain; the Dow Jones Industrial Average added 5.62% and the Russell 2000® Index added 4.81%.

Federal Reserve Chair Powell, following the mid-March meeting, which left the fed funds rate unchanged, downplayed the somewhat disappointing CPI and PPI updates. He clarified that the latest data "haven't really changed the overall story, which is that of inflation moving down, gradually on a sometimes-bumpy road towards 2%." He added that "We don't really know if this is a bump on the road or something more. We'll find out," but "we're not going to overreact . . . to these data, nor are going to ignore them." The emerging message suggests that the strong economy will permit the Fed to exercise patience in initiating rate cuts.

Enthusiasm for AI drove much of the market momentum the quarter; the S&P and the Nasdaq, home to many computer chip makers, rose 9 weeks, and 8 weeks, respectively during the quarter. The job market expansion continued with the addition of 829,000 jobs, a 30% improvement over the prior quarter's 637,000. The unemployment rate rose from 3.7% to 3.8%. The March 4.1% wage increase, below December's 4.3%, continued to outpace the CPI.

Prices for West Texas Intermediate rose from $71.89 per barrel in late December to almost $84.00 pb. Concerns including the continuing production cuts by OPEC+ countries, Middle East tensions related to the Israeli/Gaza conflict and threats to shipping disruptions in the Red Sea drove prices higher. Recent events in the Middle East have not significantly impacted prices largely due to the moderating effect of U.S. shale production. Global supply and demand remained relatively balanced.

The ISM Services Index rose slightly from 50.6% in September to 51.4%; the ISM Manufacturing Index rose from 47.4% to 50.3% to record the first month of expansion after 16 months of contraction. Consumer spending rose modestly during the quarter, including a robust 0.7% increase in retail spending in March.

Equity Investment Review

Market Review • March 28, 2024		
INDEX [1]	CLOSE	YTD PRICE RETURN
Dow Jones Industrial Average	39, 807.37	5.62%
S&P 500® Index	5,254.35	10.16%
Nasdaq	16,379.46	9.11%
Russell 2000® Index (small cap)	2,124.55	4.81%
	3/28/24	12/29/23
10-Year T-Note Yield	4.20%	3.88%

Data: Bloomberg; Federal Reserve.

The four major indices surged ahead to add to gains from the prior quarter: for the first time in eight quarters, the **S&P 500® Index** (10.16%) outperformed followed by the technology-heavy **Nasdaq** (9.11%) and **Dow Jones Industrial Average** (5.62%) the **Russell 2000® Index** (4.81%).

Ten of the eleven market sectors in the S&P 500® Index rose during the quarter. Based on total return, *Communication Services* (15.83%), *Energy* (13.68%), *Information Technology* (12.72%), *Financials* (12.46%) and *Industrials* (10.98%) outperformed the Index while *Health Care* (8.85%), *Consumer Staples* (7.54%) and *Consumer Discretionary* (4.99%) also advanced. *Real Estate* (-0.55%) was the lone sector to decline. The **Magnificent Seven** technology giants **were prominent amongst the Index's best performers**.

Fixed Income Investment Review

Treasury yields rose across all maturities. The yield on the 3-month U.S. Treasury Bill rose 6 basis points (bps) to 5.46%. Market forces drove more notable increases on intermediate and longer-maturity bonds: the yield on the 2-year U.S. Treasury Note rose 36 bps to 4.59%; similarly, the yield on the 10-year U.S. Treasury Note, which ranged between 3.87% and 4.34% during the quarter, rose 32 bps to close at 4.20%. The yield on the 30-year Bond rose 31 bps to 4.34%. Given our expectation for interest rates to remain "higher for longer," we continued to purchase intermediate-term bonds to obtain attractive interest yield while minimizing duration risk.

Looking Ahead

Continuing speculation about inflation and the Fed's interest rate announcements will dominate sentiment. Several Fed spokespersons have voiced a "no rush to cut" sentiment which, if supported by upcoming economic data, may well reset the anticipated timing of rates cuts until late 2024.

The Fed's March Summary of Economic Projections (SEP) provides the latest roadmap: **The projection for core PCE, the Fed's preferred inflation measure, rose to 2.6% (up from December's 2.4% forecast) in 2024 with subsequent declines to 2.2% (up from 2.1%) in 2025 before achieving the all-important 2.0% target in 2025.** The forecast anticipates the fed funds range between 4.6%–5.1% (again, slight increases compared to the December forecasts). Encouragingly, the SEP maintained a 4.6% forecast for the fed funds rate at year-end 2024. Thus, **several rate cuts, from the current 5.25%–5.5% rate, remain in the 2024 forecast**. The 2025 and 2026 forecasts were revised upward to 3.9% for 2025, and 3.1% for 2026.

Several factors impact the economic outlook. The number of job creations remains impressive even as signs of cooling consumer sentiment emerge. The escalation in oil prices will undoubtedly impact inflation, especially if tensions in the Middle East escalate. Still, the data suggest that GDP growth will remain in the 2.1%–2.0% range for 2024–2026 with unemployment increasing modestly to 4.0%–4.1% during the period. Thus, the Fed's expectation for a soft economic landing endures.

The latest University of Michigan consumer sentiment survey fell as the views on current conditions and expectations fell from multi-year highs. The upcoming elections factored into sentiment as many consumers noted that "the outcome could have a substantial impact on the trajectory of the economy."

A "higher-for-longer" outlook would likely delay a revenue boost for banks falling rates improve margins. Elevated valuations for some technology stocks, including AI stocks, seem unsustainable given increased competition by other chip makers and buyer cost consciousness. Also, the timelines for AI product applications, and the resulting valuation rewards, may extend far beyond investors' expectations. Many anticipate that, while several of the market-dominating **Magnificent Seven** stocks may continue to advance, others may lose momentum. If so, the indices may provide only modest returns this year; other companies, including those not participating in the recent *Technology* advance, may offer more attractive growth potential. The outlook for volatility in both equities and interest rates remains high as investors react to Fed commentaries, economic reports and geopolitical events.

[1]The Dow Jones Industrial Average is an unmanaged, price weighted measure of 30 US stocks selected by the Averages Committee to represent the performance of all US stocks outside the Transportation and Utilities sectors. The S&P 500® Index, an unmanaged, market-weighted index, measures the large cap segment of the US equities market. The Index covers approximately 75% of the US equities market and includes 500 leading companies in leading industries of the US economy. The Nasdaq Composite is an unmanaged, market-weighted measure of all domestic and international common stocks listed on The Nasdaq Stock Market. The Russell 2000® Index is an unmanaged, market-weighted measure of the stocks of the 2,000 smallest publicly traded companies of the Russell 3000® Index.