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REVIEW & COMMENTARY

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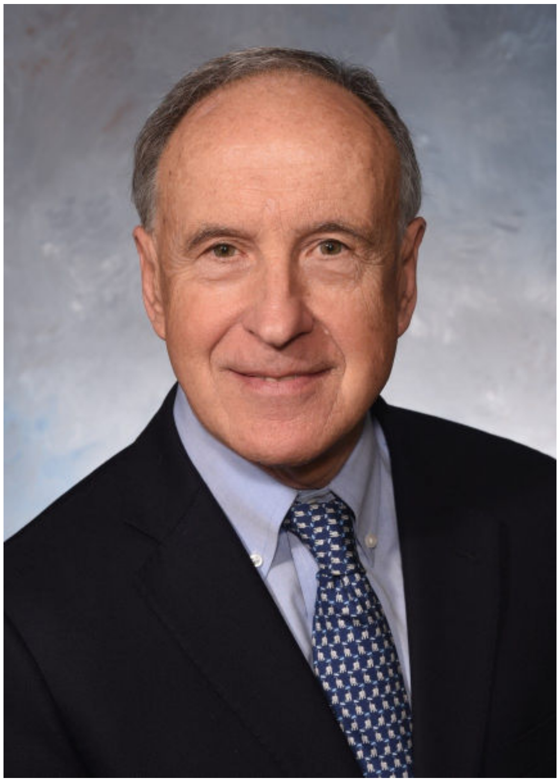
US Markets Continue Upward Trend



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We are, once again, firmly in the midst of a market that has been driven by a small number of very large-cap growth stocks.

Major U.S. equity markets continued their upward path in Q2 24, and the early part of Q3 as well. However, various other markets differed greatly in performance in the period, primarily due to size (small versus large), style (value versus growth) or index composition (equal-weight versus market-weight).

These differences make guesses as to future performance more difficult than usual, especially in a year that promises considerable volatility due to uncertainty over coming earnings, the direction of the economy, interest rates, over the country's leadership and over the various hot-spots of global turbulence that we continue to see.

As many of you probably know by now, the well-known S&P 500 index ("S&P 500") rose 4.28% in the quarter, giving it a total return of 15.29% through June 30th. The NASDAQ Composite Index rose 8.47% in Q2, giving it a total return of 18.57% through the end of Q2. Most of the gains come from companies providing products and services used in Artificial Intelligence, or "A.I." In some ways it is similar to the "dot.com" market boom of the late 1990s which ended badly in 2000.

Beyond those indices things differ. The well-known Dow Jones Industrial Average fell 1.27% in the second quarter and had a total return of 4.79% year to date. Mid-Cap stocks, represented by the S&P MidCap 400 Index fell 3.45% in Q2 while the S&P SmallCap 600 Index fell 3.11%. While the mid cap Index is up 6.17% year-to-date, the small cap Index is down 0.72%. Growth Indices trounced Value indices in the quarter as well with the S&P 500 Growth Index up 9.59% while the S&P 500 Value Index fell 2.10%. And, lastly, the equal-weight S&P 500 fell 2.63% in the quarter but remained up 5.08% for the year compared to the 4.28% and 15.29% gains in the better-known cap weighted S&P 500.

The main reason for the discrepancy in the various indices is that we are, once again, firmly in the midst of a market that has been driven by a small number of very large-cap growth stocks. If you were in those stocks, you made money in the quarter while if you were not your results suffered. The following table illustrates this well: (over)

Company	Index Weight	Y-T-D 2024 % Gain	Contribution	Company	Index Weight	Q2 2024 % Gain	Contribution
S&P 500	100.00%	15.29%	15.29%	S&P 500	100.00%	4.28%	4.28%
NVIDIA Corp.	4.93%	149.50%	4.58%	NVIDIA Corp.	5.65%	36.74%	1.90%
Microsoft Corp.	7.15%	19.29%	1.35%	Apple, Inc.	6.13%	22.99%	1.35%
Amazon, Inc.	3.71%	27.19%	0.95%	Alphabet Class A	2.25%	20.82%	0.44%
Meta Platforms	2.38%	42.74%	0.88%	Microsoft Corp.	7.13%	6.42%	0.43%
Eli Lilly & Co.	1.40%	55.84%	0.65%	Alphabet Class C	1.90%	20.60%	0.37%
Alphabet Class A	2.14%	30.54%	0.61%	Broadcom, Inc.	1.40%	21.53%	0.28%
Apple, Inc.	6.25%	9.68%	0.57%	Amazon.com Inc.	3.81%	7.13%	0.27%
Broadcom, Inc.	1.35%	44.90%	0.53%	Eli Lilly & Co.	1.45%	16.57%	0.23%
Alphabet Class C	1.81%	30.30%	0.51%	Tesla, Inc.	1.10%	12.57%	0.13%
Berkshire Hathaway	1.70%	14.06%	0.25%	Costco Corp.	0.79%	16.21%	0.13%

