MORSE ASSET MANAGEMENT, INC.
23 Old Kings Highway South, Suite 200, Darien, CT 06820

April 20, 2024

2024 Q1 Investment Commentary

Over the last five months, markets have seen persistent strength and have continued pushing to new highs. Economic expansion, earnings growth, positive breadth, and momentum support the case for the long-term uptrend in equities to remain intact. But sentiment became extended, and the market overbought. Recent data has given the Fed reason to delay cutting, causing rates to spike, and rising geopolitical tension has resulted in reset of near-term expectations at a time of seasonal weakness. The market has since pulled back as gains are consolidated but a major correction or bear market is unlikely.

The S&P 500 Index surged 25.3% over the last five months. This was only the seventh time the index has gained more than 25% over a five-month span since WWII. Following each instance, the index continued higher in the subsequent year. Surges like this also rarely come near the end of bull markets. However, corrections and volatility are normal and work to maintain the health of the market, keeping exuberance in check. Since 1928, an average year for the S&P 500 sees seven separate 3% dips, three 5% pullbacks, a 10% correction intra-year, and a 20% bear market every 3.5 years (*chart*). Seasonally, April – June are periods of choppiness, but historically election years end higher (*chart*).

The labor market remains strong. The unemployment rate in the United States dipped to 3.8% as 303,000 jobs were added in March, the most in ten months. Initial unemployment claims were only 214,000, well below a level of concern. Consumer spending also continues to power on. Retail sales increased 0.7% in March, more than double the consensus estimate of 0.3%. Additionally, the previous month was revised up to +0.9% from 0.6%. The economy will be supported if the job market, and thus consumers, remain healthy.

Both ISM Manufacturing and Non-Manufacturing Indices are expansionary, supporting further economic growth. The improvement in the manufacturing sector is notable as it has been contracting for the past 16 consecutive months and has finally turned positive. Services no longer need to carry the economy. The Atlanta Fed's GDPNow model estimate for real GDP growth in the first quarter of 2024 is now +2.9% *(chart)*. The US economy is growing moderately and remains solid.

However, recent inflation data has offered caution. CPI rose 0.4% in March led by shelter and gasoline. Deceleration in Core PCE, the Fed's preferred measure, has also stalled. As a result, Fed Chair Powell commented that recent data had "clearly" not given the FOMC greater confidence in hitting their inflation goal. Officially, the Fed still plans to cut interest rates three times this year, but members have since stated they are open to delay.

Bonds have quickly adjusted to the reality of rates being higher for longer and the economy continuing to expand. The yield curve has steeped sharply and 10-year Treasury yields spiked to over 4.6%, from 4% at the beginning of the year. Higher rates have not impacted the potential for economic growth but quick moves higher unnerve markets. Yields will need to stabilize for the market to find its footing *(chart)*.

For Q1 2024, according to Factset's April 19th *Earnings Insight*, estimated earnings growth rate for the S&P 500 is +0.5% and revenue +3.5%. If reported at these levels, it would mark the third-straight quarter of year-over-year earnings growth and fourteenth-straight quarter of year-over-year revenue growth for the index. Over the past ten years, on average the actual reported earnings by S&P 500 companies have exceeded estimates by 6.7%. Looking ahead, analysts have cautiously lowered estimates but still anticipate year-over-year earnings growth of +10.3% for 2024, accelerating and broadening though year end and into 2025 (*chart*). Valuations are not stretched. The current forward 12-month P/E ratio for the S&P 500 is 19.9, marginally above the 5-year average of 19.1. The bottom-up target for the S&P 500 is 5750, which is 15.7% above Friday's closing level of 4967.

Despite the recent pullback, markets remain healthy and supported by the weight of evidence. Valuation and sentiment are not stretched. The economy has and should continue to expand with interest rates higher for longer. Moderate economic growth, strong balance sheets, an earnings tailwind, coupled with a more normalized rate environment, should support a continued broadening of equity market returns and positive performance. Employment, and thus consumer spending (2/3 of GDP), continues to be the key economic barometer to follow.

