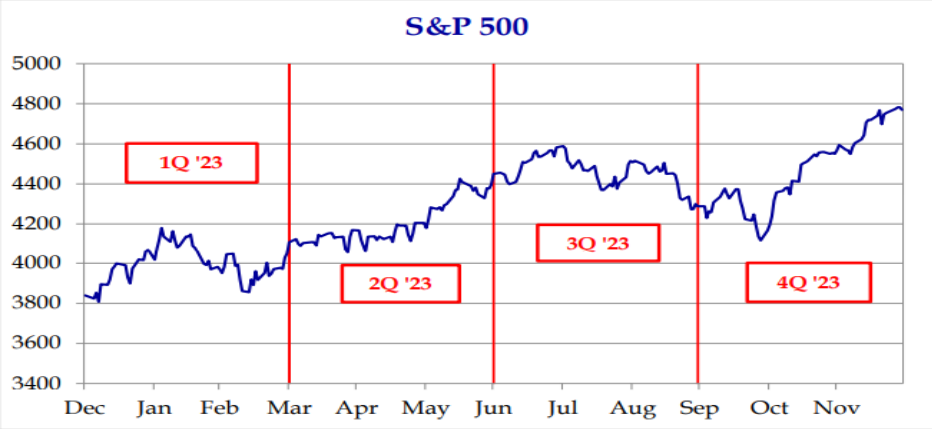
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Wealth Enhancement Group®
KINGS POINT TEAM

WHAT A DIFFERENCE A YEAR MAKES – RECAPPING 2023 AND PROVIDING OUR 2024 OUTLOOK

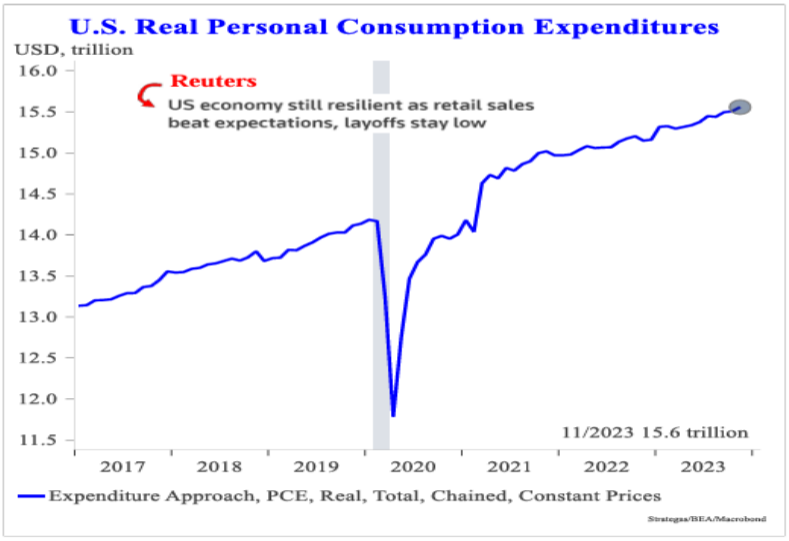
Chart I



Source: Strategas Securities, LLC as of 12/31/2023

A mere 12 months ago, the outlook for the stock market seemed bleak. Inflation was soaring, consumer defaults were on the rise, and prominent business leaders were sounding alarms about an impending recession. The echoes of a -18% market decline in 2022 lingered, casting a shadow of uncertainty over investors. However, as 2023 unfolded, a surprising resilience emerged in the economy. Despite elevated inflation, a glimmer of optimism appeared on the horizon. Consumer spending, depicted in Chart II, defied expectations, leading to a terrific year for markets. Once again, this proves that the market is both difficult to predict and even the most renowned experts are not infallible.

