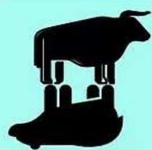
Alexis Investment Partners, LLC  Practical ✧ Tactical

The Dog Days of Summer are here, but July was positive. Seasonal weakness hit tech leaders starting mid-month. This pressured leading indexes like the Nasdaq and S&P500 into sharp pullback / correction territory. The damage was much more limited for most other stocks, as recent small / mid-cap strength sparked a rebalance trade (taking profits in tech, buying economically sensitive laggards).

The S&P500 index gained +1.2% in July, despite a mid-month drop of -4.7%, thanks to a last day bounce of +1.6%. The average stock in that index as measured by the equal weight S&P500 ETF (RSP), was much better, gaining +4.5% for the month.

Perhaps the bigger story was a sharp decline in interest rates, pushing the aggregate bond index to a very strong monthly return (AGG +2.3%). **This is also a countertrend move – reflecting a growth scare, which we are seeing play out more forcefully as the correction continues into early August.**

Last month we wrote: "Looking forward, **we remain long-term optimistic, but we believe the next few months may be more challenging.** From a practical perspective, **stocks have come a long way as year-to-date returns have already met / exceeded the 2024 targets for most analysts.** We see potential for leadership changes as leaders pause and laggards play catch up. We also see the potential for a late summer swoon – in part due to election anxiety. We prepare for these possibilities through diversification and by tactically raising our cash allocation."

Our portfolios gained, and our equity allocation generally outpaced benchmarks – but most portfolios lagged benchmarks in July as leaders lost and due to our underweight stance on bonds. Note that this same stance has been a strong contributor to year-to-date and longer-term results.

Our models, indicators, and analysis suggest a Bull market in a correction / consolidation. Despite slower growth, earnings continue to come in better than forecast. Inflation is improving and the Fed has maintained its restrictive stance, but signaled it is ready to ease as labor conditions deteriorate.

What to Expect in Portfolios

Last month we wrote: "Stocks have come a long way since the 2023 correction lows as reflected in trailing 1-year and year-to-date results. **A more neutral allocation gives us the ability to continue to participate in the bull market while allowing us to navigate potential near-term turbulence."**

Corrections are painful but it helps when we step back and note the limited damage to the very strong performance we've enjoyed despite periodic setbacks.

Summer doldrums are here, and uncertainty is likely to be unsettling at times. We do not expect a severe (bear market) outcome, so our current plan is to add to favored positions on weakness. We remain vigilant to trend changes and will continue to adapt as we work through turbulence and potential transitions.

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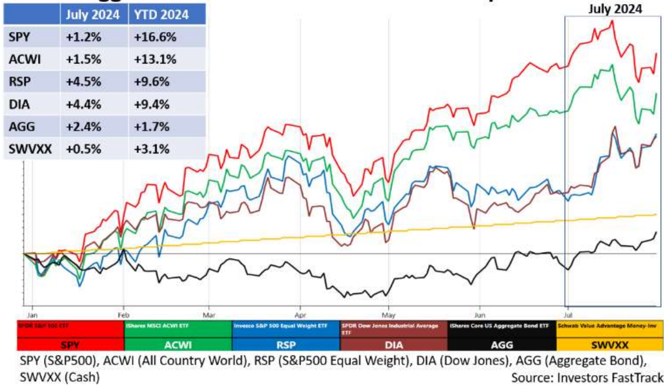
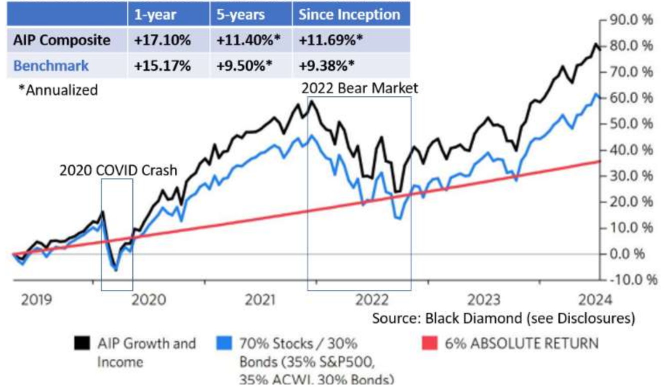
July was positive, but volatile - punctuated by countertrend moves. As you can see below, leaders lagged as investors took profits in leading names and added to previously out of favor names.
Bond yields fell sharply, pushing up AGG. This is a sign of a growth scare (fear that the Fed will wait too long to ease, ushering in a recession).



