OCTAVIA
WEALTH ADVISORS

Economic and Market Overview

First Quarter 2024

Building a Lifelong Partnership

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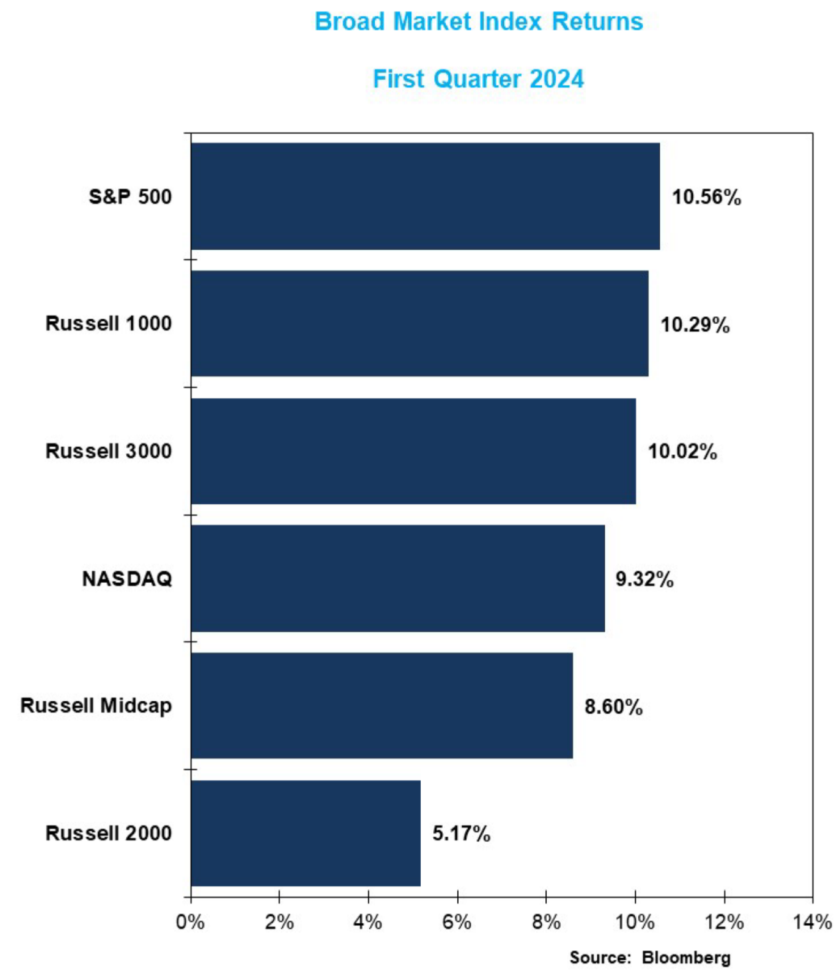
The Economy

The U.S. economy's growth slowed in the fourth quarter of 2023 compared to the prior quarter but continued at a robust pace. The Bureau of Economic Analysis' (BEA) final estimate of fourth quarter real GDP was an annualized 3.4% growth rate, slowing from 4.9% the prior quarter. Though estimates have not yet been released, economists expect another quarter of growth to kick off 2024, with projections falling between 2% and 3%. The economy's resiliency has been surprising, though economists still caution that higher interest rates and sticky inflation are likely to slow consumer spending. Still, a robust labor market has helped buoy growth. The government's non-farm payrolls report showed 303,000 new positions added in March with an unemployment rate of 3.7%. Market participants have been hopeful that the Federal Open Market Committee (FOMC) will be able to lower interest rates in 2023, providing additional fuel for growth, though recent inflation reports may call that assumption into question.