Chart II



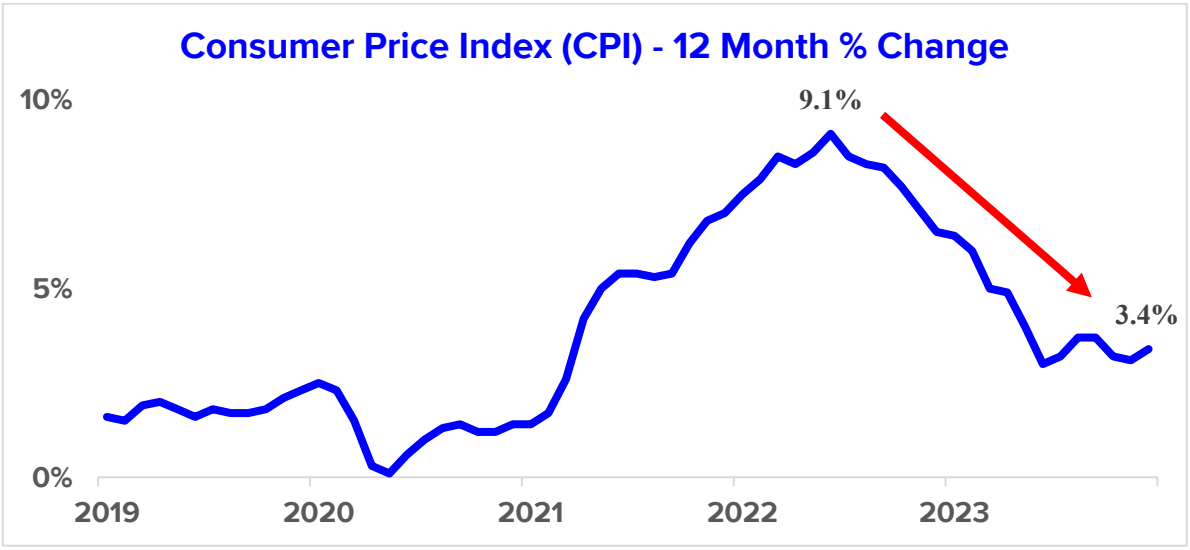
Source: Strategas Securities LLC as of 12/22/23

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Inflation Continues to Decline

Turning towards 2024, our focus remains on three key variables: inflation, interest rates, and corporate earnings. Inflation is expected to be a supportive force for equities in the upcoming year. After reaching a peak of 9.1%, inflation has steadily receded, hovering around 3.5% (refer to Chart III). Debates abound on the drivers behind this decline, with two significant factors emerging: the normalization of the global supply chain post-Covid and the impact of Fed rate hikes on slowing economic growth.

Chart III



Source: Wealth Enhancement Group using Federal Reserve data as of 1/22/2024

We've previously argued that the disruptions caused by the Covid economic shutdown lingered in global supply chains for years. These supply chain issues appear to finally be resolving. The other factor, Fed rate hikes, has effectively moderated economic growth while keeping a recession at bay thus far. The economy seems to be on solid footing given the stable unemployment rate (Chart IV) and positive GDP growth (Chart V). Some believe the Fed policy was expertly managed, or the Fed is losing efficacy as a market force. Whichever explanation you choose, the Fed is getting what it wanted without the massive repercussions so many expected to see.

