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# 2ND QUARTER LETTER 2024

**CONCENTRATED  
EQUITY RALLY,  
INTEREST RATES  
VOLATILE, INFLATION  
EASING**

# Top 4 Takeaways

## 1. Q2 2024 – EQUITIES CONTINUE TO CLIMB DRIVEN BY A HANDFUL OF STOCKS | BONDS FLAT

Global equities continued their upward trend in 2Q. A handful of US stocks, lead by AI related companies (i.e. NVIDIA), have carried U.S. returns while the remaining 495 stocks in the S&P 500 have lagged amid reduced 2024 earnings expectations. A balanced, public-only 60% global equity / 40% fixed income strategy returned **1.8%**. US Equities gained **3.9%**. The Bloomberg US Aggregate Bond index returned **0.1%** while the Bloomberg Municipal Index gained **0.0%**.

## 2. FEDERAL RESERVE MONETARY POLICY

Despite some improvement in the inflation metrics, the Federal Reserve left the Fed Funds Rate (FFR) unchanged at 5.33%. The market is expecting between a 0.25%-0.50% decrease in the FFR by year end 2024. In his speech after the June Fed meeting, Chairman Jerome Powell said lowering inflation while dealing with a “very strong” labor market and a healthy economy is a “*balancing act*”. It has been 12 months since the last Fed rate hike. Typically, the Fed begins to lower rates around the 8th month after the last hike, but inflation, especially services inflation, remains stickier this time around.

## 3. VALUATIONS

A small but influential subset of U.S. Large Cap Growth stocks have boosted Global Equity valuations (became more expensive). Typically, market peaks have been marked by high valuations due to higher prices and not from long-term fundamental growth. The rest of the major equity indices remain more favorably priced. Public fixed income yields fell from 2024 highs due to improved inflation news. Bond valuations relative to public equities remain competitive.

## 4. SEMI-LIQUID PRIVATE MARKETS

Semi-liquid private market investment returns continue to provide strong risk-adjusted returns and diversification to public allocations. All three asset classes produced positive returns, resulting in **+0.9%** for the basket of investments (GSIS Model Weights).

# 1. Equities Continue To Climb Driven By A Handful Of Stocks | Bonds Bounce Back As Spreads Tighten

+35%

2024 U.S. Large Cap Performance  
Attributed to Only 5 U.S. Stocks

## STOCKS

U.S. Equities returned **3.9%** in Q2, building on a very strong Q1, led by U.S. Large Cap Growth stocks (**8.3%**). Non-U.S. equities gained **1.0%** but have not benefited from the P/E expansion & Tech Buybacks similar to the U.S. market. International Emerging Markets was the best performer, gaining by **5.0%** in Q2, driven by strong returns from India/China.

## BONDS

Core bond indices posted flat returns in Q2 as yields rose despite improved inflation metrics and market expectations that the Fed will cut rates in 2024. Corporate Yield spreads are currently lower than pre-covid levels relative to similar duration U.S. Treasuries.

## PRIVATE MARKETS (GSIS MODEL WEIGHTS)

Semi-liquid private market returned **0.9%** during the quarter, contributing positively to portfolio returns. Cliffwater Enhanced Lending Fund was the best performer up **4.2%**.

