Quarterly Insights – April 2024

AI Enthusiasm, Fed Rate Cuts and Strong Growth Power Stocks to New Highs

The 2023 rally continued in the first quarter of 2024 as a positive combination of stable economic growth, falling inflation, impending Fed rate cuts and ever-growing enthusiasm towards artificial intelligence (AI) propelled stocks higher, as the S&P 500 rose above 5,000 for the first time and hit new all-time highs.

The year began with a modest uptick in volatility, as traders and investors initially booked profits following the strong 2023 gains. However, those initially small declines intensified shortly after the start of the year when the December Consumer Price Index, an important inflation indicator, declined less than expected. That reading challenged the idea that inflation was quickly falling towards the Fed's 2.0% target and caused investors to delay the expected date of the first Fed rate cut, as expectations for that first cut moved from March to June. Fears of potentially higher-than-expected rates pushed stocks temporarily into negative territory early in January. However, the declines didn't last. First, fourth-quarter corporate earnings were again better than feared and that helped stocks recover from those early declines. Then, in late January, the Federal Reserve clearly signaled that rate hikes were over and strongly hinted that rate cuts would occur in the coming months. Investors seized on that positive message and the S&P 500 hit a new all-time high late in the month and finished with a modest gain, up 1.59%.

The rally continued and accelerated in February as fears of a potential rebound in inflation subsided. Inflation metrics released in February largely met expectations and importantly did not imply that inflation was reaccelerating. As such, investor expectations for a June rate cut were strengthened and that helped stocks extend the year-to-date gains. Those results further fueled investors' AI enthusiasm and large-cap tech stocks powered the S&P 500 higher into month-end as the index hit a new record high above 5,000. The benchmark domestic index gained 5.34% in February.

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The final month of the quarter saw even more gains, aided by familiar factors such as solid economic growth, generally as-expected inflation data, AI enthusiasm and bullish Fed guidance. Broadly speaking, economic and inflation data largely met expectations in March and continued to point towards stable growth and (slowly) falling inflation. Then, in mid-March, updated Federal Reserve interest rate projections still pointed towards three rate cuts in 2024, further reinforcing investor expectations for a June rate cut. Those positive factors combined with additional strong AI-related earnings reports (this time from Micron) to push markets broadly higher as the S&P 500 crossed 5,200 for the first time late in the month and ended March with strong gains.

In sum, the 2023 rally continued and accelerated in the first quarter of 2024 thanks to positive news flow that implied stable growth (no recession), still falling inflation, looming Fed rate cuts and continued AI enthusiasm and those factors propelled the S&P 500 to new all-time highs.

First Quarter Performance Review

The first quarter of 2024 reflected a much more evenly distributed rally compared to the fourth quarter of 2023, where tech and tech-aligned sectors handily outperformed the rest of the markets. Over the past three months markets saw broad gains distributed more equitably amongst various sectors and industries.

However, while the rally in stocks did broaden out in the first quarter, that did not benefit small caps as they were some of the notable laggards over the past three months. Small caps registered a positive return for the first quarter but lagged large caps as concerns about stubbornly high interest rates weighed on small caps, as they are more sensitive to higher funding costs and slowing growth.

From an investment style standpoint, growth once again outperformed value in the first quarter but the margin was much closer than last year, as both investment styles logged strong quarterly returns. Continued heightened AI enthusiasm was the main reason for the modest growth outperformance over the past three months, as large-cap tech stocks again saw strong rallies in Q1.

On a sector level, as mentioned, gains were broad as 10 of the 11 S&P 500 sectors finished the first quarter with a positive return. Unlike 2023, however, tech and tech-aligned sectors didn’t substantially outperform. To that point, the best-performing sectors in the market in the first quarter were communication services, financials, energy and industrials. That sector mix reflected the influences of AI enthusiasm, strong financial stock guidance, solid U.S. economic data and rising optimism towards a rebound in Chinese economic growth. The diversified gains demonstrated that the Q1 rally was driven by a more varied set of influences beyond just AI enthusiasm.

Turning to the laggards, the only S&P 500 sector to log a negative return for the first quarter was the real estate sector, as it continues to be weighed down by concerns about the health of the commercial real estate market. Consumer discretionary also lagged and registered only a slightly positive return as numerous retailers warned about a potential slowing of consumer spending during the first quarter (this is something to monitor as we begin the second quarter).

