INVESTMENT UPDATE: FIRST QUARTER 2024

This is a quarterly update of economic conditions and investment strategy.

Equity markets were strong globally in the first quarter. Easier financial conditions and expectations of both interest rate cuts and earnings growth drove strong performance. With the short-term outlook for rate cuts and other macroeconomic factors remaining fluid, we continue to manage risk and focus our research on our long-term investment themes.

A STRONG FIRST QUARTER

The S&P 500 reached all-time highs amid a global equity rally spurred by expectations of robust earnings, economic growth and central bank easing. The S&P 500 generated a total return of almost 11% for the quarter. It is now more than 50% higher than on October 1, 2022, and 23% higher than just six months ago. Meanwhile, Japan's Nikkei Index soared over 20% in the first quarter and finally surpassed the bubble high it reached in 1989. Many other equity markets also reached all-time highs during the quarter, including France, Germany, India and Taiwan.

UNDERPINNINGS OF THE GLOBAL RISE IN EQUITIES

The most recent rallies abroad reflect a combination of fundamental improvements in earnings and financial conditions. By contrast, the U.S. rally appears to be driven less by corporate results than by excitement over the potential of artificial intelligence and fears of missing out.

U.S. investors began to embrace the "soft-landing" narrative in mid 2023, when a widely expected recession did not materialize despite the largest rate hikes in 40 years. Then optimism soared in October 2023, when Federal Reserve Chairman Jerome Powell said he would be willing to lower interest rates <u>before</u> seeing clear signs of an economic contraction.

However, better-than-expected economic growth and falling inflation were not just U.S. phenomena. Inflation slowed almost everywhere as pandemic-related supply chain issues were eliminated. Several central banks – not just the Fed – have said they are likely to lower interest rates this year. As a result, global corporate spreads have narrowed considerably and bond yields have declined, boosting equity markets and economic activity globally.

Several leading indicators suggest that global manufacturing growth is likely to pick up soon, and employment remains strong in most geographies. Throughout the developed world, unemployment is at its lowest level in more than 40 years, spurring capital investment consistent with our *Next-Generation Automation* theme. Coupled with lower inflation, rising employment typically leads to real wage growth, increased consumer demand and higher levels of business confidence. Any rebound in beleaguered China would further contribute to this improving situation.