Our playbook continues to focus on significant secular, cyclical, and structural trends. A few important themes we are following are reshoring of industry and reconfiguration of supply chains, infrastructure supporting massive investment in data center and AI, and underinvestment in energy and commodities. Additional themes include impacts of AI on productivity and innovation and rising geopolitical tensions. We favor high-quality growth at reasonable prices and businesses with stable free cashflow and healthy balance sheets. We will continue to balance growth and value and are prepared to shift defensively if necessary.

Near term, we are neutral as the market consolidates recent gains. It has been a good time to take some profits and be prepared to shift more defensively. Long term, we remain bullish and will be patient. Election years bring change, and we are optimistic.

We are pleased to welcome Peter Kissel to Morse Asset Management. Peter brings with him over 20 years of equity research experience. We look forward to his contribution to our investment team.

Robert B. Morse

Chief Investment Officer

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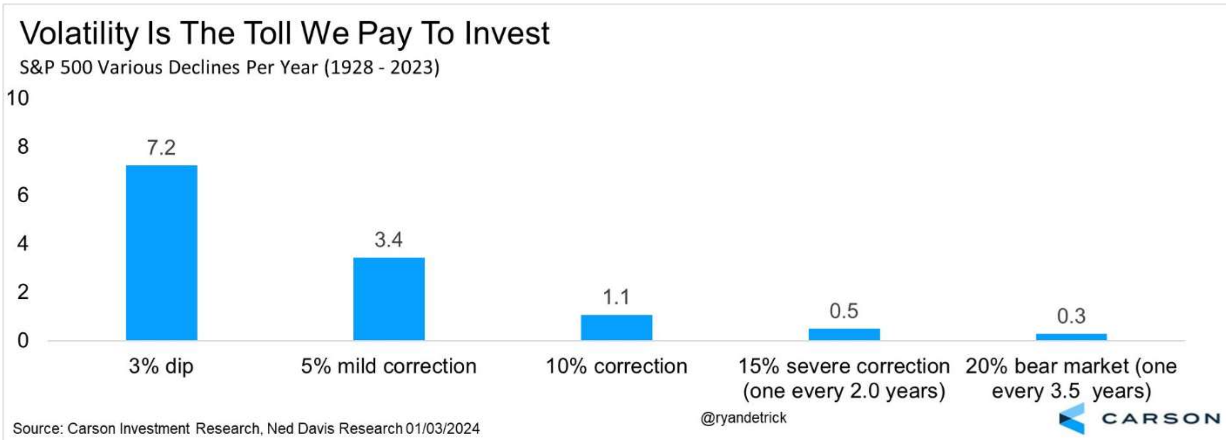

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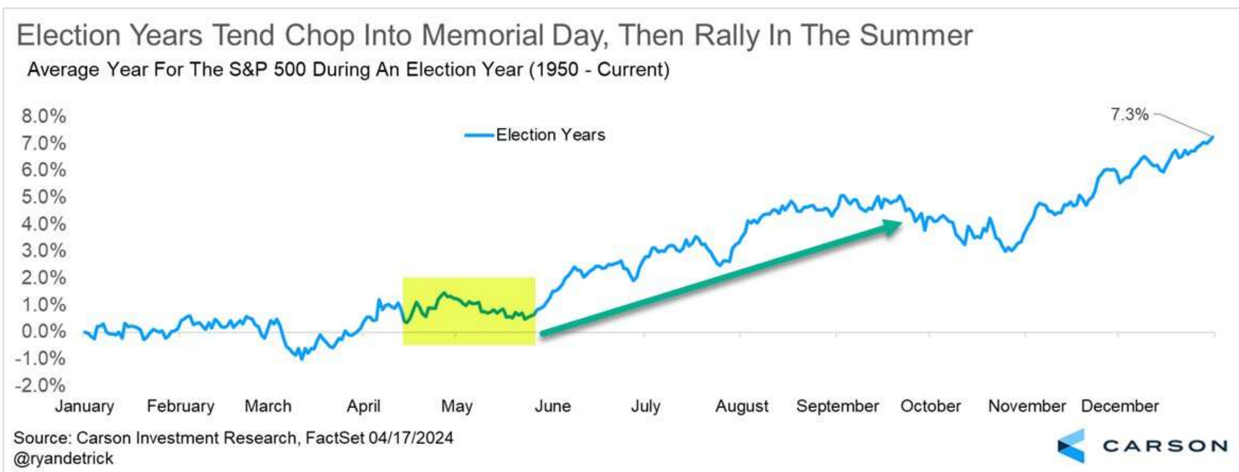