US Equity Indexes	Q1 Return	YTD
S&P 500	10.56%	10.56%
DJ Industrial Average	6.14%	6.14%
NASDAQ 100	8.72%	8.72%
S&P MidCap 400	9.95%	9.95%
Russell 2000	5.18%	5.18%

Source: YCharts

Internationally, foreign markets posted solid quarterly gains but still underperformed the S&P 500. Looking deeper, foreign developed markets outperformed emerging markets in Q1 thanks to better-than-expected economic data and as expectations rose for early summer rate cuts from the European Central Bank and Bank of England. Emerging markets, meanwhile, logged only slightly positive returns in Q1 and solidly underperformed the S&P 500 thanks to mixed Chinese economic data and a lack of substantial Chinese economic stimulus early in the quarter.

International Equity Indexes	Q1 Return	YTD
MSCI EAFE TR USD (Foreign Developed)	5.81%	5.81%
MSCI EM TR USD (Emerging Markets)	2.16%	2.16%
MSCI ACWI Ex USA TR USD (Foreign Dev & EM)	4.66%	4.66%

Source: YCharts

Commodities saw strong gains in the first quarter thanks to still-elevated geopolitical tensions, a weaker U.S. dollar and smaller-than-expected declines in inflation. Oil rallied sharply in Q1 thanks to late-quarter optimism for an acceleration in Chinese economic growth, combined with an increase in geopolitical tensions following the continued attacks on commercial ships in the Red Sea, along with an increase in Russian attacks on Ukrainian energy infrastructure. Gold hit a new all-time high in the first quarter, meanwhile, and logged solidly positive returns thanks to the aforementioned buoyant inflation data and a weaker U.S. dollar.

Commodity Indexes	Q1 Return	YTD
S&P GSCI (Broad-Based Commodities)	10.36%	10.36%
S&P GSCI Crude Oil	15.93%	15.93%
Gold Price	7.93%	7.93%

Source: YCharts/Koyfin.com

Switching to fixed income markets, the leading benchmark for bonds (Bloomberg Barclays US Aggregate Bond Index) realized a slightly negative return for the first quarter of 2024. Disappointing inflation readings were the primary reason for the weakness in bonds as they delayed the expected start of Fed rate cuts from March until June and caused bond investors to consider that rates may be higher than previously expected over the medium and longer term.

Looking deeper into the fixed income markets, longer-duration bonds handily underperformed those with shorter durations. That performance gap was due to the slower-than-expected decline in inflation, because while it won't materially delay the start of Fed rate cuts, it does threaten to keep rates "higher for longer," which is a bigger negative for longer-dated debt.

Turning to the corporate bond market, higher-yielding but lower-quality "junk" bonds outperformed investment grade debt as looming Fed rate cuts and buoyant inflation, amidst stable economic growth, led bond investors to "reach" for more yield in the riskier parts of the credit spectrum.

US Bond Indexes	Q1 Return	YTD
BBgBarc US Agg Bond	-0.78%	-0.78%
BBgBarc US T-Bill 1-3 Mon	1.32%	1.32%
ICE US T-Bond 7-10 Year	-1.35%	-1.35%
BBgBarc US MBS (Mortgage-backed)	-1.04%	-1.04%
BBgBarc Municipal	-0.39%	-0.39%
BBgBarc US Corporate Invest Grade	-0.40%	-0.40%
BBgBarc US Corporate High Yield	1.47%	1.47%

Source: YCharts

Second Quarter Market Outlook

We begin the second quarter in the midst of a positive macroeconomic environment as growth appears stable, inflation is still falling, the Fed is likely going to deliver the first rate cut in four years and AI enthusiasm keeps earnings estimates high. But while this is undoubtedly a favorable set up, the strong rally of the last six months has left the S&P 500 at previously historically unsustainable valuations while investor and analyst sentiment is very bullish and, potentially, complacent. So, while the outlook is currently positive, it's essential we continue to monitor the macroeconomic horizon for risks because at current stretched valuations and with sentiment very bullish, the market is vulnerable to a negative surprise.