	July 2024	YTD 2024
SPY	+1.2%	+16.6%
ACWI	+1.5%	+13.1%
RSP	+4.5%	+9.6%
DIA	+4.4%	+9.4%
AGG	+2.4%	+1.7%
SWVXX	+0.5%	+3.1%

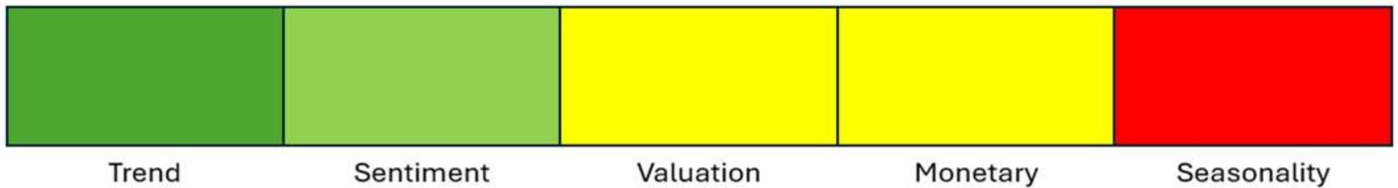
The chart below shows the net performance of our most popular composite since inception (120 accounts – see disclosures on page 4).
The last five+ years have included the COVID crash and 2022 bear market. Our strategy and discipline led to greater participation in gains than declines, allowing us to add value through this volatile time.



	1-year	5-years	Since Inception
AIP Composite	+17.10%	+11.40%*	+11.69%*
Benchmark	+15.17%	+9.50%*	+9.38%*

Insights and Commentary

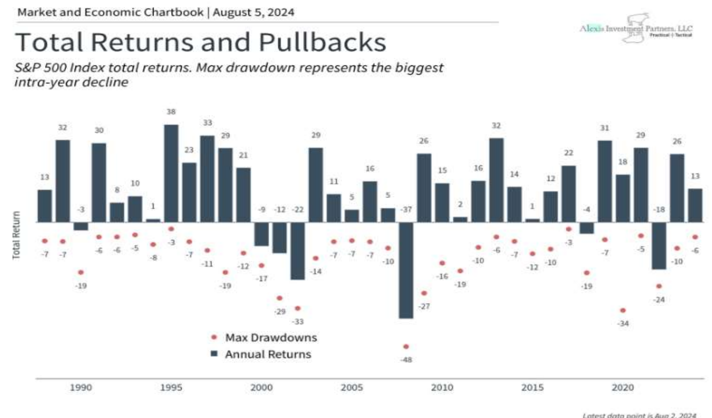
Investing can be an emotional roller coaster leading to costly mistakes. To navigate effectively as we seek greater participation in advances than declines, we have found it helpful to monitor a series of indicators and models based on 3 key tenants, (Don't Fight the Fed, Don't Fight the Trend, Follow Sentiment Except at Extremes) summarized in the chart below:



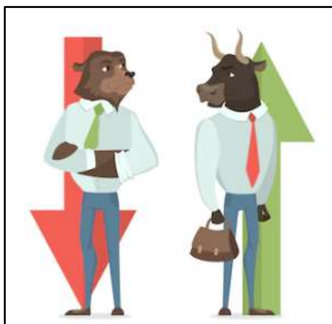
Uptrends face seasonal setback:

The uptrend broadened in July as leading tech/AI stocks fell into a sharp correction and investors rotated into small caps and neglected value stocks. Sentiment is balanced as market resilience offset uncertainty. This is likely to sour as the correction intensifies.
Monetary conditions are tight (Fed policy remains restrictive as evidenced by an inverted yield curve) but the Fed acknowledged that risks to rising unemployment and progress with respect to inflation are sufficient to prompt rate cuts in September. Some fear that the Fed is too slow to act, leading to a growth scare / recession concern. We believe this is unlikely.
Valuations are elevated for the major indexes. The average P/E on an equal weight basis is closer to long-term averages. High valuations can limit advances and lead to deeper pullbacks / corrections.
Last month we wrote: "Seasonality is a concern – not immediately, but from late July through October. This is especially true following a strong start…" We see this as the primary trigger to this correction. Seasonal volatility can be intense – in both directions.

Noting that stocks suffered a bear market only 2 years ago in 2022, it would be highly unusual for the current bull cycle to end this year. The AI craze has led to some excess optimism. Corrections like we face now are painful but tend to help sustain bull markets by tempering excess speculation.



Pullbacks and corrections happen in both bull and bear markets. In bull markets, they tend to be relatively shallow and short lived.



