# Capital Market Review

March 31, 2024

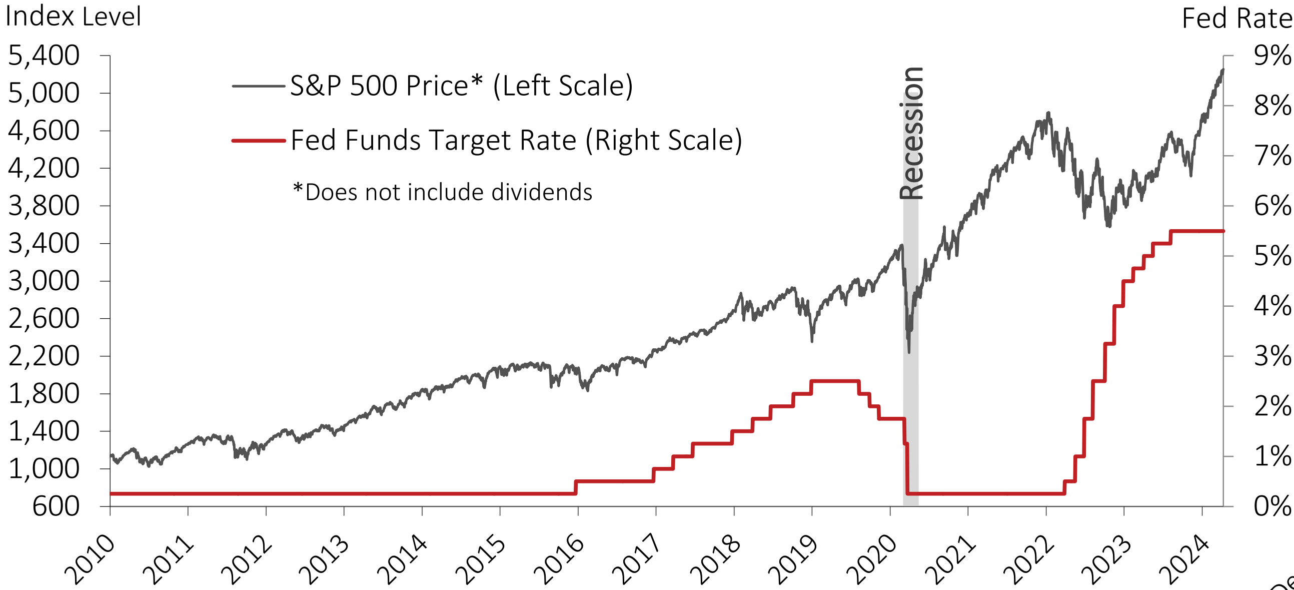


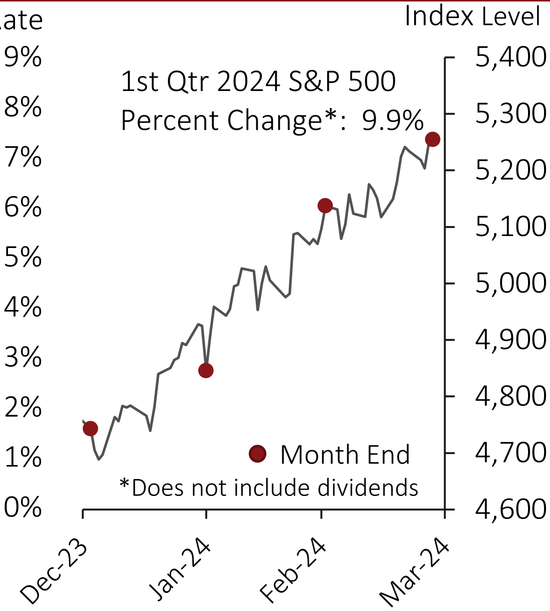

DeMarche

Watch the Capital Markets Review Key Takeaways Video

# Market / Economic Overview

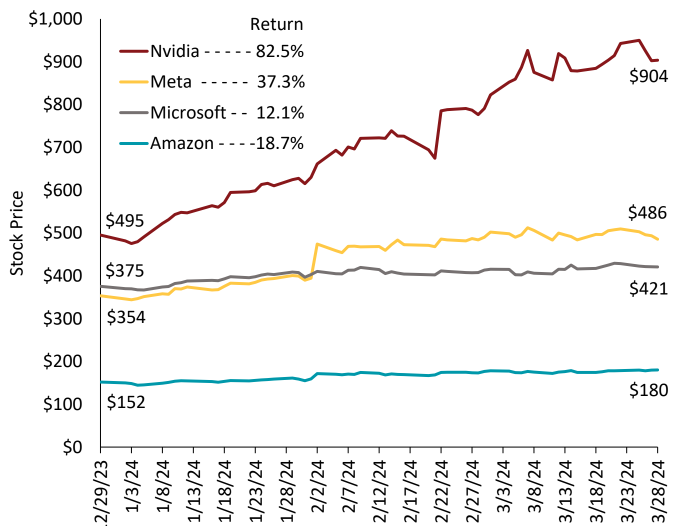
# Rates: Higher For Longer




*Source: Standard & Poor's, Federal Reserve*

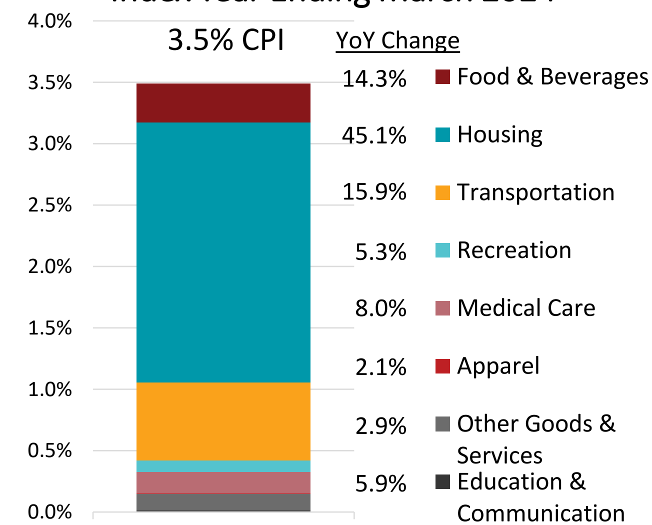
Returns of Major Stocks in S&P 500
First Quarter 2024




*Source: S&P, DeMarche*

2024 started out good for the capital markets, continuing its winning streak. The S&P 500 hit a new high in the first quarter. This quarter the so-called "Magnificent Seven" became the "Fab Four" as Nvidia and three others drove the index forward. Interest rates increased as markets digested more economic data suggesting that the Fed would keep rates "higher for longer." CPI continues to be stubborn. The chart to the right shows that shelter costs remain the sticking point as the main driver of the increase in inflation, contributing over 45% to the