Specifically, while it's true that economic growth has remained resilient in the face of higher rates, some data is pointing to a loss of momentum. Retail sales missed expectations in January and February while the unemployment rate jumped to the highest level since 2022 during the first quarter. Neither number warrants concern about the economy right now, but both serve as a reminder to watch data closely as a continued economic expansion is not guaranteed.

The scourge of Inflation, meanwhile, is still retreating but the pace of that decline has slowed meaningfully. Core CPI, one of the Fed's preferred measures of inflation, has barely declined over the past several months as it sat at 4.0% y/y in October and in February was just 3.8% y/y. Meanwhile, other anecdotal indicators of inflation have hinted at a rebound in prices. If inflation bounces back that will reduce the number of Fed rate cuts in 2024 and that disappointment could pressure stocks and bonds.

To that point, markets fully expect a June rate cut from the Fed and three rate cuts in 2024 and that assumption was central to the first-quarter rally. However, those rates cuts are not guaranteed and if the Fed does not cut as aggressively as markets expect, that will result in disappointment and a potential decline in stocks and bonds.

Finally, investor enthusiasm towards the potential for artificial intelligence remains a critical part of the bull market investors' hopes that AI integration will lead to a profitability and earnings boom, not just for tech companies, but for the entire market. However, that's also not guaranteed and so far, AI integration has produced a lot of flashy headlines but not a lot of profit maximization for non-tech industries. If AI fails to broadly boost profits and demand declines, that will be a significant negative for this market.

Bottom line, this historic rally is currently supported by positive fundamentals. But we cannot let the currently positive set up blind us to risks and that's why, while we are pleased with the market performance, we are also focused on managing both reward and risk in portfolios, because despite the strong performance this market remains vulnerable to negative news.

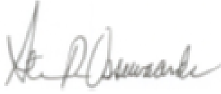
At *Ossewaarde Anderson Sanborn Peterson Wealth Management Group of Wells Fargo Advisors*, we are committed to helping you effectively navigate this challenging investment environment. Successful investing is a marathon, not a sprint, and even through both bull and bear markets, we will remain focused on the diversified approach set up to meet your long-term investment goals.

Therefore, it's critical for you to stay invested, remain patient, and stick to the plan, as we've worked with you to establish a unique, personal allocation target based on your financial position, risk tolerance, and investment timeline.

We remain vigilant towards risks to portfolios and the economy, and we thank you for your ongoing confidence and trust. Please rest assured that our entire team will remain dedicated to helping you successfully navigate this market environment.

Please do not hesitate to contact us with any questions, comments, or to schedule a portfolio review.

Sincerely,



Steven R. Ossewaarde, CFP®
Managing Director-Investment Officer
269-323-4810

Adam D. Anderson, CFP®
Managing Director-Investment Officer
269-323-4817

Jon Sanborn
First Vice President-Investment Officer
269-323-4813

Kimberly S. Peterson, CFP®
First Vice President-Investment Officer
269-323-4828

OAS&P
Ossewaarde Anderson Sanborn & Peterson
Wealth Management Group
Of Wells Fargo Advisors
7900 Moorsbridge Road
Portage, MI 49024
269-323-8400

www.oaspwmgroup.com

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The indices presented in this newsletter are to provide you with an understanding of their historical performance and are not presented to illustrate the performance of any security.

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The prices of small and mid-cap company stocks are generally more volatile than large company stocks. They often involve higher risks because smaller companies may lack the management expertise, financial resources, product diversification and competitive strengths to endure adverse economic conditions.

Technology and internet-related stocks, especially of smaller, less-seasoned companies, tend to be more volatile than the overall market.

Investments that are concentrated in a specific sector or industry may be subject to a higher degree of market risk than investments that are more diversified.

Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability, and different accounting standards. This may result in greater share price volatility. Investing in emerging markets accentuates these risks.

Investing in commodities is not appropriate for all investors. Exposure to the commodities markets may subject an investment to greater share price volatility than an investment in traditional equity or debt securities. The prices of various commodities may fluctuate based on numerous factors including changes in supply and demand relationships, weather and acts of nature, agricultural conditions, international trade conditions, fiscal monetary and exchange control programs, domestic and foreign political and economic events and policies, and changes in interest rates or sectors affecting a particular industry or commodity. Products that invest in commodities may employ more complex strategies which may expose investors to additional risks, including futures roll yield risk.

