



OUR VIEW

JULY 2024

The first half of 2024 has the U.S. equity market on track for a very good year, with the S&P 500 +15.3% (Table 1). Extreme market concentration remains a central theme in the U.S. equity market with 62% of the year-to-date (YTD) return and over 100% of the second quarter return due to a handful of stocks¹. The equal-weighted S&P 500 generated a more modest +5.1% YTD return and the Russell 2000 small-cap index only +1.7%, further evidence this has not been a broad market rally. Internationally, equities rose +6.0% in the first half of the year and U.S. bond returns have been negative, declining 0.7%, as investors wait for the Federal Reserve’s next move.

The Federal Reserve “pause” has been good for equities, as is often the case. Two factors could help support broader equity market participation: further disinflation, which could lead to lower rates, and signs of sustainable economic strength, which would support more meaningful earnings growth. There are some signs that earnings are poised to accelerate, although it is still being led by a few of the dominant mega-cap companies that are large weights in the market cap weighted equity indices.

We have often stated investors should not try to time markets, for if you miss a few critical days each year, your historical compounded returns are much lower. Today, we would note an important consideration, the number of geopolitical risks whose outcomes cannot be measured or predicted is as plentiful as we can recall. In addition, large-

Market Performance

Indices	YTD
U.S. Market-Weighted	15.3%
International Equity	6.0%
U.S. Equal-Weighted	5.1%
U.S. Small-Cap	1.7%
U.S. Bonds	-0.7%

Source: Bloomberg. Total returns as of 06/30/24. Table 1
Indices: S&P 500, MSCI ACWI ex-US, S&P 500 Equal Weighted, Russell 2000, U.S. Aggregate. Please see important disclosures at the end of this whitepaper.

cap U.S. equity valuations are relatively expensive, leading us to the conclusion that this is a good time to have some cash or liquid reserves available to deploy if or when there is a more compelling opportunity.

Global Election Uncertainty Indicates Voter Dissatisfaction

There will be more than 60 national political elections representing more than half of the world’s population over the course of 2024, and so far, incumbent parties and politicians are faring poorly. In just the last week we have

¹YTD: Nvidia, Microsoft, Apple, Alphabet, Amazon, Meta. Q2 Nvidia, Apple, Microsoft, Alphabet.



seen incumbents lose in France, the UK, and Iran. This raises an important question: why are voters demanding change? Simple conclusions may be naïve, but it seems germane to look for common threads, and the global inflation of the last few years appears to be exhibit A for voter agitation. The two most important issues for a voter are typically employment - predominantly impacting those who do not have a job - and inflation, currently impacting everyone, everywhere.

India – A Weakened Mandate: In India, Prime Minister Narendra Modi sought and won his third consecutive five-year term. Polling results and a record of legitimate economic progress led to a consensus assumption that Modi would win with ease and earn a super majority of parliament seats. However, the actual election results, finalized in early June, diverged from these expectations. Modi's BJP party did not even win a simple majority (272 seats) in parliament and had to form a coalition government with allied parties to make sure it could govern effectively. India had over 600 million people vote in their election and they sent a clear message: "do better". Ultimately, like any democracy, the receipt of such a message should help the country work towards better outcomes for all, reminding politicians that their position is a privileged one, and the masses are watching attentively. Five more years of Modi's leadership should allow India to continue its current path, one of high growth and significant reforms.

France – A No Confidence Vote: The result of the French election is highly problematic for incumbent President Emmanuel Macron's centrist government. In the last week both rounds of the election indicated voters prefer a change, first with a far-right win, but then ultimately with the far-left winning the second and final round. For Macron and his party this was essentially a vote of "no confidence." Macron's gamble has left his party scratching their collective head as to what his plan was and how it backfired. Macron is now a lame duck for the last three years of his presidency. One might wonder why anyone outside of France should care. For starters, the left-wing Nouveau Front Populaire and the right-wing Rassemblement National, while on opposite ends of the political spectrum, control more than half of

the representatives in the National Assembly and have been traditionally antagonistic toward NATO, European institutions, and the euro. Both parties' policies also call for profligate spending and a meaningful increase in the national deficit. In 2011, Greece's fiscal deficit led to a European financial crisis and a confidence crisis for the EU. France is the second largest economy in Europe behind Germany and is already facing a remarkably high fiscal deficit. A fiscal crisis in France would be significant and French bond yields and bond insurance are showing signs of concern.

United States – Incumbent Angst: A casual observer might assume President Biden would have a straightforward path to re-election: the unemployment rate was 6.7% when President Biden came into office, today it is 4.0%. The COVID pandemic has ended, the stock market has appreciated +49.5% since he entered office, GDP/capita continues to rise, and yet, on the heels of a poor debate performance, President Biden trails in the polls with just four months to go. One cannot simply blame his age (81); voter unrest is often influenced by something as simple as the cost of one's grocery basket and inflation has remained stubbornly high, especially on items that impact lower- and middle-income families. One problem is nobody feels much better off, especially those not invested in the stock market. Ironically, the U.S. "misery index," a sum of the unemployment rate and inflation rate hovers at 7.1%, the lowest level it has been for an incumbent president in the last 50 years.

Global Implications

The ramifications of these elections may have a material impact on the existing world order. Historically successful institutions like NATO could see fractures, and the EU experiment may come under further scrutiny. In the U.S., the final election result may lead to changes at the Federal Reserve and U.S. Treasury with meaningful destabilization risk across global markets. In recent years we have observed a reversal of globalization via re-shoring manufacturing, onerous import tariffs and immigration policy. The effect is a shift toward a more multipolar world. As a result, international investors should think in terms



of regional winners. India seems to us to be a notable beneficiary of the western world's shift to de-emphasize dependence on China. Asian economies with cheap labor should also benefit as supply chains move from China but stay regionally proximate. U.S. domestic manufacturing should also benefit with re-shoring efforts already underway but with the corresponding risk of higher costs. Resource nationalism is also more likely in a multipolar world as countries and regions protect their "domestic" supplies, and scarce natural resources will become even more valuable. Gold, for example, hit an all-time high as China's government has been a marginal buyer divesting away from other perceived stores of value like U.S. Treasuries. The bottom line is higher perceived risks will mean investors will have a higher affinity for perceived safety.

Portfolio Positioning

We have not changed our asset allocation but as stated earlier, we believe it makes sense to keep some cash available for the inevitable buying opportunities that will arise. Short-term U.S. Treasury Bills still yield over 5.0%, an acceptable return for a liquid reserve set aside with patience for new opportunities. We still favor the

U.S. as our primary equity market, and India remains our largest international equity market allocation. The private equity markets have been stuck for over two years but there may be some signs that these markets are beginning to improve via a modest pickup in transactions and initial public offerings ("IPOs"). Due to expected opportunities, we are also spending time on private credit. Finally, (government guaranteed) Agency mortgages are providing attractive spreads to Treasuries. The bottom line is we have not made any changes yet, but we believe investors need to be highly alert to the risks and opportunities that may occur in the near-term.

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