increase. This stubbornness should keep the Fed on the sideline most of the year. In fact, the futures markets expect only one to two rate cuts by the end of the year.

Contribution to Consumer Price Index Year Ending March 2024




*Source: Bureau of Labor Statistics, Contribution is change x weight*

# Broad Market Overview

March 31, 2024

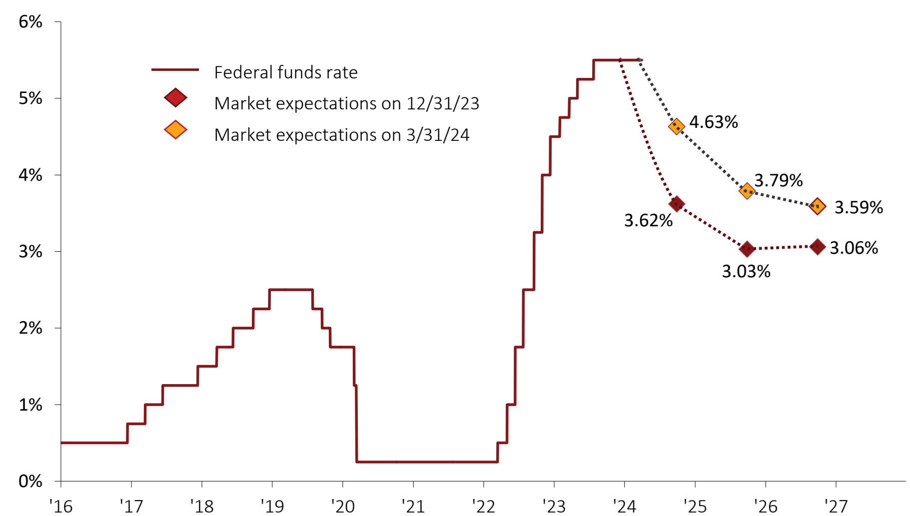
| INDEX | 1st Qtr | 1-YEAR | 3-YEAR | 5-YEAR | 10-YEAR |
|---|---|---|---|---|---|
| MSCI World | 8.9 | 25.1 | 8.6 | 12.1 | 9.4 |
| Russell 3000 | 10.0 | 29.3 | 9.8 | 14.3 | 12.3 |
| S&P 500 | 10.6 | 29.9 | 11.5 | 15.0 | 13.0 |
| MSCI EAFE USD | 5.8 | 15.3 | 4.8 | 7.3 | 4.8 |
| MSCI Emerging Markets USD | 2.4 | 8.2 | -5.1 | 2.2 | 2.9 |
| Bloomberg Aggregate | -0.8 | 1.7 | -2.5 | 0.4 | 1.5 |
| Bloomberg Global Aggregate | -2.1 | 0.5 | -4.7 | -1.2 | -0.1 |
| FTSE Non-US Gov't Bond | -3.4 | -1.5 | -8.4 | -3.7 | -1.9 |
| NAREIT (Public RE) | -1.3 | 8.4 | 2.0 | 3.6 | 6.7 |
| Bloomberg Commodity | 2.2 | -0.6 | 9.1 | 6.4 | -1.6 |