## Market Returns (Period Ending 6/30/2024)

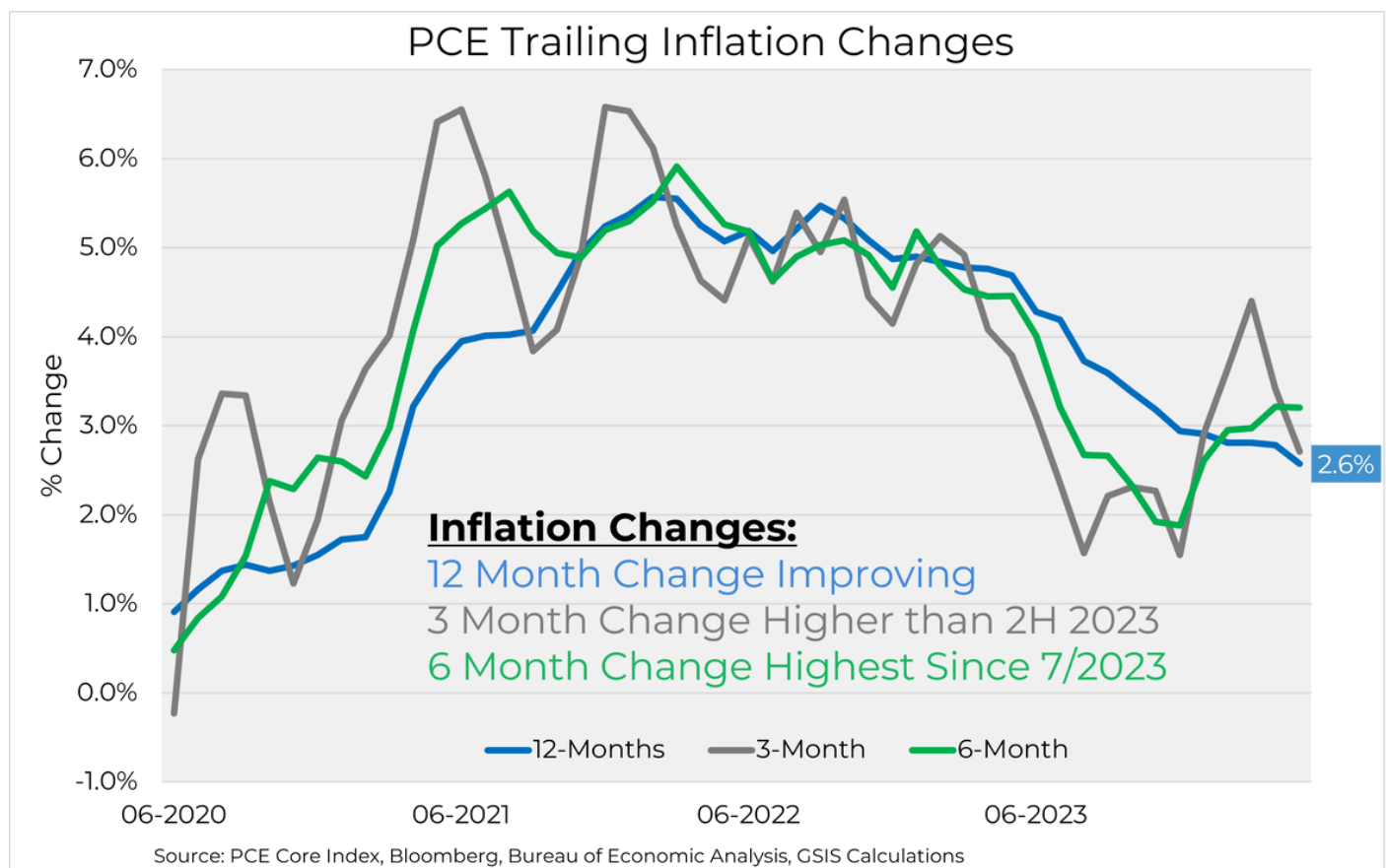
Asset Class	Index	QTD	YTD	1 Year	3 years	5 Years
Global Equity	MSCI ACWI	2.9%	8.9%	23.6%	5.1%	11.7%
US Large Cap	S&P 500	4.3%	11.3%	28.2%	9.6%	15.8%
US Large Cap Growth	Russell 1000 Growth	8.3%	13.1%	33.6%	11.1%	19.4%
US Large Cap Value	Russell 1000 Value	-2.2%	7.6%	21.7%	5.5%	10.7%
US Small Cap	Russell 2000	-3.3%	2.7%	20.1%	-1.7%	8.6%
International	MSCI EAFE	-0.4%	7.1%	18.5%	3.1%	8.0%
Emerging Markets	MSCI Emerging	5.0%	3.4%	12.4%	-6.2%	3.5%
Commodities	S&P Global Natural Resources	-1.9%	5.4%	19.9%	6.7%	11.0%
Real Estate	CRSP US REIT	-2.0%	-5.0%	8.5%	-2.4%	2.9%
Muni Bonds	Bloomberg Municipal Bond	0.0%	-1.9%	2.7%	-1.3%	0.9%
Taxable Bonds	Bloomberg Aggregate Bond	0.1%	-1.6%	1.3%	-3.1%	-0.2%
High Yield Bonds	Bloomberg High Yield Bond	1.1%	1.6%	11.2%	1.8%	4.2%

