

HOLLOW BROOK

WEALTH MANAGEMENT

The HBWM Quarterly Roundup

2Q 2024

Market Overview

By the end of the second quarter the S&P500 had gained about 14% as the rally continued, one of the best returns for the first half of a year since the late 1990's. Credit spreads remained at historical lows, although signs of stress in commercial real estate will likely become more common. Market volatility measures stayed at historical lows. Although inflation data remained stubbornly higher and falling more slowly than hoped, bond markets adjusted smoothly to discounting fewer rate cuts this year as the Fed counseled patience. The yield curve remained inverted, but expansive fiscal policy was financed successfully, and by early July bond markets had recovered to levels prevailing at the beginning of the year. The story was similar in Europe, albeit with weaker economic activity and the prospect of more rate cuts than in the US. Oil prices firmed. The price of gold rose. Those happy to rely on broad financial market aggregates could celebrate strong returns in equities and few immediate signs of stress.

For now, the only investment conclusion is that the case for long cycle change, even if what comes next isn't clear, is more and more compelling.

Many investment letters, rather than relying on the aggregates, will look beyond them and point to the dominance in equity markets of a small number of big tech stocks driven by enthusiasm for the promise of AI. Not to labor the point, 60% of market returns in the first half was attributable to five companies – Nvidia, Microsoft, Amazon, Meta and Apple. In the second quarter, the concentration became more extreme, with 90% of returns driven by Nvidia,

Microsoft and Apple. The corollary of this in the first half is that all other stocks in the S&P500 rose only 4%. For equity investment managers, choosing to be all in on AI or not determined relative returns.

Global politics was another big topic. Although several elections themselves took place after the quarter end, events were set in place well before. The French election reflecting President Macron's gamble to try to keep the far right at bay has succeeded, but at the cost of a functional government. In the UK the Labor Party won a huge majority in Parliament, routing the Conservatives, but with well less than 40% of the popular vote. Modi in India was reelected but without the landslide that was commonly expected. Financial markets took all this in stride, but investors should try to understand possible longer-term investment implications. It seems to us that electorates are fed up with the status quo. They know what they do not want, but they are not sure what they do want. These are protest votes in the developed countries, while we wait for some broad socio-economic construct to emerge. It might even be possible to imagine the US election in the same way. The other thought may be that two party political systems, founded on the old divide between capital and labor, are no longer capable of finding the middle ground that can (to some degree) accommodate the myriad views of complex informed and misinformed societies in a global economy.

As we go to press with this letter, President Biden announced he is officially out of the presidential race and Harris is likely to ascend as the Democratic Party nomination. Our friends at Strategas Research recently summed up the unprecedented last few weeks of the American presidential election stating, "We are 106 days away from the election and we just received our fourth black swan event in the past six weeks. We would not be surprised if another is coming before the winner is declared." For now, the only investment conclusion is that the case for long

cycle change, even if what comes next isn't clear, is more and more compelling.

China's domestic economy is slowing, and the government is admitting it. Real estate, leverage, and demographic challenges are the reasons. Exports are being pushed as hard as possible to make up for domestic weakness, giving grist to the mill of trade sanctions and tariffs. The more important point for investors is that Chinese economic growth has been responsible for about two thirds of global economic growth since the Great Financial Crisis. If this engine is sputtering, what can we expect for levels of activity around the world?

Finally, the Japanese Yen continued to weaken to multi decade lows in nominal and purchasing power parity terms. Were this to reverse there could be interesting consequences for investors around the world. Japan is the most significant creditor nation. A stronger yen would be both the cause and symptom of capital repatriation, a self-reinforcing loop. The implications for US capital markets might be important.

Investment Outlook

What is the starting point for financial markets today?

- ❖ Equities aren't cheap. The cyclically adjusted PE (CAPE) is 35.5X, a level only exceeded in 2000 and 2022.
- ❖ Credit spreads are at long-term low levels, but signs of stress are emerging. US banks are increasing loan loss provisions. Commercial real estate loan problems are well known and are slowly spreading to other asset categories as rates stay high.
- ❖ Volatility metrics are at all-time low levels.

- ❖ NAV lending and continuation funds are signs of stress in private equity.
- ❖ Private equity and private credit are absolutely linked (the liability of the former is often the asset of the latter). The Fed, the ECB, the BIS and the Bank of England are warning of stresses in private credit markets, a lack of good information in markets which are now nearly as large as public markets, and the consequences of covenant light lending in the days of zero interest rates.
- ❖ Fiscal deficits are at all-time high levels. In Europe investors question whether France will be tested by bond markets, as the UK was in 2022, at a time of political standoff. In the US there are all-time high peace time deficits (which have worked against efforts to control inflation) in advance of a potential new administration. Whichever candidate wins, both have the propensity to spend, and in the case of Trump, there is the likelihood of lower taxes and the certainty of higher trade tariffs.

