Investment Tally & Perspective

MAJOR ASSET CLASS RETURNS					
	1st Qtr. 2024	1-Year	3-Year	5-Year	10-Year
Equities					
S&P 500 Composite	10.6%	29.9%	11.5%	15.1%	14.1%
MSCI EAFE Net	5.8%	15.3%	4.8%	7.3%	6.0%
MSCI EM (Emerging Markets) Net	2.4%	8.2%	-5.1%	2.2%	2.9%
Fixed Income					
Bloomberg US Aggregate	-0.8%	1.7%	-2.5%	0.4%	0.9%
Bloomberg US Corp Investment Grade	-0.4%	4.4%	-1.9%	1.5%	1.9%
Bloomberg Emerging Markets Unhedged	1.5%	8.4%	-1.5%	1.1%	1.6%
Other Assets					
Dow Jones US Select REIT	-0.4%	10.5%	3.7%	3.0%	4.1%
S&P GSCI	8.0%	12.7%	9.3%	11.5%	9.1%
S&P GSCI Gold Spot	10.4%	11.1%	18.1%	7.8%	8.2%

Source: Tamarac

All returns greater than one year are annualized

* The market indices discussed are unmanaged. Investors cannot directly invest in unmanaged indices

Market Activity - U.S. stocks, as measured by the S&P 500, started the year off strongly. Their 10.6% return in the quarter ranks as the sixth best over the past 36 years, according to Refinitiv data. Encouragingly, when the start of the year is so strong, it bodes well for the remaining quarters, too. Globally, stocks performed well. China was the major downside outlier, with Chinese equities posting negative returns in the first quarter, continuing the trend that began in 2023. The best performing stock market in Q1 was Japan, which is benefiting from a weaker yen, wage growth, and continued progress on corporate governance.

Fixed income ended the quarter slightly negative, as risk-free rates ended slightly higher than where they started the year. With the Bloomberg Aggregate sporting a yield-to-maturity of around 5% (per Refinitiv), we expect fixed income returns to be pulled into positive territory by year end, barring a major inflation scare.

Economic Activity – Fears of a recession are now largely eradicated. Probabilities of a recession in 2024 – whether from prediction markets or from Wall Street economists – are now reflective of long-term average levels. It is not hard to see why. Fourth quarter GDP grew 3.4%, while expectations for the first quarter point to 2.8% growth, per the Bureau of Economic Analysis (BEA) and the Federal Reserve Bank of Atlanta. Recent periods have been supported by consumer spending. These results are remarkable since we are now two years into one of the fastest hiking cycles on record and yet still producing above average economic growth with minimal job loss.

Excess savings are continuing to support the U.S. consumer. JP Morgan estimates consumers still have $800 billion more saved today (down from a peak of $2.3 trillion in mid-2021) compared to pre-pandemic levels, while BCA Research estimates consumers are sitting on $250 billion of excess cash. Wherever the truth lies, the takeaway is there is still some dry powder to support

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Ronald E. Albert, CEO

Brittany A. Moran, CFP

Sean McGuirk, CFA

Alexander Albert, CFP

Nina Walsh

Karen Jones Ariosta

Lincoln Capital Corp.
620 Main Street, CU 2
East Greenwich
Rhode Island, 02818
401.454.3040 (phone)
info@lincolncapitalcorp.com
www.lincolncapitalcorp.com

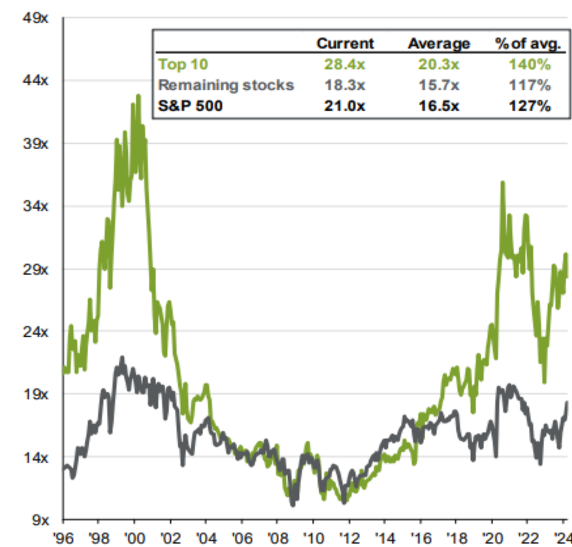
spending, but this tailwind is running out. Case in point: disposable personal income is up 2.3% from July 2023 levels while personal consumption expenditures are up 3.2%, per the BEA.