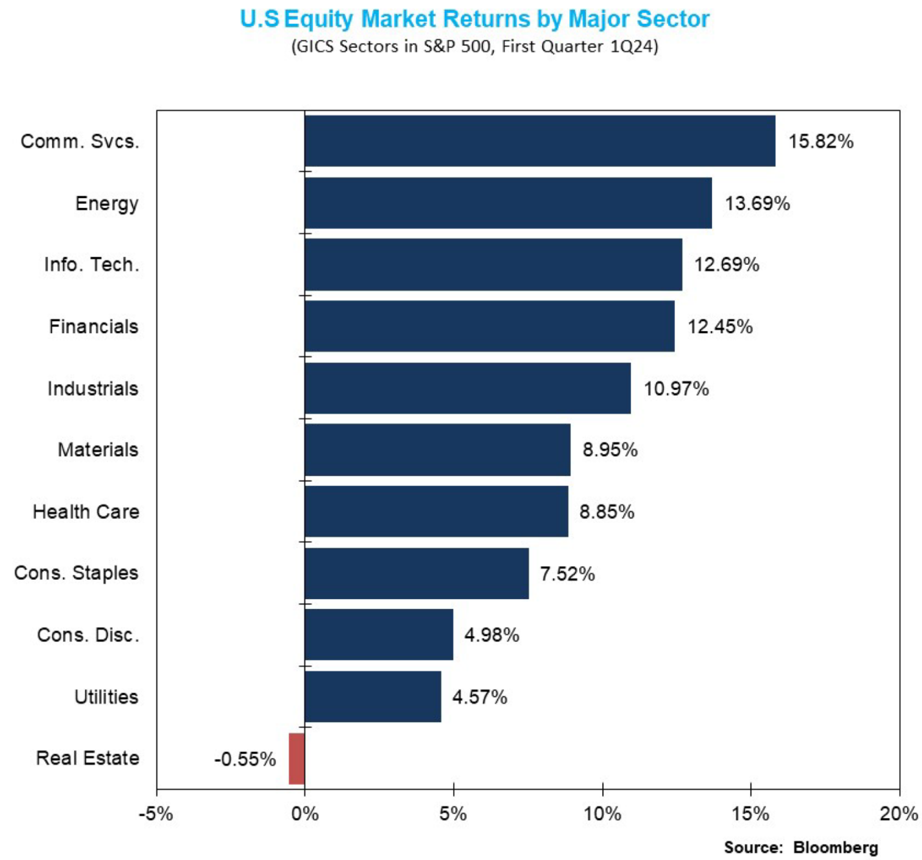
Highlights and Perspectives

GROSS DOMESTIC PRODUCT (GDP)

In its final update to fourth quarter real GDP, the BEA pegged growth at an annualized rate of 3.4%, lower than 4.9% in the third quarter but above long-term trends. Continued growth has encouraged, but also puzzled, economists, who had broadly expected the FOMC's implementation of higher interest rates to drag on growth more noticeably. Economists continue to call for slower growth in the coming months as consumer credit card balances rise and excess savings dwindle. Fourth quarter GDP growth was driven primarily by consumer spending, residential construction, and government investment. Corporate profits rose 4.1% (not annualized) during the quarter after rising 3.4% in the quarter prior.

HOUSING

The housing segment remains under pressure from the weight of elevated mortgage rates, causing sales of existing homes to remain near their lowest levels in years, despite a significant jump in February. Mortgage rates hovered around 7% throughout the quarter, and mortgage applications have been soft to start the spring buying season. Housing affordability remains near record lows as home prices have continued to rise along with mortgage rates, due in large part to a limited supply of available homes. Existing home sales rose 9.5% in February to an annualized rate of 4.3 million units, down 3.3% from a year ago. The inventory of existing homes was at 2.9 months of supply, down slightly from a year ago. Existing home prices were 5.7% higher than last February.



EMPLOYMENT

The March payrolls report showed that the labor market continues to expand at a strong clip and much faster than expected. Employers added 303,000 new positions in March, while previous months saw net positive revisions. Payroll growth averaged 267,000 new positions per month in the first quarter (subject to revisions). Average hourly earnings growth was 0.3%, reaccelerating from a meager 0.1% increase in February. Wages have risen 4.1% over the past year. Year-over-year wage growth has slowly decelerated after peaking at nearly 6% two years ago, but remains well above pre-pandemic levels. Economists believe that wage growth near 4% can coexist with 2% inflation, but only if worker productivity continues to rise. The unemployment rate fell to 3.7% in March to reverse February's jump to 3.9%. Labor force participation rose to 62.7%.