The absence of stress in current market indicators suggests that investors expect continuity. Momentum and indexed investment approaches both rely on continuity, which may be another self-reinforcing feedback loop for the moment. But if we don't rely on these approaches, how can we imagine that financial markets advance from here? Economic growth, especially with China slowing, has been disappointing. Can economic growth, which has been driven by expansive fiscal policy in the last few years, accelerate in the face of growing fiscal constraints? Is the way of the last 15 years, adding leverage and financial engineering, possible with



interest rates at higher levels? Can the economy support higher levels of debt, or even current levels of debt, at prevailing interest rates? Are slower growth and higher rates a workable backdrop for higher company earnings, or are higher prices and therefore inflation a necessary prerequisite? Is the AI phenomenon enough to support or drive higher asset prices? Or will its promise be limited by the constraints of the physical economy, particularly the large, multi-year investment needed to develop our energy infrastructure?

A clearer picture of a new cycle can only emerge when acceptance of change is forced on public and private actors by financial necessity.

These aren't the only questions, but they are the most important. It seems to us that the combination of the starting point we describe, and real financial constraints defined by fiscal policy and higher interest rates suggest at least the possibility of a poor outcome, a negative asymmetry. But we also recognize that this can continue to play out slowly in financial markets. No actors want to rock the boat.

We also wonder how the essential investments in public goods such as electricity infrastructure can be achieved. The sums are huge, the duration very long, and the financial outcomes are therefore uncertain. In the US, estimates are for a required investment of over \$600 billion by 2030. These challenges are further compounded by a lack of qualified engineers to implement the buildout of upgrading the electricity infrastructure. In China the amount is about \$800 billion. As successful as the private

sector has been in developing digital technology, which involves smaller sums and faster paybacks, there is little evidence that it has the willingness or resources to take on these challenges without significant help from governments, which face significant fiscal constraints.

We believe that there is increasing evidence accumulating for our investment case for long cycle change. A clearer picture of a new cycle can only emerge when acceptance of change is forced on public and private actors by financial necessity. We are not quite there yet. In the meantime, financial markets are full of contradictions

Portfolio Positioning

Our views on the prevailing negative asymmetries have strengthened in the course of the year, but this is a question of degree at the margin. There have been no significant portfolio changes because portfolios are designed to absorb market volatility, which permits our approach to take focus away from attempting to trade around market changes in the short term. Our asset allocation model, which reflects our aggregate views on asymmetries, has so far successfully limited downside risk.

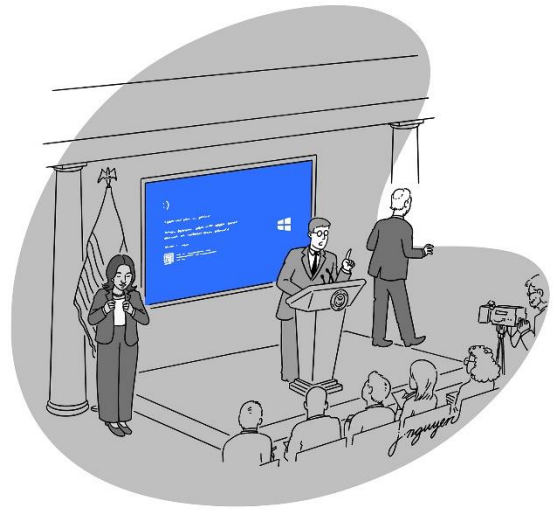
Consistent with last quarter:

We focus on long cycle change in order to position portfolios to gain advantage from long wealth creation. The transition we envisage is gathering pace. Mindful of risks to the status quo, we're building portfolio positions in ideas that we think will benefit from the following winds of the new long cycle which will define the investment context of the next decades.

- ❖ We do not believe the next ten years will be like the last ten years. We approach the successful investments of the last decade with caution.

Some have a place in the portfolio, but not to the dominant extent of the past. (Narrow market leadership is a warning flag).

- ❖ We avoid investments where returns are based on financial engineering (leverage, arbitrage, correlations etc.) rather than wealth creation, and which have broadly defined the past 16 years of very low interest rates. For this reason, we broadly avoid investment in the public and private financial industry. Problems may not be systemic, but they are symptomatic of the ways in which higher rates, which are a fact, slowly work their way through the economy. Growing Central Bank warnings of links to the regulated banking system are another relevant indicator.
- ❖ We focus on genuine innovation (as opposed to growth with no financial returns).
- ❖ We favor investments predicated on long-term, prudent capital management, both in companies and financial intermediaries.
- ❖ We maintain elevated levels of cash and precious metals while this long cycle change gathers momentum, and the related geopolitical and political pressures that are its symptoms remain elevated.
- ❖ We are comfortable being away from the crowd/consensus.
- ❖ We like the energy transition (infrastructure, carbon capture, nuclear), and Japan could be very interesting if they start repatriating capital and companies begin to return capital to investors.



