MARKET AND ECONOMIC REVIEW & OUTLOOK

AN UPDATE FROM THE ADVISORS AT GASKIN ASSET MANAGEMENT *CHARLOTTE, NORTH CAROLINA*

The following letter was written for you by the undersigned. The opinions expressed are those of your advisors at Gaskin Asset Management and do not necessarily reflect the opinions of Raymond James or its affiliates. We know this is a long letter, but we hope you will invest five minutes in reading it. Thank you.

STOCK MARKET

After an impressive run last year for the "Magnificent 7" companies (Apple, Nvidia, Microsoft, Amazon, Tesla, Alphabet, and Meta) some but not all have continued their forward progress into 2024. As we've stated in previous letters, the S&P 500 stock index is capitalization-weighted which means not all stocks have an equal impact on the index's performance. In fact, the "Mag 7" makes up nearly 30% of the index's weighting yet accounted for more than 60% of last year's performance.[i] That's not a typo. Only seven out of 503 stocks based on the current market makeup are credited with 60% of last year's performance. As of March 31, 2024, the Mag 7 is still leading the way with credit for more than 1/3 of the market's positive performance. However, not all are contributing this year with both Apple and Telsa experiencing price declines.

There are many questions facing the markets going forward including how much steam remains in the Artificial Intelligence (AI) rally that began in late 2022 following the launch of ChatGPT. We believe the future of AI is beyond imagination today in much the same way that none could have possibly known how the internet would affect future generations. But just as there were many starts and stops in the automotive industry, cell phones, and frankly every new technological breakthrough in history, there will be Artificial Intelligence winners and losers in the future. Put simply, not all AI companies will succeed. We believe a goal for growth investors is to benefit directly and indirectly in the AI future while keeping our wits about us. Speaking of wits, the average price-to-earnings (P/E) multiple for the Mag 7 stocks was nearly 34 at the end of March, whereas the average for the remaining 493 stocks was less than 20. Just as home values can differ dramatically from city to city and neighborhood to neighborhood, stock valuations will vary based on many factors including P/E multiples. The Mag 7 stocks are not necessarily expensive in our judgment, but they certainly aren't comparatively cheap either. Maybe there are opportunities with some of the other 493 …

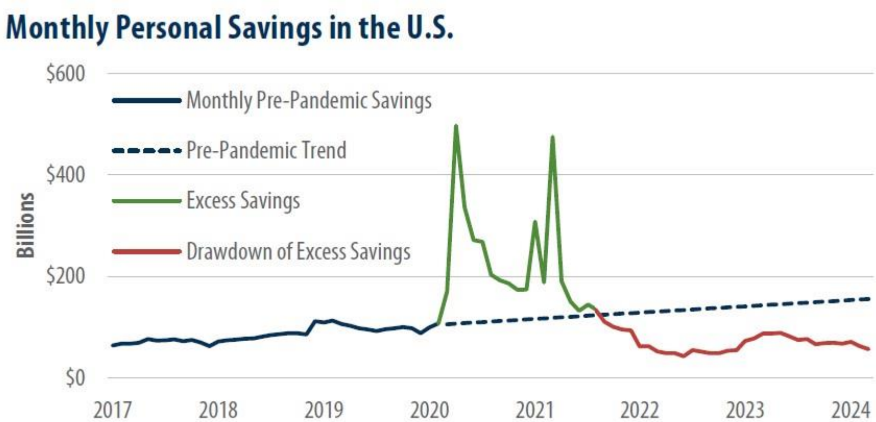
BOND MARKET

The U.S. bond market yield curve remains inverted with 1-month Treasury Bills yielding approximately 5.25% as of May 5, 2024, while 10-year Treasury Notes yield around 4.5% and the 30-year U.S. treasury hovers around 4.6%[ii]. Every recession in modern history has been preceded by an inversion of bond market yields but not every inversion has been followed by a recession. Did you catch that important detail? The current yield inversion has been in place since July 2022 and ranks as the longest yield inversion on record according to Davide Barbusia of Reuters.[iii] So, it's hard to say if the bond market is forecasting a recession or simply anticipating the Fed lowering rates later this year.

As of April 30, 2024, the S&P U.S. Treasury Bond Current 30-Year Index is down -10.47% year-to-date after a slight gain in 2023 following the loss of -33.45% in 2022.[iv] The bond market volatility has had far-reaching effects on investment portfolios and allocations of capital. For instance, according to Larry Adam, Raymond James Chief Investment Officer, cash is currently outperforming bonds on a rolling 10-year average for only the second time since 1980.[v] Bonds have been clobbered. Maybe it's time to take advantage of the bond market weakness.