## 2. Federal Reserve Monetary Policy

Once again, the Fed did not change the Fed Funds Rate at the June meeting. The markets reacted favorably to the prospect of the Fed cutting interest rates in 2024 (Market expectations for changes in the Fed Funds rate have been very volatile). The market is trading at levels that signal an expectation that the Fed will continue to engineer a “soft landing”. The Fed will need to be tempered and measured when they begin to lower interest rates to avoid reigniting inflationary pressures.

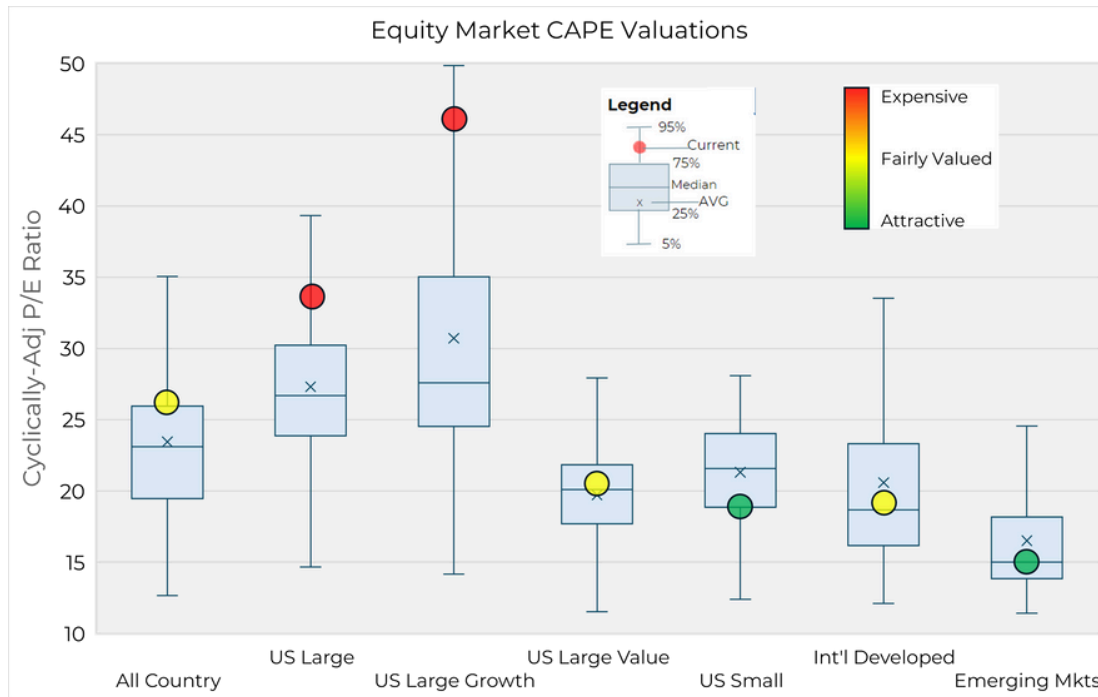
### Fed Funds Rate Policy

The May Inflation (U.S. Core - Personal Consumption Expenditures (PCE)) reading showed a move in the right direction as the 12-month change fell to 2.6%. A positive outcome, but not as positive when compared with the 3-month annualized rate of 2.7%, which was higher than any point in 2H 2023. In addition, the 6-month annualized rate was 3.2%, the highest since July 2023. The conflicting outcomes could keep the Federal Reserve on hold as it analyzes new data over the next couple of months.