Chart IV

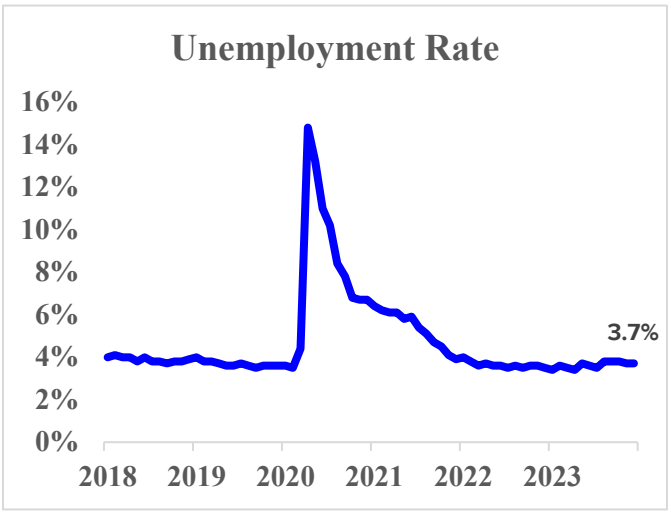
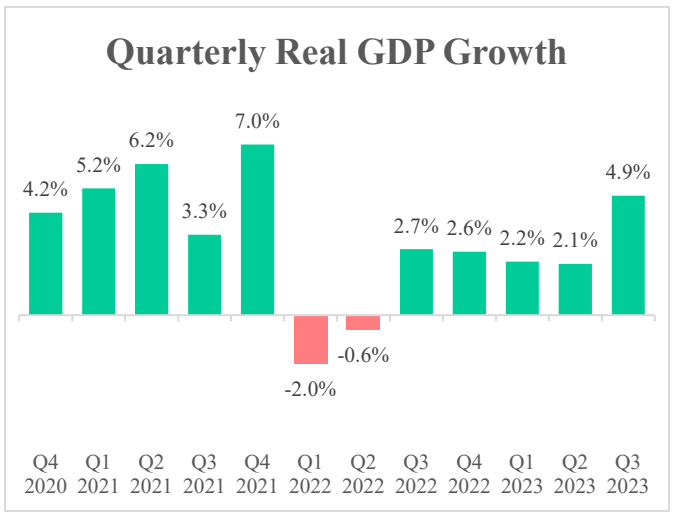


Chart V



Source: Wealth Enhancement Group using Bloomberg data as of 1/22/2024

In light of lower inflation, the Fed is expected to cut interest rates this year. Market consensus expects the Fed to cut rates to around 4% at the end of 2024, down from 5.3% currently. All else equal, equity investors prefer lower rates. Lower rates raise the value of future cash flows and therefore stock prices (see charts below).

Chart VI

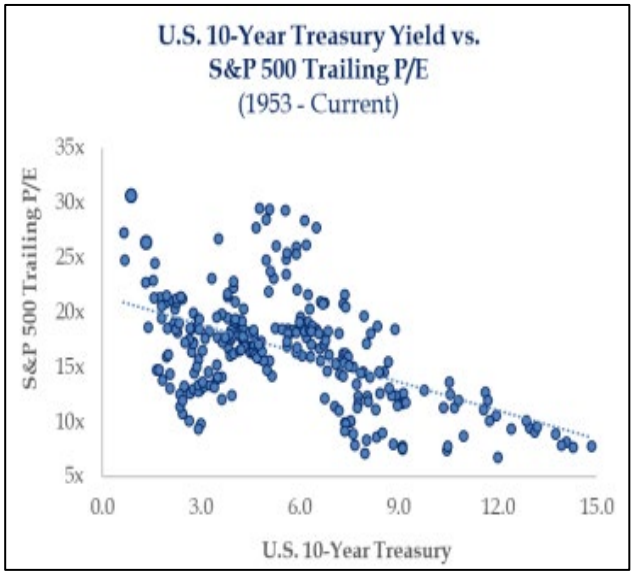
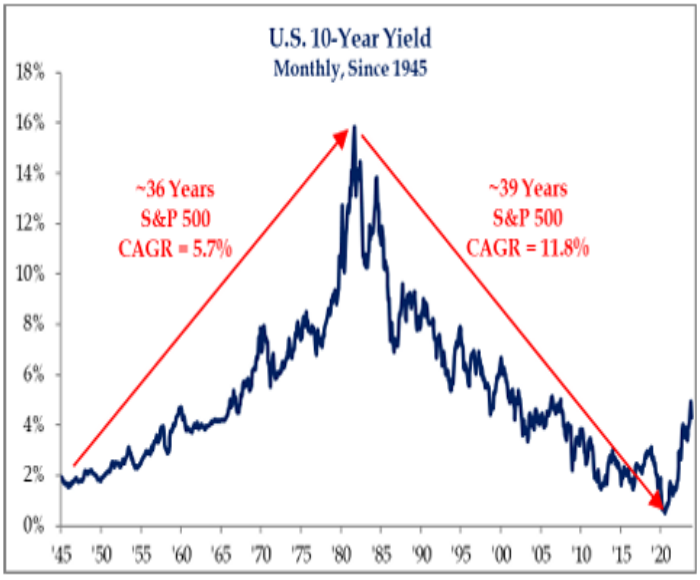


