Financial markets experienced elevated volatility in the third quarter, but as the final three months of 2024 get underway, stocks are at record highs and bonds are also producing solid returns. U.S. stocks, as measured by the S&P 500, rose throughout July, before experiencing an almost 10% decline in August due primarily to renewed recession fears. The sell-off did not last as the S&P 500 rallied to new highs and finished the quarter up 5.5% (and over 20% for the year, both excluding dividends). For the first time in a while, large U.S. stocks are not leading the way, as the Russell 2000 (index of smaller U.S. companies) was up almost 9% in the quarter and international stocks, as measured by the MSCA ACWI Ex USA index, were up over 7%. Moreover, the U.S. technology sector, which has been leading the market higher for several years, was among the worst sectors in the quarter, while utilities and real estate stocks were among the best. So, as was the case in late 2023 and into the first quarter of 2024, market breadth is improving again. As we have discussed in prior letters, we believe that is a positive development, however, it remains to be seen if that improving breadth will prove sustainable.

Equity Indexes	Q3, 2024	YTD	2023
S&P 500	5.5%	20.8%	24.2%
Russell 2000 (Small Cap)	8.9%	10.0%	15.1%
MSCI EAFE (Developed)	6.7%	10.4%	15.0%
MSCI Emerging Markets	7.8%	14.4%	7.0%
MSCI ACWI Ex USA	7.4%	11.7%	12.6%

Note: All returns exclude dividends

Fixed Income Indexes	Q3, 2024	YTD	2023
Bloomberg Barclays US Agg Bond	5.2%	4.4%	5.5%
Bloomberg Barclays Municipal Bond	2.7%	2.3%	6.4%

Source: Orion

In another positive development, bonds provided a nice offset to the equity market weakness during the August sell-off. While the equity market declined almost 10% from its peak in mid-July to early August, bond prices rose roughly 2% as the yield on the 10-year Treasury note fell almost 75 basis points from 4.48% to 3.75%. For the quarter, U.S. bonds (as measured by the Barclays Aggregate Bond Index) were up 5.2%, erasing losses during the first half of the year, bringing year-to-date gains to 4.4% and 12-month returns to over 10%. We include an allocation to bonds in most of our portfolios for the income that they generate and because they have historically been negatively correlated with stocks during years in which equity market returns were negative (see chart below).

Bonds: A Great Diversifier When Stocks Fall, Despite 2022

Year	Stocks	Bonds
2022	-18.1%	-12.5%
2018	-4.4%	0.9%
2008	-37.0%	13.7%
2002	-22.1%	11.8%
2001	-11.9%	6.7%
2000	-9.1%	13.5%
1990	-3.1%	8.5%
1981	-4.9%	9.2%
1977	-7.2%	2.7%
1974	-26.5%	7.1%

Source: Morningstar

The steady income and the negative correlation with equities helps to reduce overall portfolio volatility, which is important because it minimizes the prevalence of those panic moments and keeps investors from making emotional market-timing mistakes. Combining uncorrelated asset-classes also enables portfolio rebalancing opportunities where we can reduce exposure to the asset class that has done well recently (and may be less attractively valued) and redeploy the proceeds into the asset class that has underperformed (and may be more attractively valued). We have argued for a while now that bonds were attractively valued and well positioned to perform their historical role as a source of income and a hedge against equity market risks, so we were encouraged to see that play out during the quarter.

Underpinning the equity market's rebound was the resolution of months of investor uncertainty over interest rates. With the economy slowing, unemployment beginning to rise, and inflationary pressures easing, the Fed reduced its target rate by half a percentage point at its September meeting, and investors now expect the central bank to continue pushing rates lower.

Over the past 50 years, the S&P 500 returns 4.9% on average one year after the first interest rate cut, seeing positive returns nearly 70% of the time. However, much depends upon how much the Fed will cut interest rates and how the economy will respond to those rate cuts. If the economy falls into a recession and the Fed is forced to cut rates aggressively, equity markets tend to do poorly. For instance, U.S. equities saw double-digit declines after the first rate cuts in 1973, 1981, 2001, and 2007. On the other hand, if the rate cuts successfully stimulate economic activity and the Fed can gradually move rates lower,

equity markets tend to do well. The two most favorable outcomes were in 1982 when the S&P 500 surged 36.5% and in 1998 when it rose 27.3%. In the most recent rate cut cycle (2019), the S&P 500 jumped by 14.5% in the following year.

Finally, we want to briefly touch on the upcoming presidential election, as we continue to receive numerous inbound calls expressing concern about the impact of the election on financial markets. Back in March we sent out an email with our detailed thoughts on the election. If you would like to see it again, you can access the note on our website at https://www.whitneyandcompany.com/politics/.

In a nutshell, while we understand that political views can stir strong emotions, we don't believe making investment choices based on those feelings will lead to optimal portfolio decisions. Data suggests that whichever party occupies the White House has little to no impact on investment performance, with fundamental factors like corporate earnings growth and valuations impacting the stock market far more than political headlines. The U.S. economy's success, growth, and resiliency does not change with each new election, and neither should your long-term investment strategy.

As always, please do not hesitate to reach out with any questions or concerns you may have regarding your individual investment portfolio.

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