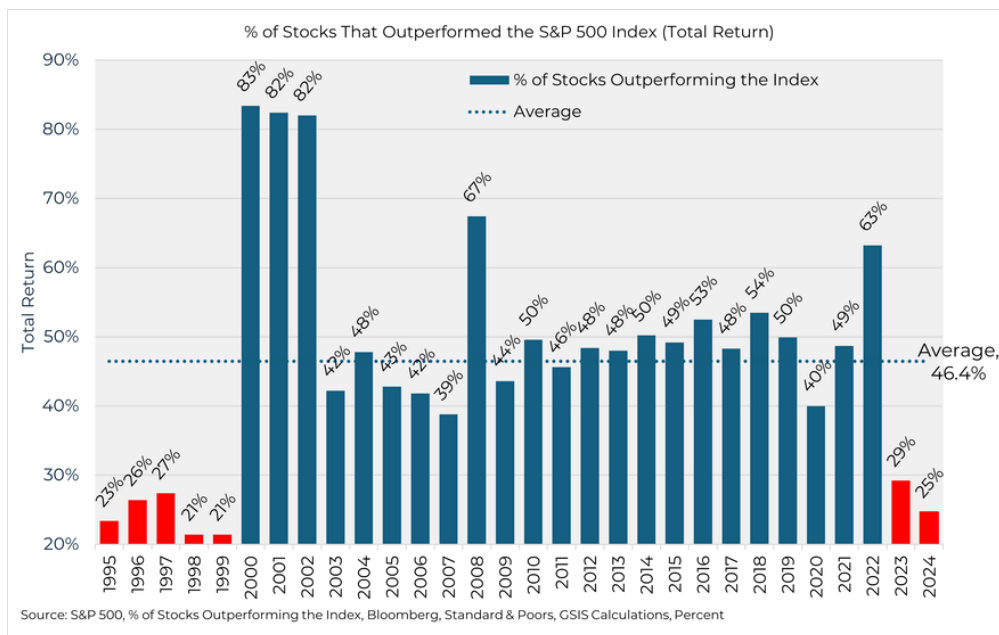
# 3. Valuations

U.S. Large Cap, specifically AI driven U.S. Large Cap Growth, continues to be the only major equity asset class that is significantly overvalued.