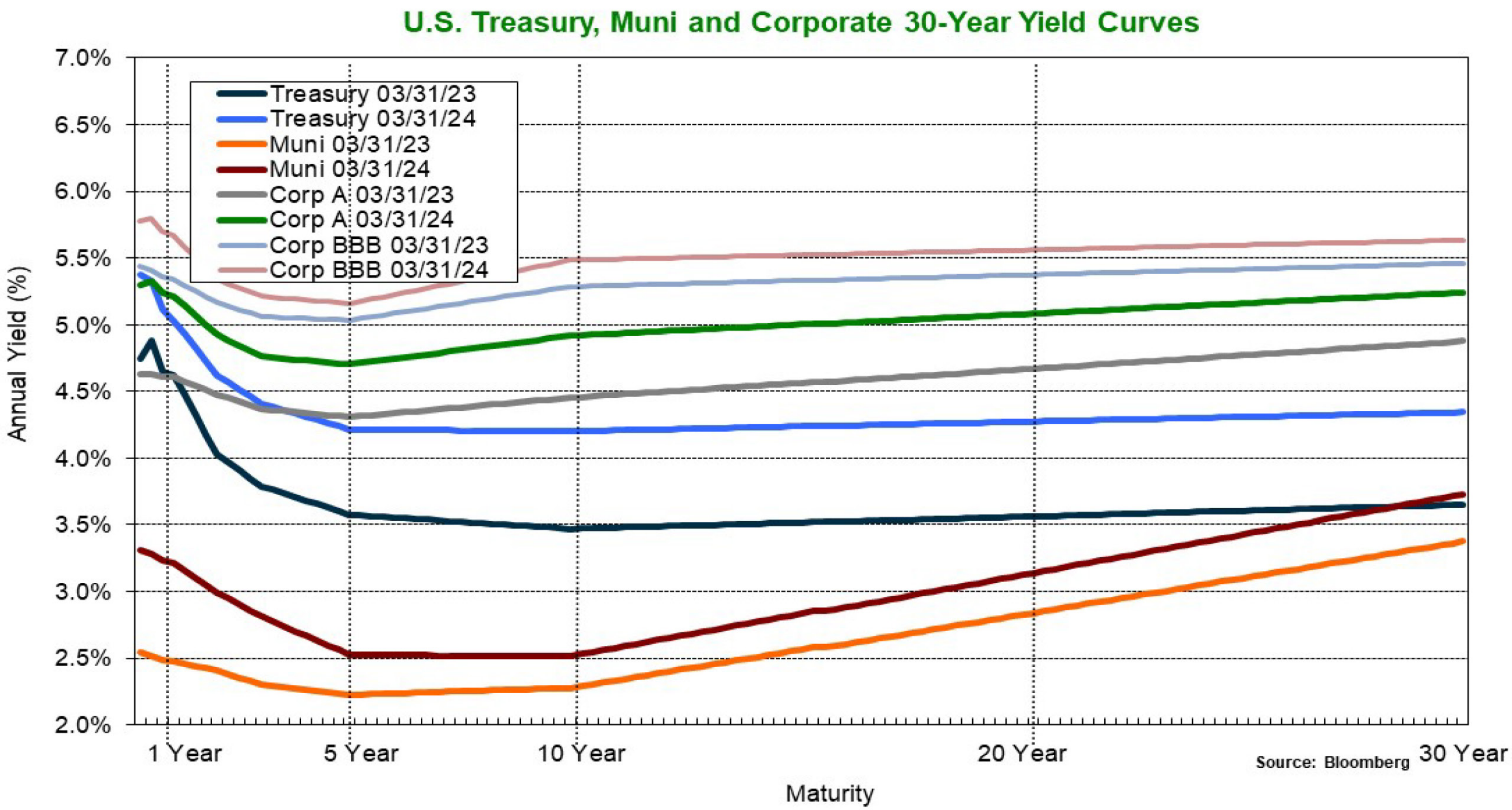
FEDERAL RESERVE POLICY

The FOMC at its latest meeting voted to maintain the federal funds target range at 5.25-5.50%, citing stable inflation, albeit at levels higher than the target of 2%. The committee's Summary of Economic Projections included an estimate that the fed funds rate would be 75 basis points lower than current levels by the end of 2024, based on assumptions that inflation will continue to recede over the coming months. Additionally, the committee had more upbeat growth expectations, revising its forecast for 2024 growth to 2.1% from 1.4%. Bond yields and equity markets were relatively flat following the release of the SEP, which may indicate that the FOMC's outlook is consistent with that of investors. However, FOMC Chairman Jerome Powell has maintained a cautious tone in his comments since that meeting, indicating that the committee will wait for further evidence that inflation is receding before making any decision to lower rates.