*Notes: Data are presented as percent returns. All 3-, 5-, and 10-year returns are annualized.*

| U.S. Indicators Yr. Ending 3/31 | 2024 | 2023 | 2022 | 2021 | 50 Yr. Average |
|---|---|---|---|---|---|
| GDP Annual Growth Rate* | 2.9 | 1.7 | 3.6 | 1.6 | 2.6 |
| Unemployment | 3.8 | 3.5 | 3.6 | 6.0 | 6.2 |
| Inflation (CPI) | 3.5 | 5.0 | 8.5 | 2.6 | 3.8 |
| 10-Year Interest Rates | 4.2 | 3.5 | 2.3 | 1.7 | 6.0 |

**Note: Prior to the GDP quarterly release from BEA, we show the annual GDP Growth rate from OECD weekly tracker as the most recent year.*

## Federal Funds Rate Market Expectations




*Source: Federal Reserve, J.P. Morgan*

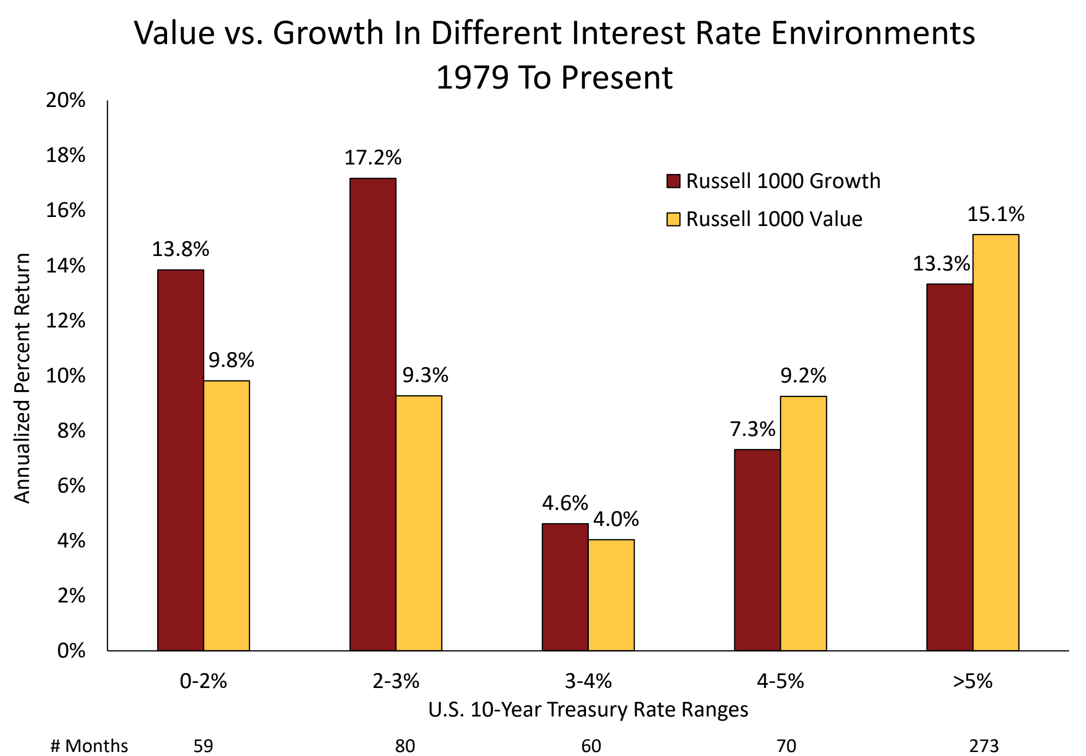
- The S&P 500 continued its winning streak in the first quarter of 2024, returning 10.6%. Market returns have been narrow, as four stocks – Nvidia, Amazon, Meta and Microsoft – account for almost half of the market's return for the quarter. These four stocks have now been coined as the "Fab Four," as Tesla and Apple posted negative first quarter returns, and Google barely made it into positive territory.
- Bond returns suffered in the quarter as interest rates increased. Expectations for a Fed rate cut waned a bit as economic data continues to show inflation to be troublesome. The yield on the 10 year Treasury increased from 3.87% at the end of 2023 to 4.21% at the end of the first quarter. The Bloomberg Aggregate posted a negative return for the quarter, after posting a 5.5% return for all of 2023.
- The last two months of 2023 provided a tailwind to international stocks as the dollar weakened. The trend reversed itself in the first quarter and the dollar strengthened as expectations for rate cuts waned. International returns trailed domestic returns in the quarter, as a result. The MSCI EAFE returned 5.8% for the quarter.
- The chart to the left shows the change in the market expectation for a fed fund rate cut. In the space of three months, the market has backed out at least 100 basis points by the end of 2024. This change in expectations has fueled the "higher for longer" mantra evident in higher interest rates along the maturity curve.