Inflation has bounced since the end of 2023, but not enough to materially change consensus expectations. The TIPs market is pricing in 2.4% inflation over the next five years, up from 2.1% at the start of the year, and a March 2022 peak of over 3.5%, per the Federal Reserve Bank of St. Louis. The bounce in five-year expectations is partly driven by recent price changes in crude oil—not the core inflation the Fed cares about. The three-month annualized core Consumer Price Index has accelerated from 3.3% in December to 4.2% in February due to spikes in housing, airfares, and healthcare, according to Morgan Stanley. Whether inflation resumes its downward trajectory over the coming months will be a critical datapoint to watch.

Monetary Policy – The Fed continues to be on hold and has so far brushed off concerns about recent economic and inflation strength. At their most recent meeting, rate expectations were held at previous forecasts for year-end 2024. There were minor hawkish tweaks, with a rate cut taken out of 2025, and an upward revision to terminal fed funds to 2.6% from 2.5%, per the Federal Reserve Board. Unlike in late 2023, the market is in a rare state of agreement with the Fed, penciling in a year-end fed funds rate of 4.72%, per Refinitiv.

The European Central Bank is in line with the Fed on their easing timeline. In March, the Swiss National Bank claimed the prize for first central bank to cut this cycle. Everyone is rowing in the same direction, save Japan. The Bank of Japan hiked in March, ending 8 years of negative rates.

P/E ratio of the top 10 and remaining stocks in the S&P 500
Next 12 months, 1996 - present



Weight of the top 10 stocks in the S&P 500
% of market capitalization of the S&P 500

Earnings contribution of the top 10 in the S&P 500
Based on last 12 months' earnings

Source: FactSet, Standard & Poor's, J.P. Morgan Asset Management.
The top 10 S&P 500 companies are based on the 10 largest index constituents at the beginning of each month. As of 3/31/2024, the top 10 companies in the index were MSFT (7.2%), AAPL (5.6%), NVDA (5.1%), AMZN (3.7%), META (2.4%), GOOGL (2.0%), BRK.B (1.7%), GOOG (1.7%), LLY (1.4%), AVGO (1.3%) and JPM (1.3%). The remaining stocks represent the rest of the 492 companies in the S&P 500.
Guide to the Markets – U.S. Data are as of March 31, 2024.

J.P.Morgan
ASSET MANAGEMENT

Valuation & Sentiment – The S&P 500 trades at 21.0x earnings today, compared to a 30-year average of 16.6x. With the top ten stocks representing 33.5% of the S&P 500, their influence on index level returns, earnings, and ratios is significant. The top ten firms trade at 28.4x forward earnings, compared to the remaining S&P 500 trading at 18.3x; the equal weighted index is closer to 17.0x. Whether the top ten deserve this premium or not can be argued, but we are far from the 1990's extravagance. Today's leaders are backed by real and growing cash flows. However, these valuations require strong earnings growth to earn attractive prospective returns from here. We will be watching closely. From a sentiment perspective, the market is universally bullish. Surveys that track individuals, traders, and advisors are all close to their highs. In general, sentiment is a contrarian indicator, meaning doing the opposite is advised.

LINCOLN CAPITAL – INVESTMENT OUTLOOK & STRATEGY

In our college economic studies, we learned an apt and useful phrase: "Mini-Max." Mini-Max is a shortcut for "Maximum Output with Minimum Input." Whether you are producing goods or providing personal service, it is a given that you want to get the most output with the minimum number of inputs. Stated differently, you want the most results while using the lowest number of resources.

We view Artificial Intelligence (AI) as a technological "steroid" for Mini-Max applications that increase the efficacies of all entities. This raises two related and timely questions: "What is the impact of AI on stock valuations, and are stock prices too high?"

The Price/Earnings (P/E) multiple is frequently used as a valuation measuring stick. By dividing the price of a stock by its earnings you derive what investors are willing to pay for $1.00 of earnings. Applied to the S&P 500 today, the index presently trades at 21.0x estimated next twelve-month earnings, which compares to a historical average of 16-17 times earnings. Does this mean the stock market is overvalued? Not necessarily.