Update, Observations, Indicators and Outlook:

In terms of our Market Pulse (right), the Bull Market remains intact. Selling mid-July was a pullback for most socks, but a correction for market leaders.

Growth Scare Triggers Seasonal Selling:

Persistent post pandemic inflation pushed the Fed to restrict monetary conditions by raising interest rates. The 2022 bear market was triggered in part by inflation and Fed tightening, and the low in last year's correction was fueled by the Fed suggesting its next move would be to ease. Throughout this time, pundits predicted "hard landing" (recession), "soft landing" (slow growth) or "no landing" (persistent economic strength) scenarios. The path to taming inflation is especially uncertain given global geopolitical risks, the pending US election, currency fluctuations due to uneven global growth and other unknowns. The Fed is likely to act in September and we are reaching the point in this inflation cycle when we'll soon know which path proved prescient.

We believe a "soft landing" is the highest probability based on what we observe today (slowing but steady earnings and economic growth, rising but low unemployment, and falling but stubborn inflation). "Soft landing" favors continued leadership from growth stocks, a more normal yield curve with cash yielding a little more than inflation and bonds offering an additional 2%-3% or more to compensate for time and default risks. We would expect the rally to broaden despite growth leadership as investors embrace diversification having been burned by the recent tech led selloff.

The current growth scare reflects concern that the Fed will act too slowly causing unemployment to rise and prompting a recession. This "hard landing" scenario implies a steeper stock selloff based on falling earnings, a sharper decline in cash yields as the Fed pushes liquidity, and a potential return to very low bond yields based on a flight to safety and scarcity of yield as the Fed acts aggressively. We see this as a low probability. We are currently in the middle of a strong earnings season. We believe the Fed will reduce rates by 1.5%-2% (to between 3% and 4%) but we see no reason for cash yields to return to 0% any time soon (even if recession ensues). Bond yields should stabilize and drift higher as stocks stabilize.

The "no landing" scenario gained in popularity on hopes that the Fed would act proactively on early signs of lower inflation trends and was reinforced by strong economic numbers and earnings as inflation ebbs closer to the Fed's target. This scenario favors economically sensitive small caps and neglected value stocks as confidence grows. This is also a low probability in our view based on recent increases in unemployment and the Fed's reluctance to act prematurely for fear that inflation re-asserts itself.

We continue to opportunistically adapt portfolios based on updated insights, prudent risk management and long-term trends.

Market Pulse:

We try to avoid jargon, but a few terms are helpful when describing financial conditions.

Bull Market: markets trending up (making higher highs on rallies and higher lows in periods of decline). We can expect periodic pullbacks and corrections, but these should be relatively short and shallow – followed by resumption of the up-trend.

Consolidation: after a period of strong gains or steep declines sometimes markets become range bound, moving up and down by 3-5% over several weeks. After consolidation, the prior trend resumes.

Pullback: a decline of 3-5% that generally happens at least twice per year. Pullbacks often resolve within a few weeks.

Correction: a decline of 5% to 10% that typically happens once per year. Like pullbacks, markets recover quickly after corrections, generally within 3-6 months. The pullback that started mid-July was a correction for leaders and resumed early August. Stocks remain in an uptrend, but we can expect volatility to continue while the correction runs its course.

Bear Market: a decline of 20% or more. Many bear markets are fully recovered within 18-24 months, but severe bear markets like 2000-2003 and 2007-2009 can take 5-7 years or longer to recover from.

Bottoming Process: After a correction or bear market, stocks often bounce and re-test lows multiple times before recovery.

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Closing Comments:

Several clients have recently been speaking with friends who are looking to make a change either because they are nearing a life transition or have been unhappy with their current advisor.

We appreciate your referrals and are pleased that our company continues to enjoy steady growth. Our focus is always on providing exceptional service and performance and we are very grateful for your confidence and support!

Although our focus is on financial planning and investments, we also have relationships and resources to help with life and LTC insurance and annuities.

Jason acts as a 3(38) Fiduciary Advisor to 401k plans and has been able to help several small business owners reduce costs, significantly improve their plans and offload some of their liability as plan sponsors while creating a better experience for employees.

Please call and/or email me personally for most of your account servicing needs and especially when you have questions or concerns.

Disclosures

This material is for informational purposes only. Statements of future expectations, estimates, projections, and other forward-looking statements are based on available information and Jason Browne's view as of the time of these statements. Accordingly, such statements are inherently speculative as they are based on assumptions that may involve known and unknown risks and uncertainties.

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