

Viewpoint

The Time Has Come

September 2024

All data, projections and opinions are as of the date of this report and subject to change.

IN BRIEF

- This month we highlight our viewpoints on forthcoming trends. It includes our expectations for a measured rate cutting cycle to begin imminently while the economy is normalizing, the consumer is stable, and corporate earnings growth is broadening out.
- In the next couple of months market activity is likely to be more on edge, in our view. This is typical during election years, whereas, historically, September and October have usually been weak months. We would view weakness as an opportunity to add to Equities and diversify at the same time.
- This month the ISC has upgraded Financials to a slight overweight from neutral and downgraded Industrials to a neutral from slight overweight to help take advantage of the adjustment to rates in the upcoming months.
- The sharp rate moves in early August confirmed our intuition about the diversifying effect of Fixed Income; at these yields—and at this part of the interest rate cycle—high-quality Fixed Income should act as a good counterweight to macro and Equity risk in a portfolio, in our opinion, and serves an important role in balanced and diversified portfolios.

One of the most profound statements coming out of the August Jackson Hole meeting by the Federal Reserve (Fed) was “the time has come.” Markets do not like uncertainty, and, clearly, they do not react well to negative surprises. That said, when the largest and most important central bank in the world declares “the time has come” to cut interest rates, we should all take notice and re-assess the path forward for the economy, rates, inflation, the yield curve, the U.S. dollar, and expected price trends in the Equity and Fixed Income markets. Below, we highlight our viewpoints on forthcoming trends. It includes our expectations for a measured rate cutting cycle to begin imminently, while the economy is normalizing, the consumer is stable, and corporate earnings growth is broadening out.

- The economy is normalizing back toward prepandemic trend line growth with jobs as the central focus.
- Although the consumers have become more selective, they have become more stable.
- Inflation trends are trending down with some stickiness in shelter.
- Capital investment is healthy.
- Corporate earnings growth is broadening out which is underpinning the equal weighted S&P 500 to all-time highs.

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CIO ASSET CLASS VIEWS

This month, the Global Wealth & Investment Management Investment Strategy Committee (GWIM ISC) adjusted our U.S. Equity sector allocations by upgrading Financials to slight overweight, and downgrading Industrials to neutral. We maintain an overweight to Equities, with a preference for higher quality U.S. Large- and Small-caps, and still favor a significant allocation to bonds in a diversified portfolio. During potential weak equity market periods, leverage portfolio rebalancing to diversify areas of over/under exposure.

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Asset Class	CIO View		
	Underweight	Neutral	Overweight
Global Equities	●	●	●
U.S. Large Cap Growth	●	●	●
U.S. Large Cap Value	●	●	●
U.S. Small Cap Growth	●	●	●
U.S. Small Cap Value	●	●	●
International Developed	●	●	●
Emerging Markets	●	●	●
Global Fixed Income	●	●	●
U.S. Governments	●	●	●
U.S. Mortgages	●	●	●
U.S. Corporates	●	●	●
International Fixed Income	●	●	●
High Yield	●	●	●
U.S. Investment-grade	●	●	●
Tax Exempt	●	●	●
U.S. High Yield Tax Exempt	●	●	●
Alternative Investments*			
Hedge Funds			
Private Equity			
Real Assets			
Cash			

*Many products that pursue Alternative Investment strategies, specifically Private Equity and Hedge Funds, are available only to qualified investors.

CIO asset class views are relative to the CIO Strategic Asset Allocation (SAA) of a multi-asset portfolio.

- Corporate margins are holding up and remain healthy even as the economy is slowing toward normal levels.
- Rates are shifting lower as the yield curve is changing its shape. The 2- to 10-year spread is now almost zero after the longest inversion on record.
- Financial conditions broadly remain healthy.
- The equity market performance and relative price trends are broadening out, thus increasing the participation outside of the mega cap Technology space.
- Dividend growth and dividend yield relative to the overall market is gaining momentum.
- Small capitalization shares are basing out and beginning to anticipate rate relief creating better relative price performance.
- Credit spreads have remained tame and normal as rates have shifted lower.
- Geopolitical risk remains high, helping to support an upward gold price trend.
- The U.S. equity markets are still more attractive than non-U.S. in our view.
- Equity valuation remains at premium multiples given the positive earnings revisions and stable environment.

As it appears some may suggest these are all “Goldilocks” characteristics. We would rather describe the current environment as one that is normalizing off from peak growth, peak inflation, peak stimulus, peak rates and potentially peak valuations. This is phase one of the march toward more normal conditions. Phase two is next which will likely have new headwinds to digest such as the wide deficit, growing debt, and whether corporate profits can grow at an attractive rate all things considered. We will cross that bridge when we get there. For now, we reaffirm our positive view on Equities and expect this to last well into 2025. In the next couple of months market activity is likely to be more on edge, in our view. This is typical during election years, whereas, historically, September and October have usually been weak months. We would view weakness as an opportunity to add to Equities and diversify at the same time. As far as the longer-term picture, we believe our asset light thesis could continue to play out in favor of the bulls. We expect the demand for investable assets to potentially rise in the future well above the overall supply which underpins an attractive equation to build wealth over time, in our opinion.

What is our overall view given the top insight bullets above?











- Remain overweight Equities relative to Fixed Income as long as earnings remain attractive, and the Fed is normalizing rates.
- Leverage portfolio rebalancing during weak equity market periods to diversify areas of over/under exposure.
- Consider increasing allocations to Small-caps and sectors with more attractive dividend yields and dividend growth characteristics.
- Upgrade Financials to a slight overweight from neutral and downgrade Industrial to a neutral from slight overweight to help take advantage of the adjustment to rates in the upcoming months.
- Maintain slightly above benchmark duration in Fixed Income.
- Leverage a bond ladder strategy as the yield curve normalizes.
- Maintain a U.S. bias with an overweight relative to non-U.S. developed and Emerging Markets (EM).
- Consider using overlay ideas to express individual themes such as infrastructure, consumer selectivity, robotics and automation, and healthcare innovation, to name a few.

The Fed told us “the time has come”, and the capital markets are beginning to follow this directive.

CIO INVESTMENT DASHBOARD AS OF SEPTEMBER 3, 2024

Equities have staged a strong recovery from the early August sell-off and remain well supported by elements like broadening earnings growth and a relatively strong economic backdrop. However, we continue to see crosscurrents in the market landscape moving forward. Long-term investors should consider using any episodic market volatility to their advantage and remain diversified across portfolios.

Current readings on the key drivers of Equities for investors to consider, with arrows representing the recent trend:

