Financial Markets

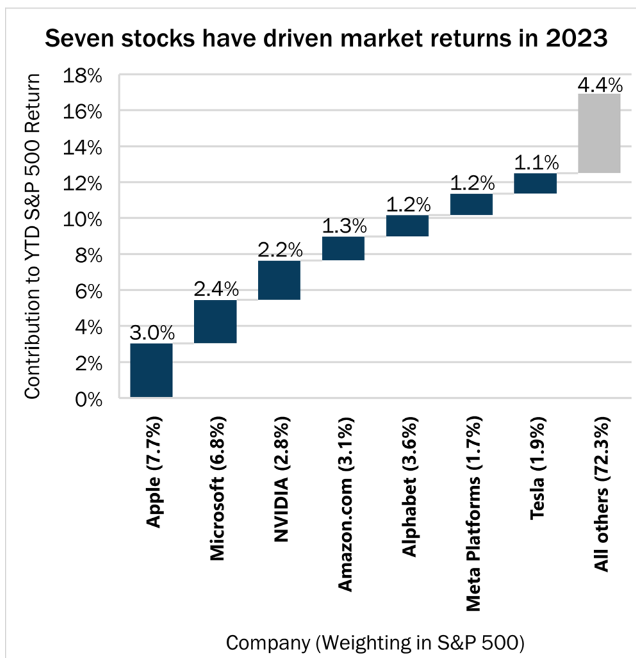
Total Returns through June 30, 2023		
US Stocks	**2nd Quarter**	**Year-to-Date**
Standard & Poor's 500	8.7%	16.9%
Russell 2000®	5.2%	8.1%
International Stocks		
MSCI World Ex-US	3.0%	11.3%
MSCI Emerging Markets	0.9%	4.9%
US Fixed Income		
Bloomberg Gov't/Credit	-0.9%	2.2%
90-Day Treasury Bill	1.2%	2.4%

Stocks around the globe continued to rally in the second quarter with US equities leading the way. We officially entered a bull market in mid-June after the S&P 500 achieved a 20% gain from its October 2022 lows, and the Index ended the month less than 8% below the all-time high achieved in early 2022. Larger technology-related companies have driven returns. The tech-heavy Nasdaq Composite and Russell 1000® Growth Index have gained 32.3% and 29.0%, respectively, in 2023; an impressive result compared to the relatively meager returns of the Russell 1000® Value Index and Russell 2000® Small Capitalization Index, which have returned 5.1% and 8.1%, respectively, in the same period. The same comparison holds relative to the primary international stock indices, which also registered positive, albeit more muted, returns.

Bonds lost ground during the quarter as prevailing yields moved higher across the maturity curve. The 10-year Treasury bond yield rose from 3.48% to 3.81% as the Federal Reserve signaled its preference to keep rates elevated for longer than the market had expected. Corporate bonds fared slightly better, however, as investors' increasing appetite for risk allowed yield spreads over Treasury bonds to narrow.

Investment Perspectives

Concentrated Gains; Concentrated Market



Tech-related companies have outperformed in general, but market leadership has been narrower than that. In the first six months of 2023, seven large companies accounted for almost three quarters of the S&P 500's total return. There are many credible reasons for these stocks' leadership: the strength of their businesses and visible growth prospects despite continued economic uncertainty; their size and related access to economical sources of capital in the face of rising interest rates; and their exposure, to varying degrees, to the nascent Artificial Intelligence (AI) market. Regardless of why, the outsized year-to-date performance of these already extraordinarily large companies has served to further concentrate the S&P 500 to historical proportions. In fact, the top 10 companies in the Index now account for almost 32% of its weight. Such concentration surpasses that of year-end 2021 when the market reached its all-time high and is several percentage points higher than the 27%

weighting of the top 10 companies registered at the peak of the tech bubble in 2000. Though technology stocks fueled the market's rise in that era, the largest weightings in the Index included businesses across economic sectors. What they had in common though, were generally high valuations that reflected overly optimistic expectations of future profit growth. As we now know, that growth did not materialize, valuations eventually came back to earth, and stock returns suffered greatly.

With few exceptions, today's largest companies *are* concentrated in technology (or technology-adjacent) businesses. And though some of these large firms do sport exorbitant valuations that are not so dissimilar from the 2000 market, others are reasonable in light of the sustainability of their business models, the ubiquitous nature of their products, and their realistic prospects for future growth.

Nonetheless, Index leadership changes over time. In past episodes, the largest companies eventually underperformed the rest of the Index, thereby reducing their weight and allowing other firms to emerge. This was not an attractive outcome for those investors with similar concentrations in their portfolios. This fate could befall some of today's largest companies and is why we remain especially focused on monitoring the businesses, valuations, and position sizes of those we own.