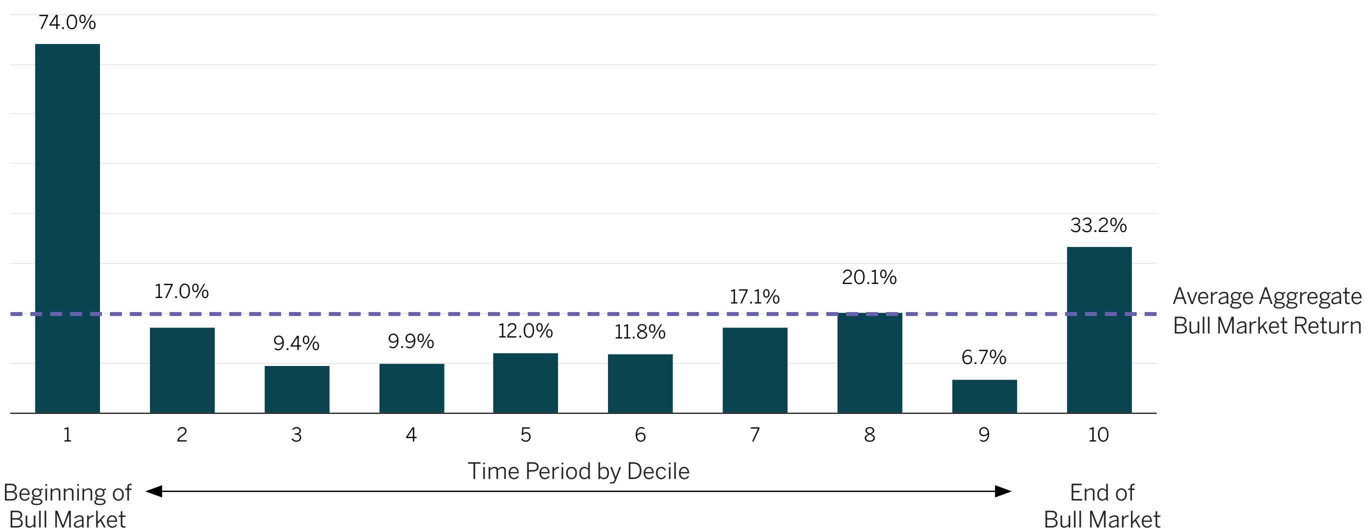
PORTFOLIO POSITIONING AND THEME UPDATES

After the rally of the past six months, the S&P 500 looks quite expensive relative to both its own history and inflation-adjusted yields on long-term U.S. bonds. Currently the S&P 500 is trading at 21 times forward earnings estimates, significantly higher than its 2012 - 2019 average of 15.8. U.S. stock and bond markets now reflect very different economic outlooks. Equity investors appear to expect the strong earnings growth associated with a growing economy. Meanwhile the still-inverted yield curve shows bond investors are far more pessimistic.

High valuations don't mean stocks won't continue to rise in the months ahead, but we must acknowledge that markets cannot continue to increase at a double-digit quarterly rate indefinitely. The last stretch of a bull market tends to be very rewarding for those who remain invested, but it can also create a false sense of complacency that encourages investors to stay in too long. One of the most difficult challenges in investing is knowing when to take profits.

Bull Markets Tend to Start and End Strong

Average Performance of the 10 Bull Markets, 1966 - 2022 From Beginning to End of Each Bull Market
(Average CAGR% with Each Bull Market Broken into 10 Equal Periods)



Source: BCA Research 2024.

Given the dynamics discussed above, we have been prudent in managing risk in portfolios, trimming some positions and ensuring a high degree of diversification across sector, style and geography. In our *Opportunities Abound Abroad* theme, we have increased holdings in Japanese and European equities.

We believe that these are times when focusing on the long-term potential of our themes is particularly important. We are excited to share several recent developments in two of these.

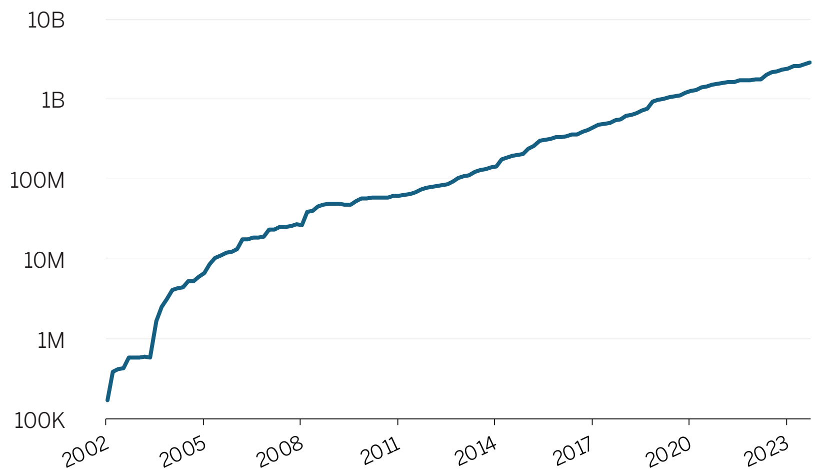
Advent of Molecular Medicine

Our *Molecular Medicine* theme – one of our oldest – continues to unfold as we expected, with many positive and mutually reinforcing developments in this transformative science highlighting the growth potential of our investments. A good example of the power of molecular medicine and its virtuous growth cycle can be seen with respect to chronic kidney disease (CKD), which affects roughly one out of seven adults in the U.S.