Factor	Implication for Equities			CIO View
	Negative	Neutral	Positive	
Earnings				According to FactSet, S&P 500 revenue and earnings grew by 2.8% and 1.0% last year, respectively. Accordingly, for 2024, consensus expects growth of 5.1% and 10.2%. Revenue growth for Q2 grew by 5.3%, compared to an expansion in Q1 of 4.3%. Profits for Q2 are anticipated to have grown by 11.4%, after a Q1 result of 5.9%. Meanwhile, according to BofA Global Research, the hint of softness in last month's three-month average of the Global Earnings Revision Ratio was short lived. It now stands at a 29-month high and above its long-term average. The number of upgrades to profit estimates surpasses downgrades in 7 of 20 countries and in 5 of 16 tracked industries.
Valuations				The S&P 500 price-to-earning (P/E) ratio (next 12 months) stands at just over 21.0x above its long-term average. This headline measure suggests that U.S. Equities remain expensive, although relative discounts can be found in areas like Small-cap and Value.
U.S. Macro				Following an expansion of 2.5% last year, growth in real gross domestic product (GDP) for the first half of this year has cooled to an average of 2.2% at a seasonally adjusted annual growth rate. Excluding volatile measures in trade and inventories, final sales to domestic purchasers averaged a solid 2.7%, from 2.3% last year. Recent data suggests a more apparent pace towards normalized economic growth. BofA Global Research expects GDP growth of 2.5% for Q3 and 2.7% for all of 2024.
Global Growth				The global economy has generally shown resilience in the face of diverse headwinds. Bolstered by the services sector, growth in the euro area remains modest. A curbed cooling of inflation has allowed for a slight loosening of monetary policy, amid an overall tightening fiscal stance. Meanwhile, the fallout of regional parliamentary elections has raised political uncertainty. In China, in response to continued economic malaise, fresh policies targeting consumption and the services sector reflect a lack of traction of policies to boost the property market and greater uncertainty over the export outlook. In the U.S., consumption in general has remained a sturdy economic support. After growth of 3.5% and 3.0% in 2022 and 2023 respectively, the global economy is expected to slightly accelerate in 2024 to growth of 3.1%, followed by an expansion of 3.3% in 2025, according to BofA Global Research. This compares to average growth of 3.8% from 2000 to 2019, according to the International Monetary Fund.
U.S. Monetary Policy / Inflation				In July, the Federal Open Market Committee (FOMC) held steady its policy interest rate. At Jackson Hole in August, Chairman Jerome Powell voiced confidence that inflation was on a sustainable path to 2%. Moreover, he revealed that further softening in labor market conditions would not be welcomed. These have solidified expectations of a cut occurring in September. He reiterated that the pace of easing policy would be data-dependent. Market expectations call for roughly four cuts of 0.25% this year. BofA Global Research expects a cut in September and another in December, which would take the present target range of 5.25%-5.50% to 4.75%-5.00% by the end of the year.
Fiscal Policy				U.S. pandemic-era fiscal support totaled nearly 31% of GDP, much of which has faded. Longer-term initiatives include the 2022 CHIPS and Science Act, a \$280 billion plan to bolster the country's technological industrial base, and the 2022 Inflation Reduction Act (IRA), a \$370 billion effort largely to develop a renewable energy supply chain, among other elements. A \$1.2 trillion spending package authorized in March will keep federal agencies funded until October.
Corporate Credit				Credit spreads generally reflect lessened concern about an economic slowdown. They have nearly fully reversed a marginal tightening of financial conditions occurring in early August. Those of U.S. High Yield (HY) have reentered a range established this year. Those of Investment-grade (IG), have also eased, though by a lesser degree.
Yield Curve				Inversions, whereby longer-dated yields are below shorter-dated ones, are normalizing in the 2/10s and 2/30s segments but remain in place in the fed funds (FF)/10s and 3-month/10s sections. These shifts suggest increased near-term economic risk, as well as a heightened anticipation of policy interest rate cuts in the future.
Technical Indicators				The S&P 500 remains above its 200-day moving average, which is also in an uptrend. Measures of market breadth, such as the percentage of New York Stock Exchange stocks closing above their 200-day moving average and the cumulative advance/decline indicator, are generally improving.
Investor Sentiment				According to the American Association of Individual Investors, bullish sentiment continues to dominate over bearish sentiment. After spiking to its highest level since the coronavirus pandemic in 2020, the Chicago Board Options Exchange Volatility Index has declined, though it remains above its year-to-date (YTD) and 12-month averages. Cash levels in institutional portfolios signal "neutral," according to the BofA Global Research Fund Manager Survey. The BofA Bull & Bear Indicator is also flashing a neutral signal at 6.2.

Source: Chief Investment Office.

EQUITIES

We are slightly overweight Equities: Softening economic data, elevated geopolitical risk and the upcoming U.S. presidential election could act as potential headwinds over the next few months. However, we ultimately maintain a positive bias for Equities amid a sustained earnings recovery, broadening market leadership, relatively stable consumers, healthy balance sheets and credit markets, and the potential for easier monetary policy this month.

We are slightly overweight U.S. Equities: The U.S. currently remains our preferred Equity region relative to the rest of the world, given a relatively stronger balance sheets in aggregate, attractive earnings growth estimates and better consumer fundamentals. U.S. Large-caps have not been exempt from high velocity rotations and market weakness recently, however, our view remains positive on strong fundamentals and the ability to produce healthy shareholder payouts. We maintain a slight Small-cap overweight considering expectations for solid economic growth, a broadening profits cycle, lower costs of capital and a potentially favorable election-year backdrop.

At this point in the cycle, we suggest a balance in Equity portfolios and broader exposure across sectors. In addition to the leadership and fundamental strength in recent years from the Technology and Communication Services sectors, we are starting to see improvement in earnings from other sectors. As the cycle starts to broaden out and as financial conditions begin to ease, it is important to have Equity exposure across cyclical, interest rate-sensitive and growth sectors. This month, we are increasing exposure to Financials as the Fed is about to start its next easing cycle with forecasts for lower interest rates that can help improve credit risks, default rates, revenues, net interest income and asset valuations on Financials balance sheets. We are also lowering exposure to Industrials after mixed results from Q2 earnings reports, few green shoots and cautious company guidance for the second half of 2024. Infrastructure-related investments and projects related to secular growth trends in electric power demand, energy transmission and distribution, cloud and data center builds, and next-generation Artificial Intelligence (AI)-focused semiconductor technology that is increasingly power hungry have come under pressure recently but could drive multiyear demand for select growth and cyclical stocks.

We continue to emphasize Healthcare to reflect a balance between Value and Growth, low positioning and negative sentiment coming out of 2023, and our preference for quality at a reasonable price. We maintain overweight exposure to Energy in the short term due to potential disruptions and as a hedge for geopolitical risks. However, the forward fundamental outlook for energy in 2025 is weaker when analyzing supply and demand dynamics. Despite some small and specific deterioration in consumer data in recent months, the overall health of the consumer remains solid, supported by a positive job market and expectations for lower interest rates. The picture for Utilities is mixed, driven by the higher cost of capital that could delay some renewable energy projects, but on the other hand, the trends in AI and data centers could drive increased power demand in the coming years and future interest rate cuts by the Fed could start to lower the cost of capital. While we are constructive on Information Technology (IT) and Communications Services as longer-term thematic trends, we maintain our neutral view in the near term on elevated valuations, crowded positioning, which was a significant factor in the early August sell-off and declining earnings growth rates sequentially, despite well above market average earnings growth from these two important sectors. We deemphasize Materials as demand is weak, especially from China, and pricing power remains questionable. With interest rates moving lower over the last couple of months, we are neutral Real Estate (RE) and prefer being selective in the RE subsectors due to positive fundamentals in some areas of RE but remain cautious of weaker trends in other areas like CRE.

We believe strategic portfolios should continue to incorporate both Growth and Value factors that would simultaneously benefit from the possibility of cyclical and secular forces gaining traction. While we ultimately believe that AI and related investments still have long-term momentum, the summer reversal in mega-cap Growth stocks acted as a reminder to avoid overexposure. Meanwhile, Value continues to trade at a relative discount to Growth and may benefit from lower interest rates moving forward. We suggest a disciplined and balanced approach between Value and Growth for long-term investors and emphasize the importance of diversification in portfolios.

We are neutral Emerging Market Equities: EM Equities appear attractively valued, but Fed rate cuts are unlikely to have a major positive effect given small current account

EQUITY WATCH LIST

- Heightened geopolitical risk and conflict in the Middle East
- Inflationary pressures are moving lower but remain above the Fed's target level
- Economic data for production, labor, consumer expectations, and credit and liquidity conditions
- Progression of earnings estimates and margins
- Reorganization of global supply chains and U.S.-China relationship
- Pressures within the Office segment of Commercial Real Estate (CRE)
- A sustained broader rotation that favors Small-caps, cyclicals and Emerging Markets (EM)
- Shifting expectations surrounding the outlook for Fed rate cuts

deficits across the EM universe. We continue to expect a wide return dispersion between individual EM countries and regions. Growth in the heavyweight China market is likely to remain soft on a protracted basis, given structural weakness in the construction sector and constraints on the Technology sector from a tighter domestic regulatory environment and global export controls. Stronger domestic demand in the broader Asia-Pacific region should help to offset external weakness from China exposure. Central and Eastern European markets remain most exposed to the Russia-Ukraine war through trade links and high dependency on natural gas imports, while market direction in Latin America, the Middle East and Africa should remain broadly tied to the direction of natural resource prices, particularly on any broadening of the Israel-Hamas conflict. The structural rise in EM consumer spending remains a big reason why we believe investors should consider maintaining a strategic allocation to EM Equities, as appropriate. The emerging world now constitutes around 40% of global Personal Consumption Expenditures, according to the United Nations, and ongoing convergence with developed economies should support GDP growth and corporate earnings over the longer term. We favor active management¹ when investing in EM, as fundamentals differ across countries based on fiscal capacity, external funding needs, corporate governance and other factors.