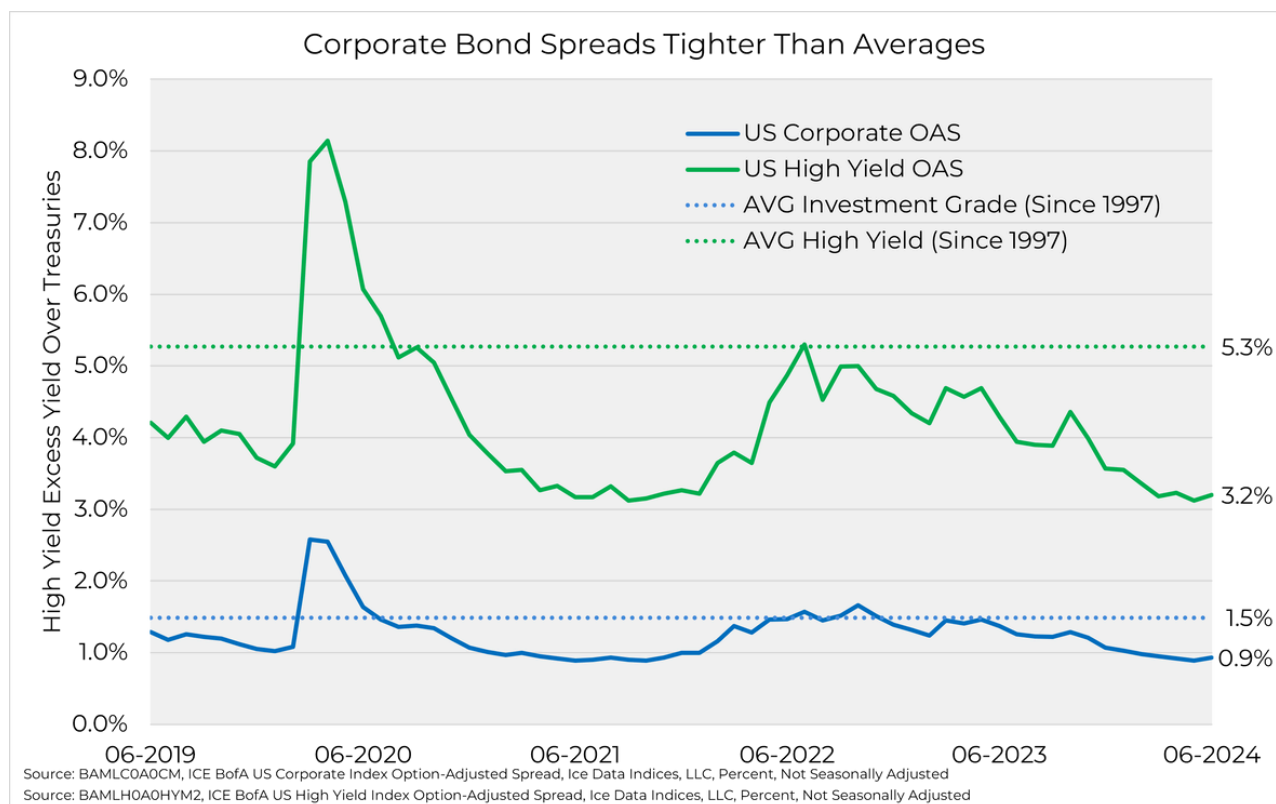


## S&P 500: PERCENTAGE OF STOCKS THE OUTPERFORMED THE INDEX

The Concentration of Stock Returns coming from a small subset of stocks has been near the “tech bubble” levels. In 2024, only 25% of companies are outperforming the index. Typically this type of outlier reverses itself.



- Corporate bond yields, both investment grade and high yield, relative to Government Bonds yields have compressed over the last 12 months. Both investment grade and high yield excess bond yields are below their 5 year averages.



## 4. Semi-Liquid Private Markets

- Private Credit outperformed public fixed income. The asset class continues to benefit from the higher interest rate environment despite loan spreads compressing.
- Private Equity returns were positive in Q2 2024 although exit activity remaining low due to higher costs of financing. Exit activity has been trending lower since the Fed first raised rates in Q1 2022. Private Equity valuations are more favorable to Public Equity valuations.
- Private Real Assets continue to produce positive returns in 2024 as new supply & building permits continue to slow and emerging sectors, like data centers, continue to benefit from the AI boom.

