PENDLETON STREET
BUSINESS ADVISORS

5 Things We're Watching in 2024:

Our U.S. Equity & Bond Market Outlook

January 11, 2024

Index Returns	4th Quarter	Year-To-Date	Trailing Twelve Months
S&P 500 US Large Cap Stock Index	11.7%	0.32%	26.29%
Russell 2000 Small Cap Stock Index	11.93%	-4.24%	3.47%
MSCI All Country World Ex-US Stock Index	9.75%	-1.50%	15.46%
Barclays Capital US Aggregate Bond Index	1.42%	-0.80%	5.39%
US Core Consumer Price Index – (Inflation)	3.1%	3.2%	3.4%

As we step into 2024, the financial markets are poised for a year of potential twists and turns—which are to be expected. To provide you with a comprehensive outlook, we've gathered insights from many sources; from Wall Street Banks, the US Federal Reserve, to our own personal observations and study of market data that's compiled for our Investment Committee. As we begin a new year with this commentary, we'll delve into five critical themes that we believe will shape the equity and bond markets this year, with a detailed look at what's happening in each area. Let's dive in!

1. Economic Growth Acceleration

What's Happening?

2024 marks a significant milestone in the post-pandemic recovery. Both Wall Street, and our clients on Main Street (business owners) both anticipate robust economic growth. Consumer spending continues to be powered by a strong job market. As of the Jobs report released by the Department of Commerce, the unemployment rate stands at 3.7%. Infrastructure spending and a resurgence in manufacturing are further bolstering the economy.

Why It Matters:

Economic growth typically translates into increased corporate earnings, which can drive stock market gains. However, the rapid economic expansion also raises concerns about inflation. Central banks may consider tightening monetary policy to curb inflation, potentially affecting market dynamics. I think Edward Yardeni of Yardeni Research puts it best:

> *"The stock and bond rallies since late October might have discounted an easier monetary policy this year than Fed officials are likely to deliver. That's even if the inflation rate drops*

down to their 2.0% target ahead of schedule. They will continue to be data dependent. As long as the unemployment rate remains below 4.0%, they are likely to hold off on easing, in our opinion. That's because their worst nightmare would be a rebound in inflation."

2. Inflation Dynamics

What's Happening?

Inflation remains a focal point in 2024. Inflation pressures are beginning to ease due to massive action taken by the FOMC to raise interest rates in 2022. We began to see this meaningfully take hold in 2023, and the results have been positive. But as in the comment above, the strong labor market may be continuing to put upward pressure on consumer prices, making it more difficult to lower interest rates AND maintain control over rising costs due to inflation.

Why It Matters:

Investors are closely monitoring inflation trends. High and persistent inflation can erode purchasing power and lead to higher interest rates, impacting bond and equity markets alike. How central banks navigate these challenges will be crucial.

3. Technology and Innovation

What's Happening?

The technology sector continues to be a driving force in 2024. Innovations in artificial intelligence, 5G technology, and clean energy solutions are at the forefront. Companies across various sectors are harnessing technology for efficiency and growth. We also think "infrastructure spending" will take on a whole new look as we think about the hardware and real estate needed to power and house internet/cloud infrastructure dedicated to AI tools. We are in the early stages of massive spending to build capacity and capability in these areas. We have exposure to these trends in our technology holdings—and we intend to keep this as a centerpiece of portfolios.

Why It Matters:

Investors should focus on opportunities in tech-driven sectors such as electric vehicles, cloud computing, and biotechnology. These innovations have the potential to revolutionize industries, offering exciting investment prospects. We have exposure to these trends in our technology holdings—and we intend to keep this as a centerpiece of portfolios.

> "*Worldwide end-user spending on public cloud services is forecast to grow 20.4% to total $678.8 billion in 2024, up from $563.6 billion in 2023, according to the latest forecast from Gartner, Inc. Cloud has become essentially indispensable*." --Sid Nag, Gartner Forecasts

4. Geopolitical Risks

What's Happening?

Geopolitical tensions persist in 2024, impacting trade, supply chains, and global stability. Ongoing disputes, including trade conflicts and territorial disputes, create uncertainty for businesses and investors alike. The Israeli/Hamas conflict is far from over. The Ukraine/Russia conflict also continues. It's also a Presidential election year in the United States—which will continue to bring partisan paralysis to Congress, as well as the electoral process (again). There's no end in sight to the paralysis.

Why It Matters:

Geopolitical events can lead to market volatility—due to the news driven nature of market declines during these periods. Markets tend to shrug off the sudden downturns with faster rebounds—but this doesn't make those periods less stressful to investors. We diversify our International holdings to avoid concentrations in areas of turmoil.

5. Bond Market Dynamics

What's Happening?

Bond markets are undergoing shifts. We experienced one of the most volatile bonds markets on record in 2022-2023. However, we began to see signs of stability and rationality as we closed 2023. Changes in interest rates, inflation expectations, and central bank policies are influencing bond yields and prices. We are expecting some volatility in bond markets this year, however, we conclude that the worst (if we call 2022 "worst") is behind us. We've seen a nice uptick in our bond portfolio performance, and we expect this to hold in 2024.

Why It Matters:

Bonds are essential for diversified portfolios, offering stability and income. In 4Q 2023, we added more active bond management via two mutual funds. We've been pleased with their performance, and we like that they have a broad investment mandate, as well as the ability to "short" bonds when conditions dictate (such as in a rising interest rate environment). We have analyzed the risks associated with this, and our Investment Committee has deemed it appropriate for our portfolios.

We remain vigilant and committed to client objectives in portfolios. We think 2024 will be like most years in the markets; difficult to predict in the short term, but longer term, they tend to rise and look for reasons to increase in value. Despite election year news cycles, and some of the risks previously outlined, we see 2024 being a year of markets balancing out Fed policy impacts and general economic conditions. Economic conditions in the US are constructive and pointing to future areas of growth. After a nice run for large cap stocks to cap off 2023, we're turning our sights to International markets, US small cap stocks, and high quality bonds as opportunities to deploy client cash.

We value the trust you place in us as advisors. We appreciate your business, and we look forward to seeing you soon. Happy New Year!

JB