We are slightly underweight International Developed Market Equities: We continue to prefer U.S. versus International Developed given our higher-quality view. We remain slightly underweight Europe. Downside risk remains from the potential for fiscal tightening in high-budget-deficit European Union (EU) countries and increased political uncertainty following EU parliamentary elections. Natural gas prices have fallen, but ongoing curtailment of Russian supply and growing demand from Asia mean that supply constraints could reemerge at a later stage. We maintain a neutral view on Japanese Equities. Unwinding of the yen carry trade and uncertainty over future Bank of Japan (BoJ) interest rate and intervention policy should make for further volatility, though sustained positive inflation and corporate reforms remain fundamental supports for valuation. As aggregate net energy importers, International Developed markets would also be more vulnerable to any potential rise in energy prices on any broadening of the Middle East conflict. We believe long-term investors should maintain some strategic exposure to International Developed Equities, as appropriate, given that they trade at a discount relative to U.S. Equities, contain more of a balance between Value and Growth sectors, can offer attractive dividend yields, and provide diversification.

FIXED INCOME

We are slightly underweight Fixed Income: We are still favorable on a significant allocation to bonds in diversified portfolios but are currently slightly overweight Equities. Yields moved lower again this month, as market volatility increased significantly. The sharp rate moves in early August confirmed our intuition about the diversifying effect of Fixed Income; at these yields—and at this part of the interest rate cycle—high-quality Fixed Income should act as a good counterweight to macro and Equity risk in a portfolio, in our opinion, and serves an important role in balanced and diversified portfolios.

We are therefore slightly overweight on U.S. governments. Nominal and real rates are still reasonably attractive and provide good income-generating power, in our opinion, as well as a decently priced hedge to macroeconomic risk. Real yields—the yield after inflation, as measured by Treasury Inflation-Indexed Securities—have moved lower but are still 1.7% to 2% across the curve, the higher end of the range since 2008. Substantially positive yields above inflation on U.S. government-guaranteed securities is a welcome relief for savers after years of financial repression. We still suggest a slightly long-duration position versus a stated benchmark to take advantage of these higher yields, protect against declining rates on cash balances, and as prudent positioning against macro risk in the increased Equity positioning of a diversified portfolio. However, given the sharp move lower in yields, the market may get ahead of itself on expected Fed rate cuts; we will carefully monitor our duration positioning in light of recent moves.

We remain slightly underweight both Investment-grade Corporates and High Yield. While we saw significant repricing wider in IG and HY during early August, credit spreads still screen rich in our view, with little room for upside, particularly if one assumes that

FIXED INCOME WATCH LIST

- Resilient or resurgent inflation
- Increased risk aversion or recessionary risk via spreads, yields or new issue activity
- Signs of significantly negative Fixed Income fund flows
- Dislocations in CRE markets
- Potential credit deterioration if economic weakness

¹ Active management seeks to outperform benchmarks through active investment decisions such as asset allocation and investment selection.

economic data could begin to confirm weaker trends. Over the last 12 months, credit markets have fully embraced the improved macro and technical backdrops. Despite recent widening, valuations, with IG at around 95 basis points (bps) and HY at around 315 bps, continue to reflect a healthy growth picture in addition to relatively strong demand despite the fact that yield buyers could step back, as IG is now trading inside of 5% for the first time since early 2023. We expect that a key test for the market and clearing levels will come in September as new issue volumes accelerate—creating the possibility for an additional source of near-term spread volatility.

To be clear, we don't see a risk or catalyst for spreads to move meaningfully wider over the short term, and we are hesitant to call one weak data point (i.e., July nonfarm payrolls) a paradigm shift in the forward outlook/trend. Bouts of volatility in credit spreads are normal, and history has shown that credit spreads can trend at low/rich levels for an extended period (i.e., late 1990s and mid-2000s). With the U.S. economy still on strong footing (albeit maybe slowing), any move wider in credit spreads could be more contained, in our view. However, the margin for error at current valuations is still slim. On average, at starting spread levels of 100 bps or less, IG underperforms duration-matched Treasuries 12 months forward.

We therefore continue to believe that an up-in-quality and defensive tilt within a corporate allocation is prudent and would look to re-risk portfolios should we see spreads move above 130 bps—all else being equal.

In HY, similar to IG, we expect the typical September pickup in new issuance to weigh on spreads and see potential for elevated volatility ahead of the election. That said, demand for HY may expand through year-end as investors rotate out of floating-rate leveraged loans in anticipation of rate cuts. Additionally, HY yield-to-worst remains around 7.5%, above the median level seen over the last 25 years and provides modest compensation for credit losses. However, spreads continue to price in a soft/no-landing outcome and an improvement in default losses, despite the looming risk of a slowdown in earnings that could pressure interest coverage ratios, especially as more HY debt is refinanced at higher, post-2022 rates. Current spreads in the BB-rated and B-rated cohorts are both roughly in the 10th percentile historically, and we would look for substantially wider levels as a more attractive entry point. We therefore maintain our slight underweight positioning and see better risk-adjusted opportunities in other asset classes such as Equities.

We remain slightly underweight both U.S. Investment-grade Tax Exempt and U.S. High Yield Tax Exempt: Muni valuations have cheapened to approximately average levels. We attribute this to higher net supply now that we have moved past the seasonally high redemption period of June to August, while new muni issuance is tracking over 35% higher than last year. At the same time, fund flows into mutual funds and exchange-traded funds have been solid since early July, making for a robust market. We expect technical factors to strengthen again after November, when new issuance generally slows and reinvestments are needed for seasonally heavy coupon payments in December and January. We believe municipal credit quality remains generally solid, with most states projecting abundant levels of rainy-day funds in fiscal years 2024 and 2025; this should allow state and local governments to maintain their creditworthiness if economic conditions worsen. However, with over 20,000 municipal issuers, there are certainly credit outliers to the downside, and some muni subsectors such as healthcare and private higher education face particular challenges. Additionally, credit spreads for low-quality munis are currently tighter than their long-term averages. Therefore, investors should be cautious in reaching down the credit spectrum.

We are slightly overweight Mortgage-backed Securities: Aiming to bring down stubbornly high inflation, the Fed has steadily tightened financial conditions by raising interest rates and engaging in quantitative tightening. Weaker technical dynamics led to a material widening of Mortgage-backed Securities (MBS) spreads last year, breaking into the 80 bps range in October 2023 before retracing back to the current 40 bps—the lowest level in 2024. This contraction occurred as the market, and the Fed gradually grew more comfortable with the prospect of unwinding quantitative tightening by starting rate cuts in Q4, while the economy maintained its resilience. In our opinion, the current level of MBS spreads after the rally still represents value when compared to corporates, using the long-term average.

Duration extension, which is a key risk for MBS investors, has been substantially mitigated, with MBS duration now significantly lengthened. Another important risk, interest rate volatility, remains elevated at levels that make MBS bonds more appealing, as their

spreads are likely to outperform should interest rate volatility subside. Although weak demand from the Fed, financial institutions holding two-thirds of the MBS market, and an unsettling geopolitical/macro environment make it possible for MBS spreads to widen further, MBS spreads and yields appear attractive relative to Treasuries and IG corporate bonds over the long term.

ALTERNATIVE INVESTMENTS

Unlike Traditional asset classes, establishing and exiting allocations to Alternative Investments (Alts) can be a long-dated process given liquidity constraints. Because of their illiquid and long-term nature, Alts should be viewed in terms of strategic allocations. Therefore, our views on Alts strategies within each asset class reflect potential tilts in new dollar deployment based on relative opportunity, in contrast to a tactical repositioning in public markets.

Some key CIO principles for qualified investors to consider when investing in Alts include:

- **Think strategically and long term:** Alts are largely illiquid and therefore require a long time horizon when incorporating into portfolios.
- **Invest methodically, including in downturns:** A properly implemented Alts program requires a consistent commitment, particularly within private markets strategies; withdrawing during periods of volatility can undermine the long-term benefits of the asset class and result in underallocation.
- **Diversify:** Seek diversification by strategies and managers. Investing methodically within private markets strategies also improves vintage year diversification.
- **Prioritize high-conviction managers:** Performance dispersion is significantly wider within Alts than in Traditional investment strategies; manager selection is therefore a potential opportunity.