# Looking Ahead

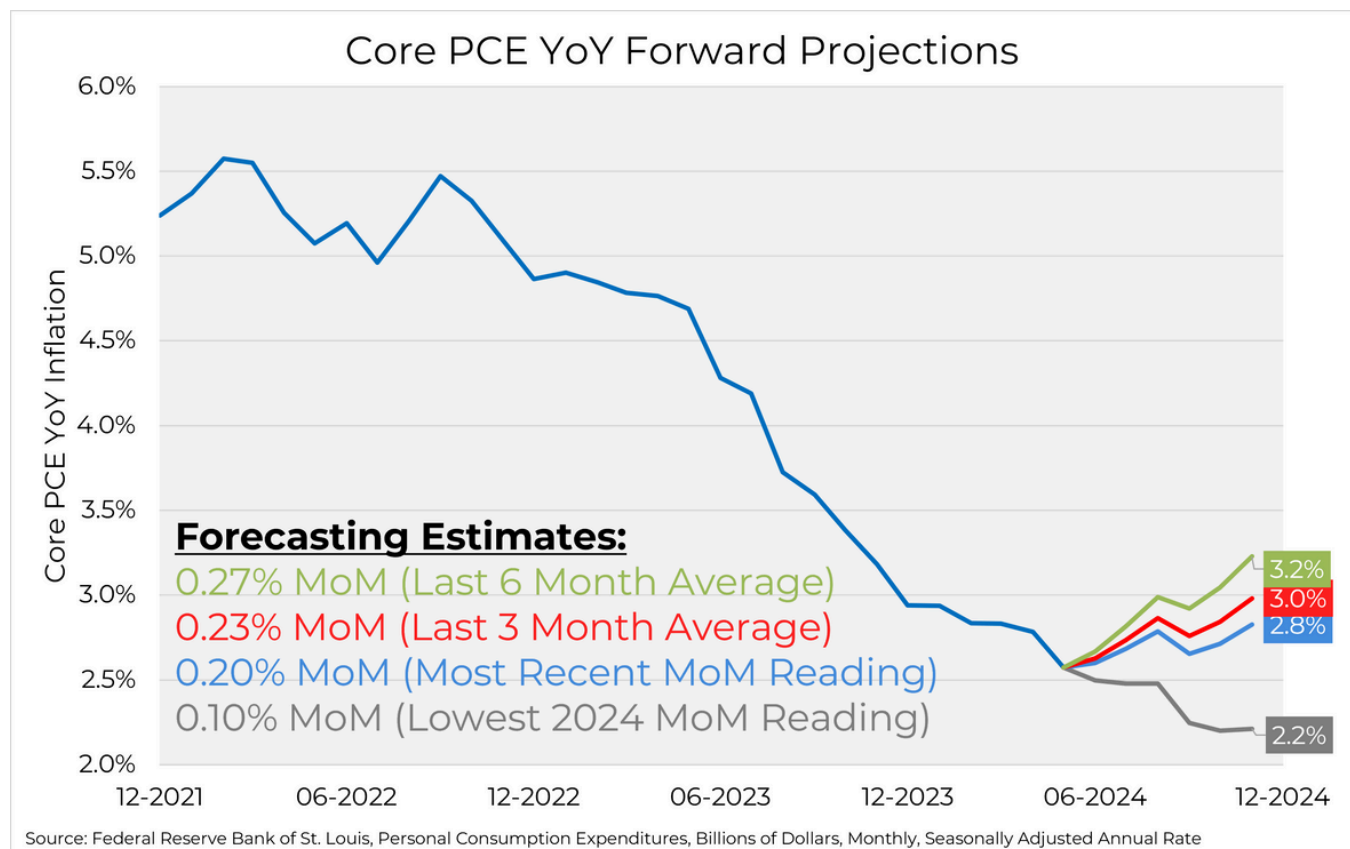
The main market drivers should continue to be the changes in Inflation and the Federal Reserve Policy response. In addition, Geopolitics and the Concentration / Quality Risk in the U.S. Stock Market could also have a large impact in the 2H 2024.

## INFLATION UNLIKELY TO DROP BELOW 2% IN 2024

Inflation has been significantly reduced following the spending surge post-Covid but has remained elevated. Portions of inflation, like service inflation, remains to be one of the areas that have been harder to corral. Core PCE inflation has slowed down but is still projected to remain above the Fed's 2% target this year, even if inflation was to slow to 0.1% month-over-month. A tough ask since the average MoM change has been 0.21% the last 12 months.

