MARKET INSIGHT MONTHLY

March Update

MONTHLY COMMENTARY

UNITED BANK Wealth Management

Although condensing the thousands of factors that contribute to financial market behavior into only a few major variables is no easy task, we examine several key drivers we all know heavily influence investor activity.

First, Federal Reserve monetary policy remains restrictive, but the Fed has indicated it will be more accommodating in 2024. Thus, interest rates will decrease as inflation continues its downward path. What is unknown, even to the Fed, is the timing and magnitude of these declines. Moreover, reductions are not likely to be linear.

Second, U.S. economic output remains healthy as employment conditions continue to defy naysayers. Those employed enjoy reasonably strong wage gains as 9 million jobs remain available. With unemployment at only 3.7%, consumers continue to spend at a reasonably healthy pace, acting as a tailwind to domestic economic expansion.

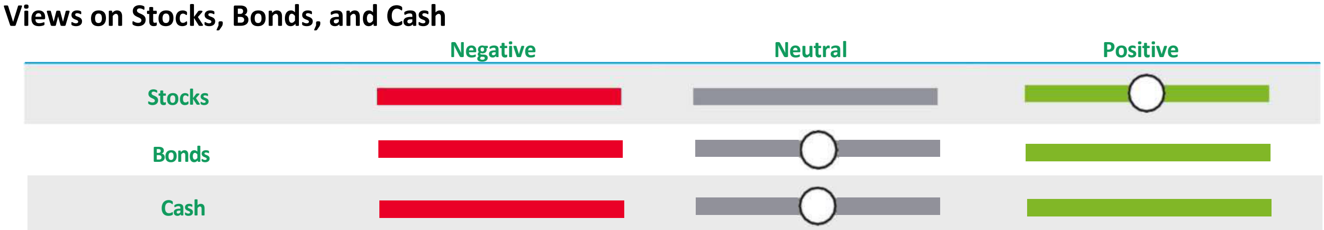
Finally, estimated 2024 earnings are forecast to increase nearly 10% from last year, which would be the largest annual increase in three years. The stock market has performed spectacularly since October after the Fed laid out its plan to reduce rates well into 2025. Investors may have displayed a bit too euphoric stance in the short-term, but this positive sentiment may well be justified over the long-term. We see no major downside potential, though we are prudently reducing risk where appropriate given the recent price expansion.

INVESTMENT TAKEAWAYS

- Interest rates are lower than they were during summer 2023. Recent inflation reports, however, are not entirely in sync with the stock and bond market's optimism of late Q4. Even though rates are lower than last summer, both the 2- and 10-year Treasury rates are now just over 30 basis points higher than year end. In essence, they have retraced about half the gain. In and of itself, this is not a huge obstacle. However, the frequency and magnitude of the Fed rate cuts may not be as favorable as investors had hoped for. The bond market has given up some gains as a result. While stocks have held steady so far, they could be vulnerable to a modest adjustment in the near term.
- To some degree, investors are repeating some of the playbook from last year. The largest of the large, the mega-cap technology and communications companies, are performing very well and carrying the S&P 500 to new highs. While this index is up mid-single digits YTD, growth is once again leading value. What is still very good news is that both growth and value are positive, and the market is advancing. Mid- and small-cap companies, which found significant traction in Q4, are succumbing to the less favorable rate news and showing little follow-through. We anticipate better performance with easing interest rate news.
- The Fed has made no changes to rate policy since July. Early November 2023 comments by Chairman Powell signaled the Fed was finally pleased with its efforts to reduce inflation. He did not suggest the Fed was finished with restrictive policies, but he did suggest inflation would continue its gradual decline into 2024 and beyond. However, since he gave those remarks, Powell has had to reemphasize the Fed's actions are data-dependent and, if inflation rises again, the Fed will be unable to reduce rates until it is no longer a sustained threat. With that being said, we believe 2-4 rate reductions will occur this year.
- We maintain our modest value bias within large-, mid-, and small-cap companies, which better protect portfolios during volatile periods. Companies with strong, less-leveraged balance sheets are often preferred during uncertain environments. Though stubborn at the moment, inflation will eventually come down, and the Fed will be able to pivot more clearly. Until the Fed's 2% target is in sight, expect a limited degree of market volatility to return.
- International developed nations' equity markets outperformed emerging markets in 2023 and thus far this year. Much like the large-cap segment in the U.S., predictability has prevailed over uncertainty. The U.S. economy is still outperforming international economies. In addition, the U.S. Dollar has shown periods of strength and weakness depending on the success of domestic inflation-fighting efforts. When stronger, the U.S. markets have done well; when weaker, the opposite. The dollar has been range-bound, nullifying any pronounced trend. We expect developed markets will continue to be preferred over emerging markets, and changes in the dollar will be heavily tied to inflation reports and economic output. Our ex-China position has been timely and profitable.
- We do not believe interest rates will experience significant upward pressure. The current yield curve is favorable for a well-balanced, moderate duration position. We favor intermediate maturities with some exposure to shorter-term maturities and the high-yield segment.