“Hold on, we’re rebooting the election.”

to discuss topics related to investing, accounting, estate planning, and general business. Often, we feature distinguished expert speakers that discuss a wide variety of topics related to professional pursuits. Recently, we hosted a FerrariSide chat with revered collector automobile expert Wayne Carini. Wayne’s wildly successful career has spanned decades, and he is most well-known for his globally syndicated television show Chasing Classic Cars. In front of over one hundred guests, Wayne provided a revealing and illuminating account of his business and life experiences. He talked in detail about his entrepreneurial drive and how perseverance and family were key to his many successes. He also shared how a positive attitude helped him overcome many seemingly insurmountable bumps in the road. You can view the exceptional interview [here](#).

A few years ago, we created the Hollow Brook Wealth Alliance as a local networking event that regularly brings together financial professionals in our local area. The popular event is a unique networking opportunity for leading business leaders



At Hollow Brook we are excited to come to work each day and serve our valued clients. We are always ready to help with financial planning, budget modeling, asset allocation, investment management, estate planning, and tax planning. We believe a goal-based, holistic approach to wealth management leads to consistent and long-term success. We are grateful for your steadfast trust in our growing team of dedicated professionals.

Sincerely,

The HBWM Team

Alan Bazaar
Co-Chairman,
CEO & Partner

Philip E. Richter
Co-Chairman,
President & Partner

Wayne Nordberg
Co-Chairman & Co-CIO

Andrew Norris
Co-CIO

Equity Indices	Price	MTD	QTD	YTD
S&P 500	5,460.48	3.59%	4.28%	15.29%
Nasdaq	17,732.60	6.03%	8.47%	18.57%
Dow Jones Industrials	39,118.86	1.23%	-1.27%	4.79%
Russell 2000	2,047.69	-0.93%	-3.28%	1.73%
Russell 3000	3,099.16	3.10%	3.22%	13.56%
S&P 500 Sectors				
Utilities	346.33	-5.51%	4.66%	9.44%
Consumer Disc.	1,492.14	4.89%	0.65%	5.66%
Telco	310.19	4.80%	9.38%	26.68%
Consumer Staples	819.86	-0.18%	1.35%	8.98%
Industrials	1,031.96	-0.94%	-2.90%	7.75%
Technology	4,341.09	9.32%	13.81%	28.24%
HealthCare	1,700.33	1.91%	-0.96%	7.81%
Materials	556.50	-3.03%	-4.50%	4.05%
Financials	684.26	-0.89%	-2.03%	10.16%
Energy	698.23	-1.29%	-2.42%	10.93%
Real Estate	241.17	2.01%	-1.91%	-2.45%
US Interest Rates				
3 Month	5.35	-0.85%	-0.13%	0.42%
2-Year Note	4.75	-2.45%	2.89%	11.85%
5-Year Note	4.38	-2.89%	3.89%	13.76%
10-Year Bond	4.40	-2.28%	4.66%	13.33%
30-Year Bond	4.56	-1.91%	4.96%	13.16%
Commodities				
Crude (WTI)	81.54	5.91%	-1.96%	13.80%
Brent	86.41	5.87%	-1.22%	12.16%
N. Gas	2.60	0.54%	47.53%	3.46%
Gold	2,326.75	-0.02%	4.34%	12.79%
Silver	29.14	-4.16%	16.74%	22.47%
Currencies				
DXY	105.87	1.14%	1.32%	4.47%
EUR	1.07	-1.24%	-0.71%	-2.95%
CAD	1.37	0.37%	1.03%	3.29%
GBP	1.26	-0.76%	0.17%	-0.68%
JPY	160.88	2.27%	6.30%	14.07%

Source: Bloomberg as of 6/30/2024

HBMW Quotes of the Quarter

“ If you are the smartest person in the room, you are in the wrong room. ”

Confucius

“ Gold is money. The rest is credit. ”

John Pierpont Morgan

“ Asking for help is a superpower anyone can have but only some people use. It is brave to ask for help. Asking for help is the first step toward finding a mentor. Mentors can help us change our lives if we let them. ”

Alexi Pappas

“ To be successful, the truth is you don't have to be special. You just have to be what most people aren't: consistent, determined and willing to work for it. ”