INTEREST RATES

Fixed income securities fell during the quarter as yields pushed higher, potentially due to concerns that inflation is still (and may remain) higher than the FOMC's target level of 2%. Inflation readings from February and March showed an uptick in prices, reversing declines from the end of 2023.

The Treasury yield curve remained inverted throughout the quarter but shifted higher compared to December 2023. Yields on maturities of up to one year rose as much as 25 basis points, while longer-term yields rose 25-40 basis points. Yields on 10-year Treasuries ended the quarter at 4.20%, compared to 3.88% on December 31. On opposite ends of the curve, 3-month Treasury yields rose 3 basis points to 5.37%, while 30-year yields climbed 31 basis points to 4.03%.



Total returns on fixed income were largely negative during the quarter. The Bloomberg Treasury 5-7 Yr. index fell 0.9%, while the Bloomberg U.S. Corporate Credit 5-10 Yr. index fell 0.2%. High yield securities were higher, rising 1.5%. Municipal bonds, as represented by the Bloomberg Municipal Bond index, fell 0.4%. Returns on bonds outside the U.S. were sharply negative, falling 3.2% for the quarter, due largely to currency factors as the dollar appreciated sharply against most of its peers.

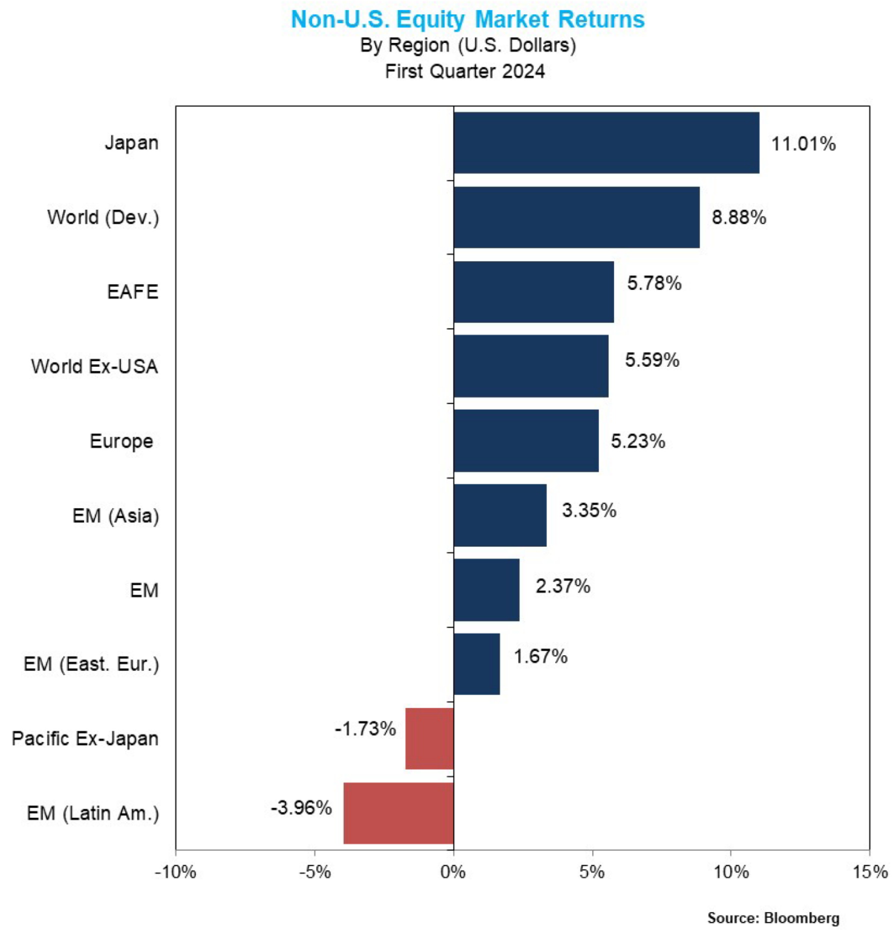
EQUITIES

Stock prices were mostly higher for a second consecutive quarter, with broad based gains across ten of the S&P 500's eleven sectors. There are several factors that may be helping to buoy equity prices, including above-trend economic growth, continued strength in the labor market, and optimism around the development of artificial intelligence. The S&P 500 advanced 10.6% for the quarter.