Buying gold, silver, platinum or palladium allows for a source of diversification for those sophisticated persons who wish to add precious metals to their portfolios and who are prepared to assume the risks inherent in the bullion market. Any bullion or coin purchase represents a transaction in a non-income-producing commodity and is highly speculative. Therefore, precious metals should not represent a significant portion of an individual's portfolio.

Investments in fixed-income securities are subject to market, interest rate, credit and other risks. Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in

interest rates can result in the decline in the bond's price. Credit risk is the risk that an issuer will default on payments of interest and/or principal. This risk is heightened in lower rated bonds. If sold prior to maturity, fixed income securities are subject to market risk. All fixed income investments may be worth less than their original cost upon redemption or maturity.

The S&P 500 Index consists of 500 stocks chosen for market size, liquidity, and industry group representation. It is a market value weighted index with each stock's weight in the Index proportionate to its market value.

The Dow Jones Industrial Average is a price-weighted index of 30 "blue-chip" industrial U.S. stocks.

The NASDAQ 100 Index is an unmanaged group of the 100 biggest companies listed on the NASDAQ Composite Index. The list is updated quarterly and companies on this Index are typically representative of technology-related industries, such as computer hardware and software products, telecommunications, biotechnology, and retail/wholesale trade.

The Russell 2000® Index measures the performance of the 2,000 smallest companies in the Russell 3000® Index, which represents approximately 8% of the total market capitalization of the Russell 3000® Index.

The S&P Midcap 400 Index is a capitalization-weighted index measuring the performance of the mid-range sector of the U.S. stock market, and represents approximately 7% of the total market value of the U.S. equities. Companies in the Index fall between the S&P 500 Index and the S&P Small Cap 600 Index in size: between $1-4 billion.

The MSCI All Country World ex USA Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets, excluding the USA. The Index consists of 45 country indices comprising 22 developed and 23 emerging market country indices. The developed market country indices included are: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Hong Kong, Ireland, Italy, Japan, Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom. The emerging market country indices included are: Argentina, Brazil, Chile, China, Columbia, Czech Republic, Egypt, Hungary, India, Indonesia, Israel, Korea, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Russia, South Africa, Taiwan, Thailand, and Turkey. Source: MSCI. MSCI makes no express or implied warranties or representations and shall have no liability whatsoever with respect to any MSCI data contained herein. The MSCI data may not be further redistributed or used as a basis for other indices or any securities or financial products. This report is not approved, reviewed or produced by MSCI. The MSCI EAFE Index is designed to represent the performance of large- and mid-cap securities across 21 developed markets, including countries in Europe, Australasia and the Far East, excluding the U.S. and Canada.

The MSCI Emerging Markets Index is designed to represent the performance of large-and mid-cap securities in 24 Emerging Markets.

Bloomberg U.S. Aggregate Bond Index is a broad-based measure of the investment grade, US dollar-denominated, fixed-rate taxable bond market.

The Bloomberg U.S. 1-3 Year Government Bond Index is composed of all publicly issued, non-convertible domestic debt of the U.S. government and its agencies. The Index also includes corporate debt guaranteed by the U.S. government. Only notes and bonds with a minimum maturity of one year up to a maximum maturity of 2.9 years are included.

The ICE U.S. Treasury 7-10 Year Bond Index is part of a series of indices intended to assess the U.S. Treasury market. The Index is market value weighted and is designed to measure the performance of U.S. dollar-denominated, fixed rate securities with minimum term to maturity greater than seven years and less than or equal to ten years.

The Bloomberg Mortgage Backed Securities Index is an unmanaged index of mortgage pools of the Government National Mortgage Association, Federal Home Loan Mortgage Corporation and Federal National Mortgage Association.

The Bloomberg Corporate High Yield Municipal Bond Index covers the universe of fixed rate, non-investment grade debt.

The Bloomberg Municipal Bond Index is an unmanaged index of a broad range of investment-grade municipal bonds that measures the performance of the general municipal bond market.

The Bloomberg Corporate Bond Index is an unmanaged market value-weighted index of investment-grade corporate fixed-rate debt issues with maturities of one year or more.

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