WhaleRock NEWSLETTER

MARKET UPDATE
Spring 2024

United States Equities are off to a strong start in 2024, with the S&P 500 up +7.4% through April 26. The move higher in stocks has been powered by investors' heightened focus on the rapid technological advancement occurring in artificial intelligence and consumers continuing to spend on events, travel, and discretionary goods, which has bolstered corporate earnings. There is much to come in 2024: The Federal Reserve is closely monitoring the impact of a Fed Funds Rate greater than 5% on economic activity, corporations are spending hundreds of billions of dollars in the race for artificial intelligence, and a presidential election in the fall. With so much happening, we wanted to share with you our views on stocks, the economy, and key data points we are evaluating to assess what comes next.

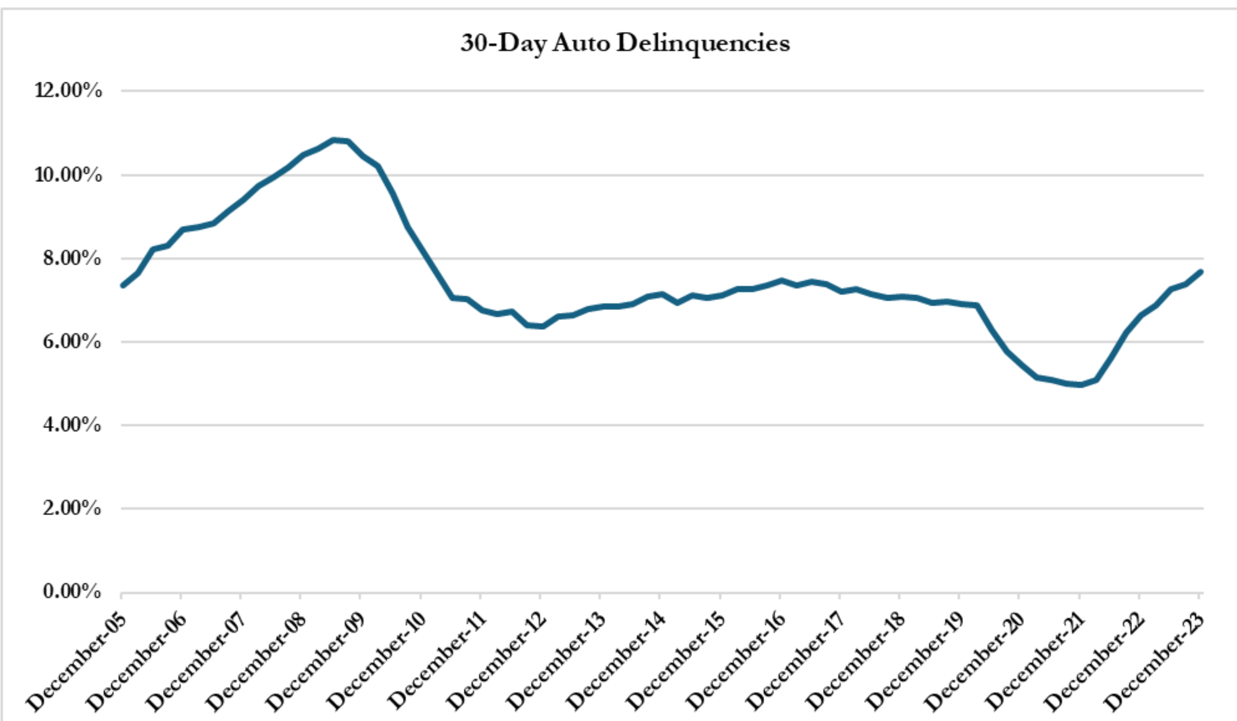
The Economy:

In our view, the best way to describe the current economy is resilient. Higher interest rates historically have served as an impediment to economic growth. However, despite the Fed Funds Rate having been over 5% for a year, the economy continues to grow at a modest pace, with the first quarter of 2024 Gross Domestic Product measured at 1.6% and consumer spending hitting record levels.