The index's best-performing sectors were Communication Services, Energy, and Information Technology, which returned +15.8%, +13.7%, and +12.7%, respectively. Real Estate was the only negative sector, returning -0.6%. Other laggards included utilities (+4.6%) and Consumer Discretionary (+5.0%).

The Russell 1000 index of large and mid-cap stocks rose 10.3% for the quarter. Small cap stocks, as represented by the Russell 2000 index, underperformed large caps, rising 5.2%. Growth stocks outperformed their value peers across the size spectrum. The Nasdaq Composite index, which is dominated by large tech stocks, rose 9.3%. The Dow Jones Industrial Average advanced 6.1%.

International stocks posted positive results but trailed their domestic peers. The MSCI ACWI ex-USA Index, which measures all markets outside the U.S., rose 4.7% for the quarter. The MSCI EAFE index of developed markets returned 5.7%, while MSCI Emerging Markets added just 2.4%. Developed markets were boosted by strong gains in Japan, while emerging markets saw weaker performance in Latin America.



Outlook

The U.S. economy has performed above trend and at likely unsustainable levels in recent quarters. Economists maintain their consensus that growth will inevitably slow in the months ahead, but that the U.S. is likely to remain in better shape than much of the rest of the world. Cautious optimism remains, with several key factors likely to influence growth in the coming months. First, the FOMC's monetary policy is expected to become more accommodative (though this could be derailed if inflation remains stuck at higher levels). Second, the labor market continues to expand faster than expected. The unemployment rate has ticked higher in recent months but remains below 4%. Third, federal fiscal policy remains extremely expansionary, with significant spending on infrastructure investments and targeted stimulus measures. The latter may help boost demand in the short term, while the former promotes longer-term growth. However, despite the generally positive outlook, significant risks remain. As mentioned, perhaps the biggest is sticky inflation that continues to erode the purchasing power of U.S. consumers. Other potential risks include tighter monetary policy crimping economic growth, financial instability arising from massive government deficit spending, and ongoing geopolitical issues in Ukraine and the Middle East.