### DeFact

Despite expectations that the Federal Reserve will begin to cut interest rates in later 2024, money market funds continue to hold record amounts of cash. Money market funds hold about $6.5 trillion in assets. Market observers have noticed that a majority of money being invested in money market funds has come since the collapse of Silicon Valley Bank suggesting investors view money market funds as a safer alternative. ~WSJ

| INDEX | 1st Qtr | 1-YEAR | 3-YEAR | 5-YEAR | 10-YEAR |
|---|---|---|---|---|---|
| S&P 500 | 10.6 | 29.9 | 11.5 | 15.0 | 13.0 |
| S&P Mid-Cap 400 | 10.0 | 23.3 | 7.0 | 11.7 | 10.0 |
| S&P Small-Cap 600 | 2.5 | 15.9 | 2.3 | 9.1 | 8.8 |
| Russell 1000 | 10.3 | 29.9 | 10.5 | 14.8 | 12.7 |
| Russell 1000 Growth | 11.4 | 39.0 | 12.5 | 18.5 | 16.0 |
| Russell 1000 Value | 9.0 | 20.3 | 8.1 | 10.3 | 9.0 |
| Russell 2000 | 5.2 | 19.7 | -0.1 | 8.1 | 7.6 |
| Russell 2000 Growth | 7.6 | 20.3 | -2.7 | 7.4 | 7.9 |
| Russell 2000 Value | 2.9 | 18.8 | 2.2 | 8.2 | 6.9 |

*Notes: Data are presented as percent returns. All 3-, 5-, and 10-year returns are annualized.*



*Source: DeMarche*

- Small cap stocks benefitted from market rate cut expectations late in 2023 but still fell short of large caps in the first quarter. Small cap stocks, as measured by the Russell 2000, gained 5.2% in the quarter, 5.1 percentage points behind their large cap cousins. Small cap financials, a large weight in the index, posted a negative return in the quarter.

- The song remains the same for large cap growth stocks in the quarter as the Fab Four led returns. Large cap growth stocks now lead value stocks in all time frames. Small cap growth stocks have done better in the quarter but still lag in the three- and five-year time frames. Small cap technology and industrials, large weights in the growth index, posted strong returns of over 34% and 28%, respectively. Small cap financials, the largest weight in the value index, posted negative returns.

- The chart to the left shows the dominance of growth stocks in low rate environments. Value stocks tend to outperform in higher interest rate environments. The reasoning is that the market is a discounting mechanism, and discounting cash-flows of growth stocks at a higher rate leads to a lower present value. The ten-year Treasury began the quarter below 4% and ended it above 4%.