Source: John Hancock Investment Management

The table shows, for example, that NVIDIA rose 149.5% between Dec. 31 and June 30th. Of the S&P 500's 15.29% return, NVIDIA accounted for 4.58% of it, or, put more simply, 30% of the S&P 500's return so far this year was due solely to NVIDIA. And the top 10 stocks year to date contributed 10.88% of the index's 15.29%. This means 71% of the S&P 500's gains came from the 10 stocks above. In the second quarter, returns were even more concentrated. NVIDIA, again the top performer of the group, accounted for 44% of the S&P 500's 4.28% return. And the top 10 accounted for 9.81% of the Index's 4.28% return, meaning the other 490 S&P 500 stocks detracted from its return by 5.53%.

Whether having returns so concentrated in a small number of stocks is healthy for markets is a good question now.

Although the valuations of market leading tech stocks such as NVIDIA are high, they pale in comparison to the valuations reached in the "dot.com" era. At its peak price of $82 on March 27, 2000, Cisco sold for about 227x trailing earnings per share, and more than 100x forward estimates. In comparison, NVIDIA sells for 35x to 40x its earnings per share figures. Microsoft and Apple sell for similar p/e (price/earnings) ratios. All three share some similar attributes: strong demand for their products and incredible balance sheets that give them tremendous financial flexibility.

With the quarter's end, we will be in the midst of the second quarter earnings season shortly. Analysts continue to expect good earnings growth this year. According to S&P Capital/IQ analysts expect S&P 500 companies to earn $243.57 per share in aggregate in 2024, an increase of 11.7% over 2023's figure. This values the S&P 500 at about 22.8x next year's earnings, a figure high in comparison to the index's five-year average p/e ratio of 19.3x earnings and its 10-year average of 17.9x earnings. Even looking out to 2025's figure of $269.23 gives the market an above long-term averages p/e ratio of 20.6x.

Recent economic statistics are a mixed blessing. The economy added 206,000 new jobs in June 2024 but revised down the number of jobs added in April and May by 110,000. This made the quarterly average 177,000 new jobs per month, down significantly from the 267,000 figures of the first quarter. In addition, about 34% of June's new jobs reflected government hiring versus private sector hiring, and the unemployment rate rose to 4.1%, the highest level since November 2021.

The positive impact of a slowing economy could be the beginning of the long-awaited reduction in short-term interest rates. Longer-term interest rates have already started falling. After peaking, for 2024, at 4.71% on April, they have fallen to the 4.28% level (July 5). (Continue to page 3)

The political and geopolitical situations we find ourselves in now could have major impacts on equity markets for the rest of the year. Historically, equity markets have not shown any consistent bias towards electing presidents of either party – markets have done both well and badly following the election of members of either party. However, two situations somewhat analogous to today's are worth remembering. The S&P 500 fell 36% in the bear market of 1968-1970 during Lyndon Johnson's term. This period includes the time after his announcement that he wouldn't seek reelection. This was a period of rapidly rising inflation exacerbated by high government spending to fund the Vietnam War. During Richard Nixon's term, which included the Watergate scandal and his resignation, the S&P 500 fell 48%. But again, separating the Watergate scandal from the economic conditions at the time (high inflation, OPEC oil embargo, deep recession) is impossible.

The global situation remains unpredictable and does present a risk to markets. The Russia-Ukraine conflict is into its third year. The China-Taiwan situation is at least that old and now, the Israeli-Hamas conflict is nine months old. All have the potential, at least, to affect global markets. All also have the potential to help markets should they show signs of ending.

Despite the many reasons to worry about the direction of equity markets, it is always wise to remember that they rise roughly two thirds of the time and fall one-third of the time. And both the timing and magnitude of the down markets are impossible to predict. For this main reason, we cringe when we hear someone say they "need to get out of the market today." It is far better to know your own tolerance for risk and build a portfolio accordingly. For those worried about stocks, short-term fixed rate investments still offer attractive yields. For those still attracted to growth, there remain many stocks with valuations attractive in comparison to their growth rates.

As always, we are here to help you with your investment needs.