Hedge Funds: On the whole, Hedge Funds (HF) appear to have navigated the August volatility deftly. Equity Hedge (EH) strategies have likely bounced back into positive territory as Equity markets recovered in the latter half of the month.² Our surveys of EH funds during the most acute phases of the spike in volatility suggested managers were taking disciplined approaches to managing gross exposures and ultimately benefited from adds to high conviction and watch-list names. Notably, quantitative EH strategies appear to have fared decently intra-month, sidestepped large factor rotations and continued to post strong YTD returns.

Macro HF strategies, meanwhile, have been front and center in the cross-asset class disruptions and, despite clawing back some of the losses, have likely posted negative returns for the month of August.³ Trend-following strategies in particular were challenged by positioning in currencies and Equity indexes, which was partly offset by gains from increasingly long positioning in government bonds.

Private Equity: Private Equity (PE) notched modest gains of approximately 1% to 2% in Q1,⁴ once again lagging public Equities. Earnings releases from prominent publicly listed Alts asset managers, which can serve as a rough gauge of industry trends, suggest modestly positive PE performance in Q2 in the low single-digits range. Buyout strategies have been resilient, if muted, over the recent rate-hiking cycle and continue to exhibit outperformance over longer time horizons. Venture Capital (VC) has been enduring a more acute valuation reset that, while not as severe as the dot-com peak-to-trough drawdown, has exceeded declines during the 2008/2009 Global Financial Crisis.⁵ Thematically, PE strategies have been contending with a slower velocity of capital recycling, though first half of the year has shown a modest pickup in exit activity of 15% year-over-year.⁶ With

CIO Views on Alts Strategies

Hedge Funds

Equity Hedge +

Bull case	Potential alpha* generation opportunities for low net strategies in volatile or high-dispersion markets; short alpha improving after difficult 2023; low net better positioned if Equities sell off
Bear case	Return of concentrated and beta**-driven market would limit opportunity set

Event Driven

Bull case	Higher rates pressuring levered balance sheets creating potential for distress; merger deal spreads moderately wide and higher risk-free rate positive for merger arbitrage
Bear case	Distress may not materialize in size or may be delayed; low mergers & acquisition volumes and high regulatory uncertainty

Relative Value

Bull case	Still in world of higher yields; economic resiliency supportive of credit; decent dispersion in HY
Bear case	Spreads not attractively wide; potential increase in credit risk and defaults in coming year

Macro +

Bull case	Possible "higher-for-longer" rate regime could create cross-asset volatility in rates and foreign exchange; inflation stickiness could exacerbate macro volatility
Bear case	Coordinated Central Bank rate cuts could limit dispersion; choppy markets difficult for trend-following; interest rate volatility declining

*Alpha is the excess return of an investment relative to the return of a benchmark index. **Beta is a measure of a stock's volatility in relation to the overall market. **Bull case** is an environment or set of factors that could represent tailwinds for the strategy. **Bear case** is an environment or set of factors that could represent headwinds for the strategy. + symbol indicates the strategies CIO views as having the most favorable opportunity set for new investment within the Alts asset classes.

² BofA Securities Capital Strategy Group, Morgan Stanley Prime Brokerage, Goldman Sachs Prime Services. As of August 23, 2024.

³ Chief Investment Office. As of August 23, 2024.

⁴ Cambridge Associates, PitchBook, Inc. As of March 31, 2024.

⁵ PitchBook, Inc. As of March 31, 2024.

⁶ PitchBook, Inc. As of June 30, 2024.

the prospect of lower interest rates coming into focus, expectations are for deal activity to accelerate further into next year. The need for capital remains high across private markets, particularly in the startup ecosystem where VC and PE growth investors have retrenched. While still contending with high interest rates for the time being, we see a potential improvement in the relative outlook for PE strategies on the horizon.

Private Credit (PC), meanwhile, has continued to perform well throughout this era of higher interest rates. Using private fund performance data, PC generated returns of 1.3% in Q1, bringing the 1-year internal rate of return to 8.9%.⁷ Other PC indexes continue to show positive performance in Q2 of 2.8%.⁸ While PC has remained resilient in the face of skepticism from pundits, market dynamics throughout most of the year have led to declining yields and spreads. Potential interest rate cuts could depress yields further.

As we have communicated, the goldilocks environment for PC has been slowly receding as new headwinds emerge. Credit losses have long been expected to increase off exceptionally low levels, given the strains of high borrowing costs on borrowers' balance sheets, yet a broad contagion in PC markets is unlikely, in our view. PC spreads in fact tightened in Q2 amid stiff competition from public leveraged-credit markets, driving yields lower by roughly 30 bps to approximately 11.4%.⁹ Given high starting yields, it is still possible to pencil out mid- to high-single-digit returns over the next 12 months under conservative scenarios with higher-than-expected default rates and recovery rates lower than the historical experience.

Deployment challenges have emerged as another headwind due to near-term supply/demand imbalances. New PC issuance has remained muted, broadly syndicated leveraged loan markets have refinanced large volumes of PC loans and competed aggressively for new deals, and demand from institutional and retail investors has remained strong. This dynamic has contributed to the narrowing of PC spreads in the first half of the year, both relative to base rates as well as relative to broadly syndicated loans. Importantly, a pickup in PE deal activity would mitigate the current imbalance and restore the structural thesis of continued PC growth. The substantial \$1.8 trillion¹⁰ of global PE dry powder that will ultimately need to be invested will likely require hundreds of billions of dollars in annual PC financing.

We continue to emphasize partnering with established and well-resourced managers, and think PC is best positioned within a diversified allocation to Alts and should be tactically compared to other Alts asset classes and strategies, in particular PE.

Private Real Estate: Overall, Private Real Estate (PRE) has shown some signs of stabilization although returns in Q1 and Q2 were still moderately negative. Cap rates have similarly been relatively steady in the first half of the year, though with variations across sectors and geographies.¹¹ PRE entered the year with optimism that the asset class would bottom out and find market clearing prices. The stickiness of interest rates during the first half likely delayed the beginning of a recovery, but recent rate declines could improve the outlook. PRE performance momentum and fair value estimates also suggest a bottom may be in sight. Accordingly, deal activity has remained anemic. Market participants are still hoping for a pick-up in activity in the second half of the year, driven by clarity on the interest rate picture and improving return expectations.

Overall, PRE values have declined 5% in the past year and approximately 20% from their recent peak,¹² suggesting the valuation reset has been working its way through the system. New supply is hampering rent growth in certain sectors and geographies, such as apartments and industrial; however, supply growth is projected to ease in the coming year. Publicly listed real estate investment trusts (REITs) have now flipped to trading at a premium relative to net asset value, suggesting public markets no longer view PRE as overvalued.¹³

We continue to expect systemic issues to be contained but for the PRE cycle to continue to play out as a slow burn. As suggested, reduced interest rate uncertainty would likely spur transaction activity and aid in price discovery. For the longer term, PRE continues to make sense as a strategic allocation given the potential diversification benefits and income features.

⁷ Cambridge Associates, Refinitiv EIKON. As of March 31, 2024.

⁸ Lincoln International, Lincoln Senior Debt Index. As of June 30, 2024.

⁹ BofA Global Research. As of June 30, 2024.

¹⁰ Preqin. As of December 31, 2023.

¹¹ Green Street, "Cap Rate Observer". As of June 13, 2024.

¹² Green Street's Commercial Price Index. As of August 6, 2024.

¹³ Green Street, "U.S. Commercial Property Outlook". August 26, 2024.