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INDEX OVERVIEW

The **Dow or DJIA** (Dow Jones Industrial Average) is an unmanaged index of 30 common stocks comprising 30 actively traded blue chip stocks, primarily industrials, and assumes reinvestment of dividends. The **NASDAQ Composite** is a stock market index of the common stocks and similar securities listed on the NASDAQ stock market. The **S&P 500 Index** is an unmanaged index comprising 500 widely held securities considered to be representative of the stock market in general. The **DJ US Select REIT Index** is a subset of the Dow Jones Americas Select RESI and includes only REITs and REIT-like securities (The Dow Jones US Select Real Estate Securities Index (RESI) represents equity real estate investment trusts (REITs) and real estate operating companies (REOCs) traded in the US). The **Bloomberg Commodity Index** is a broadly diversified commodity price index that tracks prices of futures contracts on physical commodities on the commodity market, and is designed to minimize concentration in any one commodity or sector. The **MSCI EAFE Index** is recognized as the preeminent benchmark in the US to measure international equity performance. It comprises the MSCI country indices that represent developed markets outside of North America: Europe, Australasia, and the Far East. The **MSCI Emerging Markets Index** is a free float-adjusted market-capitalization index that is designed to measure equity market performance in the global emerging markets. The **MSCI ACWI Index** is a free float-adjusted market-capitalization-weighted index that is designed to measure the equity market performance of developed and emerging markets. The MSCI ACWI consists of 46 country indices comprising 23 developed and 23 emerging markets country indices. The **MSCI Emerging Markets (EM) Eastern Europe Index** captures large and mid cap representation across four emerging markets (the Czech Republic, Hungary, Poland, and Russia) countries in Eastern Europe. With 52 constituents, the Index covers approximately 85% of the free float-adjusted market capitalization in each country. The **MSCI EM (Emerging Markets) Latin America Index** is a free float-adjusted market-capitalization-weighted index that is designed to measure the equity market performance of emerging markets in Latin America. The **MSCI ACWI Ex-US Index** is a market-capitalization-weighted index maintained by Morgan Stanley Capital International (MSCI) and designed to provide a broad measure of stock performance throughout the world, with the exception of US-based companies. The **MSCI China Index** captures large and mid cap representation across China H shares, B shares, Red chips, and P chips covering about 85% of this China equity universe. The **Bloomberg Barclays Municipal Bond Index** is an unmanaged index comprising investment-grade, fixed-rate municipal securities representative of the tax-exempt bond market in general. The **Bloomberg Barclays Global Aggregate ex-US Index** is a market-capitalization-weighted index, meaning the securities in the index are weighted according to the market size of each bond type. Most US-traded investment-grade bonds are represented. Municipal bonds and Treasury Inflation-Protected Securities are excluded, due to tax treatment issues. The Index includes Treasury securities, government agency bonds, mortgage-backed bonds, corporate bonds, and a small amount of foreign bonds traded in the US. The **Bloomberg Barclays US 5-10 Year Corporate Bond Index** measures the investment return of US dollar-denominated, investment-grade, fixed-rate, taxable securities issued by industrial, utility, and financial companies, with maturities between 5 and 10 years. Treasury securities, mortgage-backed securities (MBS), foreign bonds, government agency bonds, and corporate bonds are some of the categories included in the Index. The **Bloomberg Barclays Capital US 5-7 Year Treasury Bond Index** is a market-capitalization-weighted index, and includes Treasury bonds issued by the US with a time to maturity of at least 5 years, but no more than 7 years. The **Russell 1000 Index** is a market-capitalization-weighted benchmark index made up of the 1000 largest US companies in the Russell 3000 Index (which comprises the 3000 largest US companies). The **Russell 2000 Index** is an unmanaged index considered representative of small cap stocks. The **Russell 3000 Index** is an unmanaged index considered to be representative of the US stock market, and measures the performance of the largest 3,000 US companies representing approximately 98% of the investable US equity market. The **Russell Midcap Index** is a subset of the Russell 1000 Index. It includes approximately 800 of the smallest securities based on a combination of their market cap and current index membership. The **Housing Market Index** (HMI) is based on a monthly survey of **NAHB** members designed to take the pulse of the single-family housing market. The survey asks respondents to rate market conditions for the sale of new homes at the present time and in the next six months, as well as the traffic of prospective buyers of new homes. The **JPMorgan Emerging Market Bond Index** (EMBI Global) tracks total returns for traded external debt instruments in the emerging markets, and is an expanded version of the JPMorgan EMBI+. As with the EMBI+, the EMBI Global includes US dollar-denominated Brady bonds, loans, and Eurobonds with an outstanding face value of at least $500 million. The **CBOE Volatility Index** (VIX) is an up-to-the-minute market estimate of expected volatility that is calculated by using real-time S&P 500 Index option bid/ask quotes. The Index uses nearby and second nearby options with at least 8 days left to expiration and then weights them to yield a constant, 30-day measure of the expected volatility of the S&P 500 Index.

DEFINITIONS

The **Federal Open Market Committee** (FOMC) is the monetary policymaking body of the Federal Reserve System. The **federal funds rate** is the interest rate at which a depository institution lends funds maintained at the Federal Reserve to another depository institution overnight. The **European Central Bank** (ECB) is the central bank for Europe's single currency, the euro. The ECB's main task is to maintain the euro's purchasing power, and thus price stability, in the euro area. The euro area comprises the 19 European Union countries that have introduced the euro since 1999. The **Gross Domestic Product** (GDP) rate is a measurement of the output of goods and services produced by labor and property located in the United States. The **Bureau of Labor Statistics** (BLS) is a unit of the United States Department of Labor. It is the principal fact-finding agency for the US government in the broad field of labor economics and statistics, and serves as a principal agency of the US Federal Statistical System. The **Bureau of Economic Analysis** (BEA) is an agency in the US Department of Commerce that provides important economic statistics, including the gross domestic product of the US. It is a governmental statistical agency that collects, processes, analyzes, and disseminates essential statistical data to the American public, the US Congress, other Federal agencies, state and local governments, business, and labor representatives. The **PCE (Personal Consumption Expenditure) Index of Prices** is a US-wide indicator of the average increase in prices for all domestic personal consumption. Using a variety of data, including US Consumer Price Index and Producer Price Index prices, it is derived from personal consumption expenditures, and is essentially a measure of goods and services targeted towards and consumed by individuals. Sector performance is represented by the **Global Industry Classification Standard** (GICS) sectors, developed by Standard & Poor's and MSCI Barra.

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