While CKD was long understood to run in families, genomic sequencing has allowed diagnostic companies such as Natera to identify multiple genetic mutations that directly contribute to the development of kidney disease. This huge scientific breakthrough enabled biotech firms such as Vertex Pharmaceuticals to develop targeted medicines that could prevent or "fix" mutations and thus slow the progression of the disease. Without a treatment, patients would be unlikely to test for the mutation since the insight would not lead to an improvement in outcome. But diagnostic testing rates soar once information gained through the explosive growth in genomic sequencing leads to the development of new medicines.

Genome Sequencing Volumes Are Doubling Every 18 Months

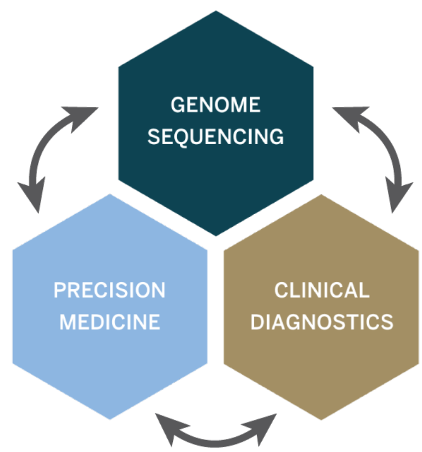
Cumulative Number of Genomes Sequenced, 2002 - 2023 (Logarithmic Scale)



Source: National Institute of Health.

Molecular Medicine's Virtuous Growth Cycle

Genomics Commercial Flywheel



Time will tell which specific companies will ultimately benefit from this virtuous cycle, but we have witnessed this pattern unfold for many diseases, and we expect it to repeat for many more. The sequencing of an increasing number of genomes leads to a better understanding of the root causes of disease, which leads to the development of targeted medicines. The development of targeted medicines, in turn, spurs increased diagnostic testing, which contributes to the scientific understanding of genetic linkages, encouraging even more advanced genomic sequencing. These mutually reinforcing trends create a flywheel that can power high rates of revenue and earnings growth across companies focused on diagnostics and treatment, as well as the technologies that enable them.

Post-Pandemic Consumer

Our consumer-related theme has evolved materially, as the COVID pandemic has ushered in work from home, potentially the biggest change to work arrangements since the Blackberry was introduced nearly 25 years ago. Working from home has had a profound impact on urban life and consumption patterns that we expect will endure. Thus, we have renamed our *Converging Consumer* theme the *Post-Pandemic Consumer*.

Pre-pandemic, U.S. consumers increasingly preferred to live close to jobs in walkable central cities. But when the economic shutdown forced people to abandon their offices four years ago, many discovered they could work effectively from home and enjoyed the freedom it created. As the economy reopened, they sought to work from home at least a few days a week. Today, work from home in the U.S. has settled at about 30% of all workdays, down from its peak of 60%, but five times its pre-pandemic level. Work from home is also becoming more common abroad.

While recent studies show that *fully* remote work reduces productivity by 10% on average, they also indicate that a *hybrid* approach (with roughly three days per week spent in the office) has little to no impact on productivity and can reduce costs. Workers prize the benefits of working from home so much that they are one-third less likely to quit jobs that permit it, reducing wage pressures. Lower wages and potential savings on space costs could increase profitability for companies with pragmatic hybrid work policies.

Working from home has spurred many people to move away from city centers, particularly higher-income employees and younger workers. It has also led to people spending more time at or near home, and on travel and leisure activities. We are focusing our research in this theme on identifying the industries and companies most likely to benefit from these trends.

In Conclusion

We continue to navigate a complex and uncertain environment, with many crosscurrents. While we remain vigilant, we see promise on a variety of fronts.

In our fourth-quarter *Investment Update*, we discussed the massive outperformance of seven of the largest stocks relative to the rest of the S&P 500. While this persists, it has begun to moderate, with the valuations of some of these companies reflecting a more realistic view of their prospects. We are encouraged by the recent broadening of U.S. equity market performance. More than 85% of companies in the S&P 500 now trade above their 200-day moving average, compared to just 32% six months ago. It remains to be seen if these trends will usher in the reordering of market leadership that we have expected.

We remain focused on our disciplined, long term–oriented and client-centered approach to investing. And as always, we are deeply grateful for our clients' trust.