Private Equity

Buyout

Bull case	Current vintages likely attractive for long-term given profitability focus; within PE, Secondaries benefiting from secular growth and institutional investors seeking liquidity; deal activity starting to pick up and could surge if momentum builds
Bear case	Higher rates require larger Equity investments; deal and exit activity still low

Venture/Growth

Bull case	Significant correction in the last two years benefits capital providers; AI could drive investment supercycle; early VC stages more insulated than later stages; falling rates would likely be tailwind
Bear case	Ex-AI VC market still challenged; VCs focused on supporting portfolio companies; initial public offering drought continues; timelines extended plus increased risk of dilution; higher rates drag on unprofitable companies

Special Situations

Bull case	Default rates rising; "higher-for-longer" would increase pressure on levered balance sheets; RE-adjacent opportunities; companies seeking creative financing before maturities
Bear case	Rate cuts could smooth out credit cycle, keeping it more average

Private Credit +

Bull case	High current yields; healthy spread to public credit over time; economic resiliency supportive of credit; secular tailwinds supporting growth; fresh capital can underwrite to current risks
Bear case	Credit risk likely to rise and lower-quality most at risk; regulatory scrutiny; public leveraged credit competition; significant capital allocating to PC

Real Assets

Private Real Estate

Bull case	Supply/demand imbalance in Residential driving secular opportunities; sectors like Data Centers rising; transaction cap rates slowly reflecting lower valuations; lower mortgage rates may unlock markets; lending strategies offering compelling profiles; distressed/opportunistic could emerge given stress
Bear case	Appraisal cap rates slower to fully adjust; transactions remain depressed; pressure rising in value-add multifamily financed with floating-rate debt

Infrastructure +

Bull case	Within RE, Infrastructure to continue benefiting from fiscal spend; large need for energy transition and upgrading aging infrastructure; potential to be inflation beneficiary if new resting rate structurally higher
Bear case	Higher rates challenging project financing; lower inflation could mitigate relative attractiveness

Tangible Assets

Bull case	Geopolitical risk could spill over and pressure commodities supply; macro factors including currency could support oil prices; potential for diversification and inflation hedge
Bear case	Muted global growth may reduce demand support; increasing energy supply has offset Middle East tensions; real rates staying high could pressure "safe" havens like gold

Bull case is an environment or set of factors that could represent tailwinds for the strategy. **Bear case** is an environment or set of factors that could represent headwinds for the strategy. **+** symbol indicates the strategies CIO views as having the most favorable opportunity set for new investment within the Alts asset classes.

Infrastructure: Within RE, Infrastructure remains a key long-term theme. The U.S. has a widely acknowledged aging infrastructure base that will require significant public and private investment. Hundreds of billions of dollars have already been earmarked for infrastructure spend through several federal bills in recent years. Infrastructure also has direct links to the Energy Transition theme, which will play out over the coming decades. In addition, Infrastructure has historically performed well on a relative basis during inflationary periods and has the potential to improve diversification in portfolios. Notably, in this era of higher inflation, PE deal activity, which can serve as a gauge of higher long-term return on investments, has shifted on a relative basis toward Infrastructure and away from Tech over the last three years.¹⁴

Tangible Assets: Global growth anchors demand for commodities and has recently lost momentum as U.S. and global economic data have consistently missed to the downside. The J.P. Morgan Global Manufacturing Purchasing Managers' Index (PMI) dropped back into contraction territory in July. The stable but weak global demand backdrop is reflected in industrial metals, where aggregate indexes have been under pressure the last few months and flattish over the last two years. We believe global growth and commodity demand will remain muted, but geopolitical risk and geoeconomic maneuvering are wild cards for energy commodity prices. Looking forward, anticipated Fed interest rate cuts, a likely weakening of the dollar from overvalued territory, untethered U.S. government debt, and geopolitical tensions should continue to support gold prices. We continue to believe gold is most effectively implemented as a strategic diversifier.

With the Fed shifting to an easier monetary policy stance as growth slows, the dollar will likely remain under pressure even as it has exhibited bouts of strength. Importantly, the U.S. dollar remains overvalued versus a number of major currencies.

MACRO STRATEGY

- The July index of leading economic indicators for the U.S. dropped 0.6%. The latest six-month decline in the index at 2.1% was less than the prior six-month drop of 3.1%, showing negative economic momentum is dissipating since the Fed's pivot late last year set off a substantial easing in financial conditions.
- The unemployment rate is rising, and job openings are falling. But new claims for unemployment compensation still show a healthy labor market with relatively few layoffs as overheated demand moves back into line with a stronger labor supply and the unemployment rate settles around the natural rate.
- The profits cycle for large U.S. companies and massive fiscal stimulus remain supportive of economic growth and risk-assets in the near term.
- Low financial obligations relative to firm nominal personal income gains and rising net worth continues to support resilient consumer spending, even as the labor market softens.
- J.P. Morgan Global Manufacturing PMI continues to suggest global cyclical momentum remains weak and is reflected in downward pressure on commodity prices.

ECONOMIC FORECASTS (AS OF 9/2/2024)

	Q1 2024A	Q2 2024A	Q3 2024E	Q4 2024E	2024E	2025E
Real global GDP (% y/y annualized)	-	-	-	-	3.1	3.3
Real U.S. GDP (% q/q annualized)	1.4	3.0	2.5	2.0	2.7	2.2
CPI inflation (% y/y)	3.2	3.2	3.0	2.9	3.1	2.3
Core CPI inflation (% y/y)	3.8	3.4	3.3	3.2	3.4	2.7
Unemployment rate (%)	3.8	4.0	4.1	4.1	4.0	4.1
Fed funds rate, end period (%)	5.33	5.33	5.13	4.88	4.88	3.88

The forecasts in the table are the baseline view from BofA Global Research. The Global Wealth & Investment Management (GWIM) Investment Strategy Committee (ISC) may make adjustments to this view over the course of the year and can express upside/downside to these forecasts. There can be no assurance that the forecasts will be achieved. Economic or financial forecasts are inherently limited and should not be relied on as indicators of future investment performance.

A= Actual. E= Estimate.

Sources: BofA Global Research; GWIM ISC as of September 3, 2024. Forecasts are subject to change.

When assessing your portfolio in light of our current guidance, consider the tactical positioning around asset allocation in reference to your own individual risk tolerance, time horizon, objectives and liquidity needs. Certain investments may not be appropriate, given your specific circumstances and investment plan. Certain security types, like hedged strategies and private equity investments, are subject to eligibility and suitability criteria. Your advisor can help you customize your portfolio in light of your specific circumstances.

S&P 500 SCENARIOS BASED ON FORWARD P/E AND 2024 EARNINGS PER SHARE (EPS)

The table below provides a rough indication of where the S&P 500 Index's central tendency could be, given various scenarios for EPS in 2024 and P/E ratio multiples. These scenarios are not official price targets and are not meant to signal levels where portfolio actions may always be needed. However, during times of market volatility, it's useful to keep this basic framework in mind when considering whether to incrementally add to or trim risk from portfolios while staying invested in one's strategic asset allocation framework.

2024 EPS	EPS Forward P/E (Next 12 months)				
	17.0x	18.0x	19.0x	20.0x	21.0x
\$265	4,505	4,770	5,035	5,300	5,565
\$255	4,335	4,590	4,845	5,100	5,355
\$245	4,165	4,410	4,655	4,900	5,145
\$235	3,995	4,230	4,465	4,700	4,935
\$225	3,825	4,050	4,275	4,500	4,725
\$215	3,655	3,870	4,085	4,300	4,515
\$205	3,485	3,690	3,895	4,100	4,305

For illustrative purposes only. Source: Chief Investment Office as of September 3, 2024.

¹⁴ Preqin. Infrastructure includes Industrials, Energy, Utilities, Raw Materials and Natural Resources. As of August 5, 2024.