Chart VII

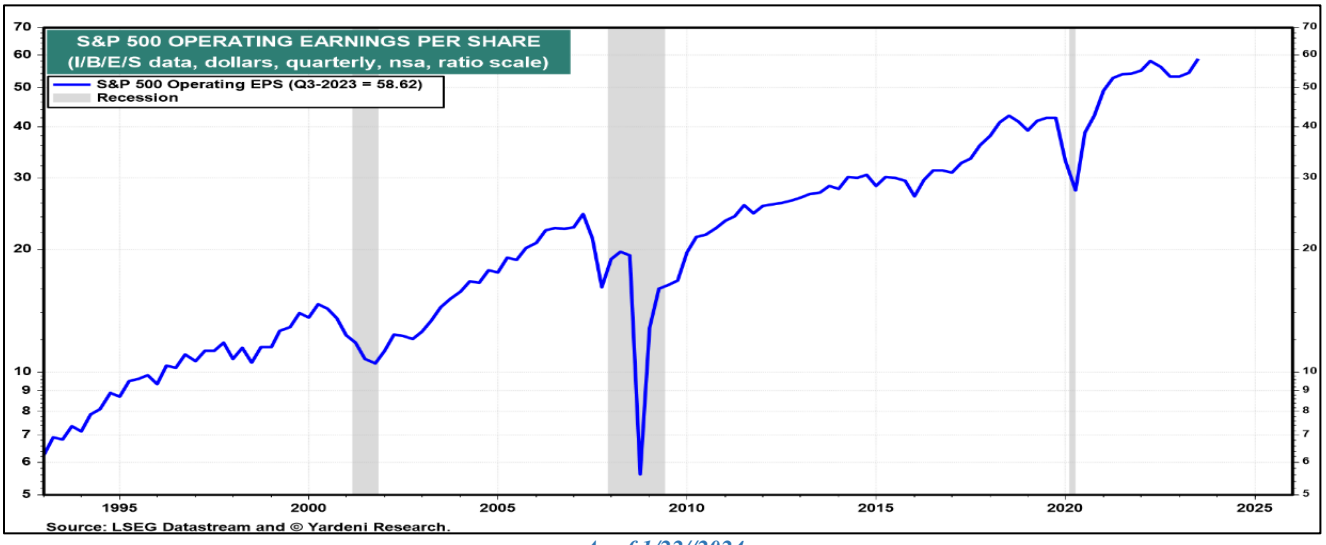


Source: Strategas Securities LLC as of 12/22/2023

Anticipating an Earnings Rebound in 2024

Interestingly, corporate earnings experienced a slight dip last year, contributing to an earnings recession. Yet investors turned increasingly bullish on the market's growth prospects as the likelihood of a severe recession waned. This shift in sentiment led to a rise in P/E multiples, propelling the impressive rally in 2023. However, the sustainability of the market rally hinges on corporate profits accelerating in 2024. Despite 0% earnings growth in 2023, analysts project a robust 10% rise in S&P 500 earnings this year (see chart VIII below). We will be closely watching the earnings growth outlooks for our portfolio companies during the upcoming earnings season.