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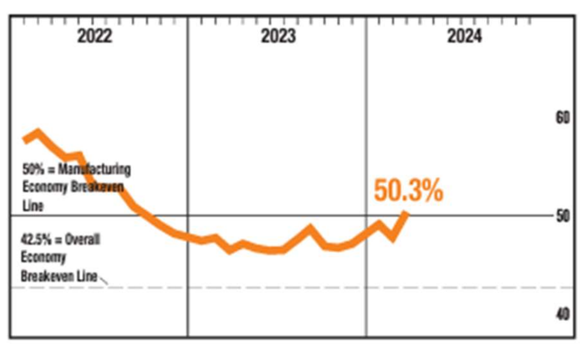
MANUFACTURING
PMI® at 50.3%

The U.S. manufacturing sector expanded in March, as the Manufacturing PMI® registered 50.3 percent, up 2.5 percentage points compared to February's reading of 47.8 percent. This is first instance of expansion in 16 months. Two out of five subindexes that directly factor into the Manufacturing PMI® are in expansion territory, up from one in February. The New Orders Index moved into expansion territory after one month of contraction.



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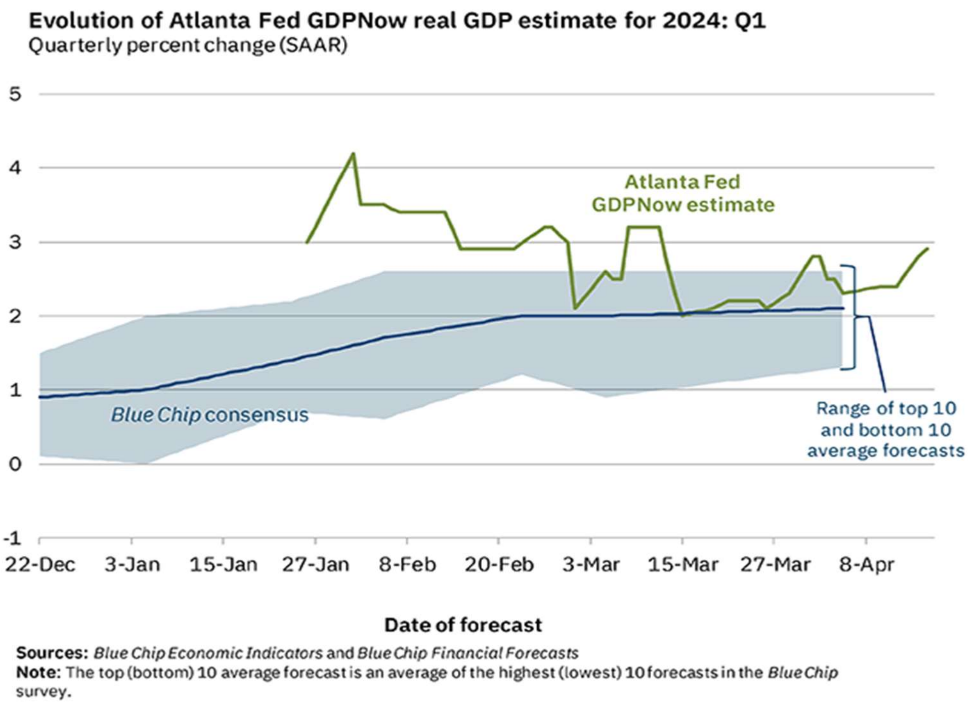

5. Chart: S&P 500 and 10-Year Treasury Yield.

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