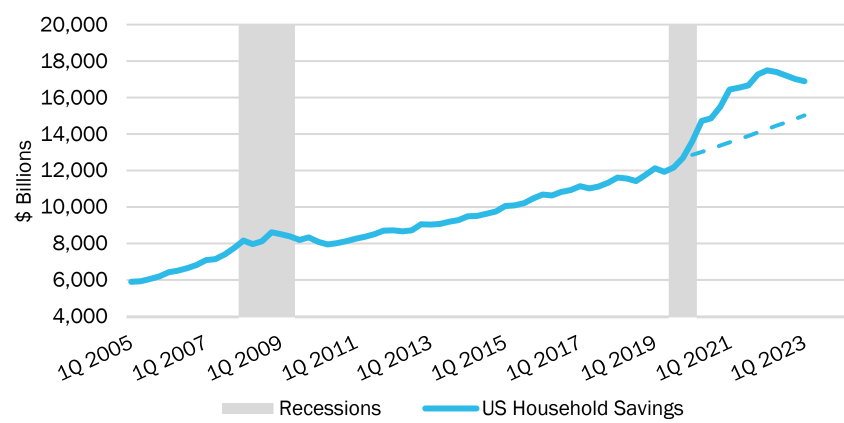
A Path to Normalization

The global economy is still feeling the impacts from a series of historical events. Chief among them remains the COVID pandemic. The resulting changes to activity (e.g., mobility, spending patterns, supply chain disruption, etc.) and economic policies, as well as their subsequent reversals, have reverberated through the economy and financial markets for the last several years. They still do. Most recently, this has been evident in the form of China's continued efforts at a full-fledged reopening and turmoil among US regional banks earlier this year. However, it seems the amplitude of these after-shocks has begun to diminish. And though these recent events added some turbulence, the economy has largely maintained its footing.

Over the past several quarters, the Federal Reserve has tried to help maneuver the economy toward a path to normalcy. Inflation readings, which reached levels not seen in 40 years, remain elevated but are down substantially from their highs. At its June meeting, the Fed cited such recent pricing trends in its decision to pause its streak of interest rate increases that began in March of last year. But the central bank also indicated the rate hiking cycle may not have reached its culmination just yet. Data-driven policy remains the Fed's modus operandi, and more rate increases are likely given still above-target inflation and the continued strength of the labor market and economy at large. In fact, the Fed governors' most recent economic forecasts expressed expectations of higher GDP growth and core inflationary pressures than previously anticipated. Accordingly, their collective projections for the level of future policy rates ratcheted upwards as well.

Despite higher interest rates and banking sector turmoil that resulted in tightening lending standards, consumer spending has remained robust. US households have overcome the headwind of higher

Household savings are declining but remain elevated



Source: Federal Reserve Bank of St. Louis
Data: Total Household Currency and Deposits including Money Market Fund Shares

financing costs by leaning on the tremendous fiscal stimulus bestowed on them during the pandemic. In fact, despite the recent spate of "revenge spending" as Americans caught up on travel and other activities that were limited during the throes of the pandemic, household balance sheets remain flush with cash. This resilient consumer demand may help the economy avoid a recession, yet it makes inflation more difficult to tamp down. The Fed will continue to try to thread the needle by slowing the economy's growth without causing it to stall entirely.

Outlook and Positioning

We remain in an uncertain environment with numerous forces impacting the economy's future path. What we can say with more definitiveness is that an era of historic policy stimuli has closed. This includes interest rates moving off the ultralow levels they had been for more than a decade, the end of pandemic-related fiscal stimulus, and a further cap on near-term government spending growth via the recent debt ceiling agreement. As the world adjusts to this new normal, it is unsurprising that investors and economists, including Fed policymakers, have a wide spectrum of anticipated economic outcomes.

Uncertainty also checkers the geopolitical landscape. Russia's ongoing incursion into Ukraine and its ramifications for Europe, China's stance on capitalism, free markets, and Taiwan, as well as political developments in other large countries can have myriad consequences for the domestic and global economies. These could include sudden actions like additional political standoffs or military conflicts, or a longer-term fracturing of economic cooperation and globalization. Either path would disrupt important forces that have aided economic growth in the past few decades and have significant impacts on financial markets.

In consideration of all of the above, we maintain our focus on building diversified portfolios populated by shares of high quality companies that can produce healthy levels of cash flows and profits in a range of economic environments. And given the run-up in some pockets of the market, we remain disciplined with respect to valuations that do not imply overly optimistic prospects. Bond investments also continue to play a key role in multi-asset portfolios. As interest rates have moved higher, Treasuries and other high quality bonds offer more enticing expected returns while retaining their historical role as a portfolio ballast in times of stress.