## DeFact

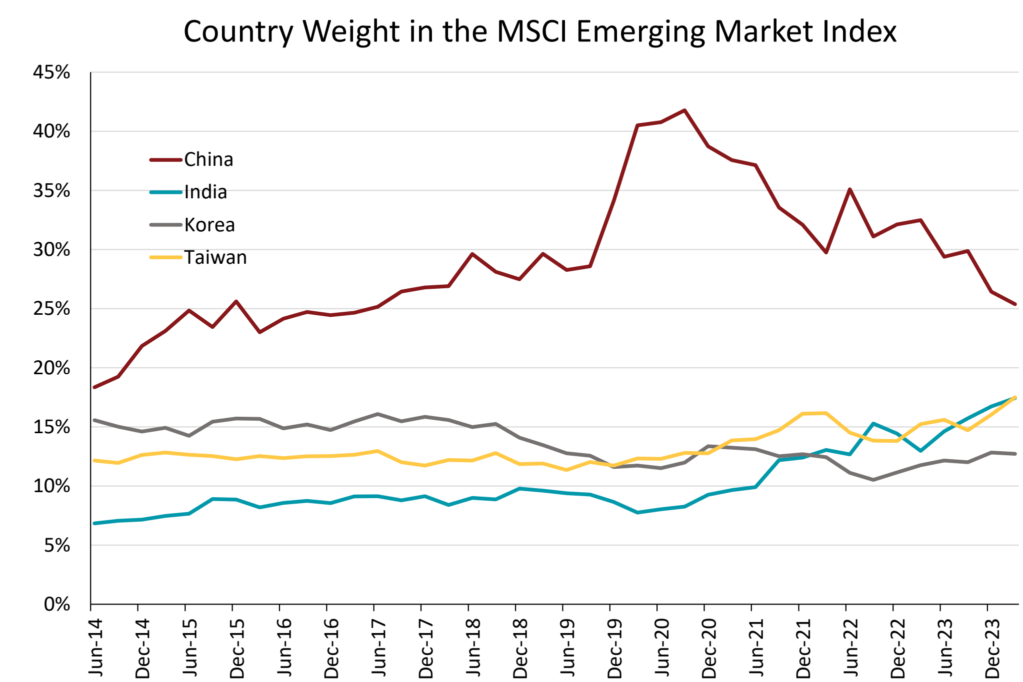
For the first time, passive investment products held more assets than their actively managed counterparts. The total on hand for ETFs and passively managed mutual funds totaled $13.3 trillion. Actively managed funds totaled $13.2 trillion. This event raises concerns among market observers that this trend will undermine the efficient market hypothesis that passive funds rely upon. A 2023 NBER study argues that indexing impedes the incorporation of information into stock prices. ~NBER, CNBC

# International Equities



| INDEX | 1st Qtr | 1-YEAR | 3-YEAR | 5-YEAR | 10-YEAR |
|---|---|---|---|---|---|
| MSCI EAFE Local | 10.0 | 18.8 | 9.4 | 9.4 | 7.7 |
| MSCI EAFE USD | 5.8 | 15.3 | 4.8 | 7.3 | 4.8 |
| Growth | 7.0 | 13.3 | 2.8 | 7.8 | 5.9 |
| Value | 4.5 | 17.3 | 6.6 | 6.4 | 3.5 |
| MSCI All Country-ex US | 4.7 | 13.3 | 1.9 | 6.0 | 4.3 |
| MSCI AC Asia-ex Japan | 2.4 | 4.0 | -6.8 | 1.9 | 4.2 |
| MSCI Emerging Markets | 2.4 | 8.2 | -5.1 | 2.2 | 2.9 |
| MSCI EAFE Small Cap | 2.4 | 10.4 | -1.4 | 4.9 | 4.7 |
| MSCI Japan | 11.0 | 25.8 | 3.7 | 7.8 | 6.7 |
| MSCI China | -2.2 | -17.1 | -18.9 | -6.3 | 1.2 |
| MSCI Germany | 7.1 | 14.8 | 1.1 | 6.3 | 2.7 |
| MSCI France | 5.9 | 12.1 | 8.4 | 9.5 | 6.0 |
| MSCI UK | 3.1 | 10.9 | 7.7 | 5.1 | 2.9 |

*Notes: Data are presented as percent returns. All 3-, 5-, and 10-year returns are annualized*