Tom Brady

“ In order to excel, you must be completely dedicated to your chosen (field). You must also be prepared to work hard and be willing to accept constructive criticism. Without 100% dedication, you won't be able to do this. ”

Willie Mays

“ When you step on the court, no matter if you are ranked No. 1 or 200, you have equal opportunity to win. ”

Coco Gauff

2Q 2024: What Happened and What Mattered

Bird Flu Hits US States

In April, the H5 influenza also known as Bird Flu hit U.S. states infecting mainly dairy cattle and even a couple of humans. Michigan reported the highest number of dairy herds infected

Celtics Make History

The Boston Celtics made history when they defeated the Dallas Mavericks to clinch their 18th NBA championship title. With this victory, the Celtics surpassed the LA Lakers to hold the most NBA championships of any team.

Total Solar Eclipse Seen Across North America

In April, a total solar eclipse was viewable across North America from Mexico to Canada. In the U.S. the eclipse was visible from Texas to Maine and was the first time in the 21st century that all three countries could view the eclipse with totality.

Taylor Swift Breaks Streaming Record

Taylor Swift released a new album, *The Tortured Poets Department*, which broke the record for the most-streamed album in a single day.

Red Lobster Closes Locations

Seafood chain, Red Lobster closed almost 100 locations throughout the country and filed Chapter 11 bankruptcy.

Dow Exceeds 40,000 Points

In May, the Dow Jones index surpassed 40,000 points for the first time.

Trump Found Guilty in NY Court

Former President Trump was found guilty in a New York court on 34 felony counts surrounding falsifying business records.

Nvidia Surpasses Microsoft

In June, Nvidia bested Microsoft as the world's largest publicly traded company after its market cap exceeded \$3.3 trillion.

NHL Team Earns First Title

The Florida Panthers won their first ever Stanley Cup title in franchise history after beating the Edmonton Oilers in a seven game nail-biting series.

Inside Out 2 is Box Office Gold

Inside Out 2 exceeded \$1 billion in worldwide box office earnings in less than three weeks, making it the first to meet that milestone in the fastest timeframe.

F1 Driver Gets First Victory

Formula One McLaren driver, Lando Norris, claimed his first ever Formula One victory at the Miami Grand Prix in May.

Tesla Recalls Cybertrucks

Tesla recalled thousands of its Cybertrucks due to safety concerns involving the accelerator pedals.

The Boy Scouts Renamed

The Boy Scouts of America announced they would be renaming their organization to Scouting America in 2025.

Protests Take Over College Campuses

Protests throughout college campuses erupted in the wake of the Israel-Hamas war. At Columbia University, a pro-Palestinian occupation resulted in the university allowing police to suppress campus protests for the first time since the 1968 demonstrations against the Vietnam War.

Mystik Dan Wins Kentucky Derby

Mystik Dan won the 150th Kentucky Derby edging out Sierra Leone and Forever Young in an exciting photo finish.

First Presidential Debate Takes Place

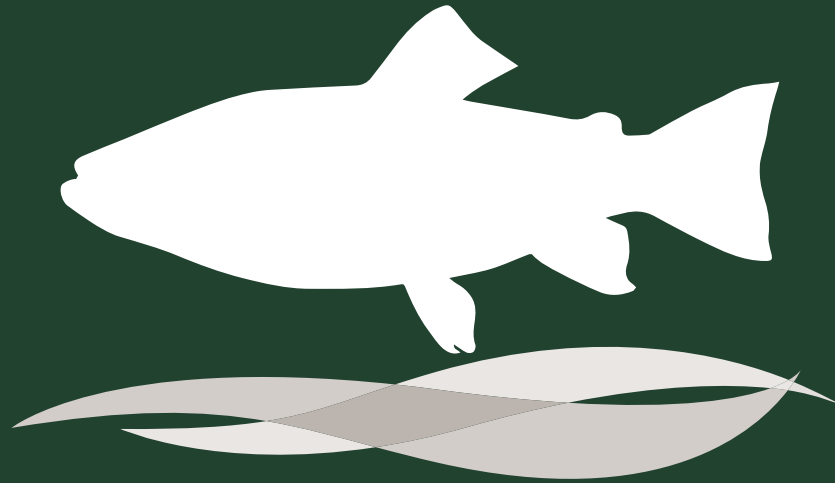
In June, the first presidential debate between President Biden and former president Trump took place in Atlanta. President Biden's debate performance resulted in an outcry for his resignation from the race.

Boeing Starliner Launches Rocket

In June, Boeing's Starliner capsule was successfully launched into space with its first crewed flight after multiple delays.

Earthquake Hits New Jersey

A 4.8 magnitude earthquake hit New Jersey with tremors affecting multiple states throughout the East Coast.



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