THE ECONOMY

U.S. real gross domestic product (GDP) increased at an annual rate of 1.6% in the first quarter of 2024 according to the "advance" estimate released by the Bureau of Economic Analysis after increasing at a rate of 3.4% in the fourth quarter of 2023.[vi] This represents a slowdown from the average of 3.1% for 2023 and likely provides the Fed with the necessary data to increase their comfort with lowering rates later this year. While much of the early economic growth during the pandemic consisted of goods sales such as autos, home building, boats, and various other goods, growth has been shifting to services. According to First Trust Advisors, "real" retail sales outside the auto sector declined at an annual rate of -3.0% in the first quarter while auto sales declined -8.7%.[vii] Interestingly, First Trust notes that while purchases of goods are declining, real services spending increased at a rate of 4.7% pace in the first quarter.



Source: Bureau of Economic Analysis, Federal Reserve Bank of San Francisco,First Trust Advisors. Monthly data 1/2017 - 3/2024.

Can growth continue at a slower rate without the economy slipping into recession? And will inflation eventually drop to the Fed's target rate of 2%? The chart to the left may provide a hint to one reason why it seems the average citizen is not exactly enthused about their economic outlook these days and why consumer confidence readings have sunk to the lowest level since July 2022.[viii]

We have commented in previous letters that we believe the inflation experienced in recent years is due to a reduction in supply of goods and limited services coupled with a simultaneous increase in demand. Any first year Economics 101 student could make this observation. Then again, anyone who has ever purchased practically anything understands the law of supply and demand. This chart focuses on demand and provides a graphic illustration of consumer demand "capacity." The green "excess savings" line tracks the excess cash consumers accumulated during the early days of the pandemic. With the combination of various government stimulus payments, supply lines gummed up, and individuals afraid to venture out, savings rates naturally increased. From March 2020 to August 2021, personal savings increased above the trendline by $2.1 trillion.[ix] Eventually, consumers started spending while supply lines remained constrained which led to the inflation rates the Fed has been fighting with higher interest rates. The red line tracks the spending levels beyond excess savings and represents the conundrum we find ourselves in now. With the $2.1 trillion in excess savings having now been absorbed, we are in a new position. This may be the very thing that slows the economy enough to depress prices and allow the Fed to claim victory over inflation and begin lowering rates. Then again, with consumers having depleted their excess savings, we may be entering a more challenging time for the U.S. consumer.

RECOMMENDATION

Our team consumes an enormous amount of financial data every day including concrete black & white numbers, trendlines, projections, estimates, opinions, and everything in-between. If we wanted to find good news about the economy and markets, we could surely find it and present it to you. On the other hand, if we wanted to paint a dreadful picture, we could do that also. All our research leads to the following "shocking" conclusion: No one knows with any certainty what the next chapter of our economy and the markets holds. That leaves us to prepare for the unknown given the experience and information we have. Since we're investors and not gamblers, you can rest assured that we plan to approach each investment decision from a long-term risk-adjusted perspective. If you would like to discuss how we envision specific investment vehicles and strategies playing out in the coming months, please give us a call or shoot us an email. We would be delighted to have the opportunity to discuss your views, plans, goals, or concerns. Until then, we hope you can get outdoors and enjoy the warmer weather.

Best wishes,

Robert J. Gaskin, CIMA®
Managing Principal
Senior Financial Advisor, RJFS

[i] "Three for Thursday", First Trust Economics. April 4, 2024.
[ii] Source: FactSet. May 5, 2024.
[iii] https://www.reuters.com/markets/rates-bonds/us-treasury-key-yield-curve-inversion-becomes-longest-record-2024-03-21/#:~:text=The%20part%20of%20the%20Treasury,in%20a%20note%20on%20Thursday.
[iv] Source: S&P Dow Jones Indices. April 30, 2024.
[v] Raymond James. Up & Adam. May 3, 2024.
[vi] U.S. Bureau of Economic Analysis. https://www.bea.gov/news/2024/gross-domestic-product-first-quarter-2024-advance-estimate
[vii] First Trust Advisors, "Continued Growth in Q1", Monday Morning Outlook. April 22, 2024.
[viii] Raymond James, "Monthly Market Review", April 2024, p.1

[ix] First Trust Advisors, "Three on Thursday", May 2, 2024.