CIO ASSET CLASS VIEWS AS OF SEPTEMBER 3, 2024

Asset Class	CIO View					Comments
	Underweight	Neutral	Overweight			
Global Equities	●	●	●	●	●	We are slightly overweight Equities and continue to view weakness as a buying opportunity for long-term investors. We remain overweight the U.S. and neutral EM, with a slight underweight to International Developed.
U.S. Large-cap Growth	●	●	●	●	●	We have a slight preference for Value over Growth, given better absolute and relative valuations. We believe portfolios should incorporate both Growth and Value factors as appropriate.
U.S. Large-cap Value	●	●	●	●	●	
U.S. Small-cap Growth	●	●	●	●	●	We maintain a slight overweight to Small-caps on attractive valuations, the declining cost of capital, and the stable U.S. consumer.
U.S. Small-cap Value	●	●	●	●	●	
International Developed	●	●	●	●	●	International Developed Equities valuations appear attractively valued, but underlying rates of nominal growth are expected to trail U.S. levels. International markets also remain more vulnerable to any potential broadening of conflicts in Ukraine and the Middle East.
Emerging Markets	●	●	●	●	●	We are neutral EM Equities overall with regional markets likely to be driven by relative exposures to weaker China growth, the ongoing Russia-Ukraine conflict and natural resource prices. Valuations appear attractive, but Fed rate cuts are unlikely to have a major positive impact.
International						
North America	●	●	●	●	●	The U.S. remains our preferred region given balance sheet strength, better fundamentals for consumer spending and healthy shareholder payouts.
Eurozone	●	●	●	●	●	Risks remain from potential fiscal tightening in high-budget-deficit EU countries, increased political uncertainty and the potential for energy supply constraints to reemerge amid the ongoing Russia-Ukraine and Middle East conflicts.
U.K.	●	●	●	●	●	Domestic demand at risk from still-high mortgage rates, alongside uncertainty over fiscal policy following general election. Withdrawal from EU single market remains a negative for medium-term growth with limited changes to UK-EU trade relations expected under new government.
Japan	●	●	●	●	●	Unwinding of yen carry trades and uncertainty over future BoJ interest rate and intervention policy should make for further volatility. Sustained positive inflation and official efforts to increase corporate returns to shareholders remain fundamental supports for valuation.
Pac Rim*	●	●	●	●	●	Regional activity to be dampened by exposure to weaker Chinese growth but offset by relative strength in domestic demand. Large weighting in Financials increases vulnerability to any potential broadening in banking sector stress.
Global Fixed Income	●	●	●	●	●	Bonds remain attractive and provide good diversification for multi-asset class portfolios with both reasonable income and the ability to decline substantially in yield in an economic downturn. Slightly long-duration positioning recommended, balancing the risk of further tightening/higher yields against significantly better valuations.
U.S. Governments	●	●	●	●	●	Nominal and real yields are very attractive across the curve relative to the last 10 to 15 years. A Treasury allocation for liquidity, principal preservation and diversification is preferred, as Treasuries can provide short-term diversification benefits to Equities among Fixed Income sectors. Rate volatility has increased and may remain high.
U.S. Mortgages	●	●	●	●	●	MBS spreads have tightened to the low-40's (bps) after a notable rally since the beginning of Q4 in 2023, and they have been range-bound YTD. This is still 1.1x the 10-year average, making MBS more attractive relative to Treasury and Corporate in terms of yield and spreads. With a longer-term horizon in mind, we are slightly overweight on the asset class, recognizing that there are near-term upside risks in spreads due to the unpredictability of QT and the macro environment.
U.S. Corporates	●	●	●	●	●	We remain slightly underweight IG Corporates despite a modest backup in spreads over the last month. This reflects our view that while all in yields may still be compelling, credit spreads have rallied sharply, YTD, and at around 95 bps, remain priced for a strong macro backdrop and leave little room for error. At current valuations, IG tends to underperform Treasuries modestly on an excess return basis 12 months forward. Therefore, a slightly underweight position is appropriate until a better entry point presents itself.
International Fixed Income	●	●	●	●	●	International rates markets have become significantly more attractive as global Central Banks raise rates to fight inflation, no longer trading at a significant discount to the U.S. except in Japan where the BoJ is still keeping longer-term rates artificially low.
High Yield	●	●	●	●	●	Valuations present more attractive medium-to-long-term returns even after estimating credit losses. However, increased recession concerns could cause near-term price losses, and spreads are not at recessionary levels. Any additions to HY, therefore, should have a long-time horizon. Within HY, we prefer balanced exposure between floating-rate loans and HY unsecured.
U.S. Investment-grade Tax Exempt	●	●	●	●	●	Muni valuations have cheapened to approximately average levels, making for a better entry point on new investments. We attribute this to higher net supply now that we have moved past the seasonally high redemption period of June to August, while new muni issuance is tracking over 35% higher than last year. Fundamental conditions remain generally favorable for state and local government bonds, but challenges exist in certain subsectors, e.g., private higher education and healthcare.
U.S. High Yield Tax Exempt	●	●	●	●	●	HY munis are rich relative to IG munis, with tighter than average credit spreads. An up-in-quality focus should help mitigate increased credit risk due to potential economic weakening.

* Pacific Rim refers to the geographic area surrounding the Pacific Ocean. The Pacific Rim covers the western shores of North America and South America, and the shores of Australia, eastern Asia and the islands of the Pacific. Tactical qualitative investment strategy weightings are relative in nature versus the strategic weightings for a fully diversified portfolio. Weightings are based on the relative attractiveness of each asset class. Tactical strategy weightings are for a 12- to 18-month time horizon. CIO asset class views are relative to the CIO Strategic Asset Allocation (SAA) of a multi-asset portfolio. Because economic and market conditions change, recommended allocations may vary in the future. Asset allocation cannot eliminate the risk of fluctuating prices and uncertain returns. All sector and asset allocation recommendations must be considered in the context of an individual investor's goals, time horizon, liquidity needs and risk tolerance. Not all recommendations will be in the best interest of all investors.

CIO EQUITY SECTOR VIEWS AS OF SEPTEMBER 3, 2024

The CIO Equity sector view is developed by applying a multi-input process combining the CIO's factor views and fundamental bottom-up industry outlook with top-down macro-economic changes and trends. The factor approach emphasizes valuation and momentum as key inputs, with a fundamental overlay taking into consideration forward-looking views of growth, profits, policy, events and sentiment as well as inclusion of certain investment themes. BofA Global Research's sector strategy views are also captured as an input into the CIO process. Our sector views are developed with a 12- to 18-month outlook but are revisited monthly by the GWIM Investment Strategy Committee.

Sector	CIO View					Comments
	Underweight	Neutral	Overweight			
Energy	●	●	●	●	●	Despite signs of slowing demand and a more cautious outlook for 2025, we remain overweight the Energy sector for three key reasons: 1) Attractive valuation as the lowest valued sector in the S&P 500 on cash flows and earnings; 2) High free cash flow (FCF) generation at current oil price levels and attractive FCF yields and 3) Hedge for potential disruptions in energy production and rising geopolitical tensions. OPEC+ extended their production cuts through the end of Q3 2024, and the decline in capital expenditures for long-cycle energy investments in recent years also supports Energy prices and stocks. Above-average energy prices combined with substantial cost-cutting initiatives and capital discipline over recent years built significant operating leverage into Energy companies. We also highlight higher cash returns to shareholders through base dividends, variable dividends, and stock buybacks. Longer term, secular headwinds still confront the sector, including the transition to clean energy, lower renewable energy costs and sustainability-focused by investors. Continue to emphasize companies that are low-cost producers with high FCF, balance sheet strength and low break-even oil prices. Energy stocks still provide attractive valuations and strong dividends with weaker momentum.
Healthcare	●	●	●	●	●	Consider positions in larger biopharma stocks with attractive relative valuations and upcoming catalysts. In an environment where financial conditions are in flux, Healthcare stocks provide attractive characteristics, including quality, dividend growth, dividend yield and lower beta. Healthcare fundamentals have been able to withstand much of the macro pressures seen globally, but flows last year were weak in the Healthcare sector. Further, in 2023 negative earnings revisions were made by analysts across the sector. Distributors, medical devices, and large biopharma are best positioned, in our view, to weather pressure on margins, while a return to a more normalized environment should benefit life science equipment and tools companies as we progress through 2024. As a whole, large pharmaceutical companies remain attractive as they trade at a material discount to Healthcare sector peers and the broader market. Further, significant cash on strong balance sheets, combined with more aggressive business development efforts and a greater focus on explaining long-term growth drivers make large pharma more attractive over the intermediate term. Over a longer duration, drug pricing headwinds may return as demographic shifts put more pressure on government payors and as value-based care initiatives gain momentum. Emphasize exposure to long-term positive trends in life science/bioprocessing equipment, innovative and differentiated medical devices and animal health, as well as more intermediate opportunities in Large-cap biopharma and diversified medical technology. Valuation remains attractive, and momentum recently improved.
Consumer Discretionary	●	●	●	●	●	With a resilient consumer, a solid job market, lower interest rates on the horizon and better-than-expected economic backdrop, we are overweight Consumer Discretionary. Slightly lower energy costs, wage increases and a strong job market with only selective job cuts confined largely to the technology-related industries is helping to maintain solid consumer spending. Consumers remain resilient and are finding ways to alter their budgets to accommodate both experiences and necessities. Further, with inflation declining from the highs experienced last summer and interest rates also moving lower, this is supporting consumer confidence. Consumer retail channels are shifting back to online spending as value-oriented consumers utilize alternative payment methods to supplement their spending and seek out bargains. More evidence of economic strength and a resilient consumer could help support relative earnings growth and relative valuation levels. Valuation for the sector is elevated and momentum improved in recent weeks.
Financials	●	●	▶	●	●	We are moving to overweight on the Financials sector concurrent with the start of a Fed easing cycle. Perhaps counterintuitively, a lower Fed funds rate benefits deposit gatherers because of the immediate decline in interest expense paid on deposits. The decline in interest revenue from loans/securities is much more gradual, so net interest income has likely bottomed for this cycle. The risks associated with the regional banking troubles in March 2023 have faded and a pickup in regional bank mergers in recent months suggests confidence has been sufficiently restored to deploy capital. Funding pressure coupled with capital discipline has modestly tightened credit standards and slowed the pace of lending, but the start of Fed cuts would alleviate pressure on both fronts. A lower Fed target rate typically lowers interest rates across the curve (and throughout the U.S. financial system), which would have the effect of increasing bond prices and shrinking losses generated by higher rates. Shrinking unrealized losses in bond portfolios should accrete to equity holders in the form of a higher book value and increased capital flexibility for banks, insurance companies, and asset managers. Capital return will likely remain the cornerstone of the investment case for most of the Financials sector. Lower interest rates should also improve credit quality (especially CRE) and facilitate workouts instead of charge-offs. Overall, the volatility of the Financials sector should improve with the recent addition of large e-payment card networks that have been stable earnings compounders historically (without taking credit risk). We also favor alternative asset managers with proven track records, billions in dry powder, that consistently draw fund inflows, and maintain management fee pricing power. Alts (especially PE) have demonstrated an ability to thrive in all kinds of economic environments, including recession. Overall, valuation is attractive and earnings driven momentum should continue to improve as rates move lower.