There are reasons to believe that the economy could continue to grow at a modest pace. An economic datapoint we pay close attention to is initial jobless claims, which measures the number of people who filed for unemployment insurance for the first time in the previous week. This is as close to real time data as possible to assess if the labor market is weakening. As it stands, initial jobless claims remain near multi-decade low levels, as is the case since early 2022. In addition to low jobless claims, the unemployment rate is at historically low levels, under 4%. For perspective, from early 2001 through 2017, the unemployment rate was not under 4% at any point. With most Americans gainfully employed, they continue to spend money because they remain confident that they will earn future income.

At the same time, most Americans are in strong financial standing with respect to their homes. While there has been substantial commentary about rising home costs with 30-year mortgage rates persisting in excess of 7%, the reality is that this is not an issue for most homeowners. Earlier this year, Redfin reported that 88.5% of homeowners who have mortgages on their homes have an interest rate below 6%. In addition, nearly 60% of homeowners with mortgages have a rate below 4%. This data only reflects those with debt on their homes; a recent Bloomberg report stated that approximately 40% of homes in the United States are owned by homeowners that are mortgage-free. There is no question that the current housing market dynamics presents a major challenge for first-time homebuyers, which could continue, however this represents a very small portion of the broad housing market.

WhaleRock is always monitoring for areas of weakness in the economy, and we do expect higher interest rates to ultimately have an impact on consumers' ability to spend. One datapoint we are monitoring, as can be seen below, is auto loans that are delinquent 30 days, which have recently risen and are now above pre-pandemic levels, though still not yet levels experienced in the 2008 recession.



Source: Bloomberg

While this is one datapoint that is rising, credit card delinquencies remain below pre-pandemic levels and substantially below levels experienced in 2008. When surveying the economic data in totality, WhaleRock's current thinking is that the ability for higher interest rates to slow down the economy will take longer than they have historically. Both individuals and corporations took advantage of long-term interest rates at historical low levels from 2019 to 2021, and as a result are in better financial standing than previous economic cycles.

The Artificial Intelligence Arms Race:

With stocks starting 2024 well, a particular area of focus has been large technology companies and the artificial intelligence movement. These companies have reached immense scale, with Amazon, Apple, Alphabet (Google), Meta Platforms (Facebook), Microsoft, and Nvidia's valuations all exceeding $1 trillion.

It is worth noting that unlike the "Dot-Com Bubble," these companies generate massive profits. Nvidia, which designs leading technology for artificial intelligence use, has experienced its earnings grow from ~$2.59 per share in fiscal year 2023, to ~$12.03 per share in fiscal year 2024. Currently, Wall Street consensus estimates are for the company to earn ~$25 per share in fiscal year 2025. This seismic jump in earnings for Nvidia has been the direct result of dominant multinational companies wanting to be at the forefront of the artificial intelligence movement.

Microsoft, for example, noted in its most recent earnings report that it spent $14 billion in the first quarter on capital expenditure to meet increasing customer demand. Further, the company noted that it is likely for its 2025 fiscal year that the company will spend more than $50 billion. Alphabet (Google) reported similar results, noting $12 billion in capital expenditure in the first quarter of the year. Meta (Facebook) told investors that its 2024 capital spending could be as high as $40 billion and set expectations for that level of spending to continue for the next few years. To provide some relativity to these staggering numbers, consider Saudi Aramco, the largest energy producer in the world by a wide margin, which reported it expects capital spending to be $50 billion in 2024.