BROAD ASSET CLASS VIEWS

Views on Stocks, Bonds, and Cash



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EQUITY ASSET CLASSES

Similar to the first ten months of 2023, investors are showing a clear preference for well known, mega-cap technology and communications services companies. Though several industry segments that underperformed last year have made better relative progress in the early stages of 2024, it is clear investors are not yet straying from what worked in the recent past. Large-cap growth companies have more than doubled the returns of value companies so far in 2024. What concerned some market analysts last year continues to be a worrisome issue; market leadership is narrow, and the vast majority of publicly traded companies are not performing in line with broad benchmarks like the S&P 500. What is commonly referred to as "market breadth," or the cumulative difference between the number of stocks going up and the number going down in a certain period, has barely budged since the end of last year. Although market leadership expanded during the significant run-up over the last two months of 2023, breadth is once again moving sideways instead of mirroring the upward direction in equity prices. This is a participation concern. It is often said that "a rising tide lifts all boats." When some boats are rising and some are not moving, one may be concerned with the factors contributing to this divergence. Q4's lower energy prices and lower interest rates have now reversed and are further weighing on small-caps and international stocks in general. Though the S&P 500 has recently set new highs, we should also recognize it has increased over 20% in less than four months and may benefit from some price consolidation given the recent elevated inflation levels just reported. We remain committed to both an intermediate and longer-term positive outlook. As of this writing, nearly all S&P 500 companies have reported their Q4 earnings, and 73% beat earnings estimates, meaning 2023 earnings will be the highest ever reported. The future looks quite bright, with 2024 earnings estimates currently growing almost 10%. The same can be said for international companies. Although we are slightly overweight small-cap stocks, the overwhelming portion of our equity allocation has been and will remain in large-cap domestic companies, which have led performance over the last twelve months.

		View	Relative Trend	Rationale
Market Capitalization	Large-Caps			Year-to-date, U.S. large-cap stocks are among the leading global equity performers. Growth companies, particularly mega-cap tech and communications companies, performed exceedingly well in 2023 and now into early 2024. While interest rates may not fall as precipitously as anticipated, we feel the rest of market will attract investor interest as some tech names may have a more difficult time attracting as much capital as they did in 2023. We will maintain our large commitment to the LC segment.
	Mid-Caps			Mid-cap companies are having a solid year, though recent inflation reports have lessened the probability of significantly lower interest rates for the near future. However, as rates decline throughout the rest of 2024, mid-caps should perform very well. Earnings are stable and valuations are attractive. We expect more sustained gains as stability is restored within the fixed-income markets. Earnings should be very healthy in 2024.
	Small-Caps			The small-cap sector was disproportionately impacted by dual concerns in 2023. They were more heavily affected by the banking crises earlier in the year, and then by rising rates through last summer. While small-cap companies recovered nicely after the initial banking issues, the rate fears prevented additional buying until Q4. Much like mid-caps, small-caps staged an impressive Q4 rally, but are flat to start 2024 as recent inflation reports dampen enthusiasm. We expect this will change with better reports later in the spring.
Style	Growth			In general, large-cap growth stocks were the primary driver of 2023 equity market performance. However, not all growth stocks participated and performed as well as those termed the "Magnificent 7." This sector benefitted greatly from the perception that inflation has less of an impact and is better absorbed by these notable companies. This segment continues to perform well in early 2024 as market leadership is limited and has returned to pre-Q4 conditions. United maintains an appropriate and healthy weighting to growth companies of all sizes and anticipates continued interest in the growth segment.
	Value			United maintains a core value stock overweight to protect portfolios from known and unknown risks. The companies held in our value-based Large Cap Dividend Strategy maintain healthy balance sheets and remain preferred by experienced and disciplined investors. Value companies staged impressive performance in Q4 2023. Our experience has proven select value companies exceed expectations while simultaneously reducing portfolio risk. We anticipate further gains in 2024 as lower rates prompt a broader expansion.
Region	United States			We believe better relative performance will be generated from the U.S. stock market over the foreseeable future, with more consistent and reliable outcomes. Large-cap U.S. stocks considerably outperformed most international indexes in 2023. Valuations are reasonable given lower anticipated inflation and interest rate levels, but large-cap growth valuations are raising some concerns. Both mid- and small-cap companies remain relatively undervalued and attractive despite the recent Q4 equity recovery. The strength of the U.S. employment environment has led to continued overall consumer health. Inflation is now much less of an obstacle. We see the U.S. continuing to take the lead in this regard and in propelling future growth.
	Developed International			Most developed nations' central banks follow the monetary policies of the Fed. As such, both international monetary policy and the global fight to combat excessive inflation have lagged that of the U.S. Success has been gradual, and foreign countries have been slower to contain inflation but have made progress. For U.S. investors, this is a double-edged sword. Lower relative rates may lead to a weaker dollar, but higher inflation reports lead to the reverse. This results in brief periods in which international equity markets may under or outperform the U.S. based on exchange rates rather than economic performance. We expect a range-bound dollar that will be generally stable in 2024.
	Emerging Markets			Although we foresee emerging market growth over the long term, uncertainties stemming from international conflicts create obstacles to consistency and predictability. Our removal of direct exposure to China has been timely and prosperous. We are encouraged by more recent productive communications between the U.S. and China but will wait for more information before altering allocations further. We continue to maintain our baseline weight.