Sector	CIO View			Comments
	Underweight	Neutral	Overweight	
Information Technology	●	●	●	<p>The Technology sector is neutral despite improvements in supply chains and AI-driven flows into mega-cap Technology stocks. However, margin risks remain for companies in the sector, and the potential remains for downward earnings revisions that are more likely to affect higher-beta, higher-valuation companies. Despite strong long-term Cloud and AI trends, software margins could continue to deteriorate, as Cloud consumption could potentially come under some pressure near term and is not immune to a macro slowdown. We suggest a neutral weight in IT, with a bias to larger and higher-quality companies with strong earnings growth, FCF and balance sheets. We continue to encourage investors to be careful about unprofitable, expensive, and long-duration IT companies. The pandemic accelerated the digital transitions for many industries, but, over the longer-term, we remain positive on the secular growth trends for Cloud computing, machine learning and AI, data centers, software, cybersecurity, and semiconductors. Valuations in the sector declined in 2022 but were still elevated after rising again in 2023 and to start 2024, especially after the rally in AI-related companies. Further, any additional moves higher in interest rates could pressure multiples for high-growth and high-valuation technology stocks with low to no profits; therefore, look for GARP (growth at a reasonable price) in software and semiconductors. The IT sector still generates significant FCF, dividend growth and remain long-term fundamental drivers for the sector. Technology is deflationary by nature; therefore, long-term investors should look to add to transformational and industry-leading businesses on market weakness. Valuations remain elevated and momentum recently slowed.</p>
Communication Services	●	●	●	<p>We are neutral on the Communication Services sector, as some of the largest companies in this sector provide high-quality fundamental characteristics and could be more attractive in a slow-growth economic environment. Despite our concern for ongoing regulatory oversight and the never-ending battle over content, management teams are now adjusting their business models to reduce costs and become more efficient. Ad spending is moving from e-commerce to travel and leisure, hence advertisers are having to shift their targeting. Retailers are suffering from rising costs and slowing sales, which could drive changes in advertising spend. We are more constructive on the sector based on three key factors: 1) Valuation multiples were largely de-risked last year; 2) Earnings estimates were reduced; and 3) More importantly, broad cost-reduction plans could create potential earnings upside. Valuations are a little rich and momentum deteriorated over the last month.</p>
Industrials	●	●	●	<p>We are lowering Industrials to neutral after mixed Q2 earnings results, a lack of significant green shoots in the industrial economy outside of AI and electrification, and cautious second half company guidance. Longer term there are multiple thematic drivers for Industrials over the next three to five years including improving outlooks for international defense budgets outside the U.S. as the global risk environment is elevated, underpinning favorable dynamics for defense companies. Recent safety and manufacturing issues in commercial aerospace weighed on the sector but longer-term aerospace should benefit from a multiyear backlog of commercial plane orders to build and delayed deliveries. Potential improvements in the global capital expenditures cycle, including the normalization and reshoring of supply chains and manufacturing, and investment in new equipment after years of focusing on productivity, and fiscal stimulus plans could support the construction, transportation, machinery, and freight and logistics industries longer term. However, weaker import/export demand from Europe and China could be a near-term drag on earnings growth for industrial conglomerates and transport stocks. Secular growth drivers like the evolution of AI and increased power demand support the longer-term view for Industrials, and near term the sector provides exposure to short-cycle/early-cycle areas. Valuation is slightly elevated, and momentum is neutral.</p>
Real Estate	●	●	●	<p>The decline in interest rates from 2023 peak levels reduces some but not all risks regarding refinancing and the cost of capital for RE projects. Further, expectations of Fed rate cuts in the future in addition to negative positioning and very bearish sentiment last year in the RE sector could lead to increased Equity portfolio exposure to the sector. However, interest rates are still elevated compared to the zero-rate policy environment, therefore increased interest expenses could still weigh on RE sector earnings in coming quarters. We would be more selective within the RE sector and prefer neutral sector exposure. There are mixed outlooks among its subsectors because of consumer and corporate changes like remote work, eCommerce, less business travel, etc., that are potential longer-term headwinds for CRE companies (e.g., office), mall operators and retail-related property owners as companies consolidate RE footprints. Furthermore, risks are rising for downward pressure on rental rates as lease contracts expire and new contracts are negotiated. Continue to emphasize longer-term secular trends in data centers, communication infrastructure (towers), storage and industrial RE. Valuation remains neutral and momentum recently improved.</p>
Utilities	●	●	●	<p>Utility investors continue to balance implications from a still-elevated cost of capital compared to the past decade with accelerating electricity demand forecasts driven by the AI boom, which are expected to drive a renewed push for investment in renewable energy and grid-hardening projects at utilities. Regulatory reviews are an important risk factor for the sector, and we note this risk is elevated in 2024 as state-level regulators have become increasingly sensitive to passing along increases to rate payers who are financially stretched by lingering inflation. Utilities historically provide reliable earnings and outperform in the late cycle and during economic growth slowdowns, especially regulated utilities that provide a defensive hedge to portfolios. Utilities have provided greater balance and lower beta and helped diversify cyclical Equity exposure in portfolios. For the longer-term, we emphasize Utilities with growing renewable power generation from solar and de-emphasize ones that rely strictly on coal-power generation. Over the next decade, the IRA legislation provides a strong runway for future renewable energy investments and projects—though we expect noise about potential IRA repeal to dominate ahead of the November election, with potential for volatility among Utility stocks perceived as IRA “leaders.” We prefer Utilities with strong balance sheets, constructive regulatory mechanisms, and low-volatility business models. Unregulated Independent Power Producers (IPPs) are a small subsector that we currently favor given exposure to growth from rising AI and data center demand. Valuation remains slightly elevated compared with other higher yield assets but beginning to improve compared to other sectors following recent earnings estimate revisions.</p>