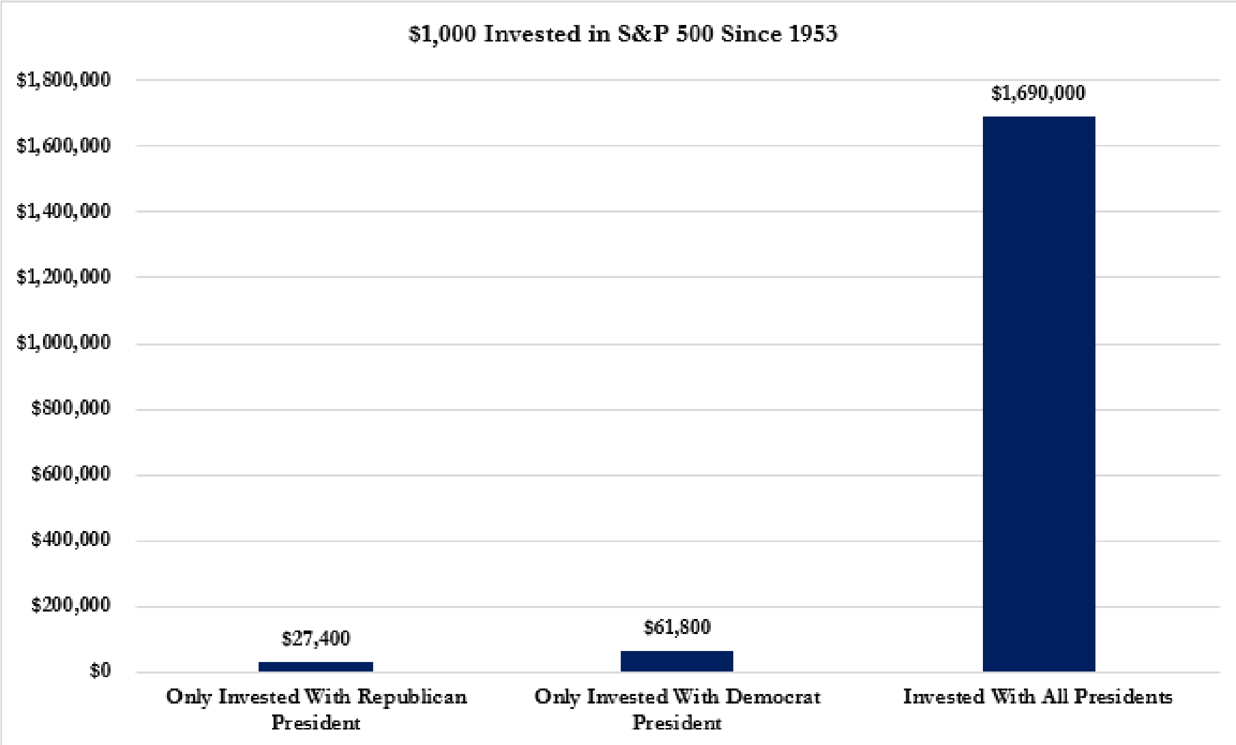
As has been the case for years, WhaleRock's firm view continues to be that many of the large technology companies have extremely wide "moats" creating durable competitive advantages. We expect this to result in meaningful earnings for shareholders in the years to come. In 2023, the "Magnificent Seven," comprised of Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia, and Tesla, grew their earnings by

31% while the earnings of the remaining 493 companies in the S&P 500 fell by 4%. This year, Wall Street expectations are that the "Magnificent Seven" will grow earnings by a further 25%, while the remaining 493 companies in the S&P 500 will grow earnings by only 8%.

With robust profits, a company such as Microsoft has tremendous flexibility in delivering returns to its shareholders. It can take a portion of its earnings and distribute cash to shareholders in the form of dividends, it can buy back stock to reduce shares outstanding which increases each remaining investor's ownership of earnings, and it can retain a portion of earnings to further invest in the business. In Microsoft's case, the company does all three: dividends to shareholders have increased by 10% per year over the last 5 years, earnings per share have doubled over the last 4 years while the number of shares outstanding has been reduced, and the company has retained billions of dollars to reinvest and power earnings growth into the future.

The Presidential Election:

With a presidential election occurring in November, WhaleRock anticipates volatility in markets could heighten as investors focus on future fiscal policy and the potential for changes in tax rates. We wanted to offer the historical data below for perspective, as you will likely hear that one party could create a positive or negative outcome for stocks. Going back to 1953, $1,000 invested in the U.S. stock market only when a Republican was president would be worth $27,400 today. Over that same period, $1,000 invested only when a Democrat was president would be worth $61,800. However, for the individual who maintained their investment in U.S. stocks regardless of the political party in charge at the time, that $1,000 invested in 1953 is worth ~$1.69 million today. WhaleRock will be vigilant in monitoring potential changes to laws that can impact your investments; as always, we take a long (4+ years) view when investing in businesses.



Source: Bespoke Investment Group

As always, if you have questions or want to discuss this more in depth please reach out, we are happy to get into more detail - 401.228.7799. Per the SEC's annual requirement, WhaleRock has updated our ADV to reflect any changes that occurred in 2023, which is attached. It can also be located on our website, www.wrpoint.com.