*Source: MSCI, DeMarche*

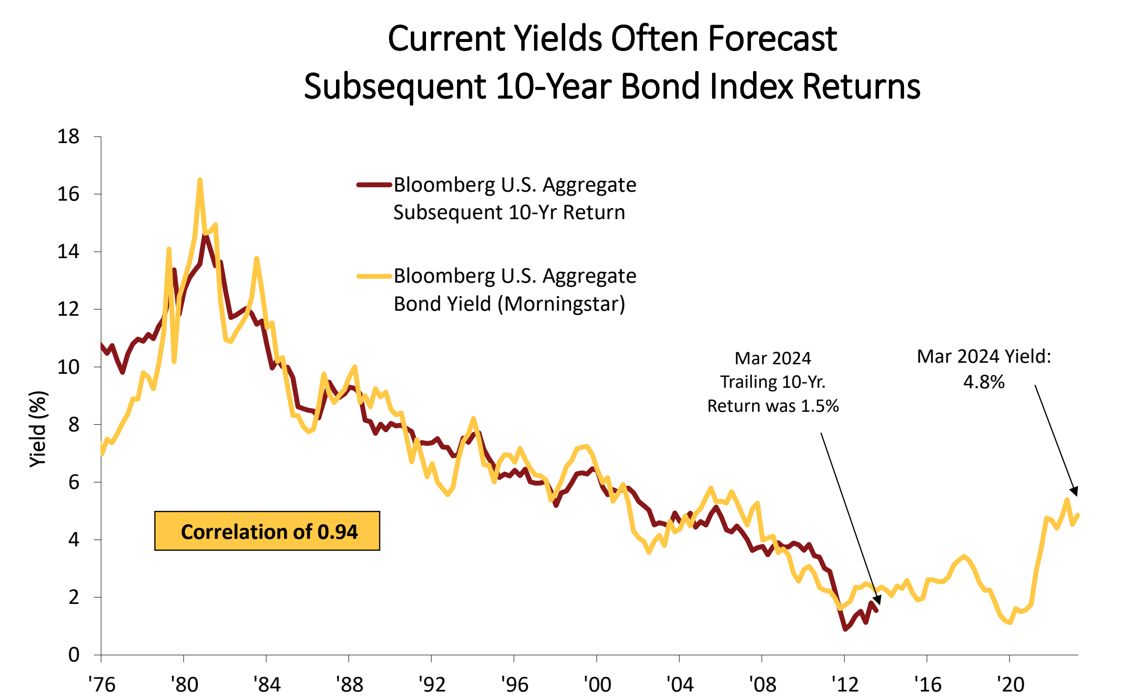
- International stocks did well in the quarter but were held back by the dollar strengthening as interest rates rose. A 10% quarterly return in local currencies translated to 5.8% in dollars. Over the past decade, the dollar has maintained strength against other global currencies as reflected in more modest longer term returns priced in dollars. For example, the ten-year return is just 4.8% in dollars versus 7.7% in local currencies.
- Chinese stocks fell 2% in the quarter and over 17% for the past year. Chinese stocks have now posted negative returns for eight of the past twelve quarters (three years). The weight of China in the emerging markets index has fallen to 25%, down from 30% at the end of third quarter.
- Japanese stocks performed the best among international developed countries. Toyota Motor gained over 37% in the quarter. Japan's market even outperformed the S&P 500 for the quarter. This performance led the Nikkei to hit an all-time high in the quarter – a height last reached in 1989.
- The chart to the left shows the dominance of Chinese stocks within the Emerging market index over the past two decades. China's weight in the index peaked above 40% in 2020 but has since eroded to about 25% due to strong relative performance from India and Taiwan and poor performance of Chinese stocks.

## DeFact

After narrowly avoiding a recession in 2023, the Eurozone (0.1% growth) continues to struggle with recession fears in the first quarter of 2024. Germany, Europe's largest economy, has been wrestling with higher energy costs. The UK actually shrank in 2023 by 0.2% as its manufacturing sector is contracting. Japan's economic growth slowed in the second half of 2023, also narrowly avoiding a recession. ~Reuters

| INDEX | 1st Qtr | 1-YEAR | 3-YEAR | 5-YEAR | 10-YEAR |
|---|---|---|---|---|---|
| Bloomberg Aggregate | -0.8 | 1.7 | -2.5 | 0.4 | 1.5 |
| Bloomberg 1-3 Gov Credit | 0.4 | 3.5 | 0.2 | 1.4 | 1.3 |
| Bloomberg Gov Credit Long | -2.4 | -1.1 | -6.0 | -0.6 | 2.3 |
| Bloomberg US TIPS | -0.1 | 0.5 | -0.5 | 2.5 | 2.2 |
| ICE BofA Merrill Lynch High Yield | 1.5 | 11.0 | 2.2 | 4.0 | 4.4 |
| CSFB Leveraged Loan (bank loans) | 2.5 | 12.4 | 5.8 | 5.3 | 4.6 |
| Bloomberg Global Aggregate | -2.1 | 0.5 | -4.7 | -1.2 | -0.1 |
| JPM EmgMkt Bd Glbl Dvrsfd (hard) | 1.3 | 9.6 | -1.5 | 0.5 | 2.7 |