Chart VIII



As of 1/22//2024

Macro Bull/Bear for 2024

Surveying the macroenvironment, numerous bullish factors come into view, beyond the anticipated move lower in interest rates. The economy is growing, market breadth is expanding, unemployment remains under 4%, inflation is falling, and mortgage rates are starting to decline.

Bears would argue that:

- Inflation is sticky and no longer coming down (and may even rise)
- The Fed historically does not execute a soft landing
- Investor sentiment is too bullish and equity markets have risen too far too fast
- There are two ongoing wars
- China is slowing and threatening a takeover of Taiwan
- The housing market is broken due to high mortgage rates and low inventory
- Consumers are running out of the funds they accumulated during Covid

But if 2023 taught us anything, it's to never underestimate the resilience and innovation of American enterprise. Innovations in technology involving generative AI could dramatically improve business productivity. In the healthcare sector, weight-loss drugs could have a broad impact on several business trends, from food consumption to fashion to healthcare treatment costs. Innovation drives growth and we seek to find those companies that will be in a position to benefit from these growth trends.

Evergreen Investing Philosophy

There will always be negative headlines. We're partially grateful for the negative headlines – they give us the opportunity to continue buying high-quality businesses at discounted prices. Just as a small business owner wouldn't sell their business based on a headline in the morning paper, we try not to overreact to short term news. Our goal is to buy high-quality businesses at fair prices and hold them for the long term. We recently added positions in companies fitting this mold—leaders in their respective industries, boasting quality management, a strong track record of execution, substantial cash flow generation, and reasonable valuations.

New Additions



Vertex Pharmaceuticals (VRTX) -

Vertex is a $100+ billion market cap biotech company based out of Boston, Massachusetts. They have $11 billion in cash on hand and generate $4 billion in free cash flow per year. The company has a dominant position in cystic fibrosis (CF), generating over $9 billion in annual revenue from CF alone. They recently announced a potential cure for sickle cell disease using CRISPR technology. CRISPR is a gene-editing therapy where Vertex takes the patient's own stem cells, edits them in a lab, then puts them back into the patient's body. The re-engineered stem cells are then able to potentially cure the disease. This is the first FDA-approved CRISPR therapy. VRTX has also developed a non-opioid pain drug that analysts think could generate over $3 billion per year.

Vertex's strength is its research. The company reinvests 1/3rd of its sales back into research and development and they generated a 28% return on that R&D over the last 10 years. We like betting on quality management teams with

a proven track record and VRTX fits that mold. Despite this strong track record, $4+ billion in annual free cash flow, and 40%+ profit margins, Vertex only trades at a slight premium to the S&P 500.
In combination with the Vertex purchase, we exited our position in Morgan Stanley (MS). At the time of sale, Morgan Stanley was trading at its richest valuation in over 10 years. We decided to take advantage of a 30%+ run-up in MS shares and exit our position.

Palo Alto Networks (PANW) -
Palo Alto Networks is a $100+ billion market cap cybersecurity company. They are the largest cybersecurity company in the world by revenue and market cap. Cyber-attacks have risen by 20x in the last 10 years and should continue to rise for the foreseeable future. In the last six months alone, MGM and Clorox had cyber-attacks that cost them an estimated $100 million and $25 million, respectively. We expect that enterprises will continue to invest more in their cyber defenses which should support double-digit growth at PANW for years to come.

Xcel Energy (XEL) -
Xcel is a $34 billion market cap electrical and gas utility with operations in the Midwest and Southwest. The company has consistently achieved ~6% earnings and dividend growth over long periods. Combining their ~6% annual earnings growth with XEL's 3.5% dividend yield should generate 8-10% annual returns for shareholders.
Current investor sentiment favors growth stocks which has caused utility valuations to fall. We think this has created an attractive buying opportunity in utilities like Xcel. Despite no material change in the business, Xcel's P/E valuation is more than 30% below its historical average. And Xcel stands to benefit from falling interest rates given their high dividend yield and reliance on debt financing.

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