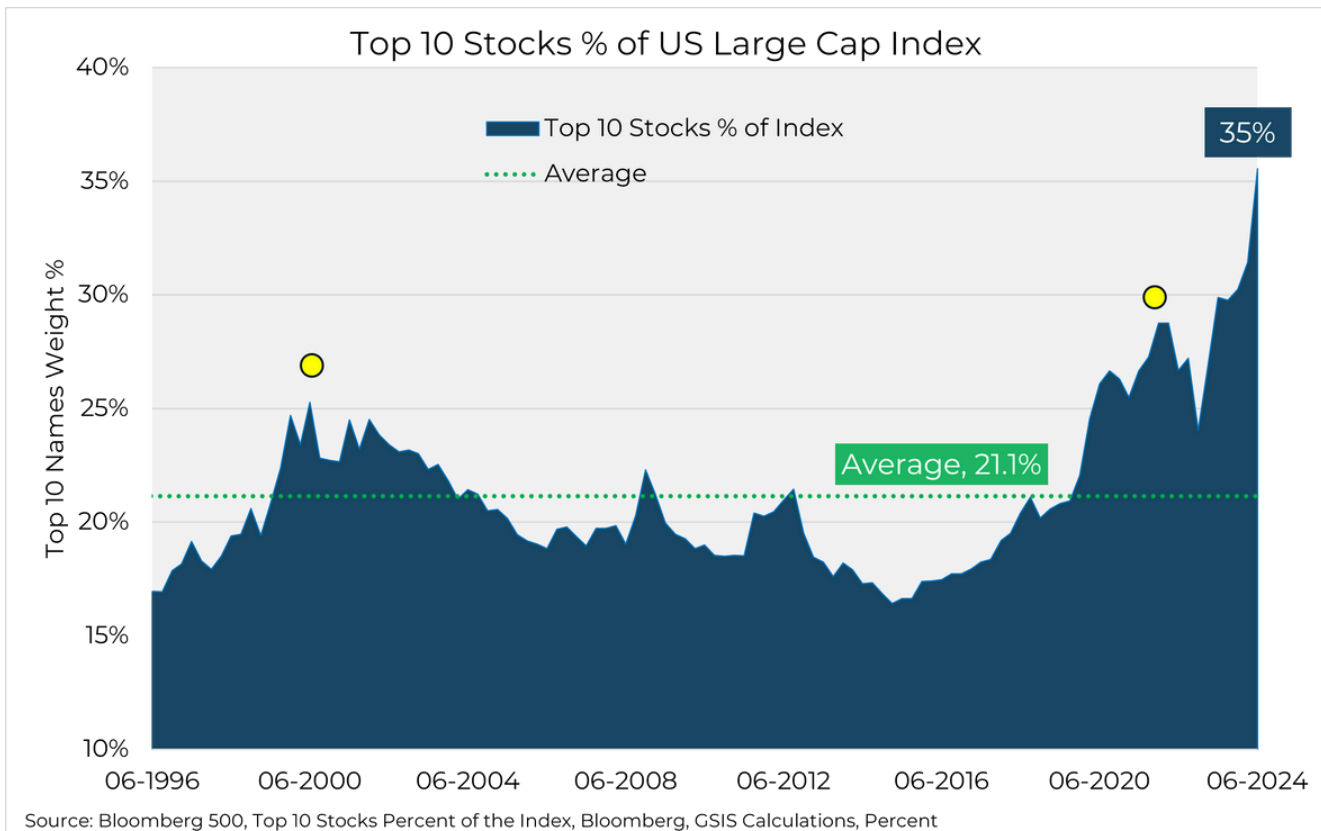
5.3%

YoY  
Services  
ex-Energy  
Inflation.