*Notes: Data are presented as percent returns. All 3, 5-, and 10-year returns are annualized.*




*Source: DeMarche, Morningstar*

- Late last year, rates fell and when coupled with higher starting yields, earned a 5.5% return for the Bloomberg Aggregate in the 4th quarter. That trend reversed itself dramatically in the first quarter as rates increased as prospects for Fed rate cuts diminished. The Aggregate posted a negative 0.8 return for the first quarter.

- Increasing interest rates hurt high yield bonds also, but the higher starting coupon helped high yield post a 1.5% return for the quarter. One-year returns are robust for high yield due to the greater credit spread when compared to investment grade bonds. Floating rate bank loans posted the best returns for the quarter at 2.5% and 12.4% for the one year.

- Increasing rates across the globe coupled with a stronger dollar drove international bonds. Longer-term global returns show the same theme as domestic returns – increasing interest rates decrease bond prices and therefore, total return.

- The chart to the left shows how subsequent long-term returns of bonds are highly correlated to their current yield. If a dollar was invested in the Aggregate in March 2014, the subsequent return was 1.5%, pretty close to what the yield was at that time. It is reasonable to assume that if a dollar was invested in the Aggregate now, the subsequent ten-year return would be close to 4.8%, the current yield.

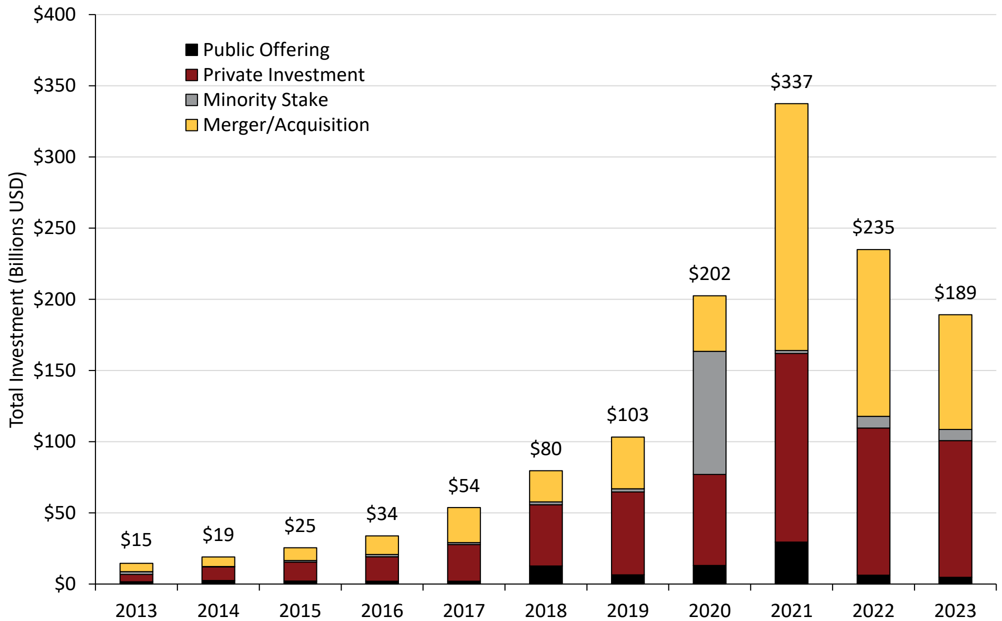
## DeFact

Finally, the Bank of Japan increased interest rates in 2024 after not raising rates for 17 years. Japan's central bank decided to increase short term interest rates to 0.0% to 0.1%. Rates were a negative 0.1% in December. In Europe, expectations now suggest interest rate cuts beginning in June 2024 as inflation cools more than expected and economic growth wanes. ~Reuters