FIXED INCOME

Inflation remains a stubborn "friend."

During the last two months of 2023, bond investors cheered the change in perceived Fed policy by liberally buying Treasury securities across the entire yield curve. Rates fell precipitously and it could be argued the entire yield curve changed to reflect where investors expected rates to be at year-end 2024, rather than conditions as they currently exist. Though the Fed has taken no action to reduce rates, it clearly indicated the process will begin at some point in 2024. Investors were left to speculate as to the timing and magnitude of these changes, and investors seemed to price in a best-case-rate-decline scenario. The economy has not yet "gotten the memo," as it remains healthy. CPI and PPI reports for both December and January came in higher than expected, driving rates considerably higher than year-end figures. In its defense, the Fed has always indicated that its actions would be data dependent. At the end of 2023, many investors expected five to six rate cuts this year. It now appears that there may be only two to four cuts in 2024. When our October Market Insight publication was written, the 10-year Treasury yield was trading between 4.90 and 4.95%. As of this writing, the yield is just below 4.15%. Progress has been made, but investors should remain patient as higher bond yields are a result of a resilient economy. Too precipitous a rate decline may signal recession and much slower growth. Our decision to extend duration in early October was extremely timely and remains profitable. We generally returned to "average" duration portfolios but kept a slight bias to short-term securities as a precaution against a strong economy and inflation that might not fall as rapidly as hoped, which has been the case. Unless another dramatic global event triggers inflationary fears once again, we do not anticipate a change in the lower inflation/lower rate environment, but we agree that rate declines in total will not be as significant as had been forecasted. We currently suggest a blend of high-quality, intermediate-term bonds in all fixed income portfolios with less exposure to the shorter-end where applicable. Quality companies and municipalities continue to perform well across the quality and size spectrum. High yield bonds issued by stable but growing entities continue to be a productive use of fixed income capital. We remain committed to a modest high-yield position in both corporate and municipal bonds. In tax-sensitive accounts, we favor municipal bonds, as infrastructure spending, strong state revenues, and the potential for higher personal tax rates provide support to municipal markets.

		Low / Medium / High	Rationale
Positioning	**Credit Quality**		To protect asset values, United prefers fixed income portfolios dominated by high-quality bonds. Credit spreads have normalized despite higher rates.
		Short / Int. / Long	
	Duration		United believes rates are near their peak. As the curve is flattening, opportunity exists in extending duration in anticipation of eventual rate reductions in 2024.

COMMODITIES

Our general view towards commodity prices is neutral. Broad baskets of commodities have increased about 3% so far in 2024 but are flat over the past year. Most of the well-known commodity benchmarks and indices are heavily influenced by price movement in energy and/or precious metals. In more granular terms, oil and gold prices are typically weighted the heaviest. As Federal Reserve policies directly impact the value of the U.S. Dollar, which in turn impacts various commodity complexes, commodity price direction is not only tied to global supply and demand factors, but also to government policy. This makes price forecasting even more precarious. The volatile price of oil is up over 10%, while gold has modestly declined influenced by a now stronger dollar. With short-term global interest rates remaining relatively high, we cannot make the case for higher commodity prices.

Over the past eighteen months, the world has had to adjust in many ways. How the world produces, manufactures, and transports various items, including commodities, has changed due to the ongoing conflicts in Eastern Europe and the Middle East. The long-term lack of any consistent U.S. energy policy stems from the absence of political compromise. This leaves the U.S. and the world dependent on the winds and whims of multiple undemocratic and often uncooperative regimes. As new and stable supply chains develop and mature, prices are likely to be better understood and underlying value better predicted.

CONCLUSION

Though obstacles remain and global conflicts have yet to ease, financial markets are much more stable than they were eighteen months ago. At the end of 2022, there was no end in sight to Fed rate increases. Rates are now expected to be lower in 2024. Under normal circumstances, lower rates are generally attributed to weaker economic conditions. However, in this case, rates were purposefully driven higher by the Fed to bring down inflation and were not directly driven by normal economic activity. Inflation is now lower and moving closer to Fed targets. Despite the nay-sayers, corporate earnings set record highs in 2023 and should grow close to 10% in 2024. Markets went through a reasonable correction in 2023, but the commentary provided by the Fed during its November press conference changed the market and have made all the difference. Now, the promise of stable rates over the next twelve months should solve multiple issues, resulting in significantly reduced anxiety and, ultimately, more reliable financial market behavior and performance.

Disclosures

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Economic forecasts set forth may not develop as predicted.

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