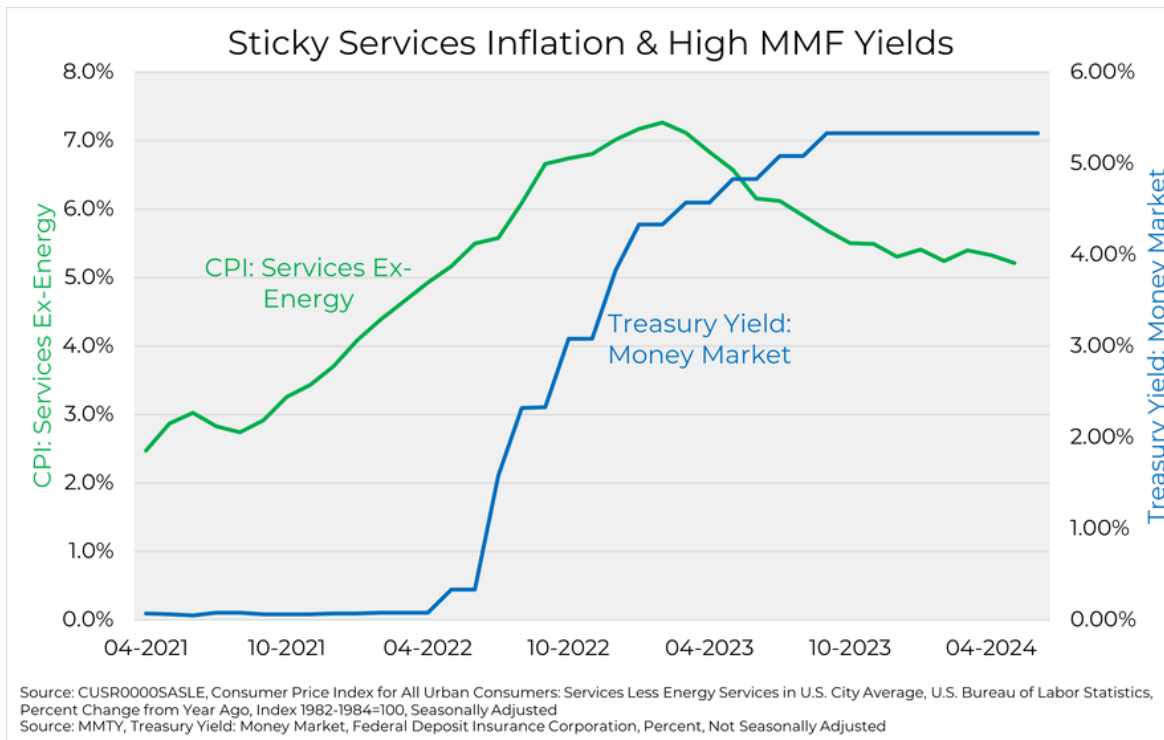
## US EQUITIES: CONCENTRATION RISK

The share of the overall U.S. Equity market accounted for by the top 10 companies is constantly changing. Recently, the share of the total market capitalization of the biggest companies had eclipsed 35% of U.S. Large Cap. This is important as it is the first time ever that the weight of 10 stocks was greater than 35%. As a comparison, in the late 1990's during the "tech bubble", the top 10 companies represented 25% allocation of the U.S. Large Cap. Extreme concentration in a few stocks reduces the benefit of market diversification, leaving investors with more single stock or idiosyncratic risk.



## CONSUMERS

The U.S. consumer will need to slow spending in order for inflation to subside to the point where the Federal Reserve can significantly lower the Fed Funds Rate. The U.S. consumer does seem to be getting tapped out when looking at the low amount of savings and high levels of credit card debt. One factor that may be a continued tailwind for consumers is the amount of additional income they are receiving from investments in money market funds (MMF).



+\$500B

Run-Rate of Dividends Received From Money Market Funds. Estimated to be ~2.5% of Consumer Spending. (BEA)

+\$184B

Increase in Household Debt in 1Q 2024. (FRB NY, "Quarterly Report on Household Debt").

## Summary

As we assess current market conditions, there are compelling reasons for both optimism and caution. Optimistically, key economic indicators such as slowing inflation, high employment rates and continued consumer spending suggest a strengthening economic foundation. Additionally, technological AI innovation continues to drive growth and earnings forecasts in both public and private markets. However, caution is warranted due to uncertainties surrounding global supply chain disruptions, inflationary pressures, and geopolitical tensions. Concerns over equity stock market concentration, elevated technology forward P/E levels pose risks to market stability and debt funded consumer spending could potentially hinder economic growth if not carefully managed. Therefore, while optimism is justified by robust economic fundamentals and technological advancements, risk management, including monitoring tail risks, continues to be necessary.

## Thank you for your Trust and Confidence.



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