Though it has some value, the P/E multiple has flaws. Example: The top 10 S&P 500 stocks today have an average return on assets of 17.8% compared to 9.0% for the top 10 of a decade ago, according to Refinitiv. Given the better return on assets, should the S&P 500 trade at the same multiple of the past, or does higher returns merit a premium valuation?

Coming back to the present time, we anticipate Artificial Intelligence propelling Mini-Max efficiencies resulting in higher levels of productivity. Two recent examples:

- *Point72 founder Steve Cohen recently told CNBC that he expects generative AI to save the firm $25 million*
- *Klarna, a buy-now-pay-later company, expects their newly introduced AI assistant to save the company $40 million dollars this year*

Could AI create unprecedented margin expansion among S&P 500 companies? Could the next killer app or apps (think Uber for smartphones) be around the corner? Could a productivity boom create near-term slack in the labor market, allowing inflation to fall and the Fed to return policy to a more normal setting? AI may be the additional resource that drives earnings higher and/or interest rates lower, thereby making an elevated P/E today justified.

While we view AI as a momentous change, we guard against getting too caught-up in today's technology excitement. Security prices reflect investor expectations about the future, and optimism abounds for AI. We are reminded of the mid-to-late 1990's when it was obvious the internet would change the world, which it did though not in a straight line and not always as expected. When there is a new game-changing technology, it typically pulls investors into emotional rollercoasters of exuberance and, oftentimes, despair. We expect more of the same in the months and years ahead.

From a stock-picking perspective, while we have benefitted from having meaningful exposure to the leading companies providing AI services, we continue to seek exposure to companies utilizing AI to increase their efficiencies and productivity.

Our view is that odds favor AI increasing productivity with global impact. While only time will tell if it develops in this manner, if Mini-Max efficiencies do become omnipresent, then it will be life changing for much of the world. Stay tuned.

Yet Another Election Season

In what is a rematch of the 2020 presidential election, Donald Trump and Joe Biden are locked in as their respective political parties' nominees. While the runup to the presidential contest will dominate the news, it is one of many political contests occurring this November, including races of the U.S. House of Representatives and Senate. Election outcomes can have sweeping impacts on public policy. However, history has shown that they have less impact on market performance than investors may assume. According to Jeremy Siegel, a well-respected finance professor of the Wharton School at the University of Pennsylvania, investor's belief in how politics and markets perform is misplaced—bull and bear markets have more to do with business cycles than presidents. Included below are historical facts about election years and presidential terms, and the impacts on stock returns.

With a blistering start to this election year, the S&P 500 returned over 10% in Q1. According to Morningstar, stocks have risen 11.6% in election years since 1926, while the approximate average annual return for the S&P over the same number of years has been closer to 10%. Does the political party elected to the presidency influence the market? According to a study by First Trust, between 1928 and 2016 the average return of the S&P 500 during years a Republican was elected is 15.3% versus 7.6% when a Democrat was elected. Of the 23 election years in that time, 19 of them provided positive stock market returns. However, when it comes to average return during a president's term, according to research done by the Motley Fool, the S&P 500 has had a compound annual growth rate (CAGR) of 9.8% under Democrats, and 6.0% under Republicans. Though, the median CAGR is 8.9% under Democrats and 10.2% under Republicans. All this data does is support the notion that both political parties can tout superior market returns while they are in office.

Which presidents had the highest stock market returns during their presidencies? According to data from Forbes, the two presidents with the highest stock market returns were democrats Bill Clinton and Barack Obama, at 210% and 182%, respectively. Both presidents were elected for two terms, or in their roles for 8 years for these returns. However, both presidents benefited from historic abnormalities; Clinton was in office during the Dotcom bubble and Obama was in office for the recovery from the Great Recession.

While we may hear that this is the most important election of our lifetime, statistics show that regardless of who wins stocks are more likely to produce positive returns in election years, like any other year. It is important to stay disciplined and to remember that market moves are driven by economic cycles, corporate earnings, interest rates and other economic factors.

Please view us a resource for any financial questions, and as always, please contact us if we may be of assistance in any manner.

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