CIO View			Comments
Sector	Underweight	Neutral	
Materials	● ● ● ● ●	●	<p>Pockets of slower global growth and weaker commodity prices factor into our more cautious view on the Materials sector for 2024. We are seeing deceleration in the pricing cycle from higher pricing levels in 2022 and 2023. Higher interest rates in the developed world and ongoing trials securing labor and materials are pushing some project timelines to the right, and, with the additional challenge of higher energy costs, we are seeing some formerly profitable projects being reconsidered. On the supply side, concerns remain around too much new capacity in the future for petrochemicals and commodity chemicals with questions regarding demand levels for 2024. Multiples could expand or contract dependent on pricing across the commodity complex. Downward pricing pressure would give some intermediaries relief on costs, but if they are also experiencing volumes decline, operating leverage could be at risk. We still see some longer-term tailwinds for demand, such as bipartisan support for U.S. infrastructure and energy transition spending, AI growth and renewable power buildouts over the longer term; however, mixed data and the slower-than-expected growth and activity in China makes the risk-reward outlook less attractive with both inflation and pricing power moving lower. Earnings revision trends could be mixed this year. As a result, the underlying sector valuation is neutral, and weak momentum.</p>
Consumer Staples	● ● ● ● ●	●	<p>Remain underweight the more defensive Consumer Staples sector and prefer exposure to the more cyclical Consumer Discretionary sector. Broad-based slowdown in demand for consumer-packaged goods products is a function of trade down, substitution and a more discerning bargain-seeking consumer. Demand for needs and necessities across personal care and household products has held up better than most other consumer packaged goods products. It's too early to tell whether the popularity of the new weight-loss drugs is affecting food and beverage volumes or whether consumers are altering their budgets to reflect the still-elevated consumer goods prices. Without a predictable return to positive volume growth, traditional consumer packaged goods companies will likely struggle to show improvement in profits and margins needed to support current relative valuation levels. Valuations are rich and momentum improved over the last couple of weeks on market volatility.</p>

Source: Chief Investment Office. All sector and asset allocation recommendations must be considered in the context of an individual investor's goals, time horizon, liquidity needs and risk tolerance. Not all recommendations will be in the best interest of all investors.

CIO THEMATIC INVESTING AS OF SEPTEMBER 3, 2024

Taking the long view, the following themes and subthemes are considered among the most powerful structural forces in the world. They are macro in nature but carry risks and reward for companies, both large and small. These themes are transformational and carry long-term implications for economic growth, the cost of capital and global earnings. Gaining exposure to these themes is a key ingredient to investing, in our view.

ARTIFICIAL INTELLIGENCE (AI)	<p>Building on last year's AI-enthusiasm, the next act for Generative AI is about adoption and deployment. The promise that AI will eventually aid productivity and efficiencies while reducing costs is also hastening the need for complementary industrial and service Robotics/Automation. Use cases of Generative AI and robotics within Healthcare Innovation abound, with the potential to aid drug discovery, age-related disease treatments and gene therapies/ mapping. The massive growth in unstructured data being created and processed by machines, devices and systems is feeding Big Data Analytics and Storage. An ongoing migration of data and applications to Cloud Computing infrastructure as well as hardware providers supports the AI data boom.</p>
DEMOGRAPHICS	<p>Several demographic transitions serve as important arbiters of future growth. That's true about the Great Wealth Transfer of over \$84 trillion in assets likely to be inherited through 2045, according to Cerulli Associates. As main recipients, both the Millennials (born 1981-1996) and Gen Z (born 1997-2012) could have greater influence on consumer spending patterns and preferences. Tax treatment and business regulation continue to drive an intra-U.S. migration, while a Global Migration cycle is also underway given displaced populations owing to conflict, forced migration and other factors. Changing the face of consumerism globally is the Emerging Market Consumer, which represents a powerful middle-class cohort with rising incomes and improved health outcomes. With lengthening life expectancies globally, Global Ageing puts a renewed focus on healthcare, aged-care, financial, and consumer products and services. So too does the Silver Tsunami of ageing and wealthy Baby Boomers, who represent the bulk of consumer spending in the U.S.</p>
INFRASTRUCTURE	<p>Infrastructure needs today span physical infrastructure well beyond its useful life, to energy assets, both traditional and renewable. As the sought-after Energy Transition toward renewable energy sources such as solar, wind, hydrogen, and nuclear remain in focus, so does reliable Energy Storage and Distribution of our energy sources. If the Future Mobility of the global car fleet is electric, Electric Vehicle (EV) production demands more mining of copper, lithium, nickel, manganese, cobalt and graphite, etc. to produce EVs as compared to internal combustion engines. Other key investment opportunities exist given disruptions through climate related events, cyber threats, or general impairments to the National Grid; but also globally, the risk of scarcity/stress to resource facilities among Water/Waste Management.</p>
SECURITY	<p>Industrial Policies are in, as the "visible hand" of the government is just as prominent as the "invisible hand" of the private sector, with hundreds of billions of dollars committed from the White House to incentivize security and self-reliance of suppliers and resources. Regulation pertaining to Surveillance and adjacent technologies, as well as legislation of data privacy rights will be a topic on Capitol Hill in 2024. Of national security concern, defense spending in the years ahead likely remains elevated given ongoing Ukraine-Russia and Israel-Hamas wars in addition to simmering U.S.-China tensions. Aerospace and Defense should benefit from the remilitarization in the wake of shrinking stockpiles. Ongoing and sophisticated ransomware and data breaches bolsters Cybersecurity budgets across industries. With the commercialization of space, security extends to Space and space-based assets (such as drones, satellites, data links, weather monitoring and Global Positioning System (GPS)).</p>
POLYCRISIS	<p>Growing conflict and crisis globally can be described as Multipolar Disorder, leading to unforeseen realities for the macroeconomic backdrop and markets. Resource Protectionism has been on the rise as the extraction, sourcing and management of the world's resources will stay in focus with commodities, metals and mining complexes already stretched. Although net zero commitments are widespread, the current path to Decarbonization targets remains narrow. Also at crisis levels, global debt reached a staggering \$307 trillion last year according to Institute of International Finance, putting in focus Debt and Deficit concerns. A million people in the U.S. have died of drug overdose since 2000 while suicide rates are at their highest level in over 80 years—All tragedies related to Deaths of Despair, and of particular impact to our healthcare system.</p>

Index Definitions

Securities indexes assume reinvestment of all distributions and interest payments. Indexes are unmanaged and do not take into account fees or expenses. It is not possible to invest directly in an index. Indexes are all based in U.S. dollars.

Equity/S&P 500 Index includes a representative sample of 500 leading companies in leading industries of the U.S. economy. Although the index focuses on the large-cap segment of the market, with approximately 75% coverage of U.S. equities, it is also an ideal proxy for the total market.

J.P. Morgan Global Manufacturing PMI data gives a detailed look at the manufacturing sector including the pace of manufacturing growth and the direction of growth for this sector.

Chicago Board Options Exchange Volatility Index is a real-time market index that represents the market's expectation of 30-day forward-looking volatility.

Lincoln Senior Debt Index is a quarterly index that tracks the fair market value of 1,600 middle market, direct lending credit investments every quarter across approximately 175+ fund clients in the U.S. and in Europe.

Green Street's Commercial Price Index is a time series of unleveraged U.S. commercial property values that captures the prices at which commercial real estate transactions are currently being negotiated and contracted.

index of leading economic indicators is an American economic leading indicator intended to forecast future economic activity. It is calculated by The Conference Board, a non-governmental organization, which determines the value of the index from the values of ten key variables.

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Investments in Infrastructure Assets will be subject to risks incidental to owning and operating infrastructure projects, including risks associated with the general economic climate, geographic or market concentration, government regulations and fluctuations in interest rates. The industries targeted for investment may be highly regulated by governmental agencies. Such regulations may impact an investor's ability to acquire, dispose of and/or manage investments.

Alternative investments are speculative and involve a high degree of risk.

Alternative investments are intended for qualified investors only. Alternative Investments such as derivatives, hedge funds, private equity funds, and funds of funds can result in higher return potential but also higher loss potential. Changes in economic conditions or other circumstances may adversely affect your investments. Before you invest in alternative investments, you should consider your overall financial situation, how much money you have to invest, your need for liquidity, and your tolerance for risk.

Nonfinancial assets, such as closely-held businesses, real estate, fine art, oil, gas and mineral properties, and timber, farm and ranch land, are complex in nature and involve risks including total loss of value. Special risk considerations include natural events (for example, earthquakes or fires), complex tax considerations, and lack of liquidity. Nonfinancial assets are not in the best interest of all investors. Always consult with your independent attorney, tax advisor, investment manager, and insurance agent for final recommendations and before changing or implementing any financial, tax, or estate planning strategy.

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