| INDEX | 1st Qtr | 1-YEAR | 3-YEAR | 5-YEAR | 10-YEAR |
|---|---|---|---|---|---|
| NCREIF ODCE | -4.8 | -12.0 | 4.9 | 4.2 | 7.3 |
| NCREIF Property (Private RE) | -3.0 | -7.9 | 4.6 | 4.3 | 6.8 |
| Apartment | -3.0 | -7.3 | 6.0 | 5.0 | 6.7 |
| Industrial | -2.3 | -4.1 | 16.3 | 14.8 | 14.2 |
| Office | -5.4 | -17.6 | -5.5 | -1.8 | 3.3 |
| Retail | -1.1 | -0.9 | 2.0 | 0.0 | 4.4 |
| NCREIF Timberland | 4.3 | 9.5 | 10.5 | 6.6 | 5.8 |
| NCREIF Farmland | 2.3 | 5.0 | 7.5 | 6.0 | 7.3 |
| HFR FOF Composite | 3.2 | 6.2 | 2.2 | 5.1 | 3.2 |
| Conservative | 1.9 | 5.5 | 4.3 | 5.2 | 3.4 |
| Diversified | 3.1 | 6.0 | 2.8 | 5.4 | 3.4 |
| Strategic | 6.5 | 9.7 | 1.0 | 5.4 | 3.3 |
| Preqin Private Equity | 1.5 | 6.3 | 13.0 | 15.9 | 14.2 |
| Preqin Private Debt | 2.8 | 10.4 | 11.9 | 9.8 | 8.4 |
| Preqin Infrastructure | 2.6 | 8.6 | 14.7 | 11.8 | 10.9 |

*Notes: Data are presented as percent returns. All 3-, 5-, and 10-year returns are annualized.*
*All data in the table above are as of 12/31*

Global Corporate Investment in AI by Investment Activity




*Source: Stanford University*

- Real estate continues to reprice in the face of a slowing economy and higher interest rates. For 2023, real estate values have declined 12%, as measured by the ODCE. Office real estate continues to reprice lower. The industrial sector, which has boosted longer-term returns, now is posting negative twelve-month returns.
- Private equity returns lag public equity returns. You see in the table that returns in the fourth quarter are slightly positive as compared to strong fourth quarter public market returns for stocks. Private equity returns also usually do not experience the high highs and the low lows of public equities quarter to quarter.
- Artificial intelligence investment has driven a lot of return mania in the past few quarters and years. Nvidia, in the AI chip market, has become a darling because of it. Other large tech companies have been in the fray by buying up others over the past few years with Apple leading the way. The chart on the left also shows that AI is prominent in the private equity space, with significant increase in investment over the past few years.

## DeFact

Office rents have held firm despite a record amount of available space. Reasoning is that lowering rents would reduce appraised values of buildings which could lead to loan covenant defaults. Instead, building landlords are trying to justify higher rents by providing tenants incentives such as paying for build-outs and rent abatements. It is figured that businesses occupy 200 million square feet less office space than they did before the Covid recession of 2020. ~WSJ

# New DeMarche Headquarters


DeMarche has a new state-of-the-art headquarters located in the Corporate Woods office park (Building 27) in the metro Kansas City area.

Our new address is:

**10975 Grandview Drive**

**Suite 500**

**Overland Park, KS 66210**

Our phone numbers and email addresses remain the same.

# 41st DeMarche Client and Investor Conference

## Theme Announced – Join us September 17-19, 2024

Our theme for the 41st DeMarche Client and Investor Conference is **Catalysts for Portfolios: The Frontier.**

The risk and return profiles of institutional investment portfolios are changing as we enter the mid-2020s. New catalysts are emerging including artificial intelligence technologies, positive real yields in risk-free securities, shifts in consumer demand, and changes to workforce demographics. Investment products are evolving and offering new solutions for our investment challenges. To achieve the efficient frontier, which offers the highest expected return for a given level of risk, investors need to stay at the forefront of understanding the ever-changing world of investing.

During the conference, DeMarche's expert consultants and investment industry leaders will provide insights on solutions for client portfolios, best practices on portfolio design in this shifting landscape, and ideas for the catalysts that may emerge to lead markets and portfolios in the years to come.

Today's institutional investors must know where to find an edge. We will explore the gaps in market benchmarks, such as style or geography, different correlations in bond strategies, and evolving alternative investing strategies that address challenges in real estate, demographic trends, and business infrastructure.

Make this a catalyst year and plan now to attend the conference from September 17-19. Registration begins in early June.